The Episcopal Church Home, Inc.

Financial Report
December 31, 2016

Contents

Independent Auditor's Report

Board of Directors
The Episcopal Church Home, Inc.

Report on the Financial Statements
We have audited the accompanying financial statements of The Episcopal Church Home, Inc., which comprise the balance sheet as of December 31, 2016, the related statement of activities, changes in net assets, and cash flows for the period July 1, 2016 through December 31, 2016, and the related notes to the financial statements.

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

Auditor's Responsibility
Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Episcopal Church Home, Inc. as of December 31, 2016, and the results of its activities, changes in its net assets and its cash flows for the period July 1, 2016 through December 31, 2016 in accordance with accounting principles generally accepted in the United States of America.

RSM US LLP

Cincinnati, Ohio
May 23, 2017

The Episcopal Church Home, Inc.

Balance Sheet
December 31, 2016

Assets	
Current assets:	
Cash and cash equivalents	$ 4,260,942
Resident accounts receivable, net (Note 2)	1,204,921
Prepaid expenses	171,525
Other assets	30,333
Investments and assets limited as to use (Note 3)	59,107
Total current assets	5,726,828
Investments and assets limited as to use, less current portion (Note 3)	155,890
Interest in net assets of financially interrelated Foundation (Note 10)	7,054,030
Property and equipment:	
Land	804,971
Land improvements	116,138
Buildings and improvements	30,968,983
Construction in progress	224,052
Furniture, fixtures and equipment	2,662,583
Vehicles	117,303
Total	34,894,030
Less: accumulated depreciation	(16,116,802)
Property and equipment, net	18,777,228
Total assets	$ 31,713,976

See notes to financial statements.

The Episcopal Church Home, Inc.

Balance Sheet
December 31, 2016

Liabilities and Net Assets	
Current liabilities:	
Current maturities of long-term debt (Note 5)	$ 339,376
Accounts payable	1,030,624
Accrued expenses and other liabilities	554,476
Refundable advance deposits	1,174,000
Deferred entrance fees	416,000
Total current liabilities	3,514,476
Long-term liabilities:	
Long-term debt, less current maturities (Note 5)	1,595,984
Refundable advance deposits, less current portion	10,928,161
Deferred entrance fees, less current portion	1,361,401
Total liabilities	17,400,022
Net assets:	
Unrestricted	6,867,955
Temporarily restricted	5,159,429
Permanently restricted (Note 6)	2,286,570
Total net assets	14,313,954
Total liabilities and net assets	$ 31,713,976

See notes to financial statements.

The Episcopal Church Home, Inc.

Statement of Activities
For the Period July 1, 2016 through December 31, 2016

Operating revenue:	
Net resident service revenue	$ 8,050,248
Amortization of entrance fees	226,041
Other operating revenue	160,264
Total operating revenue	8,436,553
Operating expenses:	
Salaries and wages	3,740,035
Employee benefits and payroll taxes	659,444
Marketing	186,103
Supplies	467,842
Food	396,652
Professional and purchased services	2,201,656
Utilities	401,652
Insurance	133,142
Depreciation and amortization	737,601
Interest	20,926
Bad debt expense	6,637
Other operating expense	716,215
Total operating expenses	9,667,905
Operating loss	(1,231,352)
Nonoperating income:	
Contributions	217,786
Investment income	174,831
Total nonoperating income	392,617
Excess of revenues under expenses	$ (838,735)

See notes to financial statements.

The Episcopal Church Home, Inc.

Statement of Changes in Net Assets
For the Period July 1, 2016 through December 31, 2016

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Balance, July 1, 2016	$ 10,756,834	$ 368,371	$ 2,238,798	$ 13,364,003
Excess of revenues under expenses	(838,735)	-	-	(838,735)
Restricted contributions	-	28,385	50	28,435
Change in market value	-	-	42	42
Change in value of beneficial interests prior to Affiliation	-	-	48,097	48,097
Member capital contributions (Note 10)	1,500,000	-	-	1,500,000
Transfers to financially interrelated foundation (Note 10)	(4,597,447)	4,597,447	-	-
Change in net assets of financially interrelated Foundation (Note 10)	-	212,529	(417)	212,112
Net assets released from restrictions - used for capital	47,303	(47,303)	-	-
Change in net assets	(3,888,879)	4,791,058	47,772	949,951
Balance, December 31, 2016	$ 6,867,955	$ 5,159,429	$ 2,286,570	$ 14,313,954

See notes to financial statements.

