DIAKON
AND CONTROLLED AFFILIATES

Consolidated Financial Statements and Schedules

December 31, 2017 and 2016

(With Independent Auditor's Report Thereon)

Arnett Carbis Toothman llp
CPAs & Advisors

DIAKON
AND CONTROLLED AFFILIATES

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Diakon and Controlled Affiliates
Middletown, Pennsylvania

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Diakon and Controlled Affiliates, which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated 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 audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Diakon and Controlled Affiliates as of December 31, 2017 and 2016, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information is presented for purposes of additional analysis rather than to present the financial position, results of operations and cash flows of the individual companies and is not a required part of the consolidated 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 consolidated financial statements. The consolidating information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Arnett Carbis Toothman LLP

New Castle, Pennsylvania
April 18, 2018

DIAKON
AND CONTROLLED AFFILIATES
Consolidated Balance Sheets
December 31, 2017 and 2016

Assets		**2017**	**2016**
Current assets:			
Cash and cash equivalents	$	4,520,783	4,043,657
Assets limited as to use		9,608,001	9,472,075
Accounts receivable (net of allowance for doubtful accounts of $3,041,000 and $3,098,000 in 2017 and 2016, respectively):			
Patients and residents		13,199,921	13,960,937
Statewide Adoption and Permanency Network		4,419,590	4,343,065
Other client services		2,565,094	2,938,956
Estimated third-party payor settlements		2,085,005	2,023,628
Prepaid expenses and other assets		2,452,991	3,831,416
Total current assets		38,851,385	40,613,734
Investments		133,066,932	58,005,785
Assets limited as to use, less current portion:			
Statutory minimum liquid reserves		7,122,163	7,205,935
Other		27,789,706	86,178,931
Investment in joint venture		958,537	596,409
Land, buildings and equipment, net		230,192,579	228,535,656
Other assets:			
Receivables from charitable gift annuities		1,233,426	1,233,426
Funds held in trust by others and beneficial interest in trust		37,685,817	34,556,795
Other assets		4,773,238	5,191,850
Total assets	$	481,673,783	462,118,521

(Continued)

DIAKON
AND CONTROLLED AFFILIATES
Consolidated Balance Sheets
December 31, 2017 and 2016

Liabilities and Net Assets		**2017**	**2016**
Current liabilities:			
Line of credit	$	1,529,382	987,238
Accounts payable and accrued expenses		19,392,465	20,654,712
Deposits – patients and residents		661,963	625,281
Estimated third-party payor settlements		1,016,430	993,609
Current maturities of long-term debt		6,668,715	6,632,277
Total current liabilities		29,268,955	29,893,117
Pension liability		34,582,892	33,650,712
Deferred revenue – entrance agreements		64,785,819	62,515,189
Refundable entrance fee liability		33,223,116	33,938,813
Other long-term liabilities		1,380,915	2,383,733
Long-term debt, less current maturities and debt issuance costs		240,315,098	247,291,528
Total liabilities		403,556,795	409,673,092
Net assets:			
Unrestricted		15,175,566	(10,569,367)
Temporarily restricted		14,155,465	12,632,857
Permanently restricted		48,785,957	50,381,939
Total net assets		78,116,988	52,445,429
Total liabilities and net assets	$	481,673,783	462,118,521

See accompanying notes to consolidated financial statements.

DIAKON
AND CONTROLLED AFFILIATES

Consolidated Statements of Operations and Changes in Net Assets

Years ended December 31, 2017 and 2016

		2017	2016
Operating revenues, gains and other support:			
Patient and resident service revenue, net of contractual allowances	$	142,818,176	141,393,245
Patient and resident service revenue, nursing home assessment		3,868,169	3,866,533
Amortization of entrance fees		9,935,291	11,104,452
Contract revenue		12,202,254	10,824,383
Other fees and services		11,207,774	12,174,687
Statewide Adoption and Permanency Network revenue		62,008,007	57,918,104
Investment income, net of expenses		7,315,778	5,240,982
Income from trusts		1,617,440	1,501,690
Contributions and bequests		824,986	2,941,467
Net assets released from restrictions – operations		1,638,403	1,451,531
Gain on disposal of assets		3,502,725	20,476
Total operating revenues, gains and other support		256,939,003	248,437,550
Expenses:			
Salaries and wages		67,728,628	66,829,858
Employee benefits		13,533,697	14,369,071
Other expenses		75,535,431	73,569,367
Other expenses – Statewide Adoption and Permanency Network		60,338,942	57,013,588
Nursing home assessment		2,060,071	2,029,793
Interest		9,815,765	10,540,290
Depreciation and amortization		17,778,621	17,637,904
Total expenses		246,791,155	241,989,871
Operating income		10,147,848	6,447,679
Decrease in fair value of swap agreement		—	(969,810)
Equity in gains of joint venture		362,128	415,502
Loss from early extinguishment of debt		—	(420,807)
Excess of operating revenues, gains and other support over expenses		10,509,976	5,472,564
Other changes:			
Pension-related changes other than net periodic pension costs		(971,950)	(52,497)
Unrealized gains on investments		8,910,261	1,087,336
Net assets released from restrictions – capital		9,072	104,277
Equity transfer		7,287,574	—
Total other changes		15,234,957	1,139,116
Increase in unrestricted net assets		25,744,933	6,611,680

(Continued)

DIAKON
AND CONTROLLED AFFILIATES
Consolidated Statements of Operations and Changes in Net Assets
Years ended December 31, 2017 and 2016

		2017	**2016**
Temporarily restricted net assets:			
Contributions and bequests	$	624,674	1,193,911
Investment gains, net of expenses		2,165,874	1,517,035
Unrealized gains on investments		2,704,800	83,071
Net assets released from restrictions – operations		(1,638,403)	(1,451,531)
Net assets released from restrictions – capital		(9,072)	(104,277)
Change in beneficial interest in trust		186,209	—
Equity transfer		(2,511,474)	—
Increase in temporarily restricted net assets		1,522,608	1,238,209
Permanently restricted net assets:			
Contributions and bequests		237,305	488,353
Increase in fair value of funds held in trust by others		2,942,813	354,086
Equity transfer		(4,776,100)	—
(Decrease) increase in permanently restricted net assets		(1,595,982)	842,439
Increase in net assets		25,671,559	8,692,328
Net assets, beginning of year		52,445,429	43,753,101
Net assets, end of year	$	78,116,988	52,445,429

See accompanying notes to consolidated financial statements.

