# Episcopal Retirement Homes – Obligated Group

Combined Financial Report
December 31, 2016

## Contents

**Independent Auditor's Report**

To the Board of Directors
Episcopal Retirement Homes – Obligated Group

**Report on the Financial Statements**
We have audited the accompanying combined financial statements of Episcopal Retirement Homes – Obligated Group, which comprise the combined statements of financial position as of December 31, 2016 and 2015, the related combined statements of activities, changes in net assets and cash flows for the years then ended, and the related notes to the combined financial statements (collectively, 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 audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits 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 Episcopal Retirement Homes – Obligated Group as of December 31, 2016 and 2015, and the results of its operations, 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.

**Emphasis of Matter**
As discussed in Note 1 to the financial statements, due to the reorganization of affiliated entities effective January 1, 2016, the financial statements of Episcopal Retirement Homes – Obligated Group are now presented on a combined basis. Our opinion is not modified with respect to this matter.

**Other Matter**
Our audits were conducted for the purpose of forming an opinion on the combined financial statements as a whole. The accompanying supplementary combining information is presented for purposes of additional analysis and is not a required part of the combined 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 combined financial statements. The information has been subjected to the auditing procedures applied in the audit of the combined financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the combined financial statements or to the combined financial statements themselves and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated in all material respects in relation to the combined financial statements as a whole.

RSM US LLP

Cincinnati, Ohio
June 2, 2017

**Episcopal Retirement Homes - Obligated Group**

**Combined Statements of Financial Position**
**December 31, 2016 and 2015**

| | 2016 | 2015 |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 3,460,665 | $ 4,636,926 |
| Resident accounts receivable, net | 843,411 | 1,204,729 |
| Other receivables | 1,000,909 | 597,797 |
| Note receivable | - | 1,914,430 |
| Assets limited as to use | 523,988 | 835,904 |
| Other current assets | 289,831 | 315,797 |
| **Total current assets** | 6,118,804 | 9,505,583 |
| Assets limited as to use | 26,956,609 | 26,990,121 |
| Property and equipment, net | 50,890,661 | 50,612,285 |
| Beneficial interest in Marjorie P. Lee Endowment Fund | 21,167,524 | 20,955,167 |
| Intangible assets | 870,241 | 309,200 |
| Due from affiliates | 1,772,432 | 1,338,238 |
| Other | 1,211,011 | 1,289,365 |
| **Total assets** | $ 108,987,282 | $ 110,999,959 |
| **Liabilities and Net Assets** | | |
| Current liabilities: | | |
| Accounts payable | $ 1,674,959 | $ 1,311,806 |
| Current portion of long-term debt | 1,280,000 | 1,208,000 |
| Deposits from residents | 388,061 | 380,524 |
| Refundable entrance fees | 1,409,000 | 1,010,000 |
| Deferred revenue from entrance fees | 435,000 | 375,000 |
| Accrued liabilities and other | 2,835,474 | 2,875,590 |
| **Total current liabilities** | 8,022,494 | 7,160,920 |
| Long-term debt, net of current portion | 21,220,000 | 22,842,000 |
| Deferred revenue from entrance fees, net of current portion | 1,374,633 | 1,713,902 |
| Refundable entrance fees, net of current portion | 13,725,400 | 14,399,500 |
| Interest rate swaps | 2,382,503 | 2,817,345 |
| Due to affiliates | 649,740 | - |
| Other long-term liabilities | 764,449 | 857,563 |
| **Total liabilities** | 48,139,219 | 49,791,230 |
| Net assets: | | |
| Unrestricted | 36,258,751 | 37,053,931 |
| Temporarily restricted | 989,409 | 752,917 |
| Permanently restricted | 23,599,903 | 23,401,881 |
| **Total net assets** | 60,848,063 | 61,208,729 |
| **Total liabilities and net assets** | $ 108,987,282 | $ 110,999,959 |

See notes to combined financial statements.

**Episcopal Retirement Homes - Obligated Group**

**Combined Statements of Activities**
**Years Ended December 31, 2016 and 2015**

| | 2016 | 2015 |
|---|---|---|
| Revenue: | | |
| Net resident revenue | $ 23,316,730 | $ 23,523,326 |
| Other operating revenue | 1,755,684 | 1,560,717 |
| Management fee income | 1,957,072 | 1,065,964 |
| Amortization of entrance fees | 429,568 | 371,775 |
| Marjorie P. Lee endowment income | 969,320 | 958,116 |
| Interest and dividend income | 273,077 | 335,746 |
| **Total revenue** | 28,701,451 | 27,815,644 |
| Expenses: | | |
| Salaries and wages | 13,338,364 | 12,222,337 |
| Employee benefits and payroll taxes | 3,651,897 | 3,309,260 |
| Supplies | 924,662 | 1,000,571 |
| Food | 1,383,320 | 1,376,827 |
| Professional services | 1,585,520 | 1,708,331 |
| Utilities | 1,285,587 | 1,323,078 |
| Insurance | 406,876 | 375,761 |
| Depreciation and amortization | 3,446,572 | 3,356,463 |
| Interest | 918,068 | 950,627 |
| Other operating expense | 4,180,886 | 3,871,269 |
| **Total expenses** | 31,121,752 | 29,494,524 |
| **Operating loss** | (2,420,301) | (1,678,880) |
| Nonoperating income (loss): | | |
| Contributions | 860,280 | 996,680 |
| Investment gain (loss) | 1,616,388 | (510,197) |
| Change in interest rate swaps | 434,842 | 94,564 |
| Other loss | (6,407) | (24,316) |
| **Total nonoperating income** | 2,905,103 | 556,731 |
| **Excess of revenue over (under) expenses** | $ 484,802 | $ (1,122,149) |

See notes to combined financial statements.

**Episcopal Retirement Homes - Obligated Group**

**Combined Statements of Changes in Net Assets**
**Years Ended December 31, 2016 and 2015**

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---|---|---|---|---|
| Balance, January 1, 2015 | $ 48,466,583 | $ 696,825 | $ 24,647,458 | $ 73,810,866 |
| Excess of revenue under expenses | (1,122,149) | - | - | (1,122,149) |
| Restricted contributions | - | 85,000 | - | 85,000 |
| Change in beneficial interest in endowment fund | - | - | (1,230,677) | (1,230,677) |
| Change in value of charitable remainder trusts | - | (7,207) | - | (7,207) |
| Other | - | - | (14,900) | (14,900) |
| Transfer from ERS Foundation to affiliated entities | (115,263) | - | - | (115,263) |
| Forgiveness of debt from affiliated entities | (10,175,240) | - | - | (10,175,240) |
| Net assets released from restriction to affiliated entities | - | (21,701) | - | (21,701) |
| **Change in net assets** | (11,412,652) | 56,092 | (1,245,577) | (12,602,137) |
| Balance, December 31, 2015 | 37,053,931 | 752,917 | 23,401,881 | 61,208,729 |
| Excess of revenue over expenses | 484,802 | - | - | 484,802 |
| Restricted contributions | - | 985,616 | 20,792 | 1,006,408 |
| Change in beneficial interest in endowment fund | - | - | 177,230 | 177,230 |
| Change in value of charitable remainder trusts | - | 2,425 | - | 2,425 |
| Transfer from ERS Foundation to affiliated entities | (793,634) | - | - | (793,634) |
| Transfer to affiliated entity | (1,200,000) | | | (1,200,000) |
| Net assets released from restriction | 713,652 | (713,652) | - | - |
| Net assets released from restriction to affiliated entities | - | (37,897) | - | (37,897) |
| **Change in net assets** | (795,180) | 236,492 | 198,022 | (360,666) |
| **Balance, December 31, 2016** | **$ 36,258,751** | **$ 989,409** | **$ 23,599,903** | **$ 60,848,063** |

See notes to combined financial statements.