The Episcopal Church Home, Inc.

Statement of Cash Flows
For the Period July 1, 2016 through December 31, 2016

Cash flows from operating activities:	
Change in net assets	$ 949,951
Adjustments to reconcile change in net assets to net cash provided by operating activities:	
Depreciation and amortization	737,601
Provision for bad debt expense	6,637
Amortization of entrance fees	(226,041)
Investment income	(174,831)
Change in net assets of financially interrelated Foundation	(212,112)
Member capital contributions	(1,500,000)
Change in operating assets and liabilities:	
Resident accounts receivable	154,077
Prepaid expenses and other assets	119,983
Accounts payable	314,169
Other liabilities	57,216
Net cash provided by operating activities	226,650
Cash flows from investing activities	
Purchase of property and equipment	(245,809)
Purchase of investments	(27,278)
Sales and maturities of investments	1,695,275
Net cash provided by investing activities	1,422,188
Cash flows from financing activities:	
Entrance fees collected	1,253,801
Entrance fees refunded	(941,100)
Member capital contributions	1,500,000
Principal payments on long-term debt	(12,130)
Net cash provided by financing activities	1,800,571
Net change in cash and cash equivalents	3,449,409
Cash and cash equivalents	
Beginning	811,533
Ending	$ 4,260,942
Supplemental disclosure of cash flow information:	
Cash paid during the year for interest	$ 28,595
Supplemental noncash investing activities:	
Transfer of investments to interest in financially interrelated Foundation	$ 6,841,918

See notes to financial statements.

Note 1. Organization and Summary of Significant Accounting Policies

Nature of operations: The Episcopal Church Home, Inc. (the Organization) is a Kentucky nonprofit organization located in Louisville, Kentucky. The Organization operates a senior residential health care facility and home known as the Episcopal Church Home (the Home). The Home has licenses to operate up to 93 skilled nursing facility beds, 46 nursing home beds, and 127 personal care beds, 52 of which are located in a designated special care unit for memory-impaired persons. St. Luke's Chapel is located adjacent to the Home and its accounts and activities are included with those of the Home. The Organization also owns and operates Dudley Square, an independent living retirement community consisting of 62 townhouses on a site adjacent to the Home. Residents of Dudley Square have lifetime occupancy rights in return for payment of residency fees including advance entrance fees that are partially refundable.

Changes in the Organization: On October 1, 2016, the Organization entered into an affiliation agreement (the Affiliation) with another organization (see Note 10). As a result of the Affiliation, the Organization changed its fiscal year from June 30 to December 31. Accordingly, the accompanying financial statements reflect the Organization's transition period from July 1, 2016 through December 31, 2016 which includes only 6 months of operations.

Basis of presentation: The accompanying financial statements are prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) in accordance with the Financial Accounting Standards Board (FASB) Accounting Standards Codification.

Use of estimates: The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported amounts of revenue and expense during the reporting period. Actual results could differ from those estimates.

Tax status: The Organization is a nonprofit organization as described in Section 501(c)(3) of the Internal Revenue Code and therefore is not subject to income taxes. Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the Organization and recognize a tax liability if the Organization has taken an uncertain position that more likely than not would not be sustained upon examination by the IRS or other applicable taxing authorities. The Organization is no longer subject to income tax examinations for fiscal years prior to 2013.

Compliance: The Organization is affected by the health care economy in the State of Kentucky and is subject to local, state, and federal rules and regulations. Compliance with these laws and regulations, particularly those relating to the Medicare and Medicaid programs, can be subject to government review and interpretation, as well as regulatory actions unknown and unasserted at this time. Violations of these regulations could result in the imposition of significant fines and penalties, as well as significant repayments of previously billed and collected revenue for resident services. Management believes that the Organization is in substantial compliance with current laws and regulations.