DIAKON
AND CONTROLLED AFFILIATES

Consolidated Statements of Cash Flows

Years ended December 31, 2017 and 2016

	2017	2016
Cash flows from operating activities:		
Increase in net assets	$ 25,671,559	8,692,328
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Net realized gains on investments	(2,726,884)	(1,121,597)
Net unrealized gains on investments	(11,615,061)	(1,170,407)
Depreciation and amortization	17,778,621	17,637,904
Amortization of debt issuance costs	169,914	175,341
Increase (decrease) in pension liability	932,180	(76,780)
Amortization of entrance fees	(9,935,291)	(11,104,452)
Proceeds from entrance fees	14,017,103	15,936,674
Change in funds held in trust by others and beneficial interest in trust	(3,129,022)	(354,086)
Decrease in fair value of swap agreement	—	969,810
Equity in gains of joint venture	(362,128)	(415,502)
Loss on early extinguishment of debt	—	420,807
Gain on disposal of assets	(3,502,725)	(20,476)
Provision for bad debts	2,426,987	2,043,177
Restricted contributions and investment income	(1,389,450)	(1,747,768)
Change in assets and liabilities:		
Accounts receivable	(1,407,190)	17,878,157
Prepaid expenses and other current assets	1,378,425	(1,918,365)
Other assets	418,612	—
Accounts payable, accrued expenses, and other liabilities	(3,074,716)	(15,363,421)
Deposits – patients and residents	36,682	(23,825)
Net cash provided by operating activities	25,687,616	30,437,519
Cash flows from investing activities:		
Purchase of investments and assets limited as to use	(26,726,029)	(30,160,547)
Proceeds from sales of investments and assets limited as to use	24,343,898	18,229,024
Purchase of property and equipment	(21,323,167)	(13,277,776)
Proceeds from sale of property and equipment	6,200,000	—
Net cash used in investing activities	(17,505,298)	(25,209,299)
Cash flows from financing activities:		
Payment of long-term debt	(10,868,924)	(34,748,122)
Retirement of swap agreement	—	(9,748,000)
Proceeds from debt issuance	3,842,181	42,223,300
Net proceeds (payment) on lines of credit	542,144	(1,736,632)
Payment of debt issuance costs	(83,164)	(895,183)
Proceeds from restricted contributions and investment income	1,389,450	1,747,768
Proceeds from entrance fees	2,937,275	2,182,094
Refunds of entrance fees	(5,464,154)	(5,198,363)
Net cash used in financing activities	(7,705,192)	(6,173,138)
Net increase (decrease) in cash and cash equivalents	477,126	(944,918)
Cash and cash equivalents, beginning of year	4,043,657	4,988,575
Cash and cash equivalents, end of year	$ 4,520,783	4,043,657
Supplemental schedule of noncash investing activity:		
Noncash purchases of property and equipment	$ 810,000	529,000

See accompanying notes to consolidated financial statements.

(1) Summary of Significant Accounting Policies

(a) Organization

Diakon is a private, nonprofit charitable organization recognized by the Internal Revenue Service as a 501(c)(3) corporation and exempt from federal income taxation under the group exemption of the Evangelical Lutheran Church in America (ELCA). Diakon is the sole member of Diakon Lutheran Social Ministries (DLSM), Diakon Lutheran Fund (DLF), Diakon Lutheran Senior Living-Maryland LLC (DLSL-MD), Diakon Child, Family and Community Ministries (DCFCM), Diakon Medical Group LLC (DMG), and Diakon Home Care Services LLC (DHCS). DLSM is the sole member of Diakon-SWAN LLC (SWAN LLC) and is related to four U.S. Department of Housing and Urban Development (HUD) senior housing projects by appointment of the boards of Diakon Lutheran Senior Housing at Heilman House and Diakon Lutheran Senior Housing at Luther Meadows, and by acting as sole member of Diakon Lutherwood Senior Housing LLC and Diakon Frostburg Senior Housing, LLC (DFSH), a sole purpose entity formed in 2016 which assumed the assets and liabilities of the Frostburg Heights project, which previously operated as a division of DLSM. DCFCM is the sole member of Old Main LLC (Old Main). Diakon is affiliated with ELCA through Lutheran Services in America (LSA), the membership alliance of Lutheran social ministry organizations and church bodies. Diakon has a relationship with the following participating synods: Delaware-Maryland, Lower Susquehanna, Northeastern Pennsylvania, Southeastern Pennsylvania, and Upper Susquehanna. Through a cooperative agreement, it also serves in the Allegheny Synod (collectively, the Synods). In accordance with Diakon's bylaws, the bishops of the Synods elect the majority of Diakon's board of directors. The bishops of the Synods also elect the majority of DLSM's and DCFCM's board of directors. The board of Diakon, in its role as sole member, appoints the board for DLF.

(b) Description of Controlled Affiliates

DLSM is a Pennsylvania nonprofit corporation recognized as a charitable organization under Section 501(c)(3) of the Internal Revenue Code and exempt from federal income taxation under the group exemption of the ELCA. DLSM provides senior living and health services in Pennsylvania.

DLSL-MD, a Maryland Limited Liability Company, began operations on January 1, 2012, and is the operating entity for the retirement living community in Maryland. DLSL-MD is a disregarded entity of Diakon for federal tax purposes.

DCFCM, a 501(c)(3) corporation, began operations on July 1, 2014, and operates various programs serving children, communities, and families.

DHCS, a Pennsylvania Limited Liability Company, was previously the operating entity for home and community based hospice and home care services in Pennsylvania. Operations were discontinued in July 2012. DHCS is a disregarded entity of Diakon for federal tax purposes.

DLF, a 501(c)(3) corporation, is authorized by its charter to provide management of DLSM's and DCFCM's investments and solicit contributions for the charitable organizations that it supports.

In the absence of donor restrictions, DLF has discretionary control over the amounts, timing, and use of its distributions to the charitable organizations that it supports. Certain of its funds are restricted to children, youth, community, and family programs.

SWAN LLC, a Pennsylvania Limited Liability Company, began operations on October 1, 2015, and provides an array of administrative and support services for the Pennsylvania Statewide Adoption and Permanency Network, a program overseen and funded by the Pennsylvania Department of Human Services. SWAN LLC is a disregarded entity of DLSM for federal tax purposes.

DMG, a Pennsylvania Limited Liability Company, began operations on January 1, 2017. DMG provides medical director and physician services to the Diakon senior living communities. DMG is a disregarded entity of Diakon for federal tax purposes.

Old Main, a Pennsylvania Limited Liability Company, was created in 2017 to be the borrower and operator of the Old Main Building project at the Lutheran Home at Topton campus. Old Main is a disregarded entity of DCFCM for federal tax purposes.

(c) Basis of Consolidation

The accompanying consolidated financial statements have been prepared to focus on Diakon and all controlled affiliated organizations (collectively, the Corporation) as a whole. All material intercompany transactions have been eliminated in consolidation.

(d) Basis of Accounting

The accompanying consolidated financial statements have been prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles and present balances and transactions according to the existence or absence of donor-imposed restrictions.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has lapsed) are reported as net assets released from restrictions on the consolidated statements of operations and changes in net assets.