**Episcopal Retirement Homes - Obligated Group**

**Combined Statements of Cash Flows**
**Years Ended December 31, 2016 and 2015**

| | **2016** | 2015 |
|---|---|---|
| Cash flows from operating activities: | | |
| Change in net assets | **$ (360,666)** | $ (12,602,137) |
| Adjustments to reconcile change in net assets to net cash provided by operating activities: | | |
| Depreciation and amortization | **3,446,572** | 3,356,463 |
| Investment gain (loss) | **(1,616,388)** | 510,197 |
| Change in interest rate swaps | **(434,842)** | (94,564) |
| Change in beneficial interest in endowment fund | **(212,357)** | 1,230,677 |
| Amortization of deferred revenue from entrance fees | **(429,568)** | (371,775) |
| Forgiveness of debt from affiliated entities | **-** | 10,175,250 |
| Changes in operating assets and liabilities: | | |
| Receivables | **(41,794)** | (253,456) |
| Other assets | **98,638** | (286,338) |
| Amounts due from affiliates | **(434,194)** | (1,416,003) |
| Accounts payable | **363,153** | (404,346) |
| Accrued and other liabilities | **524,047** | 634,027 |
| **Net cash provided by operating activities** | **902,601** | 477,995 |
| | | |
| Cash flows from investing activities: | | |
| Purchase of property and equipment | **(3,719,266)** | (2,854,636) |
| Purchase of assets limited as to use | **(2,389,757)** | (8,556,632) |
| Proceeds from sale of assets limited as to use | **4,351,573** | 8,410,226 |
| Proceeds from note receivable | **1,914,430** | 1,794,127 |
| Purchase of intangible assets | **(561,041)** | (50,000) |
| **Net cash used in investing activities** | **(404,061)** | (1,256,915) |
| | | |
| Cash flows from financing activities: | | |
| Principal payments on long-term debt | **(1,550,000)** | (1,160,000) |
| Entrance fees collected | **1,340,399** | 2,039,000 |
| Entrance fees refunded | **(1,465,200)** | (442,200) |
| **Net cash (used in) provided by financing activities** | **(1,674,801)** | 436,800 |
| | | |
| **Net change in cash and cash equivalents** | **(1,176,261)** | (342,120) |
| | | |
| Cash and cash equivalents: | | |
| Beginning | **4,636,926** | 4,979,046 |
| | | |
| Ending | **$ 3,460,665** | $ 4,636,926 |
| | | |
| Supplemental disclosure of cash flow information: | | |
| Cash paid during the year for interest | **$ 952,364** | $ 947,251 |

See notes to combined financial statements.

## Note 1. Nature of Business and Summary of Significant Accounting Policies

**Nature of business:** Effective January 1, 2016, Episcopal Retirement Services (ERS) was established as a new tax exempt parent organization and became the sole member of Episcopal Retirement Homes, Inc. (ERH), Episcopal Retirement Services Foundation (the Foundation) and other affiliated entities. Together, ERH and the Foundation are collectively referred to as the “Obligated Group”.

ERH is a not-for-profit corporation that was organized under Section 501(c)(3) of the Internal Revenue Code and was incorporated under the laws of the State of Ohio. ERH owns and operates two senior living communities (Marjorie P. Lee and Deupree House) in the Cincinnati, Ohio area as well as providing other community services focused on older adults. The Foundation is also exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. The Foundation’s sole purpose is to provide financial support to ERH and the other ERS affiliated entities.

**Basis of presentation:** The accompanying combined 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. The financial statements follow accounting procedures set forth in the AICPA Audit and Accounting Guides for *Not-for-Profit Entities* and *Health Care Entities* related to continuing care retirement communities.

**Basis of combination:** In 2015, prior to the creation of ERS, ERH was the sole member of the Foundation and other affiliated entities. Effective January 1, 2016, ERS, was created as the new parent organization of ERH, the Foundation and other affiliated entities. The accompanying subsidiary-level financial statements have been prepared on a combined basis and only include the financial statements of ERH and the Foundation which comprise the Obligated Group. This transaction was accounted for as a change in reporting entity amongst entities under common control. The combined financial statements are presented as if the aforementioned transaction occurred at the beginning of the earliest period presented, with no changes to the amounts of any financial statement line items resulting.

Presentation of the combined financial statements of these commonly controlled entities is determined to be more meaningful than separate financial statements as ERH and the Foundation are jointly responsible for the Obligated Group debt (see Note 5). All significant intercompany transactions and balances between ERH and the Foundation have been eliminated in combination.

**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 and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

**Cash and cash equivalents:** Cash equivalents include all highly liquid investments with original maturities of three months or less.

**Accounts receivable:** Accounts receivable for residents, insurance companies and governmental agencies are based on net charges. An 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 Obligated Group'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.

## Note 1. Nature of Business and Summary of Significant Accounting Policies (Continued)

**Assets limited as to use:** Assets limited as to use represent assets limited under the bond indenture, resident deposits, assets internally designated by the board of directors and those assets externally restricted by donors. Assets limited as to use consist of cash, cash equivalents and debt and equity investment securities. Investments are considered trading securities and are carried at fair value. Fair value is determined based generally upon quoted market prices for equity and debt securities. Contributed investments are recorded at the fair market value at date of gift. Gains and losses on investments sold are determined on a specific identification basis. Investments in hedge funds are recorded at fair value as provided by the most recent quarterly statements and adjusted for unrealized gains and losses and changes in net asset value of the funds. Assets limited as to use shown as current on the combined statement of financial position consist of assets restricted under the bond indenture for debt service payments of $523,988 and $835,904 as of December 31, 2016 and 2015, respectively.

Assets whose use is limited under bond indenture consist of the assets placed with a trustee pursuant to the terms of the Hamilton County, Ohio Hospital Facilities Revenue Bonds Series 2009 bond indentures. These assets consist of cash equivalents and investments in U.S. government obligations and are segregated into the following funds for the 2009 bond indentures: Debt Service Fund used to accumulate funds for bond interest and principal payments and Hamilton County Indemnity Fund used for legal and other costs incurred on behalf of Hamilton County in the event of default.