Interests in financially interrelated entities: A recipient entity and a specified beneficiary are financially interrelated entities if one of the entities has the ability to influence the operating and financial decisions of the other and one of the entities has an ongoing economic interest in the net assets of the other. On October 1, 2016, as a result of the Affiliation, The Episcopal Church Home Foundation, Inc. (the Foundation) was established and certain investments were transferred from the Organization to the Foundation. The Foundation was established for the sole purpose to support the Organization through fund-raising and investment activities. As such, the Organization recognizes and adjusts its interest in the net assets of the Foundation as reflected in the accompanying financial statements.

Note 1. Organization and Summary of Significant Accounting Policies (Continued)

Cash and cash equivalents: Cash equivalents include all highly liquid investments with original maturities of three months or less. Deposits in banks at times may exceed federally insured limits.

Resident accounts receivable: Resident accounts receivable consists of amounts due from residents and third-party payors, less an estimate for uncollectible accounts. The allowance for uncollectible accounts is established on an aggregate basis by using historical write-off rate factors applied to unpaid accounts based on aging. Loss rate factors are based on historical loss experience and adjusted for economic conditions and other trends affecting the Organization's ability to collect outstanding amounts. Uncollectible amounts are written off against the allowance for doubtful accounts in the period they are determined to be uncollectible. See Note 2.

Net resident service revenue: Net resident service revenue includes rent, room charges and ancillary services and is derived from participation in the Medicare and Medicaid programs, as well as from insurance companies and private pay residents. Revenue is considered earned when services are provided and is recorded at established billing rates, net of contractual adjustments resulting from the agreements with third-party payors, if applicable.

The Home participates in the Medicare and Medicaid programs for qualified residents. The payment methodology related to these programs is based on cost and clinical assessments that are subject to review and final approval by Medicare and Medicaid. Provisions for estimated third-party payor settlements, if any, are provided in the period the related services are rendered. Differences between the amounts accrued and the subsequent settlements are recorded into operations in the year of settlement.

The Home is paid under the Medicare Prospective Payment System (PPS) which is a per diem price-based system. Annual cost reports are required to be submitted to the designated Medicare Administrative Contractor; however, they do not contain a cost settlement. The Home is paid under the Medicaid program administered by the State of Kentucky. The Home bills the program using rates established by the State of Kentucky, based on a pricing fee methodology with adjustments based on acuity and geographic location. Such rates are subject to prospective adjustment by the State of Kentucky on a quarterly basis.

Amounts earned under the Medicaid and Medicare programs make up a significant portion of net resident service revenue earned during the period July 1, 2016 through December 31, 2016 are as follows:

Medicare	25%
Medicaid	8%

Charity care: The Organization provides care to residents who meet certain criteria under its charity care policy without charge. Key elements used to determine eligibility include a resident's demonstrated inability to pay. Because the Organization does not pursue collection of amounts determined to qualify for financial assistance, they are not reported as revenue. The Organization has estimated the costs foregone for services and supplies furnished under the Organization's charity care policy aggregated to approximately $36,000 for the period July 1, 2016 through December 31, 2016.

Performance indicator: The statement of activities includes a performance indicator of operations labeled as “excess of revenue under expenses.” Changes in net assets which are excluded from the performance indicator include the change in value of beneficial interests, restricted contributions, investment income subject to donor restriction, and contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purpose of acquiring such assets).

Note 1. Organization and Summary of Significant Accounting Policies (Continued)

Contributions: Contributions received are recorded as an increase in unrestricted, temporarily restricted or permanently restricted support, depending on the existence or nature of any donor-imposed restrictions.

Net assets: Net assets of the Organization and changes therein are classified and reported as follows:

Unrestricted: Those resources not subject to donor imposed restrictions over which the Board of Directors has discretionary control. Certain unrestricted amounts have been designated for specific purposes amounts represent those assets which the Board of Directors has set aside for a particular purpose. In connection with the Affiliation as described in Note 10, these board designated assets were transferred to a new financially interrelated Foundation.

