

Phoenix Houses of Texas, Inc.

Financial Statements
and Single Audit Reports
for the year ended June 30, 2023

Phoenix Houses of Texas, Inc.

Table of Contents

	Page
Independent Auditors' Report	1
Financial Statements:	
Balance Sheets as of June 30, 2023 and 2022	3
Statements of Operations and Changes in Net Assets for the years ended June 30, 2023 and 2022	4
Statements of Functional Expenses for the years ended June 30, 2023 and 2022	5
Statements of Cash Flows for the years ended June 30, 2023 and 2022	6
Notes to Financial Statements for the years ended June 30, 2023 and 2022	7
Supplementary Information:	
Schedule of Expenditures of Federal Awards for the year ended June 30, 2023	15
Schedule of Expenditures of State Awards for the year ended June 30, 2023	17
Note to Schedule of Expenditures of Federal and State Awards for the year ended June 30, 2023	18
Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With <i>Government Auditing Standards</i>	19
Independent Auditors' Report on Compliance for Each Major Federal Program and Major State Program and Report on Internal Control Over Compliance Required by the Uniform Guidance and the <i>Texas Grant Management Standards</i>	20
Schedule of Findings and Questioned Costs for the year ended June 30, 2023	23
Corrective Action Plan	26

Independent Auditors' Report

To the Board of Directors of
Phoenix Houses of Texas, Inc.:

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Phoenix Houses of Texas, Inc., which comprise the balance sheets as of June 30, 2023 and 2022, and the related statements of operations and changes in net assets, of functional expenses, and of cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of Phoenix Houses of Texas, Inc. as of June 30, 2023 and 2022, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

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. Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Financial Statements* section of our report. We are required to be independent of Phoenix Houses of Texas, Inc. and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about Phoenix Houses of Texas, Inc.'s ability to continue as a going concern for one year after the date that the financial statements are available to be issued.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Phoenix Houses of Texas, Inc.'s internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about Phoenix Houses of Texas, Inc.'s ability to continue as a going concern for a reasonable period of time.

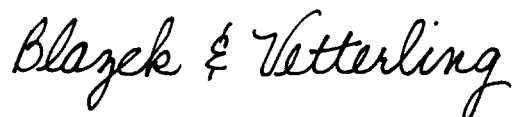
We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying supplementary information included in the schedule of expenditures of federal awards for the year ended June 30, 2023 as required by Title 2 U. S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* and in the schedule of expenditures of state awards for the year ended June 30, 2023 as required by the *Texas Grant Management Standards* is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the 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.

Report Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 8, 2024 on our consideration of Phoenix Houses of Texas, Inc.'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 solely 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 effectiveness of Phoenix Houses of Texas, Inc.'s 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 Phoenix Houses of Texas, Inc.'s internal control over financial reporting and compliance.



March 8, 2024

Phoenix Houses of Texas, Inc.

Balance Sheets as of June 30, 2023 and 2022

	<u>2023</u>	<u>2022</u>
ASSETS		
Current assets:		
Cash	\$ 1,224,470	\$ 2,209,731
Patient accounts receivable, net	527,053	480,620
Contributions receivable (Note 3)	237,500	237,500
Government grants receivable (Note 3)	280,140	307,638
Other assets	13,615	13,606
Prepaid expenses and other assets	<u>21,769</u>	<u>98,869</u>
Total current assets	2,304,547	3,347,964
Prepaid expenses	31,101	31,101
Contributions receivable (Note 3)		200,000
Right-of-use assets (Note 4)	223,237	
Property and equipment, net (Note 5)	<u>2,524,434</u>	<u>2,862,204</u>
TOTAL ASSETS	<u>\$ 5,083,319</u>	<u>\$ 6,441,269</u>
LIABILITIES AND NET ASSETS		
Liabilities:		
Accounts payable and accrued expenses	\$ 198,393	\$ 280,879
Accrued payroll and related benefits	389,565	468,569
Deferred revenue	407	103,239
Lease liabilities (Note 4)	<u>227,901</u>	<u> </u>
Total liabilities	<u>816,266</u>	<u>852,687</u>
Commitments and contingencies (Notes 10 and 12)		
Net assets:		
Without donor restrictions (Note 6)	3,931,003	4,869,934
With donor restrictions (Note 7)	<u>336,050</u>	<u>718,648</u>
Total net assets	<u>4,267,053</u>	<u>5,588,582</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 5,083,319</u>	<u>\$ 6,441,269</u>

See accompanying notes to financial statements.

Phoenix Houses of Texas, Inc.

Statements of Operations and Changes in Net Assets for the years ended June 30, 2023 and 2022

	<u>2023</u>	<u>2022</u>
CHANGES IN NET ASSETS WITHOUT DONOR RESTRICTIONS:		
OPERATING REVENUE, GAINS, AND OTHER SUPPORT:		
Patient service revenue <i>(Note 8)</i>	\$ 2,167,213	\$ 2,772,146
Contributions	1,086,971	208,551
Contributed nonfinancial assets <i>(Note 9)</i>	706,232	652,831
Other income	57,653	
Net assets released from restrictions for operating contributions	845,019	991,565
Net assets released from restrictions for operating government grants	<u>4,249,015</u>	<u>5,562,755</u>
Total operating revenue, gains, and other support	<u>9,112,103</u>	<u>10,187,848</u>
EXPENSES:		
Program services	7,871,511	7,704,525
Management and general	1,794,565	1,535,049
Fundraising	<u>384,958</u>	<u>351,010</u>
Total expenses	<u>10,051,034</u>	<u>9,590,584</u>
Excess (deficiency) of revenue, gains, and other support over expenses and changes in net assets without donor restrictions	<u>(938,931)</u>	<u>597,264</u>
CHANGES IN NET ASSETS WITH DONOR RESTRICTIONS:		
Contributions	462,421	676,361
Government grants <i>(Note 10)</i>	4,249,015	5,562,755
Net assets released from restrictions for operating contributions	(845,019)	(991,565)
Net assets released from restrictions for operating government grants	<u>(4,249,015)</u>	<u>(5,562,755)</u>
Changes in net assets with donor restrictions	<u>(382,598)</u>	<u>(315,204)</u>
CHANGES IN NET ASSETS	(1,321,529)	282,060
Net assets, beginning of year	<u>5,588,582</u>	<u>5,306,522</u>
Net assets, end of year	<u>\$ 4,267,053</u>	<u>\$ 5,588,582</u>

See accompanying notes to financial statements.

Phoenix Houses of Texas, Inc.