**Other Investments:** Investments in companies in which the Obligated Group has less than a 20 percent interest and the Obligated Group has no significant influence over the investment company are carried at cost and are included in other noncurrent assets on the combined statement of financial position. Dividends received from those companies are included in other income. Dividends received in excess of the Obligated Group's proportionate share of accumulated earnings are applied as a reduction of the cost of the investment. The total carrying amount of these cost method investments was $605,847 at December 31, 2016 and 2015. Management evaluates, on a periodic basis, whether an event or a change in circumstances has occurred in that period that may have a significant adverse effect on the fair value of these investments. No such changes in events or circumstances were noted for the years ended December 31, 2016 and 2015.

**Risk and uncertainties:** The Obligated Group invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statement of financial position.

**Property and equipment:** Property and equipment purchases are recorded at cost. Donated property and equipment are recorded at the estimated fair market value at the time of donation. Depreciation is computed principally on the straight-line basis over the estimated useful lives of the assets. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Costs of maintenance and repairs are charged to expense when incurred.

**Marjorie P. Lee Endowment Fund:** Income from the Marjorie P. Lee Endowment Fund, a fund which is held by trustees of the Episcopal Diocese of Southern Ohio, is restricted to the operation, maintenance, repair, renovation and refurbishing of the Marjorie P. Lee community. The endowment fund held in trust by the Episcopal Diocese of Southern Ohio had a fair value of $21,167,524 and $20,955,167 as of December 31, 2016 and 2015, respectively, and is reported in the accompanying statements of financial position as beneficial interest in Marjorie P. Lee Endowment Fund. Changes in the fair value of this trust are recorded as changes in beneficial interest in the accompanying combined statement of changes in net assets and amounted to an increase (decrease) in such interest of $177,230 and $(1,230,677) in 2016 and 2015, respectively.

## Note 1. Nature of Business and Summary of Significant Accounting Policies (Continued)

**Intangible assets:** Intangible assets consist of skilled nursing bed licenses that have been separately acquired. Although these licenses do not have a stated life and are presently transferrable, they are subject to regulation by the State of Ohio. During 2015, ERH entered into an agreement to purchase the operating rights to 28 additional skilled nursing bed licenses in order to relocate the beds to the Marjorie P. Lee community as part of a planned facility expansion. ERH made an initial $50,000 earnest deposit payment in 2015. During 2016, an additional $561,041 was paid to acquire these bed licenses. In accordance with accounting guidance, these intangible assets are tested for impairment annually, or whenever events or circumstances indicate that their fair value is more likely than not less than their carrying amount. As of December 31, 2016 and 2015, the carrying value of the operating licenses was $870,241 and $309,200, respectively, and no impairment loss was determined necessary.

**Note receivable:** The note receivable related to a promissory note agreement from the sale of land held for investment during 2014. The terms of the promissory note included interest of 3.25 percent and required the purchaser of the land to pay the Obligated Group approximately $1,914,000. This note was paid in full in 2016.

**Gift annuity obligations:** The Obligated Group has entered into gift annuity agreements whereby, upon receipt of an annuity gift, the Obligated Group pays the donor an annuity for the remainder of his or her life. At the time of the gift, the assets are recorded at their fair market value and an obligation is established for the present value of the annuity payments estimated to occur based upon the donor's life expectancy. The difference between the gift and the obligation is recognized as unrestricted contributions or as an increase in restricted net assets based upon the donor-imposed restrictions, if any. As of December 31, 2016 and 2015, the Obligated Group had unrestricted gift annuity obligations of approximately $262,000 and $287,000, respectively, which are included in other long-term liabilities on the statements of financial position.

**Deferred revenue from entrance fees:** A resident admitted into an independent living unit has the option of paying an entrance fee. ERH offers different types of entrance fee contracts described below:

The 60-unit independent-living Deupree House II contracts provide for a refund of the entrance fee (90 percent or 30 percent) to residents only from reoccupancy proceeds of a unit. The refundable portion of the entrance fee is recorded as a refundable liability on the statement of financial position. The nonrefundable portion of the entrance fee (10 percent or 70 percent) is deferred revenue and is being amortized into income using the straight-line method over the estimated remaining life expectancy of the resident.

Deupree House I and Marjorie P. Lee offered continuing care contracts. In these contracts, the entrance fee is deferred revenue and is amortized to income using the straight-line method over the estimated remaining life expectancy of the resident. Any unamortized entrance fees at the time of the resident's death are recorded as revenue. The refundable portion of entrance fees is reduced in the event of death or withdrawal by one percent of such fee for each month of residence. ERH has calculated the present value of the net cost of future services and the use of facilities to be provided to current residents and has compared that to the balance of unamortized deferred revenue from entrance fees. As the present value of this net cost does not exceed the amount of recorded unamortized entrance fees, no additional liability has been reflected in the accompanying combined financial statements.

The total of deferred revenue of the nonrefundable portion of the entrance fees amounted to approximately $1,810,000 and $2,088,000 at December 31, 2016 and 2015, respectively.

At December 31, 2016 and 2015, ERH had entrance fee contracts with gross potential refund obligations totaling approximately $15,134,000 and $15,410,000, respectively.

## Note 1. Nature of Business and Summary of Significant Accounting Policies (Continued)

**Net resident revenue:** The Obligated Group's principal activities are providing housing, health care and other related services for older adults. Revenue is derived from participation in the Medicaid and Medicare programs, as well as from private pay residents and insurance companies. Revenue is recorded at standard billing rates and differences between billing rates and amounts paid under these programs are recorded as contractual adjustments. Amounts earned under the Medicaid and Medicare programs make up a significant portion of net resident revenue earned during 2016 and 2015 is as follows:

| | Percent | |
|---|---|---|
| | 2016 | 2015 |
| Medicaid | 5% | 4% |
| Medicare | 8% | 11% |

The payment methodology related to these programs is based on cost and clinical assessments that are subject to review and final approval by Medicaid and Medicare. Any adjustment that is a result of this final review and approval will be recorded in the period in which the adjustment is made. In the opinion of management, adequate provision has been made for any adjustments that may result from such third-party review.

Services rendered to Medicare program beneficiaries are paid at prospectively determined rates based upon clinical assessments completed by the Obligated Group.

Services rendered to Ohio Medicaid program beneficiaries are paid at per diem rates prospectively determined by the Ohio Department of Job and Family Services, adjusted semi-annually for changes in patient acuity.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Management believes it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoings. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation. Noncompliance with such laws and regulations may result in significant regulatory action including fines, penalties and exclusion from the Medicare and Medicaid programs.

During 2016, the Obligated Group began the initial stages of the plan to renovate Marjorie P. Lee (the Master Plan). New admittances into the independent and assisted living facilities of Marjorie P. Lee were stopped in order to begin renovations on the units and execute the Master Plan. As a result, the Obligated Group experienced a decline in net resident revenue in 2016 and anticipates additional declines in 2017 until the Master Plan is complete and normal occupancy levels are reestablished.