Temporarily restricted: Those resources subject to donor imposed restrictions which will be satisfied by specific actions of the Organization and/or by the passage of time. A portion of the interest in the financially interrelated Foundation is also reported as temporarily restricted.

Permanently restricted: Those resources are subject to a donor imposed restriction that they be maintained permanently by the Organization. The donors of these resources generally permit the Organization to use all or part of the income earned, including capital appreciation for unrestricted or temporarily restricted purposes.

Unconditional promises to give cash and other assets are accrued at estimated fair value at the date each promise is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction is satisfied, net assets are released and reported as an increase in unrestricted net assets. Contributions received with donor-imposed restrictions, where the restrictions are met in the same fiscal year, are reported as unrestricted net assets.

Investments: Investments are considered trading securities and are carried at fair value with unrealized gains or losses included in the statement of activities unless the investment income is restricted by donor or law. Contributed investments are recorded at fair value on the date of the gift. Realized gains or losses on investments sold are determined on a specific identification basis.

Investments also include beneficial interests in perpetual trusts held by parties other than the Organization. Under the terms of the trust, the Organization has the irrevocable right to receive the income earned on the trust assets in perpetuity, but never receive the assets held in trust. Under this arrangement, the present value of the estimated future cash receipts from the trust assets (generally equal to the fair value of the assets contributed to the trust) is recorded as permanently restricted contribution revenue in the year the trust is established. Annual distributions are reported as contribution income and classified according to any restrictions on distributions. Adjustments to the amount reported as an asset are based on an annual review using the same basis that was used to measure the asset initially and are recorded in the statement of changes in permanently restricted net assets under the caption "change in value of beneficial interests."

Investments held by the Organization or in a trust for the beneficial interest of the Organization are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investments, it is at least reasonably possible that changes in the fair value of investments will occur in the near term and such changes could materially affect the amounts reported in the balance sheet.

Certain investments, including the beneficial interests in perpetual trusts, were transferred to a new financially interrelated Foundation entity that was established as a result of the Affiliation (see Note 10).

Note 1. Organization and Summary of Significant Accounting Policies (Continued)

Assets limited as to use: Assets limited to use consist of cash, cash equivalents and investments and are limited as to use and include certain amounts internally designated as limited by the Board of Directors.

Financial instruments: The organization reports investments at fair value as further described in Note 9. Other financial instruments, which primarily include accounts receivable, accounts payable and debt are recorded at cost and approximate fair value.

Property and equipment: Property and equipment are recorded at cost if purchased, or fair market value as of the date of donation, and depreciated over their estimated useful lives using the straight-line method of depreciation. Estimated useful lives are as follows:

Land improvements	10-20 years
Buildings and improvements	10-40 years
Furniture, fixtures and equipment	5-10 years
Vehicles	5 years

Property and equipment is subject to an impairment assessment whenever events or circumstances indicate that the carrying amount of an asset, or group of assets, may not be recoverable from future cash flows. If the carrying amount is considered impaired, an impairment charge is recorded for the amount by which the carrying value exceeds its fair value. Management has concluded that no events or circumstances indicating potential impairment occurred for the period July 1, 2016 through December 31, 2016.

Refundable advance deposits and deferred entrance fees: Residents entering into a Dudley Square independent living unit are required to execute a resident agreement. The agreements require the residents to pay an entrance fee prior to occupancy. The agreements stipulate that a portion of the entrance fee is partially refundable within 90 days after the death of the resident, permanent transfer of the resident out of the Dudley Square units to other units of the Home or another organization, or termination of the agreement by the resident. For agreements entered into subsequent to July 1, 2006, the residency fee is refundable, less 1% for each month of occupancy, up to 25% for a minimum refund of 75%. For agreements entered into prior to July 1, 2006, the minimum refund is 82%.

The refundable portion of the entrance fees is reported as “Refundable advance deposits” in the accompanying balance sheet with a portion classified as a current liability based on the Organization’s prior experience with refund requests.

The nonrefundable portion of the entrance fees is reported as “Deferred entrance fees” in the accompanying balance sheet with a portion classified as a current liability based on estimates of amounts expected to be amortized to revenue in the next fiscal year. The nonrefundable portion of the deferred entrance fee is amortized to revenue using the straight-line method over the estimated remaining useful life expectancy of the residents. Any unamortized entrance fees at the time of the resident's death are recorded as revenue.