Statements of Functional Expenses for the years ended June 30, 2023 and 2022

	PROGRAM SERVICES	MANAGEMENT AND GENERAL	FUNDRAISING	2023 TOTAL EXPENSES
Salaries and employee benefits	\$ 4,926,638	\$ 1,274,344	\$ 276,890	\$ 6,477,872
Professional fees and contracted services	1,007,545	132,305	28,803	1,168,653
Occupancy	616,374	73,831	19,489	709,694
Supplies, equipment and maintenance	551,924	62,224	5,876	620,024
Depreciation	366,182	55,326	68	421,576
Insurance	262,041	21,133	8,522	291,696
Travel	64,828	68,960	17,519	151,307
Licenses, permits and fees	61,365	6,041		67,406
Other	14,614	100,401	27,791	142,806
Total expenses	<u>\$ 7,871,511</u>	<u>\$ 1,794,565</u>	<u>\$ 384,958</u>	<u>\$ 10,051,034</u>

	PROGRAM SERVICES	MANAGEMENT AND GENERAL	FUNDRAISING	2022 TOTAL EXPENSES
Salaries and employee benefits	\$ 4,961,918	\$ 955,652	\$ 267,266	\$ 6,184,836
Professional fees and contracted services	805,535	193,135	27,651	1,026,321
Occupancy	581,222	65,350	16,468	663,040
Supplies, equipment and maintenance	629,640	69,863	7,304	706,807
Depreciation	343,619	69,600	4	413,223
Insurance	242,170	20,695	8,023	270,888
Travel	64,045	50,358	6,027	120,430
Licenses, permits and fees	59,772	6,250		66,022
Other	16,604	104,146	18,267	139,017
Total expenses	<u>\$ 7,704,525</u>	<u>\$ 1,535,049</u>	<u>\$ 351,010</u>	<u>\$ 9,590,584</u>

See accompanying notes to financial statements.

Phoenix Houses of Texas, Inc.

Statements of Cash Flows for the years ended June 30, 2023 and 2022

	<u>2023</u>	<u>2022</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Changes in net assets	\$ (1,321,529)	\$ 282,060
Adjustments to reconcile changes in net assets to net cash provided (used) by operating activities:		
Depreciation	421,576	413,223
Changes in operating assets and liabilities:		
Patient accounts receivable	(46,433)	128,992
Contributions receivable	200,000	537,500
Government grants receivable	27,498	38,530
Prepaid expenses and other assets	77,091	73,027
Accounts payable and accrued expenses	(161,490)	(86,719)
Deferred revenue	(102,832)	(3,892)
Operating lease assets and liabilities	4,664	
Refundable advance – Paycheck Protection Program		<u>(1,015,600)</u>
Net cash provided (used) by operating activities	<u>(901,455)</u>	<u>367,121</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	<u>(83,806)</u>	<u>(115,381)</u>
NET CHANGE IN CASH	(985,261)	251,740
Cash, beginning of year	<u>2,209,731</u>	<u>1,957,991</u>
Cash, end of year	<u>\$ 1,224,470</u>	<u>\$ 2,209,731</u>

See accompanying notes to financial statements.

Phoenix Houses of Texas, Inc.

Notes to Financial Statements for the years ended June 30, 2023 and 2022

NOTE 1 – ORGANIZATION AND SUMMARY OF ACCOUNTING POLICIES

Organization – Phoenix Houses of Texas, Inc. (Phoenix Houses of Texas) was formed in 1995 to provide compassionate, expert care for individuals, families and communities challenged by substance use disorders and related mental health conditions. Phoenix Houses of Texas is committed to treating the whole person — and their families — with caring, qualified professionals in the fields of psychiatry, medicine, mental health, social work, education, and recovery support. The goal is to address the underlying causes of substance abuse and behavioral patterns to guide patients toward lasting recovery. See Note 13 for changes in program services in 2024.

Federal income tax status – Phoenix Houses of Texas is exempt from federal income tax under §501(c)(3) of the Internal Revenue Code and is classified as a public charity under §509(a)(1) and §170(b)(1)(A)(iii).

Cash includes demand deposits. Demand deposits exceed the federally insured limit per depositor per institution.

Patient accounts receivable are from patients and third-party payors and are based on amounts that reflect the consideration to which Phoenix Houses of Texas expects to be entitled in exchange for services provided. Phoenix Houses of Texas provides services regardless of the patient’s ability to pay, does not require collateral, and does not provide financing. An allowance for uncollectible accounts is established for patient accounts in which there has been an adverse change in the patient’s or third-party payors’ ability to pay. Accounts are written off after all collection efforts have been exhausted and the account is deemed uncollectible. The allowance for uncollectible accounts at June 30, 2023 and 2022 was approximately \$288,000 and \$253,000, respectively.

Receivables from patients and third-party payors are as follows at June 30:

	<u>2023</u>	<u>2022</u>
Medicaid managed care	63%	64%
Commercial insurance carriers	37%	35%
Self-pay	<u>1%</u>	<u>1%</u>
Total	<u>100%</u>	<u>100%</u>

Contributions and government grants receivable that are expected to be collected within one year are reported at net realizable value. Amounts expected to be collected in future years are discounted, if material, to estimate the present value of their estimated future cash flows. Discounts are computed using risk-free interest rates applicable to the years in which the contributions or government grants are received. Amortization of discounts is included in contributions and government grant revenue.

Property and equipment is reported at cost if purchased or at fair value at the date of gift if donated. Depreciation is calculated using the straight-line method over estimated useful lives of 3 to 7 years for furniture and equipment and 15 to 30 years for buildings and leasehold improvements. Phoenix Houses of Texas capitalizes additions and improvements that have a tangible future economic life and a cost of more than \$1,000.

Asset impairment – Phoenix Houses of Texas reviews assets for impairment whenever events or changes in circumstances indicate that the carrying amounts may not be recoverable. Recoverability is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. There were no impairment losses recognized in 2023 or 2022.

Net asset classification – Net assets, revenue, gains, and losses are classified based on the existence or absence of donor-imposed restrictions, as follows:

- *Net assets without donor restrictions* are not subject to donor-imposed restrictions even though their use may be limited in other respects such as by contract or board designation.

- *Net assets with donor restrictions* are subject to donor-imposed restrictions. Restrictions may be temporary in nature, such as those that will be met by the passage of time or use for a purpose specified by the donor, or may be perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Net assets are released from restrictions when the stipulated time has elapsed, or purpose has been fulfilled, or both. Contributions of long-lived assets and of assets restricted for acquisition of long-lived assets are released when those assets are placed in service unless the donor also has placed a time restriction on the use of the long-lived asset, in which case the release occurs over the term of the time restriction.