**Benevolent care:** The Obligated Group provides benevolent care to residents who meet certain criteria under its benevolent care policy without charge. This care is provided in the form of benevolent assistance. Benevolent care is granted by the board of directors, as resources permit, in keeping with the Obligated Group's charitable purpose. The estimated cost of providing benevolent care is based on a calculation which applies a ratio of cost to charges to the gross uncompensated charges associated with providing benevolent care to qualifying residents. The Obligated Group estimates that it provided services to residents receiving benevolent care with costs totaling $179,000 and $290,000 during 2016 and 2015, respectively.

## Note 1. Nature of Business and Summary of Significant Accounting Policies (Continued)

**Contributions:** The Obligated Group reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of changes in net assets as net assets released from restrictions.

The Obligated Group reports gifts of property and equipment as unrestricted support, unless explicit donor stipulations specify how the donated assets must be used. Gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Obligated Group reports the expiration of donor restrictions when the assets are placed in service.

**Performance indicator:** The combined statement of activities includes a performance indicator of operations labeled as “excess of revenue over (under) expenses.” Changes in unrestricted net assets which are excluded from the performance indicator include transfers of assets to and from other affiliated entities for other than goods and services, forgiveness of debt from affiliated entities and net assets released from restriction.

**Hamilton County Bond Issue:** In connection with the Hamilton County (the County), Ohio Hospital Facilities Revenue Bonds, ERH leases various facilities to the County, which, in turn, subleases the facilities back to ERH. Under terms of the bond indenture between the County and the trustee, certain funds are required to be maintained as described above under "assets whose use is limited under bond indenture."

**Tax status:** The Internal Revenue Service has ruled that the Obligated Group is exempt from federal income taxes as an other than private foundation under Section 501(c)(3) of the Internal Revenue Code; therefore, they are not subject to federal or state income tax.

Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the Obligated Group and recognize a tax liability if the Obligated Group has taken an uncertain position that more likely than not would not be sustained upon examination by the IRS or other applicable taxing authorities. Management has analyzed the tax positions taken by the Obligated Group and has concluded that as of December 31, 2016 and 2015, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the combined financial statements . Accordingly, no provision has been made for federal income tax in the accompanying combined financial statements.

The Obligated Group is subject to examination by taxing authorities; however, no examinations are in progress. Management believes these entities are not subject to tax examinations for years prior to 2013.

**Recent accounting pronouncements:**

**Revenue recognition:** In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This guidance supersedes most revenue recognition requirements in U.S. generally accepted accounting principles, including most industry-specific guidance on revenue recognition. 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 Obligated Group is currently evaluating the impact of this guidance on its combined financial statements.

## Note 1. Nature of Business and Summary of Significant Accounting Policies (Continued)

**Fair value:** In May 2015, FASB issued ASU 2015-07, *Fair Value Measurement (Topic 850): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent*), which removes the requirement to categorize within the fair value hierarchy all investments for *which* fair value is measured using the net asset value per share practical expedient. ASU 2015-07 also limits certain disclosures to investments for which the entity has elected to measure the fair value using the practical expedient. This ASU will be effective for the Organization for fiscal years beginning after December 15, 2016. Early adoption is permitted and the amendments in ASU 2015-07 should be applied retrospectively to all periods presented. As ASU 2015-07 only amends and eliminates certain disclosures, the adoption did not have a material impact on its combined financial statements.

**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 Obligated Group is currently evaluating the impact of the pending adoption of the new standard on its combined 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 Obligated Group is currently evaluating the impact of the adoption of this ASU on its combined financial statements.

**Reclassifications:** Certain amounts in the prior year financial statements have been reclassified to conform with the current year presentation.

**Subsequent events:** The Obligated Group has evaluated subsequent events for potential recognition and/or disclosure through June 2, 2017 the date the combined financial statements were available to be issued.

## Note 2. Resident Accounts Receivable

Resident accounts receivable at December 31 is as follows:

| | 2016 | 2015 |
|---|---|---|
| Resident accounts receivable | $ 943,411 | $ 1,337,041 |
| Allowance for uncollectible accounts | (100,000) | (132,312) |
| **Net resident accounts receivable** | $ 843,411 | $ 1,204,729 |

### Note 2. Resident Accounts Receivable (Continued)

The Obligated Group provides services without collateral to its residents, most of whom are local residents and insured under third-party payor agreements. The mix of receivables from residents and third-party payors is as follows:

| | Percent | |
|---|---|---|
| | 2016 | 2015 |
| Medicare | 24% | 24% |
| Medicaid | 9% | 13% |
| Insurance | 22% | 28% |
| Private and other | 45% | 35% |
| **Total** | 100% | 100% |

### Note 3. Assets Limited as to Use

Assets limited as to use at December 31 are as follows:

| | 2016 | 2015 |
|---|---|---|
| Assets limited as to use: | | |
| Current assets | $ 523,988 | $ 835,904 |
| Noncurrent assets | 26,956,609 | 26,990,121 |
| **Total** | $ 27,480,597 | $ 27,826,025 |
| | | |
| Cash and cash equivalents | $ 1,736,283 | $ 3,204,853 |
| Mutual funds | 9,838,394 | 8,940,129 |
| Money market funds | 95,460 | 655,794 |
| Equity securities | 6,315,975 | 6,072,888 |
| Corporate obligations | 50,370 | 20,167 |
| Commingled trust funds | 5,494,149 | 4,735,466 |
| Hedge funds | 3,949,967 | 4,196,728 |
| **Total assets limited as to use** | $ 27,480,597 | $ 27,826,025 |

Designations and restrictions at December 31 are as follows:

| | 2016 | 2015 |
|---|---|---|
| Bond indentures | $ 724,499 | $ 1,035,964 |
| Resident deposits | 388,061 | 380,524 |
| Externally restricted by endowment | 2,077,106 | 2,056,314 |
| Internally designated by board of directors (see table below) | 23,911,366 | 23,989,735 |
| Externally restricted for specific purposes | 379,565 | 363,488 |
| **Total designations and restrictions** | $ 27,480,597 | $ 27,826,025 |

## Note 3. Assets Limited as to Use (Continued)

Assets limited as to use – internally designated by the board of directors are designated at December 31 as follows:

| | 2016 | 2015 |
|---|---|---|
| Marjorie P. Lee Home Fund | $ 9,432,518 | $ 8,881,353 |
| Development and operations | 4,796,207 | 4,244,377 |
| Working capital | 978,550 | 2,159,914 |
| Parish Health Ministry | 300,556 | 300,556 |
| Library | 50,000 | 50,000 |
| Chaplaincy | 384,044 | 384,044 |
| Financial aid - all programs | 1,294,562 | 1,294,562 |
| Clergy subsidy | 108,534 | 108,534 |
| Financial aid for Deupree | 419,767 | 419,767 |
| Central Ohio Development | 5,796,628 | 5,796,628 |
| Continuing education - Marjorie P. Lee | 350,000 | 350,000 |
| **Total internally designated by board of directors** | $ 23,911,366 | $ 23,989,735 |