The agreements require the residents to pay a monthly service charge for services provided and use of the Organization’s facilities. Management has determined that the monthly service charge is sufficient to cover the costs of any future service obligations of the residents. As such, the Organization has not recorded a liability for the present value of the net costs of any future service obligations.

Advertising: Advertising costs are charged to operations when incurred. Advertising expense was approximately $186,000 for the period July 1, 2016 through December 31, 2016.

Note 1. Organization and Summary of Significant Accounting Policies (Continued)

Retirement plan: The Organization sponsors a defined contribution retirement plan covering all full time employees age 21 and older with at least one year of employment with the Organization. The Organization matches each participant's contribution up to a maximum percentage of annual compensation. Retirement plan expense was approximately $7,000 for the period July 1, 2016 through December 31, 2016.

Subsequent events: The Organization has evaluated subsequent events for potential recognition and/or disclosure through May 23, 2017, the date the financial statements were available to be issued.

Note 2. Resident Accounts Receivable

The Organization provides services without collateral to its facility residents, many of whom are local residents and who are insured under third-party payor agreements. The mix of receivables from residents and third-party payors at December 31, 2016 is as follows:

Medicare	$ 306,329
Medicaid	220,657
Insurance	355,477
Private and other	463,922
	1,346,385
Less: allowance for uncollectable accounts	(141,464)
Resident accounts receivable, net	$ 1,204,921

Bad debt expense for the period July 1, 2016 through December 31, 2016 was $6,637.

Note 3. Investments and Assets Limited as to Use

The composition of investments as of December 31, 2016 is set forth in the following table:

Cash and cash equivalents	$ 59,107
Certificates of deposit	155,890
	214,997
Less: current portion	(59,107)
Total investments, less current portion	$ 155,890

Note 3. Investments and Assets Limited as to Use (Continued)

The portion of investments that are limited as to use as of June 30, 2016 is set forth in the following table:

Internally designated cash and cash equivalents	$	59,107
Internally designated certificates of deposit		155,890
Total investments	$	214,997

Investment income is comprised of the following for the period July 1, 2016 through December 31, 2016:

Realized gain	$	3,040
Unrealized gain		148,894
Interest and dividends		22,897
Investment income	$	174,831

Note 4. Line of Credit

The Organization has an available line of credit with maximum borrowings of $900,000 and is collateralized by the real property of the Organization and all future rents due to the Organization on such property. The interest rate is variable based on the U.S. Prime Rate, but may never be less than 4.00%. The applicable interest rate during the period was 4.00%. This line of credit was closed prior to December 31, 2016.

Note 5. Long-Term Debt

The following is a summary of long-term debt at December 31, 2016:

City of Graymoor-Devondale, Kentucky, Health Care Facilities Revenue Bond, Series 2001, due in annual installments through April 2018, with a fixed interest rate of 2.85%	$	1,878,218
Note payable, no interest, varying payments due monthly May 2015 through April 2019; collateralized by certain building improvements and equipment with a depreciated cost of $166,667		57,142
		1,935,360
Less: current maturities		(339,376)
Long-term debt, less current maturities	$	1,595,984

Note 5. Long-Term Debt (Continued)

On October 1, 2011, the Series 2001 Revenue Bonds were issued under a financing arrangement with Stock Yards Bank and Trust Company and the City of Graymoor-Devondale, Kentucky with an original principal amount of $7,000,000. The Organization has pledged its land, building, equipment (excluding Dudley Square property) and any future improvements as collateral for the loan.

Scheduled principal payments of long-term debt as of December 31, 2016 are due as follows:

Year ending December 31:	
2017	$ 339,376
2018	1,586,841
2019	9,143
Total	$ 1,935,360

Note 6. Net Assets and Endowments

The Organization's endowment fund includes both donor-restricted endowment funds and funds internally designated by the Board of Directors to function as endowments. Donor-restricted funds are presented as permanent and temporarily restricted net assets and consist of amounts restricted for the purpose of charity care, specified capital expenditures and other miscellaneous operational purposes.

