

MARRAKECH, INC.

**Consolidated Financial Statements
and Supplementary Information
with Independent Auditor's Report**

June 30, 2011 and 2010

MARRAKECH, INC.

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INDEPENDENT AUDITOR'S REPORT



GUILMARTIN • DIPIRO • SOKOLOWSKI LLC

CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITOR'S REPORT

The Board of Directors
Marrakech, Inc.:

We have audited the accompanying consolidated statements of financial position of Marrakech, Inc. (a nonprofit organization referred to as the Organization) as of June 30, 2011 and 2010, and the related consolidated statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Organization, as of June 30, 2011 and 2010 and the changes in their net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 20, 2012 on our consideration of the Organization's internal control over financial reporting and on our tests of their compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements of the Organization taken as a whole. The supplementary data included in Schedules 1 through 3 is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. The accompanying schedule of expenditures of state financial assistance is also presented for purposes of additional analysis as required by the Office of Policy and Management, *Compliance Supplement to the State Single Audit Act*, and is not a required part of the basic consolidated financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic consolidated financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic consolidated financial statements taken as a whole.

Guilmartin, DiPiro, Sokolowski LLC

Middletown, Connecticut
January 20, 2012

FINANCIAL STATEMENTS

MARRAKECH, INC.

Consolidated Statements of Financial Position

June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
<u>Assets</u>		
Current assets:		
Cash and cash equivalents	\$ 1,350,683	\$ 1,401,941
Restricted cash held by bank on deposit as compensating balance	508,755	566,498
Accounts receivable, net of allowance for doubtful accounts of \$296,031 in 2011 and \$326,399 in 2010	3,935,047	3,781,608
Due from Habilitative Resource Services, Inc.	6,722	209,562
Prepaid expenses	191,908	475,101
Total current assets	<u>5,993,115</u>	<u>6,434,710</u>
Fixed assets:		
Property and equipment, net	<u>13,499,741</u>	<u>12,429,323</u>
Other assets:		
Due from Whalley Housing Services I, Inc., net of allowance for doubtful accounts of \$78,000 in both years	59,120	55,157
Other assets	163,434	23,604
Total other assets	<u>222,554</u>	<u>78,761</u>
Total assets	<u>\$ 19,715,410</u>	<u>\$ 18,942,794</u>
<u>Liabilities and Net Assets</u>		
Current liabilities:		
Accounts payable	\$ 526,835	\$ 758,761
Accrued liabilities	2,273,868	2,585,467
Due to grantors	621,650	684,991
Deferred revenue, current portion	129,402	260,212
Current portion of mortgages and loans	2,352,953	2,080,140
Current portion of obligations under capital lease	-	58,742
Total current liabilities	<u>5,904,708</u>	<u>6,428,313</u>
Long-term liabilities:		
Mortgages payable, less current portion	5,405,489	5,249,963
Loans payable, less current portion	2,707,133	1,593,784
Obligations under capital lease, less current portion	-	394,973
Derivative debt agreements	275,616	-
Deferred revenue, less current portion	459,371	457,195
Cash advance payable	429,909	429,909
Contingent liabilities - see Note 7	-	-
Total long-term liabilities	<u>9,277,518</u>	<u>8,125,824</u>
Total liabilities	<u>15,182,226</u>	<u>14,554,137</u>
Net assets:		
Unrestricted	3,990,707	3,818,165
Temporarily restricted	542,477	570,492
Total net assets	<u>4,533,184</u>	<u>4,388,657</u>
Total liabilities and net assets	<u>\$ 19,715,410</u>	<u>\$ 18,942,794</u>

See accompanying notes to financial statements.

MARRAKECH, INC.

Consolidated Statements of Activities

For the years ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
<u>Changes in Unrestricted Net Assets</u>		
Revenue and other support:		
Operating revenue	\$ 30,823,253	\$ 28,086,427
Donations and fund-raising	217,016	175,458
Interest income	3,253	2,315
Net assets released from restrictions	<u>28,015</u>	<u>33,792</u>
Total unrestricted revenue and other support	<u>31,071,537</u>	<u>28,297,992</u>
Operating expenses:		
Salary	19,131,774	17,522,256
Non-salary	7,127,691	6,328,094
Employee benefits	<u>4,911,571</u>	<u>3,973,243</u>
Total operating expenses	<u>31,171,036</u>	<u>27,823,593</u>
(Decrease) increase in unrestricted net assets before other income	<u>(99,499)</u>	<u>474,399</u>
Other income (expense):		
Contribution associated with capital lease obligation release (see Note 11)	547,657	-
Change in fair value of derivative debt agreements (see Note 5)	<u>(275,616)</u>	<u>-</u>
Total other income (expense)	<u>272,041</u>	<u>-</u>
Increase in unrestricted net assets	172,542	474,399
Unrestricted net assets, beginning of year as restated (see Note 10)	<u>3,818,165</u>	<u>3,343,766</u>
Unrestricted net assets, end of year	<u>\$ 3,990,707</u>	<u>\$ 3,818,165</u>
<u>Changes in Temporarily Restricted Net Assets</u>		
Donations	\$ -	\$ 73,629
Net assets released from restrictions	<u>(28,015)</u>	<u>(33,792)</u>
(Decrease) increase in temporarily restricted net assets	<u>(28,015)</u>	<u>39,837</u>
Temporarily restricted net assets, beginning of year	<u>570,492</u>	<u>530,655</u>
Temporarily restricted net assets, end of year	<u>\$ 542,477</u>	<u>\$ 570,492</u>
Total change in net assets	<u>\$ 144,527</u>	<u>\$ 514,236</u>

See accompanying notes to financial statements.