Patient service revenue recognition – Patient service revenue is recognized as performance obligations are satisfied and are reported at the amount that reflects the consideration Phoenix Houses of Texas expects to receive in exchange for the services provided. These amounts are due from patients and third-party payors and include variable considerations, such as explicit and implicit price concessions. Explicit price concessions include contractual adjustments provided to patients and third-party payors. Implicit price concessions include discounts provided to self-pay, uninsured patients or other payors, adjustments resulting from payment reviews, and adjustments arising from the lack of supporting billing documentation or authorization. These adjustments are estimated based on the most likely amount subject to the terms of the payment agreements with the payors and historical activity. Amounts are generally billed daily at the time of service and are due upon receipt.

Subsequent changes to the estimate of the transaction price are recorded as adjustments to patient service revenue in the period of change. Phoenix Houses of Texas has no material adjustments related to subsequent changes in the estimate of the transaction price for the periods reported.

Phoenix Houses of Texas' services are provided on a daily basis and the type of service provided is determined based on a physician's determination of each patient's specific needs on that given day. Reimbursement rates for residential services are on a per diem basis regardless of the type of service provided or the payor. Reimbursement rates for outpatient services are on an hourly or partial-hourly basis, depending on the service provided. Reimbursement rates for private pay are based on established rates of Phoenix Houses of Texas. Reimbursement rates from government programs are established by the appropriate governmental agency and are standard across all similar treatment providers adjusted for the regional wage index. Reimbursement rates from commercial health insurers are individually negotiated with each payor.

Each level of care represents services provided as a series of either days or hours of patient care and are satisfied over time. Phoenix Houses of Texas recognizes revenue based on the service output method. Phoenix Houses of Texas believes this to be the most faithful depiction of the transfer of control of services as the patient simultaneously receives and consumes the benefits provided by the service. Revenue is recognized on a daily or hourly basis for each patient in accordance with the reimbursement model for each type of service.

Phoenix Houses of Texas provides other ancillary services, such as meals and laundry for residential patients, which are included in the per diem rates and are not treated as separate performance obligations.

Phoenix Houses of Texas has elected the practical expedient to not adjust the promised amount of consideration for the effects of a significant financing component due to expectations that the periods between the time services are provided and the time payment is received will be one year or less. Since performance obligations relate to contracts with a duration of less than one year, Phoenix Houses of Texas has elected to apply the optional exemption and, therefore, is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. The unsatisfied or partially unsatisfied performance obligations are generally completed when the patients are discharged, which generally occurs within days or weeks of the end of the reporting period.

Charity care policy – Care is provided to patients regardless of their ability to pay. Phoenix Houses of Texas has established a policy that defines charity services as those services for which no payment is anticipated. In assessing a patient's ability to pay, Phoenix Houses of Texas utilizes generally recognized minimum income guidelines relevant to the community in which the services are provided. No revenue or accounts receivable is recognized for charity care, but the relevant costs and expenses incurred in providing these services are included in operating expenses. The cost of charity care is calculated based on the number of patient days provided for patients determined to qualify for charity care multiplied by the average cost per patient day. The cost of charity care provided was approximately

\$4 million for the year ended June 30, 2023 and approximately \$3.5 million for the year ended June 30, 2022. During the years ended June 30, 2023 and 2022, there were approximately \$105,000 and \$112,000, respectively, of contributions received that were restricted for charity care.

Contributions and government grants are recognized as revenue at fair value when an unconditional commitment is received from the donor. Contributions and government grants received with donor stipulations that limit their use are classified as *with donor restrictions*. Conditional contributions and government grants are subject to one or more barriers that must be overcome before Phoenix Houses of Texas is entitled to receive or retain funding. Conditional contributions and government grants are recognized in the same manner when the conditions have been met. Funding received before conditions are satisfied is reported as refundable advances.

Deficiency of revenue, gains and other support over expenses includes transactions deemed by management to be ongoing, and major or central to the provision of services provided by the organization. Revenue and expenses to provide these services are reported as elements of operating income for the fiscal year end.

Functional allocation of expenses – Expenses are reported by their functional classification. Program services are the direct conduct or supervision of activities that fulfill the purposes for which the organization exists. Fundraising activities include the solicitation of contributions of money, securities, materials, facilities, other assets, and time. Management and general activities are not directly identifiable with specific program or fundraising activities. Expenses that are attributable to more than one activity are allocated among the activities benefitted. Salaries and related costs are allocated on the basis of estimated time and effort expended. Utilities, repairs and maintenance are directly charged by location based on the programs or support services conducted at the location. Technology costs are allocated based on the number of full-time employees in each department.

Estimates – Management must make estimates and assumptions to prepare financial statements in accordance with generally accepted accounting principles. These estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, the amounts of reported revenue and expenses, and the allocation of expenses among various functions. Actual results could vary from the estimates that were used.

Adoption of accounting standard – Phoenix Houses of Texas' adopted Accounting Standards Update (ASU) No. 2016-02, *Leases (Topic 842)*. Under the new guidance, lessees are required to recognize lease assets and lease liabilities in the statement of financial position for all leases with terms longer than 12 months and to provide expanded disclosures related to the amount, timing and uncertainty of cash flows arising from leases. Phoenix Houses of Texas' elected to adopt the ASU using the modified retrospective method and recorded the impact of adoption as of July 1, 2022 without restating any prior year amounts or disclosures. The adoption had no impact on beginning net assets reported as of July 1, 2022. Certain accounting policy elections were required for the implementation of the new lease standard. Phoenix Houses of Texas' has made the following elections:

- *Relief package* – For leases that commenced before the effective date, Phoenix Houses of Texas' did not reassess 1) whether any expired or existing contracts contain leases, 2) the lease classification for any expired or existing leases, or 3) initial indirect costs for any existing leases.
- *Hindsight* – Phoenix Houses of Texas' did not make the practical expedient election to use hindsight in determining the lease term and in assessing impairments of right-of-use assets.
- *Short-term leases* – Phoenix Houses of Texas' elected to not apply the recognition requirements to short-term leases. Instead, these leases are recognized as expense on a straight-line basis over the lease term.
- *Discount rates* – Phoenix Houses of Texas' elected to use the risk-free discount rate when the rate implicit in a lease is not readily determinable.

NOTE 2 – LIQUIDITY AND AVAILABILITY OF RESOURCES

Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use within one year of June 30 comprise the following:

	<u>2023</u>	<u>2022</u>
Financial assets:		
Cash	\$ 1,224,470	\$ 2,209,731
Patient accounts receivable	527,053	480,620
Contributions and government grants receivable	517,640	745,138
Other assets	<u>13,615</u>	<u>13,606</u>
Total financial assets	2,282,778	3,449,095
Less financial assets not available for general expenditure:		
Contributions restricted for future use		(200,000)
Board-designated reserve	<u>(500,000)</u>	<u>(850,000)</u>
Total financial assets available for general expenditure	<u>\$ 1,782,778</u>	<u>\$ 2,399,095</u>

Phoenix Houses of Texas is substantially supported by patient service revenue, contributions and government grants and regularly monitors liquidity required to meet its operating needs while striving to maximize the investment of available funds. For purposes of analyzing resources available to meet general expenditures over a 12-month period, Phoenix Houses of Texas considers all expenditures related to its ongoing activities of providing evidence-based care to teens, adults, and families, as well as the conduct of services undertaken to support those activities, to be general expenditures.