Investment gain (loss) is comprised of the following for the years ended December 31:

| | 2016 | 2015 |
|---|---|---|
| Realized gain | $ 586,897 | $ 1,268,732 |
| Unrealized gain (loss) | 1,029,491 | (1,778,929) |
| **Total investment gain (loss)** | $ 1,616,388 | $ (510,197) |

## Note 4. Property and Equipment

Property and equipment and depreciable lives at December 31 are as follows:

| | 2016 | 2015 | Depreciable Life - Years |
|---|---|---|---|
| Land and improvements | $ 2,805,139 | $ 2,699,699 | 0-10 |
| Buildings and improvements | 74,327,967 | 74,203,206 | 20-40 |
| Equipment, furniture and fixtures | 10,721,289 | 11,902,867 | 5-10 |
| Computer equipment and software | 1,195,646 | 1,210,566 | 5-10 |
| Transportation equipment | 269,857 | 269,857 | 4-5 |
| Rental property | 89,441 | 89,441 | |
| Construction in progress | 2,606,661 | 578,107 | |
| **Total cost** | 92,016,000 | 90,953,743 | |
| Accumulated depreciation | (41,125,339) | (40,341,458) | |
| **Net carrying value** | $ 50,890,661 | $ 50,612,285 | |

Depreciation expense on property and equipment totaled $3,440,890 and $3,350,781 in 2016 and 2015, respectively.

## Note 5. Long-Term Debt

Long-term debt at December 31 is as follows:

| | 2016 | 2015 |
|---|---|---|
| 2009 Hamilton County, Ohio Hospital Facilities Revenue Bonds, varying interest rates, payable through 2029. | $ 22,500,000 | $ 23,700,000 |
| Ohio Housing Financing Agency note payable, accruing interest at a fixed rate of 2% annually; paid in full in 2016. | - | 350,000 |
| Less: current portion | (1,280,000) | (1,208,000) |
| **Long-term debt** | $ 21,220,000 | $ 22,842,000 |

In 2012, ERH completed a refunding of the 2009 bonds to modify the interest rate. The 2009 Series A and B Bonds carry interest rates that vary monthly based on a factor of LIBOR. The effective interest rate was 1.70 percent and 1.43 percent at December 31, 2016 and 2015, respectively. The final maturity of the bonds is January 1, 2029. Both series are subject to put agreements for which both have a bank put option date of January 2, 2021, which may be extended for additional periods of one year each through the maturity date. The bonds are collateralized by the first mortgages on the Marjorie P. Lee and Deupree House, assignments of basic rents and gross revenues and the assets of the Foundation.

In connection with the Series A and B 2009 Bond issuances, ERH entered into four interest rate swap agreements with banks in order to mitigate economic risks associated with fluctuation in interest rates for a portion of its variable rate debt (see Note 6).

At December 31, the aggregate maturities of long-term debt during the next five years and thereafter are as follows:

| | |
|---|---|
| 2017 | $ 1,280,000 |
| 2018 | 1,336,000 |
| 2019 | 1,400,000 |
| 2020 | 1,472,000 |
| 2021 | 1,544,000 |
| Thereafter | 15,468,000 |
| | $ 22,500,000 |

## Note 6. Derivative Financial Instrument

The Obligated Group is exposed to certain risks in the normal course of its business operations. The Obligated Group manages risks relating to the variability of future cash flows through the use of derivatives. The only derivative instruments used by the Obligated Group are interest rate swaps. Interest rate swaps are used by the Obligated Group to manage the risk associated with interest rates on variable-rate borrowings and do not qualify for hedge accounting. All interest rate swaps are reported in the combined statement of financial position at fair value and all gains and losses recognized on interest rate swaps are included in excess of revenue over (under) expenses.

As of December 31, 2016 and 2015, the Obligated Group held four "receive variable/pay fixed" interest rate swaps for a total notional amount of $22,470,000 and $23,678,000, respectively. Three of the swaps require the Obligated Group to pay between 2.433 and 3.365 percent on $21,900,000 and $23,100,000, at December 31, 2016 and 2015, respectively, and receive 65 percent of LIBOR through January 1, 2020, the expiration date of these three swap agreements. The fourth swap requires the Obligated Group to pays 3.130 percent on $570,000 and $578,000 at December 31, 2016 and 2015, respectively, and receives 65 percent of LIBOR through October 1, 2029, the expiration date of this swap agreement. The Obligated Group has recorded the fair value of these interest rate swap agreements, which resulted in a liability of $2,382,503 and $2,817,345 at December 31, 2016 and 2015, respectively.

**Note 6. Derivative Financial Instrument (Continued)**

For the years ended December 31, 2016 and 2015, the amounts of loss recognized in the combined statement of activities attributable to derivative instruments not designated as hedging instruments and their locations in the combined statement of activities are as follows:

| | 2016 | |
|---|---|---|
| | Amount of Income (Loss) Recognized | Reported in Combined Statement of Activities |
| Net settlements of interest rate swaps | $ (573,496) | Interest expense |
| Change in fair value of interest rate swap agreement | 434,842 | Change in swap |
| **Net loss** | $ (138,654) | |

| | 2015 | |
|---|---|---|
| | Amount of Income (Loss) Recognized | Reported in Combined Statement of Activities |
| Net settlements of interest rate swaps | $ (673,990) | Interest expense |
| Change in fair value of interest rate swap agreement | 94,564 | Change in swap |
| **Net loss** | $ (579,426) | |

**Note 7. Net Assets**

Unrestricted net assets include internally designated net assets of $23,911,366 and $23,989,735 at December 31, 2016 and 2015, respectively. The remaining unrestricted net assets are undesignated as of December 31, 2016 and 2015.

Temporarily restricted net assets consist of charitable remainder trusts of $28,454 and $33,235 at December 31, 2016 and 2015, respectively, with the remaining net assets consisting of gifts restricted for capital expenditures. The charitable remainder trusts are temporarily restricted due to a time restriction.

Permanently restricted net assets (net asset balances outlined below) are restricted to investments in perpetuity, the income from which is expendable for the following purposes:

| | 2016 | 2015 |
|---|---|---|
| Marjorie P. Lee Fund operations | $ 22,466,197 | $ 22,289,014 |
| Other | 1,133,706 | 1,112,867 |
| **Total** | $ 23,599,903 | $ 23,401,881 |

## Note 8. Donor-Restricted and Board-Designated Endowments

The Obligated Group's endowment includes both donor-restricted and board-designated endowment funds. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

The Obligated Group has interpreted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Obligated Group classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment and (c) 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.

Donor-restricted endowment funds totaled $23,599,903 and $23,401,881 at December 31, 2016 and 2015. Changes in the donor-restricted endowment net assets are detailed in the combined statement of changes in net assets.