MARRAKECH, INC.

Consolidated Statements of Cash Flows

For the years ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Cash flows from operating activities:		
Change in net assets	\$ 144,527	\$ 514,236
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	789,136	666,661
Derivative debt agreements	275,616	-
Loss on disposal of assets	2,671	18,075
Contribution associated with capital lease obligation release	(547,657)	-
(Increase) in accounts receivable	(153,439)	(420,901)
Decrease (increase) in prepaid assets	283,193	(109,998)
(Increase) decrease in other assets	(139,831)	33,873
(Decrease) increase in accounts payable	(231,927)	371,212
(Decrease) increase in accrued liabilities	(311,599)	395,078
(Decrease) increase in due to grantors	(63,341)	29,693
Decrease (increase) in due from others	198,878	(38,273)
(Decrease) in due to others	-	(17,781)
(Decrease) in deferred revenue	(128,634)	(16,672)
Total adjustments	(26,934)	910,967
Net cash provided by operating activities	<u>117,593</u>	<u>1,425,203</u>
Cash flows from investing activities:		
Cash payments for the purchase and development of property	(1,642,083)	(2,229,621)
Net cash (used) by investing activities	<u>(1,642,083)</u>	<u>(2,229,621)</u>
Cash flows from financing activities:		
Proceeds of line of credit	4,450,000	3,950,000
Repayment of line of credit	(3,950,000)	(3,570,000)
Proceeds of long-term debt	1,613,855	1,433,553
Principal payments on loans and capital leases	(698,366)	(652,256)
Net cash provided by financing activities	<u>1,415,489</u>	<u>1,161,297</u>
Net (decrease) increase in cash and cash equivalents	(109,001)	356,879
Cash and cash equivalents, beginning of year	<u>1,968,439</u>	<u>1,611,560</u>
Cash and cash equivalents, end of year	<u>\$ 1,859,438</u>	<u>\$ 1,968,439</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest expense	\$ 577,505	\$ 492,625
Non-cash investing and financing activities:		
Acquisition and development of property and acquisition of vehicles through debt financing	\$ 220,142	-
Transfer of property at net book value to HRS	-	<u>\$ 180,900</u>

See accompanying notes to financial statements.

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2011 and 2010

NOTE 1

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of activities

These consolidated financial statements include Marrakech, Inc. and its sister corporations, Marrakech Housing Options, Inc., Marrakech Day Services, Inc. and Marrakech Residential Services, Inc. (the Agencies).

Marrakech, Inc. operates programs for persons with disabilities in the State of Connecticut. Additionally, it provides management services for Marrakech Housing Options, Inc., Marrakech Day Services, Inc. and Marrakech Residential Services, Inc.

Marrakech Housing Options, Inc. and Marrakech Residential Services, Inc. operate private group homes, supported living arrangements and day programs for persons with disabilities in the State of Connecticut. The operating revenue for the Agencies comes primarily from the Connecticut Departments of Developmental Services (DDS) and Social Services (DSS) and the Social Security Administration (SSA).

Marrakech Day Services, Inc. operates vocational day programs which are licensed by the State of Connecticut for disadvantaged and developmentally disabled persons. It is principally funded through cost reimbursements from the State of Connecticut Department of Mental Health and Addiction Services (DMHAS).

Basis of presentation

The consolidated financial statements of the Agencies have been prepared on the accrual basis of accounting. Significant intercompany accounts and transactions have been eliminated on the consolidated statements of financial position, consolidated statements of activities and consolidated statements of cash flows.

A summary of the Agencies' significant accounting policies is as follows:

Income tax status

The Agencies have received exemption from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. The Agencies have also been classified as entities that are not private foundations within the meaning of Section 509(a) and qualify for deductible contributions as provided in Section 170(b)(1)(A)(vi).

Management has reviewed the Agencies reporting and believe that no tax positions have been taken that are more likely than not to be determined to be incorrect by the Internal Revenue Service and therefore no adjustments or disclosures are required.

Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the certain reported amounts. Accordingly actual results could differ from those estimates.

Cash and cash equivalents

For the purpose of the statements of cash flows, the Agencies consider all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Allowance for bad debts

The allowance for doubtful accounts is based on management's evaluation of specific accounts receivable at the end of the year. Receivables are written off to the allowance when it is probable that the amounts will not be collectible.

Property and equipment

The Agencies follow the practice of capitalizing at cost all property and equipment with costs in excess of stated amounts as required by the Agencies' funding sources. Depreciation is computed using the straight-line method over the estimated useful lives of the assets which range from 3 to 30 years. Maintenance and repairs are charged to expenses as incurred.

Derivative debt agreements and interest rate risk management

During the fiscal year ended June 30, 2011, Marrakech, Inc. entered into variable rate debt agreements (interest rate swaps) related to the first and second mortgages on its newly developed Clinton Harbor intermediate care facility as well as its refinance of the balloon payment due on its Whalley Avenue property in New Haven, Connecticut. These arrangements enabled Marrakech, Inc. to fix the currently low interest rates on these obligations for ten years. Under the interest rate swap contracts, Marrakech, Inc. agrees to pay an amount equal to a specified fixed-rate of interest times a notional principal amount, and to receive in return an amount equal to a specified variable-rate of interest times a notional amount.