Phoenix Houses of Texas has designated a portion of its resources without donor restrictions as a board-designated reserve. These funds are held in an interest-bearing money market account but remain available to be spent with the Board of Directors' approval.

NOTE 3 – CONTRIBUTIONS AND GOVERNMENT GRANTS RECEIVABLE

Contributions and government grants receivable are as follows:

	<u>2023</u>	<u>2022</u>
Contributions receivable – current	\$ 237,500	\$ 237,500
Contributions receivable – long term		200,000
Government grants receivable	<u>280,140</u>	<u>307,638</u>
Total contributions and government grants receivable	<u>\$ 517,640</u>	<u>\$ 745,138</u>

Contributions and government grants receivable at June 30, 2023 are expected to be collected within one year.

Conditional federal grants – A portion of Phoenix Houses of Texas' revenue is derived from federal grants, which are conditioned upon certain performance requirements and/or the incurrence of allowable qualifying expenses. At June 30, 2023, approximately \$1,328,000 of federal grants have not been recognized in the accompanying financial statements because the conditions have not been met.

NOTE 4 – OPERATING LEASES

Phoenix House of Texas leases office space, vehicles, and equipment under non-cancelable operating leases. Right-of-use assets are recognized at the present value of the lease payments at the inception of the lease adjusted, as

appropriate, for certain other payments and allowances related to obtaining the lease and placing the asset in service. Operating leases reported as right-of-use assets are amortized so that lease costs remain constant over the lease term.

During 2023, total lease costs were \$167,794. Lease costs recognized during 2022, prior to the adoption of the new accounting standard was \$207,000.

During the year ended June 30, 2023, cash paid for amounts included in the measurement of operating lease liabilities was \$171,280.

As of June 30, 2023, the weighted-average remaining lease term for all operating leases is 15 months. The weighted-average discount rate associated with operating leases as of June 30, 2023 is 4.6%.

Cash flows related to operating leases as of June 30, 2023 with terms exceeding one year are as follows:

2024	\$ 136,089
2025	<u>99,672</u>
Total undiscounted cash flows	235,761
Less discount to present value	<u>(7,860)</u>
Total discount present value of lease liabilities	<u>\$ 227,901</u>

NOTE 5 – PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

	<u>2023</u>	<u>2022</u>
Buildings and leasehold improvements	\$ 6,389,412	\$ 6,362,910
Furniture and equipment	1,104,803	1,047,498
Land	<u>428,000</u>	<u>428,000</u>
Property and equipment, at cost	7,922,215	7,838,408
Accumulated depreciation	<u>(5,397,781)</u>	<u>(4,976,204)</u>
Property and equipment, net	<u>\$ 2,524,434</u>	<u>\$ 2,862,204</u>

NOTE 6 – NET ASSETS WITHOUT DONOR RESTRICTIONS

Net assets without donor restrictions are comprised of the following:

	<u>2023</u>	<u>2022</u>
Property and equipment, net	\$ 2,524,434	\$ 2,862,204
Undesignated	906,569	1,157,730
Board-designated reserve	<u>500,000</u>	<u>850,000</u>
Total net assets without donor restrictions	<u>\$ 3,931,003</u>	<u>\$ 4,869,934</u>

The Board of Directors of Phoenix Houses of Texas does not have a specific policy establishing board-designated reserves. However, the Board of Directors may designate excess cash flow for reserves or specific projects, as deemed prudent.

NOTE 7 – NET ASSETS WITH DONOR RESTRICTIONS

Net assets with donor restrictions are restricted as follows:

	<u>2023</u>	<u>2022</u>
Subject to passage of time for future operating periods	\$ 308,333	\$ 616,667
Subject to expenditure for specified purpose:		
Renovations at Feinberg Academy		45,342
Feinberg Academy operations	10,697	37,000
Other	<u>17,020</u>	<u>19,639</u>
Total net assets with donor restrictions	<u>\$ 336,050</u>	<u>\$ 718,648</u>

NOTE 8 – PATIENT SERVICE REVENUE

Phoenix Houses of Texas disaggregates revenue from contracts with customers by type of services and payor source as this depicts the nature, amount, timing, uncertainty, and cash flows as affected by economic factors. Revenue from contracts with customers consist of the following for the year ended June 30:

	<u>2023</u>		
	<u>RESIDENT CARE</u>	<u>OUTPATIENT CARE</u>	<u>TOTAL</u>
Medicaid managed care	\$ 1,131,159	\$ 108,027	\$ 1,239,186
Commercial insurance carriers	635,518	244,992	880,510
Self-pay	<u>38,262</u>	<u>9,255</u>	<u>47,517</u>
Total	<u>\$ 1,804,939</u>	<u>\$ 362,274</u>	<u>\$ 2,167,213</u>
	<u>2022</u>		
	<u>RESIDENT CARE</u>	<u>OUTPATIENT CARE</u>	<u>TOTAL</u>
Medicaid managed care	\$ 1,489,904	\$ 280,877	\$ 1,770,781
Commercial insurance carriers	671,486	301,508	972,994
Self-pay	<u>4,776</u>	<u>23,595</u>	<u>28,371</u>
Total	<u>\$ 2,166,166</u>	<u>\$ 605,980</u>	<u>\$ 2,772,146</u>

NOTE 9 – NONFINANCIAL CONTRIBUTIONS

Phoenix Houses recognized the following nonfinancial contributions:

CONTRIBUTED NONFINANCIAL ASSETS	MONETIZED OR UTILIZED IN PROGRAMS/ACTIVITIES	VALUATION TECHNIQUES AND INPUTS		
			<u>2023</u>	<u>2022</u>
Teacher services	Utilized in program services	Fair value estimated based upon teacher pay rates in the area.	\$393,294	\$206,928
Building usage	Utilized in program services	Fair value estimated based upon current space rental rates in areas of service.	268,896	269,096

CONTRIBUTED NONFINANCIAL ASSETS	MONETIZED OR UTILIZED IN PROGRAMS/ACTIVITIES	VALUATION TECHNIQUES AND INPUTS	2023	2022
Program supplies	Utilized in program services	Fair value estimated based on value of supplies in active market.	13,321	3,315
Consulting services	Utilized in program, management and general, and fundraising services	Fair value estimated based on current rates for similar services.	30,721	105,965
Construction services	Utilized in program services for Sports Field	Fair value estimated based on current rates of similar supplies and services.		67,527
Total contributed nonfinancial assets			<u>\$706,232</u>	<u>\$652,831</u>

There are not any restrictions on nonfinancial contributions in fiscal year 2023 and 2022.