There are three classes of net assets – permanently restricted, temporarily restricted, and unrestricted.

> *Permanently restricted net assets* are net assets subject to donor-imposed stipulations that are required to be maintained permanently by the Corporation. Generally, the donors of these assets permit the institution to use all or part of the income earned on related investments for general or specific purposes. Permanently restricted net assets consist principally of funds held in trust by others.

Temporarily restricted net assets are net assets subject to donor-imposed stipulations that may or will be met by actions of the Corporation and/or the passage of time.

Unrestricted net assets are net assets not subject to donor-imposed stipulations.

(e) Cash and Cash Equivalents

Cash and cash equivalents include interest-bearing instruments with an original maturity of three months or less from the date of purchase, excluding amounts classified as assets limited as to use.

The Corporation has exposure to credit risk related to cash on deposit at financial institutions in excess of FDIC insured limits. As of December 31, 2017, the amount held in excess of the FDIC insured limits at financial institutions was approximately $4,435,000.

(f) Accounts Receivable

Accounts receivable from patients, residents, and clients are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, the Corporation analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payor sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts. Additionally, for receivables associated with self-pay patients the Corporation routinely reviews the provision for bad debts for delinquent accounts and adjusts reserves as appropriate for such accounts where there is a reasonable likelihood the resident is unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

(g) Investments and Investment Income

Investments are measured at fair value on the consolidated balance sheets.

Certain investments and assets limited as to use are maintained in investment pools (pooled funds). To equitably allocate investment income, including gains and losses, each participating fund is assigned a number of units using the market value method.

Investment income and gains and losses on the sale of investments are added to or deducted from the appropriate net asset classification depending on the existence of donor-imposed restrictions.

A decline in market value of any investment below its cost basis that is deemed to be other-than-temporary results in a reduction in carrying amount to the fair value. The impairment is recognized as a loss and a new cost basis for the investment is established. No such losses were recognized in 2017 or 2016.

(h) Assets Limited as to Use

Assets limited as to use include assets set aside by the board of directors for future capital improvements and other designated purposes, over which the board retains control and may, at its discretion, use for other purposes; assets held by trustees under mortgage agreements with agencies of the U.S. government; assets held by trustees under bond indentures; and donor and other restricted funds. Investment income and gains and losses on assets limited as to use are included in investment income.

(i) Investment in Joint Venture

Investment in joint venture represents an investment in a less than 50% owned information technology joint venture. The Corporation accounts for the equity interest it has in a for-profit joint venture where it has significant influence under the equity method of accounting.

Changes in the venture's equity have been reflected on the consolidated statements of operations and changes in net assets as equity in gains (losses) of joint venture and classified consistent with the characteristics of the joint venture's activities.

In December 2016 the joint venture entered into an agreement with the Corporation to convert additional paid in capital of $350,000 to debt in the form of a note receivable to be paid over ten years. As of December 31, 2016, the note receivable is included in other assets on the consolidated balance sheet. The note receivable was paid in full in December 2017.

(j) Land, Buildings, and Equipment

Land, buildings, and equipment are recorded at cost. The cost of maintenance and repairs is expensed as incurred, whereas significant renewals and betterments are capitalized. Depreciation is calculated on the straight-line method over the estimated useful lives of the depreciable assets.

Depreciable lives are determined as follows:

Land improvements	10 to 25 years
Buildings	10 to 40 years
Furniture and equipment	3 to 20 years
Vehicles	4 to 7 years
Leasehold improvements	Lesser of lease term or life of the asset

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and 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, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

(Continued)

Interest cost incurred on borrowed funds less interest income earned on these funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

(k) Impairment of Long-Lived Assets

Long-lived assets, such as property and equipment, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset.

If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented on the consolidated balance sheets and reported at the lower of the carrying amount or fair value less costs to sell, and would no longer be depreciated.

The assets and liabilities of a disposal group classified as held-for-sale would be presented separately in the appropriate asset and liability sections of the consolidated balance sheets. No impairment was recognized in 2017 or 2016.

(l) Deferred Debt Issuance Costs and Other Assets

Debt issuance costs are amortized over the period the obligation is outstanding. Amortization expense was $169,914 and $175,341 in 2017 and 2016, respectively. Debt issuance costs incurred and subject to amortization totaled approximately $4,600,000 and $4,500,000 as of December 31, 2017 and 2016, respectively. Accumulated amortization as of December 31, 2017 and 2016, totaled $933,233 and $763,319, respectively.

Other noncurrent assets include goodwill of approximately $4,600,000 related to the acquisition of a continuing care retirement community within the senior living services line of service. Goodwill is analyzed at least annually by management to assess whether it is more likely than not that the senior living services reporting unit goodwill is impaired based upon qualitative factors. The Corporation did not recognize an impairment loss on goodwill for the years ended December 31, 2017 or 2016.

(m) Receivables from Charitable Gift Annuities

Independent trustees maintain charitable gift annuities for which the Corporation has been named beneficiary of the corpus and will receive these funds upon the death of the annuitant.

(n) Funds Held in Trust by Others and Beneficial Interest in Trust

DLSM, or its predecessor entities, and DLF (the beneficiaries) have been named as the beneficiaries of a number of trusts that are administered and controlled by independent trustees. The trusts are recorded as contribution revenue when the beneficiaries are notified of the trust's existence. The beneficiaries receive the earnings from these trusts whose principal is to be held in perpetuity. The earnings from the trusts are recorded as investment income.

Funds held in trust by others and the beneficial interest in trust are valued at the fair value of the underlying investments. The change in the fair value of funds held in trust by others is reported as a change in permanently restricted net assets and the change in the fair value of the beneficial interest in trust is reported as a change in temporarily restricted net assets. Lifecare residents at one community requiring financial assistance have been named as the beneficiaries of a trust administered and controlled by independent trustees.

(o) Self Insurance

Accounts payable and accrued expenses and other long-term liabilities include a provision for estimated self-insured workers' compensation and health insurance claims for both reported claims not yet paid and claims incurred but not reported.

(p) Deposits – Patients and Residents

Deposits – patients and residents represents security deposits paid in advance to cover possible costs when patients and residents vacate their apartments or personal care units.

These deposits are taken into income only if earned upon the termination of a residency agreement. Deposits – patients and residents also includes nursing home patients' funds held in safekeeping by the Corporation for the patients' personal use.

(q) Pension Benefits

The Corporation has a noncontributory defined benefit pension plan covering certain employees upon their retirement. The benefits are based on years of service and the employee's compensation. On August 17, 2011, DLSM (the plan sponsor) amended the pension plan to freeze benefit accruals, effective December 31, 2011, and to freeze participation with respect to new participants, effective January 2, 2012.