Interpretation of relevant law: The Organization has interpreted the Uniform Prudent Management of Institutional Funds Act (the Act) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment fund absent explicit donor stipulations to the contrary. As a result of this interpretation, the Organization classifies as permanently restricted net assets (1) the original value of gifts donated to the permanent endowment, (2) the original value of subsequent gifts to the permanent endowment, and (3) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund.

The remaining portion of the donor-restricted endowment fund that is not classified as permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Organization in a manner consistent with the standard of prudence prescribed in the Act.

At December 31, 2016, the Organization had the following endowment net asset composition by type of fund:

Donor designated endowment funds - temporarily restricted	$ 4,937
Donor designated endowment funds - permanently restricted	42,516
Total endowment funds	$ 47,453

Note 6. Net Assets and Endowments (Continued)

The following is the change in endowment net assets for the period July 1, 2016 through December 31, 2016:

	Unrestricted - Board Designated	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	$ 6,139,099	$ 4,937	$ 42,424	$ 6,186,460
Investment gain	23,540	-	-	23,540
Net appreciation (realized and unrealized)	134,808	-	42	134,850
Total investment return	158,348	-	42	158,390
Contributions	-	-	50	50
Transfer to financially interrelated Foundation	(4,597,447)			(4,597,447)
Appropriation of endowment assets for expenditures	(1,700,000)	-	-	(1,700,000)
Endowment net assets, end of year	$ -	$ 4,937	$ 42,516	$ 47,453

Funds with deficiencies: From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or the Act requires the Organization to retain as a fund of perpetual duration. In accordance with current guidance, deficiencies of this nature are reported in unrestricted net assets. There were no such deficiencies as of December 31, 2016.

Return objectives and risk parameters: The Organization has adopted investment policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment. Endowment assets include those assets designated by the Board for specified purpose. Under these policies, as approved by the Board of Directors, the endowment assets are invested in a manner that is intended to preserve and grow capital, strive for consistent absolute returns, preserve purchasing power by striving for long- term returns which either match or exceed the set payout, fees and inflation without putting the principal value at imprudent risk, and diversify investments consistent with commonly accepted industry standard to minimize the risk of large losses.

Strategies employed for achieving objectives: To satisfy its long-term rate-of-return objectives, the Organization relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Organization targets a diversified asset allocation that meets the Organization's long-term rate-of-return objectives while avoiding undue risk from imprudent concentration in any single asset class or investment vehicle.

Spending guidelines and how the investment objectives relate to spending guidelines: The Organization has policies, based upon the intent of the donor-restricted endowed assets, to invest cash deposits in a timely manner while maintaining sufficient liquidity for appropriations to the operating fund. This is consistent with the Organization's objective of preservation of the fair value of the original gift of the endowment assets held in perpetuity as well as to provide additional real growth through new gifts and investment return.

Note 7. Functional Expenses

Functional classification of expenses for the period July 1, 2016 through December 31, 2016 consisted of the following:

Program services	$ 7,492,879
Management and administrative support	2,151,195
Fundraising	23,831
Total functional expenses	$ 9,667,905

Note 8. Commitments and Contingencies

Litigation: The Organization is subject to asserted and unasserted claims encountered in the normal course of business. The Organization's management and legal counsel assess such contingent liabilities and such assessment inherently involves an exercise of judgment. In assessing loss contingencies related to legal proceedings that are pending against the Organization or unasserted claims that may result in such proceedings, the Organization's legal counsel evaluates the perceived merits of any legal proceedings or unasserted claims as well as the perceived merits of the amount of relief sought or expected to be sought therein. In the opinion of management, disposition of these matters will not have a material effect on the Organization's financial condition or results of operations.

Health plan: The Organization sponsors a partially self-funded health benefit plan for its employee's health care costs. The Organization is responsible for the first $55,000 of claims per employee incurred annually, up to approximately $1,120,000 in the aggregate for all plan participants claims incurred annually. Third party insurance coverage is responsible for amounts in excess per employee and in excess of the aggregate limit. The health insurance expense is based upon actual claims paid, reinsurance premiums, administration fees, and provisions for unpaid and unasserted claims at year-end.