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2011 and 2010

Derivative debt agreements and interest rate risk management, continued

No other cash payments are made unless the contract is terminated prior to maturity, in which case the amount paid or received in settlement is established by agreement at the time of the termination and usually represents the net present value, at current rates of interest, of the remaining obligations to exchange payments under the term of the contract. Marrakech, Inc. accounts for these swaps as cash flow hedges. Marrakech, Inc. does not issue or hold derivative contracts for speculative purposes.

Net asset categories

To ensure observance of limitations and restrictions placed on the use of resources available to the Agencies, the limitations and restrictions are maintained in the following net asset categories:

Unrestricted

All of the Agencies' unrestricted net assets are for general use by the corporations.

Temporarily restricted

Temporarily restricted net assets represent costs of buildings, building renovations and vehicles acquired via donation or grant awards. The Agencies must utilize the respective properties to which these contributions or grants pertain in accordance with any restrictive covenants and for any designated time periods set forth as conditions of the awards.

Where specific time frames have been stipulated for qualified use, assets are released from restriction either ratably over the period of restriction or in full at the period's end, in keeping with grantor restrictions. Where no designated time frame for qualified use has been set, assets are released from restriction in amounts equal to the annual depreciation taken over their useful lives in accordance with the Agencies' depreciation policies.

As of June 30, 2011, there are temporarily restricted net assets of \$542,477.

NOTE 2

CONCENTRATIONS

The Agencies maintain their cash balances with various financial institutions. Such deposits at times have exceeded federal depository limits; however, the Agencies believe their cash deposits are not subject to significant credit risk.

A substantial portion of the Agencies' revenue is derived from grant contracts. Because the grants are evidenced by signed contracts with government and other agencies, management believes there is nominal credit risk associated with any outstanding grants receivable.

NOTE 3

REVENUES

Grants and contracts

The operating revenue for the Agencies comes primarily from the State of Connecticut Departments of Developmental Services (DDS), Children and Families (DCF) and Social Services (DSS), the Social Security Administration (SSA), the Department of Labor (DOL) and the Department of Mental Health and Addiction Services (DMHAS).

Grants and contracts are agreements in which the grantor or contractor requires expenditures for the performance of specified activities. The Agencies record their grant or contract revenue equal to the expenditure of funds in accordance with grant specification. Grant and contract receipts in excess of allowable expenditures are recorded as deferred revenue if the grant extends beyond the Agencies' fiscal year and as due to grantor if the grant was completed within the fiscal year.

Bond revenue

Contributions received under grant-in-aid bonding and other agreements, to finance the acquisition and development of property to be dedicated to a specific use over a required number of years, are recorded as deferred revenue on the Agencies' statements of financial position. Revenue is then recognized ratably over the restricted use period as the liability for repayment to the donor is reduced by any applicable forgiveness provisions.

Fund-raising

Marrakech conducts various fund-raising activities during the year including various special events and appeals for donations. The total cost of fund-raising activities was \$62,411 and \$63,475 for the years ended June 30, 2011 and 2010, respectively which included salary and benefits associated with Marrakech staff involved in fund-raising activities of \$19,311 in both years.

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2011 and 2010

NOTE 4

PROPERTY AND EQUIPMENT

Components of property and equipment are as follows:

	<u>2011</u>	<u>2010</u>
Furniture and equipment	\$ 1,233,014	\$ 1,159,168
Transportation equipment	2,674,524	2,460,893
Buildings, land and improvements	16,271,410	12,749,481
Construction-in-progress	<u>7,931</u>	<u>2,024,126</u>
	20,186,879	18,393,668
Less: accumulated depreciation	<u>6,687,138</u>	<u>5,964,345</u>
Total	<u>\$13,499,741</u>	<u>\$12,429,323</u>

Depreciation expense was \$789,136 and \$665,997 for the years ended June 30, 2011 and 2010, respectively.

NOTE 5

DEBT OBLIGATIONS

Line of credit

Marrakech has a revolving line of credit with Citizens Bank which expired as of September 30, 2010 and was renewed by the bank through June 30, 2012. Advances on the line of credit are payable on demand and bear interest at a variable rate under the note agreement. The maximum amount which may be withdrawn under the agreement is \$2,000,000. The interest rate was 4.25% as of June 30, 2011 and 2010 and the balances due were \$1,750,000 and \$1,250,000, respectively. The obligation has been guaranteed by each Agency.

Construction loan financing for Clinton Harbor facility

During the fiscal year ended June 30, 2010, Marrakech entered into a construction loan agreement with Citizens Bank for the build-out of its Clinton Harbor property, a 15 bed intermediate care facility for developmentally disabled individuals. Advances on the loan were made by the bank as construction progressed and totaled \$1,086,145 through June 30, 2010. During the fiscal year ended June 30, 2011, the bank had advanced additional funds of \$1,613,855 up to the maximum amount permitted of \$2,700,000 as of January 31, 2011.