The Corporation records annual amounts relating to its pension plan based on calculations that incorporate various actuarial and other assumptions, including discount rates, mortality, assumed rates of return, compensation increases, and turnover rates. The Corporation reviews its assumptions on an annual basis and makes modifications to the assumptions based on current rates and trends when it is appropriate to do so. The effect of modifications to those assumptions is recorded as an other change in unrestricted net assets on the consolidated statements of operations and changes in net assets. These amounts are amortized to net periodic cost over future periods using the corridor method. The Corporation believes that the assumptions utilized in recording its obligations under its plan are reasonable based on its experience and market conditions.

The net periodic costs are recognized as employees render the services necessary to earn the pension benefits. The funded status of the plan is reported in the pension liability caption on the consolidated balance sheets. The Corporation is required to recognize the funded status of defined benefit pension and other postretirement plans as a net asset or liability and to recognize changes in that funded status in the year in which the changes occur through other changes in unrestricted net assets on the consolidated statements of operations and changes in net assets to the extent those changes are not included in the net periodic cost.

(r) Derivative Instruments

The Corporation entered into an interest rate swap agreement to limit its exposure to interest rate changes on its variable rate revenue bonds. Hedge accounting has not been elected; therefore, variations in fair value are marked-to-market and reported within its performance indicator on the consolidated statements of operations and changes in net assets. In June 2016, the Corporation terminated the swap agreement (Note 8).

(s) Entrance Agreement Contracts

Entrance fees paid by residents of the Corporation's independent living units, including certain cottages and apartments, are recorded as deferred revenue. A resident, upon termination of occupancy, is entitled to receive a refund of a portion of the entrance fee pursuant to the terms of the contract, which is required to be paid only upon the subsequent receipt of an entrance fee from a new resident for that independent living unit. These entrance fee agreements guarantee occupancy rights to residents for life. In certain contracts related to two of the Corporation's facilities, there are lifetime health care services.

The nonrefundable portion of entrance fees as stated in each contract is recorded as deferred revenue and amortized to revenue over the estimated life expectancy of each resident. The component of entrance fees which is guaranteed refundable per the terms of a contract is recorded as refundable entrance fee liability.

A refund payment can be triggered on the portion of a contract that is non-refundable, as the contracts contain provisions whereby the nonrefundable portion of the entrance fee is earned by the respective community over a future time period following the date of initial occupancy, generally 46 months or less. Nonetheless, all nonrefundable portions of the entrance fee are recorded as deferred revenue and amortized to revenue over the estimated life of the resident. Such entrance fees are amortized to income, as the Corporation does not have a reasonably objective basis to identify in advance which contracts are likely to trigger refunds.

The amount of entrance fees, which is refundable to residents as of December 31, 2017 and 2016, under contractual refund provisions, was approximately $56,140,000 and $58,116,000, respectively. Proceeds and refunds of refundable entrance fees are classified as financing activities on the consolidated statements of cash flows.

The Corporation may receive entrance fee payments prior to the date an independent living resident occupies a living unit. Such entrance fee deposits received during 2017 and 2016 amounted to $680,535 and $650,795, respectively, and are included in refundable entrance fee liability on the accompanying consolidated balance sheets. The Corporation maintains a separate entrance fee escrow account, which is a component of cash and cash equivalents. The amount in the entrance fee escrow account covers deposit liabilities to prospective independent living residents. Such amounts in the entrance fee escrow account totaled $843,392 and $751,416 as of December 31, 2017 and 2016, respectively.

(t) Conditional Asset Retirements

The Corporation has evaluated its facilities to determine if it has a liability for the fair value of a conditional asset retirement obligation. The types of asset retirement obligations evaluated are those for which an entity has a legal obligation to perform an asset retirement activity; however, the timing and (or) method of settling the obligation is conditional on a future event that may or may not be within the control of the Corporation. No material conditional asset retirement obligations have been identified by the Corporation as of December 31, 2017 or 2016.

(u) Obligation to Provide Future Services to Continuing Care Residents

The Corporation annually calculates the present value of the net cost of future services using a discount rate of 5% and compares that amount with the balance of deferred revenue from entrance fees. If the present value of the net cost of future services and the use of facilities exceeds the deferred revenue from entrance fees, a liability would be recorded (obligation to provide future services and use of facilities) with the corresponding charge to income. Periodically, the Corporation engages an actuary to perform the present value calculation, which it did in 2016. As a result of the calculation, and additional analysis performed in 2017, the present value of the net cost of future services did not exceed deferred revenue; accordingly, no obligation was recorded as of December 31, 2017 or 2016.

(v) Income Taxes

Diakon and its controlled affiliates are not-for-profit corporations as described in Section 501(c)(3) of the Internal Revenue Code (Code) and have been recognized as tax exempt under 501(a) of the Code.

The Corporation uses a threshold of more likely than not for recognition and derecognition of tax positions taken or expected to be taken in a tax return. The Corporation does not believe that there are any unrecognized tax benefits or liabilities that should be recorded. Generally, tax returns for years ended December 31, 2014, and thereafter remain subject to examination by federal and state taxing authorities.

(w) Patient and Resident Service Revenue

Patient and resident service revenue is reported at the estimated net realizable amount to be received from patients, residents, and others including Medicare, Medicaid, and other third-party payors for services rendered.

Skilled nursing facilities derive a significant portion of their revenues from federal and state reimbursement programs. These reimbursements are subject to audit and periodic adjustment.

Services provided to Medicare beneficiaries are paid under terms of a prospective payment system at predetermined rates based on clinical, diagnostic, and other factors. Services provided to Medicaid beneficiaries are paid at prospectively determined rates per day.

(Continued)

These rates vary according to a resident classification system that is based on clinical diagnostic and other factors, and the reimbursement methodology is subject to various limitations and adjustments. The Corporation's current concentration of skilled nursing facilities in Pennsylvania exposes it to the risk of changes in Medicaid reimbursement in this state.

(x) Contributions and Donor Restrictions

Contributions received with donor-imposed restrictions that are met in the same year as received are reported as increases in temporarily restricted net assets, and reclassified to unrestricted net assets as net assets released from restrictions.

Contributions, including unconditional promises to give, if any, are recognized as revenues in the period received. Conditional promises to give are not recognized until they become unconditional, that is when the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value as of the date of contribution. Contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved. An allowance for uncollectable contributions receivable is provided based upon management's judgment including such factors as prior collection history, type of contributions, and nature of fund-raising activity.