Changes in board-designated endowment funds for the years ended December 31 are as follows:

| | 2016 | 2015 |
|---|---|---|
| Endowments, January 1, | $ 24,899,693 | $ 25,505,772 |
| Interest income | 163,298 | 300,584 |
| Net unrealized gain | 1,029,491 | 1,268,732 |
| Net realized gain (loss) | 586,897 | (1,817,047) |
| Deposits | 250,000 | 7,598,046 |
| Distributions | (985,893) | (7,956,394) |
| **Endowments, December 31,** | $ 25,943,486 | $ 24,899,693 |

Total endowments include $181,574 and $285,144, which is included in cash and cash equivalents at December 31, 2016 and 2015, respectively.

**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 UPMIFA requires the Obligated Group to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature are to be reported in unrestricted net assets; however, no deficiencies existed at December 31, 2016 and 2015.

**Return objectives and risk parameters:** The Obligated Group has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Obligated Group must hold in perpetuity. The Obligated Group expects its endowment funds, over time, to provide an average rate of return of approximately 8 percent annually. Actual returns in any given year may vary from this amount.

**Strategies employed for achieving objectives:** To satisfy its long-term rate-of- return objectives, the Obligated Group 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 Obligated Group targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

## Note 8. Donor-Restricted and Board-Designated Endowments (Continued)

**Spending policy and how the investment objectives relate to spending policy:** The Obligated Group has a policy of appropriating for distribution approximately 5 percent of the average market value over the previous 12 quarters. In establishing this policy, the Obligated Group considered the long-term expected return on its endowment.

## Note 9. Retirement Plans

ERH sponsors a tax-deferred annuity retirement plan under Section 403(b) of the Internal Revenue Code for all employees who meet certain requirements as to length of service and percentage of employee contributions up to a maximum percentage of annual compensation. Expense for the plan was approximately $324,000 and $295,000 for 2016 and 2015, respectively.

## Note 10. Professional Liability Coverage

ERH maintains a claims-made policy for professional and general liability through Caring Communities, a Reciprocal Risk Retention Group domiciled in the District of Columbia, U.S.A. As a subscriber to Caring Communities, the Obligated Group's interest of approximately $490,000 is recorded as an investment using the cost method and is included in other noncurrent assets on the combined statements of financial position for the years ended December 31, 2016 and 2015.

The Obligated Group is responsible for the first $50,000 per claim and Caring Communities is responsible for amounts over $50,000, up to $1,000,000 per claim and $3,000,000 in the aggregate. Premiums are actuarially determined based on claims history and were approximately $202,000 for the policy years (calendar years) beginning January 1, 2015. Depending on loss history and adequacy of capital, Caring Communities may, but is not obligated to, return a portion of premiums paid. Conversely, the Obligated Group may be called upon to contribute additional funds to its subscriber account to maintain adequate capital in Caring Communities.

## Note 11. Functional Expenses

The Obligated Group provides general healthcare services to residents within its geographic location, including residential care, assisted living and independent living. Expenses related to providing these services for the years ended December 31 are as follows:

| | 2016 | 2015 |
|---|---|---|
| Program services | $ 23,914,328 | $ 23,137,174 |
| General and administrative | 6,523,663 | 5,779,515 |
| Fundraising | 683,761 | 577,835 |
| **Total** | $ 31,121,752 | $ 29,494,524 |

## Note 12. Fair Value Measurements

A summary of the methods and significant assumptions used to estimate the fair values of each major class of financial instruments is as follows:

**Interest rate swaps:** Interest rate swaps are recorded at fair value, based on current market conditions and computations.

**Assets limited as to use:** Assets limited as to use are recorded at fair value in the accompanying combined financial statements. Fair value is determined based on the fair value framework noted below.

The following table present information about the Obligated Group's assets and liabilities measured at fair value on a recurring basis at December 31, 2016 and 2015 and the valuation techniques used by the Obligated Group to determine those fair values.

In general, fair values determined by Level 1 inputs use quoted prices in active markets for identical assets or liabilities that the Obligated Group has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets and liabilities in active markets and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset or liability.

In instances whereby inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Obligated Group's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset or liability.

Assets and liabilities measured at fair value on a recurring basis at December 31:

| | 2016 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Assets: | | | | |
| Assets limited as to use: | | | | |
| Cash and cash equivalents | $ 1,736,283 | $ - | $ - | $ 1,736,283 |
| Corporation obligations | - | 50,370 | - | 50,370 |
| Equity securities | 6,315,975 | - | - | 6,315,975 |
| Money market funds | - | 95,460 | - | 95,460 |
| Mutual funds | 9,838,394 | - | - | 9,838,394 |
| **Total assets limited as to use** | 17,890,652 | 145,830 | - | 18,036,481 |
| Beneficial interest in Marjorie P. Lee | | | | |
| Endowment Fund | - | - | 21,167,524 | 21,167,524 |
| **Total assets measured at fair value** | 17,890,652 | 145,830 | 21,167,524 | 39,204,005 |
| Assets limited as to use measured at net asset value: | | | | |
| Commingled trust funds | - | - | - | 5,494,149 |
| Hedge funds | - | - | - | 3,949,967 |
| **Total assets measured at net asset value** | - | - | - | 9,444,116 |
| **Total assets** | $ 17,890,652 | $ 145,830 | $ 21,167,524 | $ 48,648,121 |
| Liabilities: | | | | |
| Interest rate swaps | $ - | $ 2,382,503 | $ - | $ 2,382,503 |

## Note 12. Fair Value Measurements (Continued)

| | 2015 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Assets: | | | | |
| Assets limited as to use: | | | | |
| Cash and cash equivalents | $ 3,204,853 | $ - | $ - | $ 3,204,853 |
| Corporation obligations | - | 20,167 | - | 20,167 |
| Equity securities | 6,072,888 | - | - | 6,072,888 |
| Money market funds | - | 655,794 | - | 655,794 |
| Mutual funds | 8,940,129 | - | - | 8,940,129 |
| **Total assets limited as to use** | 18,217,870 | 675,961 | - | 18,893,831 |
| Beneficial interest in Marjorie P. Lee Endowment Fund | - | - | 20,955,167 | 20,955,167 |
| **Total assets measured at fair value** | 18,217,870 | 675,961 | 20,955,167 | 39,848,998 |
| Assets limited as to use measured at net asset value: | | | | |
| Commingled trust funds | - | - | - | 4,735,466 |
| Hedge funds | - | - | - | 4,196,728 |
| **Total assets measured at net asset value** | - | - | - | 8,932,194 |
| **Total assets** | $ 18,217,870 | $ 675,961 | $ 20,955,167 | $ 48,781,192 |
| Liabilities: | | | | |
| Interest rate swaps | $ - | $ 2,817,345 | $ - | $ 2,817,345 |

Changes in Level 3 assets measured at fair value on a recurring basis for the years ended December 31:

| | Beneficial Interest in Marjorie P. Lee Endowment Fund |
|---|---|
| Balance, January 1, 2015 | $ 22,185,844 |
| Contributions | - |
| Withdrawals | (928,628) |
| Net unrealized losses included in change in net assets | (1,444,729) |
| Net realized gains | 782,944 |
| Interest income, net of fees | 359,736 |
| Balance, December 31, 2015 | 20,955,167 |
| Contributions | 94,622 |
| Withdrawals | (59,495) |
| Net unrealized losses included in change in net assets | 177,230 |
| **Balance, December 31, 2016** | $ 21,167,524 |

Both observable and unobservable inputs may be used to determine the fair value of positions classified as Level 3 assets and liabilities. As a result, the unrealized gains and losses for these assets and liabilities presented in the tables above may include changes in fair value that were attributable to both observable and unobservable inputs.