Permanent financing of the construction loan

The construction loan was subsequently converted into two term loans of \$1,700,000 and \$1,000,000 as provided under

the original agreement. As of June 30, 2011, the balances owed on these loans are \$1,639,104 and \$988,492, respectively and are payable in equal monthly amounts of principal of \$10,149 and \$1,918, respectively plus interest on each loan's respective monthly balance at 6.88% and 7.17% per annum on each loan, respectively. Principal balances on the loans are reset on an annual basis in accordance with each loan's amortization schedule. Both loans mature on January 1, 2021 (ten years). The \$1,700,000 loan is being amortized on a ten year schedule and the \$1,000,000 loan is amortized over a twenty year time frame. The loans are secured by Marrakech's Clinton Harbor Home and Woodbridge main office properties, including all improvements on each. These loans are included in the schedule of debt obligations at Table 5.1 at the end of these footnotes.

The aforementioned loans, along with another term loan which had been refinanced during the fiscal year ended June 30, 2011, have been financed as "interest rate swap loans" as per the terms of a master agreement of the International Swap Dealers Association, Inc. These loans include credit-risk-related contingent features whereby the Agency could incur additional liabilities should the agreements be terminated before maturity by Marrakech (see Note 1). As of the fiscal year ended June 30, 2011, the agreements are in a net liability position totaling \$275,616, which is shown on the Agency's consolidated statements of financial position under long-term liabilities as "derivative debt agreements." Please see Note 1 under "Derivative debt agreements and interest rate risk management" for additional information.

Other mortgages, loans and capital lease obligations

The Agencies have additional mortgages, notes payable and capital lease obligations as of June 30, 2011 and 2010. Please see the schedule of debt obligations (Table 5.1) and their respective terms at the end of these footnotes.

NOTE 6

LEASE OBLIGATIONS

Capital leases

Marrakech Housing Options, Inc. has entered into five residential lease agreements with CIL Realty, Inc. (CIL) and is responsible for operating costs such as insurance, property taxes and maintenance. Upon the expiration of these leases, the facilities will be donated to Marrakech Housing Options, Inc. On December 10, 2010, CIL had transferred one property (60 Knollwood Drive, New Haven, Connecticut) to the Agency. The remaining four properties have been transferred to the Agency by CIL effective March 31, 2011 prior to the original lease term. Further payments are not required. The remaining lease liability at the date of the

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2011 and 2010

Capital leases, continued

transfer totaling \$409,657 has been recorded as other income in the accompanying statements of activities.

The following capitalized leased assets have been included in property and equipment (Note 4).

	<u>2011</u>	<u>2010</u>
Building and improvements	\$1,301,976	\$1,301,976
Land	<u>210,098</u>	<u>210,098</u>
	1,512,074	1,512,074
Less: accumulated amortization	<u>931,432</u>	<u>888,655</u>
	<u>\$ 580,642</u>	<u>\$ 623,419</u>

Depreciation expense on the capitalized leased assets was \$42,777 in both fiscal years ended June 30, 2011 and 2010 and has been included within depreciation expense in Note 4.

Interest expense incurred on the above lease was \$29,096 and \$44,658 for the years ended June 30, 2011 and 2010, respectively.

Leased facilities

The Agencies conduct a significant part of their operations from leased facilities. Lease commitments include leases which expire at certain dates through January 30, 2016, as well as certain leases which are on a month-to-month basis. Management expects that in the normal course of business, leases will either be renewed or replaced by other leases. In certain leases the Agencies are required to pay certain operating costs. Various leases contain restrictions as to the use of the properties and subletting arrangements.

At June 30, minimum lease payments due under operating leases for facilities for the next five years ended June 30 are as follows:

2012	\$ 63,451
2013	65,036
2014	66,988
2015	68,988
2016	<u>11,557</u>
Total	<u>\$276,020</u>

Rent expense for the years ended June 30, 2011 and 2010 for these leased facilities was \$215,370 and \$262,167, respectively.

NOTE 7

CONTINGENCY

Marrakech has been awarded grant funding for acquisition of various properties and for building improvements over several years. These grant awards stipulate that if the Agency were to discontinue usage of the property for its specified grant purpose, the grant funds would be repayable, either in whole or a ratable portion (depending on years of usage), back to the grantor.

NOTE 8

CASH ADVANCES

The cash advance payable of \$429,909 as of June 30, 2011 and 2010 represents cumulative amounts advanced to Marrakech Housing Options, Inc. from the Connecticut Department of Developmental Services (DDS) for the first month's operating expenses for each of the residential programs. Each of these advances must be repaid if and when Marrakech Housing Options, Inc. no longer provides services under their respective facility license from DDS.

NOTE 9

DEFINED CONTRIBUTION PLAN

The Agencies have adopted a profit sharing plan covering all full-time employees who are at least twenty-one years old and have worked for the Agencies for at least one year. Each participant's interest in the employer's contributions and the earnings thereon are vested 20% after three years of service with an additional 20% vesting for each additional year of service thereafter, up to the maximum vesting of 100%. The Board of Directors determines the amount of the contribution each fiscal year which is allocated to each participant in the same proportion as his or her compensation bears to the compensation of all participants. Total expenses for the years ended June 30, 2011 and 2010 was \$ 573,954 and \$512,818, respectively.

NOTE 10

RESTATEMENTS

The June 30, 2010 financial statements have been restated for the following adjustments:

Capital lease versus operating lease

Marrakech Housing Options, Inc. leased five homes from CIL Realty, Inc. in fiscal year 2010 and prior years under agreements whereby ownership of the leased properties were to transfer to Marrakech Housing Options, Inc. at the conclusion of their lease terms.

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2011 and 2010

Capital lease versus operating lease, continued

Due to management's uncertainty with respect to this future transfer, the Agency recorded these obligations as operating leases on the June 30, 2010 and prior audited financial statements.