NOTE 10 – GOVERNMENT AWARDS

Phoenix Houses of Texas is a party to agreements with government agencies. Should these agreements not be renewed, a replacement for this source of support may not be forthcoming and related expenses would not be incurred. Sources of significant government grants recognized include the following:

	2023	2022
Federal government awards:		
U. S. Department of Health and Human Services	\$ 3,203,008	\$ 3,968,487
U. S. Department of Agriculture	95,480	125,834
U. S. Small Business Administration	79,494	
U. S. Department of Treasury		<u>1,029,085</u>
Total federal government awards	<u>3,377,982</u>	<u>5,123,406</u>
State government awards:		
Texas Health and Human Services Commission	<u>871,033</u>	<u>439,349</u>
Total government awards	<u>\$ 4,249,015</u>	<u>\$ 5,562,755</u>

Government awards require fulfillment of certain conditions as set forth in the agreements and are subject to review and audit by the awarding agencies. Such reviews and audits could result in the discovery of unallowable activities and unallowable costs. Consequently, any of the funding sources may, at their discretion, request reimbursement for expenses or return of funds as a result of non-compliance by Phoenix Houses of Texas with the terms of the agreements. Management believes such disallowances, if any, would not be material to Phoenix Houses of Texas' balance sheet or changes in net assets.

NOTE 11 – EMPLOYEE BENEFIT PLAN

Retirement benefits – Through March 2020, Phoenix Houses of Texas was a participating employer in The Phoenix Houses 403(b) Tax-Deferred Annuity Plan (the Plan) to provide retirement benefits to eligible employees. Under the Plan, all employees of Phoenix Houses of Texas became participants in the Plan following the completion of one year

of service and were immediately vested. The Plan provided annual safe harbor non-elective contributions to the Plan of 3.5% of eligible compensation and a 50% match on participant contributions (maximum match is 2.5%). Effective April 1, 2020, all employees are eligible to participate in the Plan immediately and also are 100% vested immediately. The employer match is discretionary up to 6% of an employee's compensation. Phoenix Houses of Texas' contributions to the Plan were approximately \$108,578 for the year ended June 30, 2023 and \$80,800 for the year ended June 30, 2022.

NOTE 12 – COMMITMENTS AND CONTINGENCIES

Phoenix Houses of Texas maintains claims-made policies for its malpractice coverage to cover any claims in the ordinary course of business. Primary limits of \$1,000,000 per occurrence with an annual aggregate limit of \$3,000,000 apply with no deductibles. Claims that are insured under the claims-made policies are covered only if the occurrence is reported prior to expiration of the policy period. In the event the current policies are not renewed or replaced with equivalent insurance coverage, claims based on occurrences during their term, but reported subsequently, will be uninsured. There are claims from unknown incidents that may be asserted arising from services provided. Management does not expect such claims to have a material adverse effect on Phoenix Houses of Texas' financial position.

NOTE 13 – OPERATIONAL CHANGES

In September 2023, Phoenix Houses of Texas declared a temporary closure of the last Dallas residential program and six outpatient locations, resulting in the suspension of treatment services. The impact of this suspension in outpatient and residential drug treatment will reduce federal and state grants revenue by approximately \$2 million. Management has already taken steps to reduce staffing and expenses related to these grants, including placing property for sale. The Austin property currently is under contract for sale. Phoenix Houses of Texas will continue to provide preventative and educational services for those experiencing family and individual substance use disorders and related mental health challenges in several existing locations.

NOTE 14 – SUBSEQUENT EVENTS

Subsequent to June 30, 2023, Phoenix Houses of Texas entered into a promissory note for \$1.25 million. No amounts have been drawn on this note.

Management has evaluated subsequent events through March 8, 2024, which is the date that the financial statements were available for issuance. As a result of this evaluation, no other events except as described in Note 13 and above were identified that are required to be disclosed or would have a material impact on reported net assets or changes in net assets.

Phoenix Houses of Texas, Inc.

Schedule of Expenditures of Federal Awards for the year ended June 30, 2023

<u>FEDERAL GRANTOR</u> <u>Pass-through Grantor</u> <u>Program Title & Period</u>	<u>Assistance</u> <u>Listing</u> <u>Number</u>	<u>Pass-through</u> <u>Grantor</u> <u>Number</u>	<u>Federal</u> <u>Expenditures</u>
U. S. DEPARTMENT OF AGRICULTURE			
Passed through Texas Department of Agriculture:			
#1 School Breakfast Program 07/01/22 – 06/30/23	10.553	N/A	\$ 32,336
#2 National School Lunch Program 07/01/22 – 06/30/23	10.555	N/A	<u>63,143</u>
Total U. S. Department of Agriculture – Child Nutrition Cluster			<u>95,479</u>
U. S. DEPARTMENT OF HEALTH AND HUMAN SERVICES			
Direct federal funding:			
#3 Provider Relief Fund and American Rescue Plan (ARP) Rural Distribution 01/01/20 – 06/30/23	93.498	N/A	421,266
Passed through Texas Health and Human Services Commission: Block Grants for Prevention and Treatment of Substance Abuse			
#4 Houston Youth Prevention – Selective 09/01/21 – 08/31/22	93.959	HHS000539700235 SA/YPS	36,101
09/01/22 – 08/31/23	93.959	HHS000539700235 SA/YPS	221,756
#5 Austin Youth Prevention – Selective 09/01/21 – 08/31/22	93.959	HHS000539700236 SA/YPS	29,198
09/01/22 – 08/31/23	93.959	HHS000539700236 SA/YPS	122,323
#6 Houston Youth Prevention – Universal 09/01/21 – 08/31/22	93.959	HHS000539700235 SA/YPU	18,507
09/01/22 – 08/31/23	93.959	HHS000539700235 SA/YPU	196,463
#7 Austin Youth Prevention – Universal 09/01/21 – 08/31/22	93.959	HHS000539700236 SA/YPU	17,717
09/01/22 – 08/31/23	93.959	HHS000539700236 SA/YPU	144,000
#8 Houston Community Coalition Partnership 09/01/21 – 08/31/22	93.959	HHS000539700235 SA/CCP	6,274
09/01/22 – 08/31/23	93.959	HHS000539700235 SA/CCP	91,500
#9 Houston Youth Prevention – Indicated 09/01/21 – 08/31/22	93.959	HHS000077600235 SA/YPI	33,132
09/01/22 – 08/31/23	93.959	HHS000077600235 SA/YPI	274,500
#10 Houston Treatment Services – Youth 09/01/21 – 08/31/22	93.959	HHS000663700276	6,000
09/01/22 – 08/31/23	93.959	HHS000663700276	40,641
#11 Austin Treatment Services – Youth 09/01/21 – 08/31/22	93.959	HHS000663700277	64,429
09/01/22 – 08/31/23	93.959	HHS000663700277	653,291

(continued)

Phoenix Houses of Texas, Inc.