The Obligated Group's policy is to recognize transfers in and transfers out of Level 1, 2 and 3 fair value classifications as of the end of the reporting period. There were no transfers between levels for the years ended December 31, 2016 and 2015.

## Note 12. Fair Value Measurements (Continued)

**Investments in entities that calculate net asset value per share:** The Obligated Group holds shares or interests in investment companies at year end, whereby the fair value of the investment held is estimated based on the net asset value per share (or its equivalent) of the investment company.

Unfunded commitments and redemption rules of those investments at December 31 are as follows:

| | Fair Value | | | | Unfunded | Redemption Frequency, if | Redemption |
|---|---|---|---|---|---|---|---|
| | 2016 | | 2015 | | Commitments | Eligible | Notice Period |
| Commingled trust funds | $ | 5,494,149 | $ | 4,735,466 | N/A | Monthly | Five days |
| Hedge funds: | | | | | | | |
| Silvercreek | | 951,032 | | 1,238,881 | N/A | [a] | [a] |
| Mercer | | 2,043,178 | | 2,010,281 | N/A | [b] | [b] |
| Archstone | | 955,757 | | 947,566 | N/A | Quarterly | Ninety days |

[a] Redemption is scheduled based on the continuation fund over the next three years at the fund's determination. There are no redemption rights.

[b] The underlying liquidity of the fund changes over time and the redemption schedule is dependent upon, among other things, the liquidity provisions of the underlying funds, which allow for restrictions on redemption timing in certain circumstances. Further, the fund invests in illiquid investments. As such, it may take several years to receive all proceeds. During the redemption process, a stockholder remains at investment risk for those portfolios' funds for which redemption proceeds have not yet been received.

The commingled trust funds are invested in individual small- to large-cap equity securities in various industries to provide diversified risk. The values of the investments in this class have been estimated using the net asset value per share of the investments.

The hedge funds category invests in hedge funds that pursue multiple strategies to diversify risk and reduce volatility. The values of the investments in this class have been estimated using the net asset value per share of the investments. The fair value of the beneficial interest in the Marjorie P. Lee Foundation is based on the underlying fair value of the investments held directly by the Marjorie P. Lee Foundation.

## Note 13. Related Party Transactions

The Obligated Group provides certain management services to the other affiliated entities. During 2016 and 2015, ERH recognized net management fee income of $1,957,072 and $1,065,964, respectively, for management services provided to the other affiliated entities. During 2016, ERH transferred $1,200,000 of cash to ERS to provide funds for ERS to invest in a new affiliated entity.

The Foundation also provides support to ERH and the other affiliated entities. Transfers of unrestricted net assets to the other affiliated entities totaled $793,634 and $115,263 for the years ended December 31, 2016 and 2015, respectively. Net assets released from restriction and transferred to other affiliated entities totaled $37,897 and $21,701 for the years ended December 31, 2016 and 2015, respectively.

Amounts due from affiliated entities totaled $1,122,692 and $1,338,238 at December 31, 2016 and 2015, respectively. During 2015, the Obligated Group forgave certain amounts due from the other affiliated entities totaling $10,175,240, respectively. There was no forgiveness of amounts due from affiliated entities in 2016.

# Supplementary Information

**Episcopal Retirement Homes - Obligated Group**

**Combining Statement of Financial Position**
**December 31, 2016**

| | Episcopal Retirement Homes, Inc. | Episcopal Retirement Services Foundation | **Total** |
|---|---|---|---|
| **Assets** | | | |
| Current assets: | | | |
| Cash and cash equivalents | $ 2,364,175 | $ 1,096,490 | **$ 3,460,665** |
| Resident accounts receivable, net | 843,411 | - | **843,411** |
| Other receivables | 474,995 | 525,914 | **1,000,909** |
| Assets limited as to use | 523,988 | - | **523,988** |
| Other current assets | 289,831 | - | **289,831** |
| **Total current assets** | 4,496,400 | 1,622,404 | **6,118,804** |
| Assets limited as to use | 1,194,697 | 25,761,912 | **26,956,609** |
| Property and equipment, net | 50,890,661 | - | **50,890,661** |
| Beneficial interest in Marjorie P. Lee Endowment Fund | - | 21,167,524 | **21,167,524** |
| Intangible assets | 870,241 | - | **870,241** |
| Due from affiliates | 1,772,432 | - | **1,772,432** |
| Other | 1,182,557 | 28,454 | **1,211,011** |
| **Total assets** | $ 60,406,988 | $ 48,580,294 | **$ 108,987,282** |
| **Liabilities and Net Assets** | | | |
| Current liabilities: | | | |
| Accounts payable | $ 1,674,959 | $ - | **$ 1,674,959** |
| Current portion of long-term debt | 1,280,000 | - | **1,280,000** |
| Deposits from residents | 388,061 | - | **388,061** |
| Refundable entrance fees | 1,409,000 | - | **1,409,000** |
| Deferred revenue from entrance fees | 435,000 | - | **435,000** |
| Accrued liabilities and other | 2,801,739 | 33,735 | **2,835,474** |
| **Total current liabilities** | 7,988,759 | 33,735 | **8,022,494** |
| Long-term debt, net of current portion | 21,220,000 | - | **21,220,000** |
| Deferred revenue from entrance fees, net of current portion | 1,374,633 | - | **1,374,633** |
| Refundable entrance fees, net of current portion | 13,725,400 | - | **13,725,400** |
| Interest rate swaps | 2,382,503 | - | **2,382,503** |
| Due to affiliates | - | 649,740 | **649,740** |
| Other long-term liabilities | 502,361 | 262,088 | **764,449** |
| **Total liabilities** | 47,193,656 | 945,563 | **48,139,219** |
| Net assets: | | | |
| Unrestricted | 13,213,332 | 23,045,419 | **36,258,751** |
| Temporarily restricted | - | 989,409 | **989,409** |
| Permanently restricted | - | 23,599,903 | **23,599,903** |
| **Total net assets** | 13,213,332 | 47,634,731 | **60,848,063** |
| **Total liabilities and net assets** | $ 60,406,988 | $ 48,580,294 | **$ 108,987,282** |