As indicated in the June 30, 2010 Auditor's Report this was a departure from accounting principles generally accepted in the United States of America. The accompanying financial statements reflect restatements to June 30, 2010 balances in order to properly record the above leases as capital leases versus operating leases.

Statements of financial position

The prior year statement has been adjusted to include five residential properties under property and equipment as well as the related capital lease liability obligations.

Statements of activities

The prior year statements of activities has been adjusted to reduce the lease payments previously recorded as rent and record depreciation for the building costs and interest expense on the capital lease obligation.

Statements of cash flows

This statement has been adjusted to correctly restate the changes in net assets and total adjustments accordingly based on the changes discussed above to the statements of financial position and statements of activities.

Summary of restatements

A tabular summary of the restatement of the change in unrestricted net assets for the fiscal year ended June 30, 2010 is as follows:

Effect on statements of financial position:

Net increase of property and equipment	\$623,419
Increase in current debt	58,742
Increase in long-term debt	<u>394,973</u>
Increase in net assets	<u>\$169,704</u>

Effect on statements of activities:

Decrease in lease payments	\$104,832
Increase in depreciation	42,777
Increase in interest expense	<u>44,658</u>
Increase in June 30, 2010 net income	17,397
Increase in unrestricted net assets, beginning of year	<u>152,307</u>
Increase in unrestricted net assets, end of year	<u>\$169,704</u>

NOTE 11

CONTRIBUTION ASSOCIATED WITH CAPITAL LEASE OBLIGATION RELEASE

As discussed in Note 6, CIL had transferred all properties to Marrakech Housing Options, Inc. effective March 31, 2011 and Marrakech Housing Options, Inc.'s remaining lease liability of \$409,657 has been forgiven and recorded as income. The Agency also had an outstanding debt owed to CIL of \$138,000 for working capital advances provided to Marrakech Housing Options, Inc. for operation of two of the properties in prior years. These liabilities have been forgiven by CIL. The total debt released and recorded as other income on the statements of activities for June 30, 2011 was \$547,657.

NOTE 12

SUBSEQUENT EVENTS

Evaluation of subsequent events

Management has evaluated subsequent events through January 20, 2012, the date on which the financial statements were available to be issued.

New mortgages taken to acquire property and finance capital repairs to group home

On December 22, 2011, The Agency acquired a building at 50 Oak Tree Avenue, Waterbury, Connecticut for the purpose of consolidating several day programs that had previously been operating out of two leased premises. The purchase price of \$840,000 was 80% financed by a mortgage for \$672,000. On the same date, the Agency also took out a mortgage loan in the amount of \$200,000 to finance various capital repairs needed to one of its group homes located at 60 Knollwood Drive, New Haven, Connecticut.

Variable rate debt agreements were executed for both loans (as described in Note 1). The mortgage on the Waterbury property is repayable over ten years, in equal monthly

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2011 and 2010

New mortgages taken to acquire property and finance capital repairs to group home, continued

payments of \$4,226, principal and interest. The mortgage on the New Haven property is repayable over ten years in equal monthly payments of \$1,104, principal and interest. The interest rate on the Waterbury and New Haven property loans is fixed at 4.43%. Monthly payment amounts were calculated using twenty and twenty-five year amortization periods, respectively.

NOTE 13

LITIGATION

The Agencies are periodically subject to claims and lawsuits that arise in the normal course of business. Management believes that any financial responsibility that may be incurred in settlement of such claims and lawsuits will be reported when the outcome can be accurately estimated.