Schedule of Expenditures of Federal Awards for the year ended June 30, 2023

(continued)

<u>FEDERAL GRANTOR</u> <u>Pass-through Grantor</u> <u>Program Title & Period</u>	<u>Assistance</u> <u>Listing</u> <u>Number</u>	<u>Pass-through</u> <u>Grantor</u> <u>Number</u>	<u>Federal</u> <u>Expenditures</u>
U. S. DEPARTMENT OF HEALTH AND HUMAN SERVICES <i>(continued)</i>			
#12 Dallas Treatment Services – Youth			
09/01/21 – 08/31/22	93.959	HHS000663700275	48,848
09/01/22 – 08/31/23	93.959	HHS000663700275	623,665
#13 San Antonio Treatment Services – Youth			
09/01/21 – 08/31/22	93.959	HHS000663700278	1,750
09/01/22 – 08/31/23	93.959	HHS000663700278	49,845
#14 Houston Community Coalition Partnership – COVID			
09/01/21 – 08/31/22	93.959	HHS000539700235 SA/CCP-COV	41,567
09/01/22 – 08/31/23	93.959	HHS000539700235 SA/CCP-COV	131,512
#15 Dallas Youth Prevention – Selective			
09/01/21 – 08/31/22	93.959	HHS000539700232 SA/YPS	11,528
09/01/22 – 08/31/23	93.959	HHS000539700232 SA/YPS	160,000
Passed through North Texas Behavioral Health Authority: Block Grants for Prevention and Treatment of Substance Abuse			
#16 Dallas Treatment Services – Youth NTBHA			
09/01/21 – 08/31/22	93.959	HHS000779800001	28,391
09/01/22 – 08/31/23	93.959	HHS000779800001	143,892
#17 Dallas Treatment Services – COPSD – Youth			
09/01/22 – 08/31/23	93.959	HHS000779800004	603
Total U. S. Department of Health and Human Services and Assistance Listing #93.959			<u>3,618,699</u>
TOTAL FEDERAL AWARDS			<u>\$ 3,714,178</u>

See accompanying note to schedule of expenditures of federal and state awards.

Phoenix Houses of Texas, Inc.

Schedule of Expenditures of State Awards for the year ended June 30, 2023

<u>STATE GRANTOR</u> <u>Pass-through Grantor</u> <u>Program Title & Period</u>	<u>Pass-through</u> <u>Grantor</u> <u>Number</u>	<u>State</u> <u>Expenditures</u>
TEXAS HEALTH AND HUMAN SERVICES COMMISSION		
Block Grants for Prevention and Treatment of Substance Abuse		
#S1 Houston Youth Prevention – Selective		
09/01/21 – 08/31/22	HHS000539700235 SA/YPS	\$ 27,216
09/01/22 – 08/31/23	HHS000539700235 SA/YPS	60,637
#S2 Houston Youth Prevention – Universal		
09/01/22 – 08/31/23	HHS000539700235 SA/YPU	59,100
#S3 Austin Youth Prevention – Universal		
09/01/21 – 08/31/22	HHS000539700236 SA/YPU	18,268
09/01/22 – 08/31/23	HHS000539700236 SA/YPU	239
#S4 Houston Community Coalition Partnership		
09/01/21 – 08/31/22	HHS000539700235 SA/CCP	15,470
09/01/22 – 08/31/23	HHS000539700235 SA/CCP	12,061
#S5 Houston Youth Prevention – Indicated		
09/01/21 – 08/31/22	HHS000077600235 SA/YPI	40,855
09/01/22 – 08/31/23	HHS000077600235 SA/YPI	57,601
#S6 Houston Treatment Services – Youth		
09/01/21 – 08/31/22	HHS000663700276	9,050
#S7 Austin Treatment Services – Youth		
09/01/21 – 08/31/22	HHS000663700277	255,800
#S8 Dallas Treatment Services – Youth		
09/01/21 – 08/31/22	HHS000663700275	208,266
#S9 San Antonio Treatment Services – Youth		
09/01/21 – 08/31/22	HHS000663700278	2,765
#S10 Dallas Youth Prevention – Selective		
09/01/21 – 08/31/22	HHS000539700232 SA/YPS	32,789
09/01/22 – 08/31/23	HHS000539700232 SA/YPS	<u>24,362</u>
Total Texas Health and Human Services Commission		<u>824,479</u>
NORTH TEXAS BEHAVIORIAL HEALTH AUTHORITY		
Block Grants for Prevention and Treatment of Substance Abuse		
#S11 Dallas Treatment Services – Youth NTBHA		
09/01/21 – 08/31/22	HHS000779800001	<u>46,554</u>
TOTAL STATE AWARDS		<u>\$ 871,033</u>

See accompanying note to schedule of expenditures of federal and state awards.

Phoenix Houses of Texas, Inc.

Note to Schedule of Expenditures of Federal and State Awards for the year ended June 30, 2023

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation – The schedules of expenditures of federal and state awards are prepared on the accrual basis of accounting. The information in these schedules are presented in accordance with the requirements of Title 2 U. S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) and the *Texas Grant Management Standards*. Federal and state expenditures include allowable costs funded by federal and state grants. Allowable costs are subject to the cost principles of the Uniform Guidance and the *Texas Grant Management Standards* and include costs that are recognized as expenses in Phoenix Houses of Texas' financial statements in conformity with generally accepted accounting principles. Phoenix Houses of Texas has not elected to use the 10% de minimis cost rate for indirect costs but uses its approved indirect cost rate from the U. S. Department of Health and Human Services. Phoenix Houses of Texas does not have any subrecipients.

Because the schedule presents only a selected portion of the operations of Phoenix Houses of Texas, it is not intended to and does not present the financial position, changes in net assets, or cash flows of Phoenix Houses of Texas.