(y) Charity Care and Support of Those in Need

The Corporation provides charity care and other support of those in need to many of the programs and individuals that it serves. In addition, DLF provides support of children, youth, and family programs. Support of those in need includes services provided to persons who cannot afford health care because of inadequate resources and/or who are uninsured or underinsured. A number of programs operated by DCFCM do not receive sufficient funding from the sponsoring organizations or from program fees to meet the needs of the people they serve. The Corporation has elected to underwrite the operating deficits of certain programs in order to serve as many of the identified needs as possible.

The Corporation maintains records to identify and monitor the amount of charity care it provides. These records include direct and indirect costs for services and supplies furnished under its charity care policy. The total cost of charity care under these policies amounted to $2,970,117 and $3,175,172 for the years ended December 31, 2017 and 2016, respectively. The cost of charity care is estimated by management based upon the cost to gross charges ratio multiplied by the gross uncompensated charges associated with providing care. The Corporation received $691,000 and $616,000 for the years ended December 31, 2017 and 2016, respectively, to offset or subsidize charity care services provided, which is reported as an offset to amounts shown for children and family ministries.

The following is a summary of the Corporation's support of these programs during the years ended December 31:

		2017	2016
Medical assistance cost in excess of contractual reimbursement	$	13,707,377	14,912,730
Charity care in support of those in need		3,720,738	3,096,666
Children and Family Ministries supported by DLSM and DLF (charity care):			
Children's services		492,715	476,286
Behavioral health		373,468	372,924
Community services		91,267	361,978
Total Children and Family Ministries supported by DLSM and DLF		957,450	1,211,188
Scholarships		61,095	68,624
Total	$	18,446,660	19,289,208

(z) Loss from Early Extinguishment of Debt

During the year ended December 31, 2016, the Corporation entered into a transaction that involved the issuance of the Cumberland County Municipal Revenue Bonds Series 2016 (Note 5). The proceeds from these bonds were used to fully refund the previously outstanding Series 2014 B Bonds, fund a portion of the costs related to termination of the interest rate swap, fund certain capital expenditures at the DLSM facilities, and to pay for issuance costs. This transaction resulted in the recognition of a loss from early extinguishment of debt in the amount of $420,807 which is recorded on the consolidated statement of operations and changes in net assets for the year ended December 31, 2016.

(aa) Operating Income

The consolidated statements of operations and changes in net assets include an intermediate measure of operations labeled "Operating income." Changes that are excluded from this measure include joint venture equity changes, changes in the fair value of swap agreement, and loss from early extinguishment of debt.

(bb) Performance Indicator

The consolidated statements of operations and changes in net assets include a performance indicator of operations labeled "Excess of operating revenues, gains and other support over expenses." Changes in unrestricted net assets that are excluded from this measure include unrealized gains on investments, pension-related changes other than net periodic pension costs, net assets released from restrictions for capital purposes, and a net asset transfer.

(cc) Use of Estimates

The preparation of consolidated financial statements in accordance with U.S. generally accepted accounting principles 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 consolidated financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(dd) Statutory Reserve Requirement

The Pennsylvania Continuing Care Provider Registration and Disclosure Act requires a statutory reserve equivalent to the greater of the total of debt service payments due during the next 12 months on account of any loan or 10% of the projected annual operating expenses of the facilities exclusive of depreciation, computed only on the proportional share of financing or operating expenses that is applicable to residents under entrance fee agreement contracts. This statutory reserve requirement is considered to be fulfilled from equity and fixed income funds included within assets limited as to use. The Pennsylvania statutory reserve as of December 31, 2017 and 2016, was $7,122,163 and $7,205,935, respectively.

The State of Maryland regulation 32.02.01.20 requires licensed continuing care retirement communities to maintain an operating reserve equal to fifteen percent of the facility's net operating expenses for the most recent fiscal year. The regulations allow a provider to meet the requirement at a minimum rate of 10% per year as of the date of its first initial certificate of registration up to a total of 100% as of the end of the tenth fiscal year. DLSL-MD was required to maintain a reserve of 9% of net operating expenses, or $1,416,840, as of December 31, 2017, its sixth year of operation, and 7.5% of net operating expenses, or $1,184,213, as of December 31, 2016, its fifth year of operation. The reserves must be maintained in a reasonably liquid form in the judgment of the provider and in accordance with the provider's investment policies.

(ee) Change in Accounting Principle

On January 1, 2016, the Corporation adopted the provisions of Accounting Standards Update (ASU) 2015-03, Simplifying the Presentation of Debt Issuance Costs. Prior to the adoption, the Corporation's policy was to present debt issuance costs in other assets on the consolidated balance sheets. These costs are now presented as a direct deduction to the related long-term debt on the consolidated balance sheets. Details regarding amortization of these costs are included under Note 1(l) – Deferred Debt Issuance Costs and Other Assets.

(ff) Reclassifications

Certain prior period amounts have been reclassified to conform with the current period consolidated financial statement presentation.

(2) Assets Limited as to Use and Investments

The composition of assets limited as to use as of December 31 is set forth in the following table:

	2017	2016
Under bond indentures for debt service reserve fund:		
Cash and short-term investments	$ 971,501	967,350
Debt Service Sinking Fund:		
Cash and short-term investments	9,608,211	6,655,083
Under bond indentures for construction projects:		
Cash and short-term investments	—	2,640,146
Endowment funds:		
Cash and short-term investments	685,341	907,685
Fixed income funds	3,382,796	3,891,608
Equity funds	8,104,338	12,072,569
Donor and other temporarily restricted funds:		
Cash and short-term investments	834,080	760,995
Equity funds	6,972,343	6,356,675
Fixed income funds	3,227,757	2,347,110
Assets Limited to Use for HUD Reserves:		
Cash and short-term investments	2,817,155	4,312,904
By board for designated purposes:		
Funded depreciation:		
Cash and short-term investments	—	235,356
Equity funds	—	2,195,419
Fixed income funds	—	1,541,592
Entrance fees and other designated purposes:		
Cash and short-term investments	365,537	3,663,173
Equity funds	—	27,551,532
Fixed income funds	428,648	19,551,809
Statutory minimum liquid reserves:		
Equity funds	4,170,560	4,233,342
Fixed income funds	2,951,603	2,972,593
Total assets limited as to use	44,519,870	102,856,941
Less assets limited as to use – required for current liabilities:		
Other	9,608,001	9,472,075
Assets limited as to use, less current portion	$ 34,911,869	93,384,866

A summary of investments as of December 31 is as follows:

		2017	2016
Cash and short-term investments	$	5,641,559	3,467,115
Equity funds		72,101,098	32,266,536
Fixed income funds		51,027,627	17,673,815
Alternative investment		4,296,648	4,598,319
Investments	$	133,066,932	58,005,785

The combined composition of assets limited as to use and investments as of December 31 is as follows:

	2017			2016		
Cash and short-term investments	$	20,923,384	11.8%	$	23,609,807	14.7%
Equity funds		91,348,339	51.4%		84,676,073	52.6%
Fixed income funds		61,018,431	34.4%		47,978,527	29.8%
Alternative investment		4,296,648	2.4%		4,598,319	2.9%
	$	177,586,802	100.0%	$	160,862,726	100.0%

Total investment return for the years ended December 31 consists of the following:

		2017		
		Unrestricted	Temporarily restricted	Total
Interest and dividends, net of expenses	$	5,291,728	1,463,040	6,754,768
Net realized gains on investments		2,024,050	702,834	2,726,884
Investment income, net of expenses		7,315,778	2,165,874	9,481,652
Unrealized gain on investments		8,910,261	—	8,910,261
Changes in unrealized gains on temporarily restricted net assets		—	2,704,800	2,704,800
Total investment return	$	16,226,039	4,870,674	21,096,713

	2016		
	Unrestricted	**Temporarily restricted**	**Total**
Interest and dividends, net of expenses	$ 4,405,935	1,230,485	5,636,420
Net realized gains on investments	835,047	286,550	1,121,597
Investment income, net of expenses	5,240,982	1,517,035	6,758,017
Unrealized gain on investments	1,087,336	—	1,087,336
Changes in unrealized gains on temporarily restricted net assets	—	83,071	83,071
Total investment return	$ 6,328,318	1,600,106	7,928,424

As described in Note 1(g), a summary of unrestricted investments with fair values below cost as of December 31 is as follows:

	Less than 12 months		12 months or longer		Total	
December 31, 2017	**Fair value**	**Unrealized losses**	**Fair value**	**Unrealized losses**	**Fair value**	**Unrealized losses**
Description of funds:						
Fixed income funds	$ —	—	34,933,162	1,060,555	34,933,162	1,060,555
Equity funds	114,400	425	7,904,690	1,164,887	8,019,090	1,165,312
Total temporarily impaired funds	$ 114,400	425	42,837,852	2,225,442	42,952,252	2,225,867

	Less than 12 months		12 months or longer		Total	
December 31, 2016	**Fair value**	**Unrealized losses**	**Fair value**	**Unrealized losses**	**Fair value**	**Unrealized losses**
Description of funds:						
Fixed income funds	$ —	—	14,794,796	390,032	14,794,796	390,032
Equity funds	4,736,921	13,079	19,755,618	2,290,891	24,492,539	2,303,970
Total temporarily impaired funds	$ 4,736,921	13,079	34,550,414	2,680,923	39,287,335	2,694,002

The Corporation monitors its investment portfolio and reviews investments that have experienced a decline in fair value below cost to evaluate whether the decline is other than temporary. Such evaluations consider, among other things, the magnitude and reasons for a decline, the prospects for the fair value to recover in the near term, and the Corporation’s intent and ability to retain the investment for a period of time sufficient to allow for a recovery in value. The declines in fair value as of December 31, 2017 and 2016, are considered temporary.

(3) Third-Party Reimbursement

The Corporation's nursing care facilities and other programs primarily derive their revenues from private-pay, Medicare, and Medicaid patients. Private-pay rates are established on the basis of the cost of delivering services and competitive considerations and, as such, are essentially market driven. In contrast, Medicare and Medicaid payment rates are regulated by the federal and state governments and, as a result, the industry is sensitive to related legislative changes and is affected by reductions in governmental spending for these programs. Additionally, laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by material amounts in the near term.

Revenues from Medicare and Medicaid represent approximately 49% and 47% of patient and resident service revenue, net of contractual allowances, for the years ended December 31, 2017 and 2016, respectively. Medicare and Medicaid receivables represent approximately 50% and 47% of patient and resident accounts receivable as of December 31, 2017 and 2016, respectively.

Pennsylvania nursing providers are subject to a Nursing Home Assessment (the Assessment) which was approved by the Centers for Medicare and Medicaid Services (CMS) in September 2003. The Assessment requires all Pennsylvania nursing homes, except for county homes, to pay a fee to the Department of Human Services (DHS) based upon all non-Medicare days. DHS makes supplemental payments back to nursing home facilities based upon a standard rate per Medicaid day claimed. Total nursing home assessment revenues and expenses were $3,868,169 and $2,060,071 for 2017, respectively, and $3,866,533 and $2,029,793 for 2016, respectively.

(4) Land, Buildings and Equipment

Land, buildings and equipment and accumulated depreciation as of December 31 are as follows:

		2017	2016
Land	$	16,385,689	16,441,933
Land improvements		27,764,753	28,509,912
Buildings		354,655,266	347,939,753
Furniture and equipment		42,783,395	40,780,403
Vehicles		503,009	503,009
		442,092,112	434,175,010
Accumulated depreciation		(222,276,148)	(208,983,537)
		219,815,964	225,191,473
Construction in progress		10,376,615	3,344,183
	$	230,192,579	228,535,656

Depreciation expense for the years ended December 31, 2017 and 2016, was $17,778,621 and $17,618,747, respectively.

Construction in progress as of December 31, 2017 and 2016, is principally capitalized costs related to the repositioning of the Corporation's Senior Living Service (SLS) campuses.

Non-cash purchases of land, buildings and equipment totaled approximately $810,000 and $529,000 for the years ended December 31, 2017 and 2016, respectively.

(5) Long-Term Debt

The Corporation has established an obligated group (the Obligated Group) comprised of the assets/liabilities and activities of the DLSM corporate entity, excluding the following assets/liabilities and activities: Frostburg Heights Apartments affordable housing community and the Medical Arts Building in Allentown, Pennsylvania. Additionally, the Obligated Group excludes the activities of the following legal entities, of which DLSM is the sole member: Diakon – SWAN LLC and the four HUD entities outlined in Note 1 (a).

Long-term debt of the Corporation consists of the following as of December 31:

	2017	2016
Cumberland County Municipal Authority Bonds Series 2016, $34,780,000 of tax exempt fixed interest rate bonds with principal payable in annual installments ranging from $640,000 to $4,430,000 through 2039. Interest rates range from 2.5% to 5.0% and the bonds were issues at an aggregate premium of $4,003,300, which is being amortized ratably over the life of the issue, to yield an effective interest rate of 3.14%.	$ 32,765,000	$ 34,780,000
Cumberland County Municipal Authority Bonds Series 2015, $147,545,000 of tax-exempt fixed interest rate bonds with principal payable in annual installments ranging from $2,465,000 to $12,855,000 through 2038. Interest rates range from 3.0% to 5.0% and the bonds were issued at an aggregate premium of $8,559,916, which is being amortized ratably over the life of the issue, to yield an effective interest rate of 4.25%.	142,410,000	145,080,000
Cumberland County Municipal Authority Bonds Series A 2014, $22,728,000 of tax-exempt variable interest rate bonds with principal payable in monthly installments ranging from $35,000 to $136,000 through 2039. The Series A 2014 are direct placement notes with PNC Bank with an interest rate of 1.45% as of December 31, 2017.	20,937,000	21,473,000
Washington County, Maryland Bonds Series C 2014, $18,798,000 of tax-exempt variable interest rate bonds with principal payable in monthly installments ranging from $43,000 to $131,000 through 2033. The Series C 2014 are direct placement notes with PNC Bank with an interest rate of 1.45% as of December 31, 2017.	16,449,000	17,153,000