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2011 and 2010

Table 5.1 - Schedule of Debt Obligations

<u>Lender/Collateral</u>	<u>Interest Rate</u>	<u>Monthly Payment</u>	<u>Maturity Date</u>	<u>2011</u>	<u>2010</u>
<u>Mortgages payable</u>					
CCO Mortgage Corporation 106-108 Sherman Avenue, New Haven, Connecticut	4.25%	\$ 903	05/01/18	\$ 64,147	\$ 72,722
CCO Mortgage Corporation 60 Plainfield Avenue, New Haven, Connecticut	8.25%	270	07/01/30	31,090	31,795
CCO Mortgage Corporation 615-617 Whalley Avenue, New Haven, Connecticut	8.25%	338	08/01/30	38,933	39,807
CCO Mortgage Corporation 106-108 Hobart Street, New Haven, Connecticut	6.50%	484	09/01/31	65,115	66,755
CCO Mortgage Corporation 158R Meetinghouse Road, Durham, Connecticut	5.50%	1,416	03/01/36	229,058	233,667
CCO Mortgage Corporation 27-29 Robbins Street, Waterbury, Connecticut	5.63%	1,151	05/01/36	184,657	188,256
CCO Mortgage Corporation 85 Talmadge Hill Road, Prospect, Connecticut	5.88%	2,395	08/01/36	376,741	383,146
CCO Mortgage Corporation 88-90 Sherman Avenue, New Haven, Connecticut	5.63%	1,891	11/01/36	305,616	311,385
CCO Mortgage Corporation 25 Kreger Drive, Wolcott, Connecticut	5.63%	1,917	06/01/37	313,233	318,655
CCO Mortgage Corporation 32-34 Plant Street, New Haven, Connecticut	4.13%	894	10/01/40	182,128	-
Citizens Bank 514-526 Whalley Avenue, New Haven, Connecticut	2.69%	1,512	05/18/21	234,749	252,434
Citizens Bank 6 Lunar Drive, Woodbridge, Connecticut	5.90%	2,880	12/02/11	16,905	53,037
Community Capital Fund Properties located in Bridgeport, Connecticut at 1041-1043 Main Street, 1053-1057 East Main Street, 224 Beach Street and 426-436 Artic Street	3.00%	1,054	01/01/18	232,194	238,243
Connecticut Department of Developmental Services 43 Ramsdell Street, New Haven, Connecticut	6.00%	1,120	03/01/18	72,943	83,142
Connecticut Department of Developmental Services 159 Osborn Avenue, New Haven, Connecticut	6.00%	1,675	06/01/19	126,219	139,332
Connecticut Department of Developmental Services 25 Kreger Drive, Wolcott, Connecticut	6.00%	1,441	07/01/38	230,926	234,263
Connecticut Housing Finance Authority 21 Victor Hill Road, Branford, Connecticut	7.34%	2,017	09/01/26	221,773	229,400
Connecticut Housing Finance Authority 33 Lake Street, West Haven, Connecticut	6.93%	2,343	07/16/27	272,830	281,686
Connecticut Housing Finance Authority 92 Hurd Road, Trumbull, Connecticut	6.63%	1,734	10/01/30	226,515	232,113
Connecticut Housing Finance Authority 92 View Terrace, East Haven, Connecticut	6.63%	1,740	10/01/30	227,323	232,940
Connecticut Housing Finance Authority 2 Anton Circle, Bridgeport, Connecticut	5.75%	2,425	01/01/33	359,303	367,482
TD Bank Properties located in Bridgeport, Connecticut at 1041-1043 Main Street, 1053-1057 East Main Street, 224 Beach Street and 426-436 Artic Street	7.00%	3,210	12/28/16	417,676	426,217
Wachovia Bank 597 East Street, New Haven, Connecticut	6.66%	1,999	10/01/16	105,877	122,109
Wachovia Bank 118 Migeon Avenue, Torrington, Connecticut	6.25%	1,242	06/01/18	83,260	92,563
Wachovia Bank 615-617 Whalley Avenue, New Haven, Connecticut	7.25%	1,141	08/01/19	85,027	92,182
Wachovia Bank 450 Island Lane, West Haven, Connecticut	7.15%	10,957	10/27/21	953,991	1,013,936
Total mortgages payable				5,658,229	5,737,267
<u>Capital lease obligations</u>					
CIL Realty, Inc./Five group homes, land and buildings and various improvements. Debt was forgiven as of March 31, 2011.	2.5% to 11.20%	\$20 to \$2,582	01/31/13 to 12/30/25	-	453,715
				5,658,229	6,190,982
Less: current portion				(252,740)	(546,046)
Total mortgages and capital leases payable, net of current portion				\$ 5,405,489	\$ 5,644,936

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2011 and 2010

Table 5.1 - Schedule of Debt Obligations, Continued

<u>Lender/Collateral</u>	<u>Interest Rate</u>	<u>Monthly Payment</u>	<u>Maturity Date</u>	<u>2011</u>	<u>2010</u>
<u>Loans payable</u>					
CIL Realty, Inc./Accounts receivable	8.50%	\$ 486	01/01/13	\$ -	\$ 27,103
CIL Realty, Inc./All of the Agencies' contract rights and accounts receivable pertaining to certain group homes of Marrakech	0.00%	-	Various	-	138,000
Citizens Bank Construction loan - see Note 5	3.10%	-	Various	-	1,086,146
Citizens Bank promissory note - see Note 5	2.94%	1,918	01/01/21	988,492	-
Citizens Bank promissory note - see Note 5	2.94%	10,149	01/01/21	1,639,104	-
Citizens Bank Line of Credit - see Note 5	4.25%	-	12/31/10	1,750,000	1,250,000
Connecticut Department of Developmental Services/Unsecured	6.00%	207	07/01/10	-	206
Connecticut Department of Developmental Services/Unsecured	6.01%	193	01/01/12	940	3,323
Connecticut Department of Developmental Services/Unsecured	6.01%	106	09/01/12	1,430	2,587
Connecticut Department of Developmental Services/Unsecured	6.01%	187	01/01/13	3,279	5,192
Connecticut Department of Developmental Services/Unsecured	6.00%	201	10/01/13	5,060	7,102
Connecticut Department of Developmental Services/Unsecured	6.00%	116	10/01/13	2,933	4,115
Connecticut Department of Developmental Services/Unsecured	6.00%	181	04/01/16	8,957	10,669
Connecticut Department of Developmental Services/Unsecured	6.01%	523	06/01/16	8,772	14,524
Connecticut Department of Developmental Services/Unsecured	6.00%	98	07/01/16	5,043	5,889
GMAC/Automobile	6.00%	129	10/01/18	9,067	10,037
GMAC/Automobile	9.15%	567	11/02/09	-	-
GMAC/Automobile	9.15%	567	11/02/09	-	-
JP Morgan Chase Bank/Automobile	6.83%	482	03/01/12	3,739	9,020
JP Morgan Chase Bank/Automobile	6.64%	432	05/07/12	4,197	8,929
Lakeland Bank/Automobile	10.82%	1,164	04/20/14	33,950	-
New Alliance Bank/First lien interest in personal property acquired with loan proceeds	7.01%	9,867	01/01/11	-	34,725
New Alliance Bank/First lien interest in personal property acquired with loan proceeds	7.07%	9,680	05/01/12	94,213	199,269
New Alliance Bank/Security agreement for specified corporate assets of Marrakech, Inc.	7.25%	6,940	08/01/14	229,280	293,002
Peoples Bank/Various non real estate assets of group homes located at 20 Cortina Road, East Haven, Connecticut and 470 Stevenson Road, New Haven, Connecticut and a \$100,000 Certificate of Deposit	8.45%	4,385	09/01/11	8,755	61,385
Toyota Credit Corporation/Automobile	6.96%	514	04/15/13	10,135	15,397
				4,807,346	3,186,620
				(2,100,213)	(1,592,836)
Less: current portion					
Total loans payable, net of current portion				\$ 2,707,133	\$ 1,593,784