Independent Auditors' 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 of
Phoenix Houses of Texas, Inc.:

We have audited, 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, the financial statements of Phoenix Houses of Texas, Inc. (Phoenix Houses of Texas), which comprise the balance sheet as of June 30, 2023 and the related statements of operations and changes in net assets, of functional expenses, and of cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated March 8, 2024.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Phoenix Houses of Texas' internal control over financial reporting (internal control) as a basis for designing 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 Phoenix Houses of Texas' internal control. Accordingly, we do not express an opinion on the effectiveness of Phoenix Houses of Texas' 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 a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. 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.

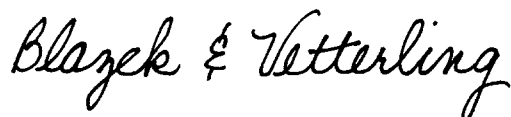
Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not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

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether Phoenix Houses of Texas' 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 financial statements. 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*.

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 entity'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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

The logo for Blazek & Vetterling is written in a cursive, handwritten-style font.

March 8, 2024

**Independent Auditors' Report on Compliance for Each Major
Federal Program and Major State Program and Report on Internal Control Over
Compliance Required by the Uniform Guidance and the *Texas Grant Management Standards***

To the Board of Directors of
Phoenix Houses of Texas, Inc.:

Report on Compliance for Each Major Federal Program

Opinion on Each Major Federal Program and Major State Program

We have audited Phoenix Houses of Texas, Inc. (Phoenix Houses of Texas) compliance with the types of compliance requirements identified as subject to audit in the OMB *Compliance Supplement* and in the *Texas Grant Management Standards* that could have a direct and material effect on each of Phoenix Houses of Texas' major federal and major state programs for the year ended June 30, 2023. Phoenix Houses of Texas' major federal and major state programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

In our opinion, Phoenix Houses of Texas complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal and major state programs for the year ended June 30, 2023.

Basis for Opinion on Each Major Federal Program and Major State Program

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 audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) and in the *Texas Grant Management Standards*. Our responsibilities under those standards and the Uniform Guidance and in the *Texas Grant Management Standards* are further described in the *Auditors' Responsibilities for the Audit of Compliance* section of our report.

We are required to be independent of Phoenix Houses of Texas and to meet our other ethical responsibilities, in accordance with relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion on compliance for each major federal program. Our audit does not provide a legal determination of Phoenix Houses of Texas' compliance with the compliance requirements referred to above.

Responsibilities of Management for Compliance

Management is responsible for compliance with the requirements referred to above and for the design, implementation, and maintenance of effective internal control over compliance with the requirements of laws, statutes, regulations, rules and provisions of contracts or grant agreements applicable to Phoenix Houses of Texas' federal and state programs.

Auditors' Responsibilities for the Audit of Compliance

Our objectives are to obtain reasonable assurance about whether material noncompliance with the compliance requirements referred to above occurred, whether due to fraud or error, and express an opinion on Phoenix Houses of Texas' compliance based on our audit. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards,

Government Auditing Standards, the Uniform Guidance and the *Texas Grant Management Standards* will always detect material noncompliance when it exists. The risk of not detecting material noncompliance resulting from fraud is higher than for that resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Noncompliance with the compliance requirements referred to above is considered material if there is a substantial likelihood that, individually or in the aggregate, it would influence the judgment made by a reasonable user of the report on compliance about Phoenix Houses of Texas' compliance with the requirements of each major federal or state program as a whole.

In performing an audit in accordance with generally accepted auditing standards, *Government Auditing Standards*, the Uniform Guidance and the *Texas Grant Management Standards*, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material noncompliance, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding Phoenix Houses of Texas' compliance with the compliance requirements referred to above and performing such other procedures as we considered necessary in the circumstances.
- Obtain an understanding of Phoenix Houses of Texas' internal control over compliance relevant to the audit in order to design audit procedures that are appropriate in the circumstances and to test and report on internal control over compliance in accordance with the Uniform Guidance and the *Texas Grant Management Standards*, but not for the purpose of expressing an opinion on the effectiveness of Phoenix Houses of Texas' internal control over compliance. Accordingly, no such opinion is expressed.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and any significant deficiencies and material weaknesses in internal control over compliance that we identified during the audit.

Other Matter

The results of our auditing procedures disclosed an instance of noncompliance which is required to be reported in accordance with Uniform Guidance and *Texas Grant Management Standards* which is described in the accompanying schedule of findings and questioned costs as item #2023-002. Our opinion on each major federal and each major state program is not modified with respect to this matter.

Government Auditing Standards requires the auditor to perform limited procedures on Phoenix Houses of Texas' response to the noncompliance finding identified in our audit described in the accompanying schedule of findings and questioned costs. Phoenix Houses of Texas' response was not subjected to the other auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control Over Compliance

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. However, as discussed below, we did identify certain deficiencies in internal control over compliance that we consider to be a material weakness and a significant deficiency.

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 or state program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or a 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 or state program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiency in internal control over compliance described in the accompanying schedule of findings and questioned costs as item #2023-02 to be a material weakness.

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 or state program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiency in internal control over compliance described in the accompanying schedule of findings and questioned costs as item #2023-01 to be a significant deficiency.

Our audit was not designed for the purpose of expressing an opinion on the effectiveness of internal controls over compliance. Accordingly, no such opinion is expressed.

Government Auditing Standards requires the auditor to perform limited procedures on Phoenix Houses of Texas' response to the internal control over compliance findings identified in our audit described in the accompanying schedule of findings and questioned costs. Phoenix Houses of Texas' response was not subjected to the other auditing procedures applied to the audit of compliance and, accordingly, we express no opinion on the response.

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 the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Blazek & Vetterling

March 8, 2024

Phoenix Houses of Texas, Inc.

Schedule of Findings and Questioned Costs for the year ended June 30, 2023

Section I – Summary of Auditors’ Results

Financial Statements

Type of auditors’ report issued: unmodified qualified adverse disclaimer

Internal control over financial reporting:

- Material weakness(es) identified? yes no
- Significant deficiency(ies) identified that are not considered to be material weakness(es)? yes none reported

Noncompliance material to the financial statements noted? yes no

Federal and State Awards

Internal control over major programs:

- Material weakness(es) identified? yes no
- Significant deficiency(ies) identified that are not considered to be material weakness(es)? yes none reported

Type of auditors’ report issued on compliance for major programs: unmodified qualified adverse disclaimer

Any audit findings disclosed that are required to be reported in accordance with 2 CFR §200.516(a) and the *Texas Grant Management Standards*? yes no

Identification of major programs:

<u>Assistance Listing Number(s)</u>	<u>Name of Federal Program or Cluster</u>
93.498	COVID-19 Provider Relief Fund and American Rescue Plan (ARP) Rural Distribution
93.959	Block Grants for Prevention and Treatment of Substance Abuse

<u>Contract Number(s)</u>	<u>Name of State Program or Cluster</u>
HHS000539700235 SA/YPS	Houston Youth Prevention – Selective
HHS000539700235 SA/YPU	Houston Youth Prevention – Universal
HHS000539700236 SA/YPU	Austin Youth Prevention – Universal
HHS000539700235 SA/CCP	Houston Community Coalition Partnership
HHS000077600235 SA/YPI	Houston Youth Prevention – Indicated
HHS000539700232 SA/YPS	Dallas Youth Prevention – Selective
HHS000779800001	Dallas Treatment Services – Youth NTBHA

Dollar threshold used to distinguish between Type A and Type B federal programs: \$750,000

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

Auditee qualified as a low-risk auditee? yes no

Section II – Financial Statement Findings

There were no findings related to the financial statements which are required to be reported in accordance with *Government Auditing Standards*.