	2017	2016
Cumberland County Municipal Authority Bonds Series 2009, $123,210,000 of tax-exempt fixed interest rate bonds with post refunding principal payable in annual installments ranging from $60,000 to $1,365,000 through 2039. Interest rates post refunding range from 6.175% to 6.375%.	9,180,000	9,420,000
Mortgage notes payable, U.S. Department of Housing and Urban Development (HUD) and Wells Fargo, four individual notes collateralized by the property and equipment of the HUD Senior Housing properties. The notes bear interest at fixed rates ranging from 3.07% to 4.22% and monthly payments, including interest, ranging from $12,144 to $30,274 through 2051.	14,083,537	14,328,843
Maxatawny Township Municipal Authority, Revenue Note Series 2017, with a maximum principal amount of $6,100,000. The mortage note is collateralized by rental proceeds of Old Main, LLC. The note bears interest at a floating rate of 2.0% plus sixty-seven percent (67%) of 30-day LIBOR. Monthly payments are interest only through March 2019. Effective April 1, 2019, monthly interest and principal installments are payable. Final maturity of the note is March 1, 2044.	3,842,181	-
Mortgage note payable, JP Morgan Chase Corporation, $4,500,000 nonrecourse mortgage note payable collateralized solely by the property and rental proceeds of DLSM's Medical Arts Building. Per the terms of an amendment executed November 15, 2016, the note bears interest at a floating interest rate of 30-day LIBOR plus 2.50%.	-	3,666,834
	239,666,718	245,901,677
Less current maturities of bonds and mortgages payable	(6,668,715)	(6,632,277)
Unamortized debt issuance costs	(3,684,850)	(3,771,484)
Unamortized premium	11,001,945	11,793,612
	$ 240,315,098	$ 247,291,528

(Continued)

All of the outstanding bonds described herein are obligations of the Obligated Group. On June 29, 2016, the Cumberland County (PA) Municipal Authority issued $34,780,000 of Series 2016 revenue bonds, the proceeds of which the Obligated Group utilized to fully refund the previously outstanding Series B 2014 Bonds, fund certain capital projects at Obligated Group facilities, and to fund a portion of the costs associated with terminating the swap.

The outstanding bonds have been issued pursuant to the terms of a 1998 Master Trust Indenture, as amended and supplemented over time. The effect of these amendments was to consolidate the entities comprising the Obligated Group and to grant all bondholders and credit providers equal standing. The master trust indenture contains certain provisions that require the Obligated Group to maintain certain cash deposits with a trustee as well as meet certain financial covenants on an annual basis. The master trust indenture also places various restrictions on the Obligated Group's ability to incur additional indebtedness. The cash deposits held with the trustee are included in assets limited as to use on the consolidated balance sheets.

To secure the required loan payments for the outstanding bonds, the Obligated Group has granted the Cumberland County Municipal Authority and the County Commissioners of Washington County, MD (the Washington issuer) (issuer of the Series C 2014 bonds) a parity security interest in their gross receipts and a parity first lien mortgage on substantially all of the Obligated Group's property and equipment, with the exception of the property leased to DLSL-MD.

The Obligated Group is also subject to certain financial and other restrictive covenants through a Loan and Agency Agreement with the conduit issuers of the outstanding bonds.

A mortgage note totaling $3,440,000 was issued on December 28, 2016, for Diakon Frostburg Senior Housing, LLC, the proceeds of which were utilized to fully repay the outstanding balance of the loan for the Frostburg Heights affordable housing property, to fund certain building renovations and improvements at Frostburg, to fund certain reserves required by the U.S. Department of Housing and Urban Development, and to pay costs of debt issuance.

A mortgage note with a maximum principal amount of $6,100,000 was issued on March 23, 2017, for Old Main, LLC, the proceeds of which were utilized to undertake a substantial renovation of a portion of the Old Main building located on the campus of the Lutheran Home at Topton. Proceeds were drawn as project expenditures were incurred, with draws on the note totaling $3,842,181 as of December 31, 2017. Final completion of the renovation project occurred approximately January 31, 2018. Old Main, LLC executed lease arrangements with DLSM and DCFCM, which will occupy space in the renovated building, and such lease payments serve as collateral for the loan obligation.

(Continued)

The following is a summary of scheduled annual maturities of long-term debt as of December 31, 2017:

		Scheduled maturity
2018	$	6,668,715
2019		7,067,252
2020		7,399,357
2021		7,722,469
2022		8,080,026
Thereafter		202,728,899
	$	239,666,718

The amount of cash paid for interest (including the net cost of the interest rate swap agreement and letter of credit support fees) was $10,527,968 and $10,956,713 for the years ended December 31, 2017 and 2016, respectively. There was no capitalized interest in 2017 or 2016.

The effective interest rates paid for the years ended December 31 are as follows:

	2017	2016
DLSM Obligated Group	3.89%	4.17%
Obligations outside of the Obligated Group	3.73	4.40
Combined	3.88	4.18

(6) Lines of Credit

DLSM has a line of credit with Manufacturers and Traders Trust Company (M&T) with maximum allowable borrowings of $20,000,000, which is payable on demand. The line of credit bears interest at 30-day LIBOR plus 2.75% (4.31% as of December 31, 2017). Amounts ranging from $0 to $4,880,948 were outstanding for various periods during 2017 and 2016. Borrowings outstanding under the line of credit totaled $0 as of December 31, 2017 and 2016. The bank line of credit is secured on a parity basis with the Obligated Group’s outstanding bonds. In addition to the line of credit, DLSM had unused outstanding letters of credit with M&T in the amount of $3,516,347 and $4,130,318 as of December 31, 2017 and 2016, respectively.

In 2014, DCFCM entered into a line of credit with Manufacturers and Traders Trust Company (M&T) with maximum allowable borrowings of $3,000,000, which is payable on demand. The line of credit bears interest at 30-day LIBOR plus 2.35% (3.91% as of December 31, 2017). Amounts ranging from $0 to $2,723,870 were outstanding for various periods during 2017 and 2016. Borrowings outstanding under the line of credit totaled $1,529,382 and $987,238 as of December 31, 2017 and 2016, respectively. The bank line of credit is secured by DCFCM’s accounts receivable and a $1,000,000 guarantee by DLF’s investments.