**Episcopal Retirement Homes - Obligated Group**

**Combining Statement of Financial Position**
**December 31, 2015**

| | Episcopal Retirement Homes, Inc. | Episcopal Retirement Services Foundation | Total |
|---|---|---|---|
| **Assets** | | | |
| Current assets: | | | |
| Cash and cash equivalents | $ 2,511,546 | $ 2,125,380 | $ 4,636,926 |
| Resident accounts receivable, net | 1,204,729 | - | 1,204,729 |
| Other receivables | 429,236 | 168,561 | 597,797 |
| Note receivable | 1,914,430 | - | 1,914,430 |
| Assets limited as to use | 835,904 | - | 835,904 |
| Other current assets | 315,797 | - | 315,797 |
| **Total current assets** | 7,211,642 | 2,293,941 | 9,505,583 |
| Assets limited as to use | 2,375,573 | 24,614,548 | 26,990,121 |
| Property and equipment, net | 50,612,285 | - | 50,612,285 |
| Beneficial interest in Marjorie P. Lee Endowment Fund | - | 20,955,167 | 20,955,167 |
| Intangible assets | 309,200 | - | 309,200 |
| Due from affiliates | 809,687 | 528,551 | 1,338,238 |
| Other | 1,256,129 | 33,236 | 1,289,365 |
| **Total assets** | $ 62,574,516 | $ 48,425,443 | $ 110,999,959 |
| **Liabilities and Net Assets** | | | |
| Current liabilities: | | | |
| Accounts payable | $ 1,311,806 | $ - | $ 1,311,806 |
| Current portion of long-term debt | 1,208,000 | - | 1,208,000 |
| Deposits from residents | 380,524 | - | 380,524 |
| Refundable entrance fees | 1,010,000 | - | 1,010,000 |
| Deferred revenue from entrance fees | 375,000 | - | 375,000 |
| Accrued liabilities and other | 2,820,458 | 55,132 | 2,875,590 |
| **Total current liabilities** | 7,105,788 | 55,132 | 7,160,920 |
| Long-term debt, net of current portion | 22,842,000 | - | 22,842,000 |
| Deferred revenue from entrance fees, net of current portion | 1,713,902 | - | 1,713,902 |
| Refundable entrance fees, net of current portion | 14,399,500 | - | 14,399,500 |
| Interest rate swaps | 2,817,345 | - | 2,817,345 |
| Other long-term liabilities | 570,250 | 287,313 | 857,563 |
| **Total liabilities** | 49,448,785 | 342,445 | 49,791,230 |
| Net assets: | | | |
| Unrestricted | 13,125,731 | 23,928,200 | 37,053,931 |
| Temporarily restricted | - | 752,917 | 752,917 |
| Permanently restricted | - | 23,401,881 | 23,401,881 |
| **Total net assets** | 13,125,731 | 48,082,998 | 61,208,729 |
| **Total liabilities and net assets** | $ 62,574,516 | $ 48,425,443 | $ 110,999,959 |

**Episcopal Retirement Homes - Obligated Group**

**Combining Statement of Activities**
**Year Ended December 31, 2016**

| | Episcopal Retirement Homes, Inc. | Episcopal Retirement Services Foundation | **Total** |
|---|---|---|---|
| Revenue: | | | |
| Net resident revenue | $ 23,316,730 | $ - | **$ 23,316,730** |
| Other operating revenue | 1,755,684 | - | **1,755,684** |
| Management fee income | 1,957,072 | - | **1,957,072** |
| Amortization of entrance fees | 429,568 | - | **429,568** |
| Marjorie P. Lee endowment income | 969,320 | - | **969,320** |
| Interest and dividend income | 109,779 | 163,298 | **273,077** |
| **Total revenue** | 28,538,153 | 163,298 | **28,701,451** |
| Expenses: | | | |
| Salaries and wages | 13,338,364 | - | **13,338,364** |
| Employee benefits and payroll taxes | 3,651,897 | - | **3,651,897** |
| Supplies | 924,662 | - | **924,662** |
| Food | 1,383,320 | - | **1,383,320** |
| Professional services | 1,585,520 | - | **1,585,520** |
| Utilities | 1,285,587 | - | **1,285,587** |
| Insurance | 406,876 | - | **406,876** |
| Depreciation and amortization | 3,446,572 | - | **3,446,572** |
| Interest | 918,068 | - | **918,068** |
| Other operating expense | 4,027,440 | 153,446 | **4,180,886** |
| **Total expenses** | 30,968,306 | 153,446 | **31,121,752** |
| **Operating (loss) income** | (2,430,153) | 9,852 | **(2,420,301)** |
| Nonoperating income (loss): | | | |
| Contributions | - | 860,280 | **860,280** |
| Investment gain | - | 1,616,388 | **1,616,388** |
| Change in interest rate swaps | 434,842 | - | **434,842** |
| Other income (loss) | 3,583 | (9,990) | **(6,407)** |
| **Total nonoperating income** | 438,425 | 2,466,678 | **2,905,103** |
| **Excess of revenue (under) over expenses** | $ (1,991,728) | $ 2,476,530 | **$ 484,802** |

**Episcopal Retirement Homes - Obligated Group**

**Combining Statement of Activities**
**Year Ended December 31, 2015**

| | Episcopal Retirement Homes, Inc. | Episcopal Retirement Services Foundation | Total |
|---|---|---|---|
| Revenue: | | | |
| Net resident revenue | $ 23,523,326 | $ - | $ 23,523,326 |
| Other operating revenue | 1,560,717 | - | 1,560,717 |
| Management fee income | 1,065,964 | - | 1,065,964 |
| Amortization of entrance fees | 371,775 | - | 371,775 |
| Marjorie P. Lee endowment income | 958,116 | - | 958,116 |
| Interest and dividend income | 136,612 | 199,134 | 335,746 |
| **Total revenue** | 27,616,510 | 199,134 | 27,815,644 |
| Expenses: | | | |
| Salaries and wages | 12,222,337 | - | 12,222,337 |
| Employee benefits and payroll taxes | 3,309,260 | - | 3,309,260 |
| Supplies | 1,000,571 | - | 1,000,571 |
| Food | 1,376,827 | - | 1,376,827 |
| Professional services | 1,708,331 | - | 1,708,331 |
| Utilities | 1,323,078 | - | 1,323,078 |
| Insurance | 375,761 | - | 375,761 |
| Depreciation and amortization | 3,356,463 | - | 3,356,463 |
| Interest | 950,627 | - | 950,627 |
| Other operating expense | 3,684,641 | 186,628 | 3,871,269 |
| **Total expenses** | 29,307,896 | 186,628 | 29,494,524 |
| **Operating (loss) income** | (1,691,386) | 12,506 | (1,678,880) |
| Nonoperating income (loss): | | | |
| Contributions | - | 996,680 | 996,680 |
| Investment loss | - | (510,197) | (510,197) |
| Change in interest rate swaps | 94,564 | - | 94,564 |
| Other income (loss) | 657 | (24,973) | (24,316) |
| **Total nonoperating income** | 95,221 | 461,510 | 556,731 |
| **Excess of revenue (under) over expenses** | $ (1,596,165) | $ 474,016 | $ (1,122,149) |