Health insurance expense for the period July 1, 2016 through December 31, 2016 was approximately $244,000. A liability for estimated claims outstanding at December 31, 2016 of approximately $101,000 has been recorded for management’s estimate of claims incurred but not yet reported and is included in accrued expenses on the accompanying balance sheet.

Note 9. Fair Value Measurements

For amounts reported at fair value, the Organization adheres to the GAAP framework for measuring fair value which establishes a fair value hierarchy consisting of three levels of inputs that may be used to measure fair value as follows:

Level 1 - Inputs that utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that the Organization has the ability to access.

Level 2 - Inputs that include quoted prices for similar assets and liabilities in active markets and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument. Fair values for these instruments are estimated using pricing models, quoted prices of securities with similar characteristics, or discounted cash flows.

Level 3 - Inputs that are unobservable inputs for the asset or liability, which are typically based on an entity's own assumptions, as there is little, if any, related market activity.

Note 9. Fair Value Measurements (Continued)

In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the valuation methodologies used at December 31, 2016.

Beneficial interest in assets held: Beneficial Interest in assets held is recorded at fair value on a recurring basis. Fair value measurement is based upon the fair value of the assets held in the perpetual trusts as reported by the trustees at December 31, 2016. The Organization considers the measurement of its beneficial interest in the perpetual trusts to be a Level 3 measurement within the fair value hierarchy because even though that measurement is based on the unadjusted fair values of the trust assets reported by the trustee, the Organization will never receive those assets or have the ability to direct the trustee to redeem them.

There are no investments measured at fair value on a recurring basis as of December 31, 2016.

The following is a reconciliation of the beginning and ending balances of assets measured at fair value on a recurring basis using significant unobservable (Level 3) inputs for the period July 1, 2016 through December 31, 2016:

	Beneficial Interest in Assets Held
Balance, July 1, 2016	$ 2,196,374
Unrealized gain	61,912
Distributions	(13,815)
Transfer to financially interrelated foundation	(2,244,471)
Balance, December 31, 2016	$ -

Note 10. Affiliation Agreement and Interest in Financially Interrelated Foundation

Effective November 1, 2015, the Organization entered into management service agreement with Episcopal Retirement Homes, Inc. (ERH). Under the agreement, ERH began providing certain management services to assist the Organization manage its operations. For the period July 1, 2016 through December 31, 2016, management fees of $137,193 were paid to ERH as part of this management agreement. At December 31, 2016, $3,799 was owed to ERH and is included in “Accounts payable” on the accompanying balance sheet.

Effective October 1, 2016, the Organization entered into the Affiliation with ERH’s parent organization, Episcopal Retirement Services (ERS). As a result, the management service agreement with ERH was terminated. However, ERS continued providing management services under the terms of the Affiliation. Annual management fees to be paid to ERS were established at amounts ranging from $1,582,000 to $1,692,000 annually through June 30, 2019. Fees paid to ERH under the affiliation agreement totaled $395,499 for the period July 1, 2016 through December 31, 2016.

Note 10. Affiliation Agreement and Interest in Financially Interrelated Foundation (Continued)

Concurrently with the affiliation with ERS, the Organization amended and restated its articles of incorporation and bylaws. The Organization revised its legal name to be The Episcopal Church Home, Inc. and established a new legal entity, The Episcopal Church Home Foundation, Inc. (the Foundation). The Foundation will be governed by an independent Board of Directors. The Foundation was organized to solely support the Organization. In connection with the Affiliation, investments and beneficial interests in assets held totaling $6,841,918 were transferred from the Organization to the Foundation. From the date of the Affiliation through December 31, 2016, the Organization recognizes its interest, and any changes in its interest, in the net assets of the Foundation as a financially interrelated entity. The Organization recognized an increase in its interest in the Foundation of $212,112 for the period July 1, 2016 through December 31, 2016. The Organization's interest in the net assets of the Foundation are classified as $2,244,054 of permanently restricted net assets and $4,809,976 of temporarily restricted net assets on the accompanying statement of changes of net assets.