Section III – Federal and State Award Findings and Questioned Costs

Finding #2023-001 – Significant Deficiency

Applicable federal program:

U. S. Department of Health and Human Services
Assistance Listing #93.959
Passed through Texas Department of Health and Human Services
Contract #'s: HHS000663700275, HHS000663700276, HHS000663700277, HHS000663700278,
HHS000779800001, HHS000779800004
Contract years: 09/21 – 08/22; 09/22 – 08/23

Applicable state program:

Texas Department of Health and Human Services
Contract #'s: HHS000779800001
Contract year: 09/21 – 08/22

Criteria: Allowable Costs – The Uniform Guidance §200.430 and the Texas Grant Management Standards require that charges to awards for salaries and wages must be based on records that accurately reflect the work performed. These records must 1) be supported by a system of internal control which provides reasonable assurance the charges are accurate, allowable and properly allocated; 2) reasonably reflect the total activity for which the employee is compensated; 3) comply with the established accounting policies and practices of the agency; and 4) support the distribution of the employee’s salary or wages among specific activities or cost objectives if the employee works on more than one activity. Additionally, the Uniform Guidance requires costs to be necessary and reasonable for the performance of the federal award.

Condition and context: During our testing of 40 payroll transactions, we noted instances where the shift differential was not properly calculated and allocated to the grant departments.

Cause: The errors in the payroll allocations to the grant occurred during the correction by the Agency for a single payroll period for individuals receiving shift differentials. Failure to follow established review policies and procedures resulted in these employees being overpaid for shift differential only.

Effect: Failure to follow established internal control policies and procedures which requires reviews of payroll, could result in unallowable costs being charged to the grant cost center used for reporting costs under fee for service contracts.

Recommendation: Emphasize adherence to established policies and procedures to ensure payroll, including allocations methodology, are properly followed and reviewed.

Views of responsible officials and planned corrective actions: Management agrees with the finding. See Corrective Action Plan.

Finding #2023-002 – Material Weakness and Other Noncompliance

Applicable federal program:

U. S. Department of Health and Human Services
Assistance Listing #93.959
Passed through Texas Department of Health and Human Services
Contract #'s: HHS000663700277 and HHS000663700278
Contract years: 09/21 – 08/22; 09/22 – 08/23

Applicable state program:

Texas Department of Health and Human Services
Contract #'s: HHS000663700277 and HHS000663700278
Contract year: 09/21 – 08/22

Criteria: Eligibility – Texas Administrative Code (TAC) requirements, as referenced in the Substance Use Disorder (SUD) Utilization Management (UM) Guidelines requires that Federal Block Grant-funded SUD treatment services will be provided to all eligible Texas residents. Client eligibility for Texas residency, financial eligibility, and clinical eligibility must be performed prior to billing HHSC for SUD treatment services. Further, providers are to conduct and document in CMBHS the financial eligibility determination. If the client is unable to provide proof of financial status, the individual can attest by signing an attestation statement.

Condition and context: During our testing of 40 clients for proper eligibility, three clients had documented income verification that did not meet the income guidelines specified under the grant. Despite this, services were provided to these clients, and the costs were billed to the grant. Furthermore, one client out of the 40 tested did not have proper documentation to support the financial eligibility determination, and there was no attestation statement from the client explaining the inability to provide the necessary information.

Cause: The finding occurred as a result of Phoenix House not following its internal control procedures requiring review of documentation to ensure the client files are complete with eligibility documentation and that only eligible clients are being billed to the grant.

Effect: Failure to follow internal control procedures resulted in incomplete client files and ineligible persons served.

Questioned costs: The grant was billed \$282.54 for the four clients in the billing months selected in our testing.

Recommendation: Provide additional staff training to ensure internal control procedures over client eligibility and required documentation are followed.

Views of responsible officials and planned corrective action: Management agrees with the finding. See Corrective Action Plan.

CORRECTIVE ACTION PLAN

March 8, 2024

Phoenix Houses of Texas respectfully submits the following Corrective Action Plan for the year ended June 30, 2023. The audit was performed by: Blazek & Vetterling, 2900 Wesleyan, Suite 200, Houston, Texas, 77027.

The findings from the June 30, 2023 schedule of findings and questioned costs are discussed below. The findings are numbered consistently with the numbers assigned in the schedule.

FEDERAL AND STATE AWARD FINDINGS AND QUESTIONED COSTS

Finding #2023-001 – Significant Deficiency

Recommendation: Emphasize adherence to established policies and procedures to ensure payroll, including allocations methodology, are properly followed and reviewed.

Planned corrective action: Management has emphasized to HR that adherence to established policies and procedures for reviewing the payroll calculations of the 3rd party payroll vendor must be strictly followed. This finding for shift differential was limited to a very small number of residential treatment employees at one location that worked during overnight hours for 2 pay periods. Changes to shift differential are rare and are not needed in the cost reimbursement business model that took effect on October 1, 2023. In the future, Management will ensure that closer coordination and testing is done with the 3rd party payroll vendor to ensure that all payroll changes are calculated correctly during the correct pay period.

Responsible officer: Drew Dutton, President and CEO

Estimated completion date: Completed December 31, 2023

Finding #2023-002 – Material Weakness and Other Noncompliance

Recommendation: Provide additional staff training to ensure internal control procedures over client eligibility and required documentation are followed.

Planned corrective action: Client eligibility and documentation requirements do not pertain to cost reimbursement grants; these regulations exclusively apply to fee-for-service grants. The fee-for-service grant programs concluded on September 30, 2023. Consequently, starting from October 1, 2023, the business model shifted to cost reimbursement only. As a result, no corrective actions are needed for fee-for-service grants.

Responsible officer: Drew Dutton, President and CEO

Estimated completion date: Completed October 1, 2023

If there are questions regarding this plan, please call Drew Dutton at (214) 920-1628.

Sincerely,



Drew Dutton, Executive Director