Minimum future principal payments on mortgages and loans for the next five years are as follows:

2012	\$ 2,352,953
2013	515,174
2014	536,522
2015	483,474
2016	493,046
Thereafter	6,222,406
	<u>\$ 10,603,575</u>

Interest expense related to the above mortgages and loans and the Agencies' line of credit for the years ended June 30, 2011 and 2010 was \$577,505 (inclusive of capitalized interest of \$34,893 for the Agencies' construction of it's Clinton facility) and \$492,625, respectively.

SUPPLEMENTARY INFORMATION

MARRAKECH, INC.

Consolidated Supporting Schedule of Operating Revenue

For the years ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Department of Developmental Services	\$ 18,208,093	\$ 16,499,296
Department of Social Services Room and Board	4,127,462	3,378,577
Caning revenue	21,790	20,354
Rental revenue	280,413	271,724
ABI revenue	2,430,687	1,967,599
BESB revenue	90,459	288,006
DMHAS	2,944,633	2,739,399
DCF Work/Learn and Children Services programs	1,215,509	1,605,501
HSTP revenue	366,187	450,395
BRS revenue	467,623	446,848
Other revenue	<u>670,397</u>	<u>418,728</u>
	<u>\$ 30,823,253</u>	<u>\$ 28,086,427</u>

MARRAKECH, INC.

Consolidated Supporting Schedule of Non-Salary

For the years ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Rent	\$ 214,259	\$ 269,457
Utilities	787,454	656,317
Food and household supplies	416,437	341,311
Plant maintenance and repairs	434,042	313,506
Depreciation and amortization	794,667	666,661
Professional fees	207,599	179,919
Interest	542,612	492,625
Property taxes	112,725	117,938
Transportation	928,685	830,250
Consultants	1,078,560	891,490
Insurance	373,839	354,056
Advertising	91,448	61,807
Program supplies	310,063	260,596
Medical supplies	128,295	66,042
Equipment expenses	180,787	282,286
Training	181,455	152,875
Dues, fees and licenses	37,571	22,394
Miscellaneous	<u>307,193</u>	<u>368,564</u>
	<u>\$ 7,127,691</u>	<u>\$ 6,328,094</u>

MARRAKECH, INC.

Consolidated Supporting Schedule of Employee Benefits

For the years ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
FICA	\$ 1,423,873	\$ 1,301,473
Health insurance benefits	1,646,332	1,286,404
Unemployment insurance	523,392	368,583
Workers' compensation insurance	715,502	472,260
Miscellaneous	28,518	31,960
Pension expense	<u>573,954</u>	<u>512,563</u>
	<u>\$ 4,911,571</u>	<u>\$ 3,973,243</u>

MARRAKECH, INC.

Schedule of Expenditures of State Financial Assistance

For the year ended June 30, 2011

State Grantor Pass-Through Grantor Program Title	State CORE - CT Number	Expenditures
Department of Developmental Services:		
Community Living Arrangements	11000-DDS50000-16122	\$ 9,239,818
Community Training Home Support	11000-DDS50000-16122	97,664
Supported Living Arrangements	11000-DDS50000-16122	3,232,443
Day Services	11000-DDS50000-16108	3,461,070
Fee For Service (Waiver)	11000-DDS50000-unknown	1,934,683
Department of Mental Health and Addiction Services:		
Mental Health Service Grants	11000-MHA53000-16053	325,758
Employment Opportunities	11000-MHA53000-16070	638,708
Discharge and Diversion Services	11000-MHA53000-12330	3,128
Special Population	11000-MHA53000-12250	1,920,934
Department of Social Services:		
Bureau of Rehabilitation Services	11000-DSS60771-16004	277,667
Department of Labor:		
Passed-through Northwest Regional Workforce Investment Board, Waterbury, Connecticut:		
Jobs First Employment Service	11000-DOL40000-12212	105,477
Passed-through Workforce Alliance, New Haven, Connecticut:		
Jobs First Employment Service	11000-DOL40000-12212	61,129
Passed-through The Workplace, Inc., Bridgeport, Connecticut:		
Jobs First Employment Service	11000-DOL40000-12212	62,778
Department of Children & Families:		
Work Learn Program	1100-DCF91110-16135	386,525
Work Learn Program	1100-DCF91110-16120	373,171
Total State Financial Assistance		<u>\$22,120,953</u>

See notes to schedule.

MARRAKECH, INC.