The purpose of the Affiliation with ERS is to further the charitable missions of both ERS and the Organization through various shared affiliation benefits and goals. The Organization amended and restated its articles and bylaws and established a nonprofit corporate membership structure with ERS obtaining 80% interest and the Foundation obtaining 20% interest in the Organization. A new Board of Directors of the Organization is comprised of 9 voting members and 1 non-voting member with ERS appointing 5 of the 9 voting member positions. For its consideration, ERS provided the Foundation with an unrestricted cash contribution of $500,000 and made a member capital contribution of $1,200,000 to the Organization for its 80% member interest. The Foundation in turn made a member capital contribution of $300,000 to the Organization for its 20% member interest. The total of these two capital contributions is included in the accompanying statement of changes in net assets as “Member capital contributions.”

The Foundation has agreed to make certain specified contributions to Organization in addition to operational support contributions as approved by the Foundation Board annually. There were no operational support contributions for the period July 1, 2016 through December 31, 2016. For the period July 1, 2016 through December 31, 2016, the Foundation provided $135,000 in required annual development capacity grants to the Organization. The Foundation is required to provide an additional $135,000 in development capacity grants to the Organization on September 1, 2017 and 2018. In addition, the Foundation has agreed to make a one-time grant of $1,100,000 to enhance the Organization's credit standing contingent upon certain future events occurring.

The Affiliation agreement is scheduled to terminate on October 31, 2021. The termination will have no impact on the Organization's governance and ERS will continue to maintain its 80% interest in the Organization. ERS and the Foundation may unwind the Affiliation by providing written notice between July 1, 2018 and October 31, 2018. The Foundation's ability to unwind can be made unilaterally by its Board of Directors based on their evaluation of achievement of shared affiliation goals. If the unwind provision is exercised by the Foundation, all legal relationships between ERS and the Organization will terminate, ERS will cease managing the Organization and will have its rights to participate in the Board revoked, and its 80% member interest will transfer to the Foundation.

Note 10. Affiliation Agreement and Interest in Financially Interrelated Foundation (Continued)

Following is a summarization of the transactions associated with the Affiliation for the period July 1, 2016 through December 31, 2016:

Funds transferred to financially interrelated Foundation:	
Investments (unrestricted, board designated)	$ 4,597,447
Beneficial interests (permanently restricted)	2,244,471
Total	$ 6,841,918

Ending balance sheet of financially interrelated Foundation at December 31, 2016:	
Assets:	
Cash	$ 65,000
Investments	4,444,976
Beneficial interests	2,244,054
Investment in The Episcopal Church Home, Inc.	300,000
	$ 7,054,030
Net assets	$ 7,054,030
Change in market value of investments held at financially interrelated Foundation, net of contribution to The Episcopal Church Home, Inc.	$ 212,112

Note 11. Recent Accounting Pronouncements

Revenue recognition: In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*. The updated standard will replace most existing revenue recognition guidance in GAAP when it becomes effective and permits the use of either a full retrospective or retrospective with cumulative effect transition method. In August 2015, the FASB issued ASU 2015-14, which defers the effective date of ASU 2014-09 one year, making it effective for annual reporting periods beginning after December 15, 2018. The Organization is currently assessing what impact this new standard may have on its financial statements and is determining the transition method that will be used.

Not-for-profit entities: In August 2016, the FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements for Not-for-Profit Entities.* This accounting standard is intended to make improvements to the information provided in the financial statements and accompanying notes of not-for-profit entities. The standard sets forth improvements to net asset classification requirements and the information presented about a not-for-profit entity's liquidity, financial performance and cash flows. ASU 2016-14 will be effective for its fiscal years beginning after December 15, 2017 with early adoption permitted. The Organization is currently evaluating the impact of the pending adoption of the new standard on its financial statements.

Restricted cash: In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*, which provides guidance on the presentation of restricted cash or restricted cash equivalents in the statement of cash flows. This ASU is effective for period beginning after December 15, 2018 with early adoption permitted. The Company is currently evaluating the impact of the adoption of this ASU on the financial statements.