Notes to the Schedule of Expenditures of State Financial Assistance

For the year ended June 30, 2011

Various departments and agencies of the State of Connecticut have provided financial assistance to Marrakech, Inc., Marrakech Housing Options, Inc., Marrakech Day Services, Inc. and Marrakech Residential Services, Inc. through grants and other authorizations in accordance with the General Statutes of the State of Connecticut. These financial assistance programs fund several programs including Community Living Arrangements, Day Services, Family Support Services, Respite Services and General Assistance.

NOTE 1

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of Marrakech, Inc., Marrakech Housing Options, Inc., Marrakech Day Services, Inc. and Marrakech Residential Services, Inc. conform to generally accepted accounting principles as applicable to not-for-profit agencies. The following is a summary of the more significant policies relating to the aforementioned grant programs.

Basis of accounting

The financial statements contained in Marrakech, Inc.'s, Marrakech Housing Options, Inc.'s, Marrakech Day Services, Inc.'s and Marrakech Residential Services, Inc.'s annual audit report are prepared on the modified accrual basis of accounting. The following is a summary of such basis:

- Revenues are recognized when earned.
- Expenditures are recorded when incurred.

The Schedule of Expenditures of State Financial Assistance, contained in this report, is prepared based on regulations established by the State of Connecticut Office of Policy and Management. In accordance with these regulations (Section 4-236-22), certain grants are not dependent on expenditure activity, and accordingly, are considered to be expended in the fiscal year of receipt. These grant program receipts are reflected in the expenditures column of the Schedule of Expenditures of State Financial Assistance.

SUPPLEMENTARY REPORTS



GUILMARTIN ▪ DIPIRO ▪ SOKOLOWSKI LLC

CERTIFIED PUBLIC ACCOUNTANTS

**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**

The Board of Directors
Marrakech, Inc.:

We have audited the consolidated financial statements of Marrakech, Inc. as of and for the year ended June 30, 2011, and have issued our report thereon dated January 20, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Marrakech, Inc.'s internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of Marrakech, Inc.'s internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Marrakech, Inc.'s internal control over financial reporting.

A *deficiency* in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Marrakech, Inc.'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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

Guilmartin, DiPiro & Sokolowski, LLC

Middletown, Connecticut
January 20, 2012



GUILMARTIN • DIPIRO • SOKOLOWSKI LLC

CERTIFIED PUBLIC ACCOUNTANTS

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS THAT
COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH THE STATE SINGLE AUDIT ACT**

The Board of Directors
Marrakech, Inc.:

Compliance

We have audited Marrakech, Inc.'s compliance with the types of compliance requirements described in the *Office of Policy and Management Compliance Supplement* that could have a direct and material effect on each of Marrakech, Inc.'s major state programs for the year ended June 30, 2011. The major state programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major state programs is the responsibility of Marrakech, Inc.'s management. Our responsibility is to express an opinion on Marrakech, Inc.'s compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the State Single Audit Act (C.G.S. Sections 4-230 to 4-236). Those standards and the State Single Audit Act 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 state program occurred. An audit includes examining, on a test basis, evidence about Marrakech, Inc.'s compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Marrakech, Inc.'s compliance with those requirements.

In our opinion, Marrakech, Inc. complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major state programs for the year ended June 30, 2011.

Internal Control Over Compliance

Management of Marrakech, Inc. is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to state programs. In planning and performing our audit, we considered Marrakech, Inc.'s internal control over compliance with the requirements that could have a direct and material effect on a major state program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with the State Single Audit Act, 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 Marrakech, Inc.'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 state program on a timely basis. A *material weakness* in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a state program will not be prevented, or detected and corrected, on a timely basis.

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

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

Guilmartin D. P. & Sokolowski, LLC.

Middletown, Connecticut
January 20, 2012

MARRAKECH, INC.

Schedule of Findings and Questioned Costs

For the year ended June 30, 2011

1. SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued:

Unqualified

Internal control over financial reporting:

- Material weakness(es) identified?
- Significant deficiency(ies) identified?

____ Yes

 x No

____ Yes

 x None reported

Noncompliance material to financial statements noted?

____ Yes

 x No

State Financial Assistance

Internal control over major programs:

- Material weakness(es) identified?
- Significant deficiency(ies) identified?

____ Yes

 x No

____ Yes

 x None reported

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

Unqualified

Any audit findings disclosed that are required to be reported in accordance with Section 4-236-24 of the Regulations to the State Single Audit Act?

____ Yes

 x No

The following schedule reflects the major programs included in the audit:

<u>State Grantor and Program</u>	<u>State CORE - CT Number</u>	<u>Expenditures</u>
Department of Developmental Services:		
Community Living Arrangements	11000-DDS50000-16122	\$ 9,239,818
Community Training Home Support	11000-DDS50000-16122	97,664
Supported Living Arrangements	11000-DDS50000-16122	<u>3,232,443</u>
		<u>\$12,569,925</u>
Day Services	11000-DDS50000-16108	<u>\$ 3,461,070</u>
Fee For Service (Waiver)	11000-DDS50000-unknown	<u>\$ 1,934,683</u>

Dollar threshold used to distinguish between type A and type B programs: \$442,419

2. FINANCIAL STATEMENT FINDINGS

- We issued reports, dated January 20, 2012, 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.
- Our report on compliance indicated no reportable instances of noncompliance.
- Our report on internal control over financial reporting indicated no significant deficiencies.

3. STATE FINANCIAL ASSISTANCE FINDINGS AND QUESTIONED COSTS

No findings or questioned costs are reported relating to State Financial Assistance Programs.