(7) Fair Value

(a) Financial Instruments

The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Those fair value measurements maximize the use of observable inputs. However, in situations where there is little, if any, market activity for the asset or liability at the measurement date, the fair value measurement reflects the Corporation's own judgments about the assumptions that market participants would use in pricing the asset or liability. Those judgments are developed by the Corporation based on the best information available in the circumstances.

The following methods and assumptions were used to estimate the fair value of each class of financial instrument:

Cash and cash equivalents, accounts receivable, estimated third-party payor settlements, prepaid expenses and other assets, accounts payable and accrued expenses, deposits, and lines of credit – The carrying amounts, at face value or cost plus accrued interest, approximate fair value because of the short maturity of these instruments.

Investments and assets limited as to use – These assets are carried at fair value, which is based primarily on quoted market prices at the reporting date. When quoted market prices in active markets are not available, the Corporation relies on a pricing service to estimate fair value. The fair value of mutual fund holdings is based on the net asset value as reported by the fund.

Alternative investments – Alternative investments are recorded under the equity method of accounting using net asset value (NAV). The NAV of alternative investments is based on valuations provided by the administrators of the specific financial instrument. The underlying investments in these financial instruments may include marketable debt and equity securities, commodities, foreign currencies, derivatives, and private equity investments. The underlying investments themselves are subject to various risks, including market, credit, liquidity, and foreign exchange risk. The Corporation believes the NAV is a reasonable estimate of its ownership interest in the alternative investments. The Corporation's risk of alternative investments is limited to its carrying value. Alternative investments can be divested only at specific times in accordance with terms of the subscription agreements. The financial statements of all of the Corporation's alternative investments are audited annually.

Funds held in trust by others and beneficial interest in trust – These assets are carried at fair value, which is based on quoted market prices for the underlying securities held by the trusts multiplied by the Corporation's percentage interest in the trusts. The inputs to fair value of these trusts are classified as Level 3 based upon the Corporation's inability to redeem its investment at the net asset value. The activity for the Level 3 classified input from December 31, 2016, to December 31, 2017, is the increase in the fair value of the underlying assets.

(Continued)

Long-term debt (including mortgages and bonds payable) – The fair value of mortgages and fixed rate bonds payable is determined by discounting future cash flows of each instrument at rates that reflect, among other things, market interest rates and the Corporation's credit standing which are deemed to be Level 2 inputs. The carrying amounts of variable rate bonds payable included in long-term debt on the consolidated balance sheets for bonds payable approximate fair value.

The fair value of the Corporation's long-term debt was $299,459,662 and $262,599,665 as of December 31, 2017 and 2016, respectively.

(b) Fair Value Hierarchy

The Corporation determines fair value measurements using the fair value hierarchy, which prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

Level 1 Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Corporation has the ability to access.

Level 2 Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

The following tables present assets and liabilities that are measured at fair value on a recurring basis as of December 31:

	Fair value measurements as of December 31, 2017			
	Quoted prices in active markets for identical assets (Level 1)	**Significant other observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**	**Total**
Assets:				
Investments and assets limited as to use:				
Cash and short-term investments	$ 20,923,384	—	—	20,923,384
Fixed income funds:				
Short term	16,272,840	—	—	16,272,840
Intermediate term	44,745,591	—	—	44,745,591
Equity funds:				
International	40,098,120	—	—	40,098,120
Large cap	44,254,709	—	—	44,254,709
Small cap	6,995,510	—	—	6,995,510
Funds valued at NAV				
Master Limited				4,224,488
Other				72,160
Funds held in trust by others and beneficial interest in trust	—	—	37,685,817	37,685,817
Total	$ 173,290,154	—	37,685,817	215,272,619

	Fair value measurements as of December 31, 2016			
	Quoted prices in active markets for identical assets (Level 1)	**Significant other observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**	**Total**
Assets:				
Investments and assets limited as to use:				
Cash and short-term investments	$ 23,609,807	—	—	23,609,807
Fixed income funds:				
Short term	14,148,997	—	—	14,148,997
Intermediate term	33,829,530	—	—	33,829,530
Equity funds:				
International	34,324,575	—	—	34,324,575
Large cap	43,330,661	—	—	43,330,661
Small cap	7,020,837	—	—	7,020,837
Funds valued at NAV				
Master Limited				4,517,643
Other				80,676
Funds held in trust by others and beneficial interest in trust	—	—	34,556,795	34,556,795
Total	$ 156,264,407	—	34,556,795	195,419,521

Alternative investments measured at net asset value were excluded from the fair value hierarchy as of December 31, 2017 and 2016, as required by ASU 2015-07 *Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent).*

(Continued)

	Investments measured at fair value based on net asset value (NAVs) per share as of December 31, 2017			
	Fair Value	**Unfunded Commitments**	**Redemption Frequency (if currently eligible)**	**Redemption Notice Period**
Master Limited	$ 4,224,488	—	Daily	1 Day
Other	72,160	—	Daily	1 Day
Total	$ 4,296,648	—		

	Investments measured at fair value based on net asset value (NAVs) per share as of December 31, 2016			
	Fair Value	**Unfunded Commitments**	**Redemption Frequency (if currently eligible)**	**Redemption Notice Period**
Master Limited	$ 4,517,643	—	Daily	1 Day
Other	80,676	—	Daily	1 Day
Total	$ 4,598,319	—		

(8) Derivative Instruments

The Obligated Group had a prior interest rate swap agreement with Wells Fargo Bank, subsequently amended in 2014 to a novation transaction with Wells Fargo Bank and PNC Bank in order to manage interest rate risk associated with $71,341,000 variable rate bonds (the issue amount of the Series 2014 variable rate bonds). On June 29, 2016, the Obligated Group terminated the swap by paying Wells Fargo $6,224,434 and PNC Bank $3,523,566.

(9) Pension Benefits

The Corporation has a noncontributory defined benefit pension plan covering certain employees upon their retirement. On August 17, 2011, the Corporation amended the pension plan to freeze benefit accruals, effective December 31, 2011, and to freeze participation with respect to new participants, effective January 2, 2012. The benefits are based on years of service and the employee's compensation. The measurement date used for the defined benefit plan is December 31.

Actuarial gains and losses are generally amortized subject to a corridor, over the average remaining life of the Corporation's active employees.

The following table sets forth the pension benefit obligation, fair value of plan assets, and funded status as of December 31:

	Pension benefits	
	2017	**2016**
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 96,576,856	96,421,017
Interest cost	3,692,141	3,847,443
Change in assumptions	5,071,928	705,241
Actuarial (gain) loss	553,853	(58,754)
Benefit payments	(4,551,099)	(4,338,091)
Benefit obligation at end of year	101,343,679	96,576,856
Change in plan assets:		
Fair value of plan assets at beginning of year	62,926,144	62,693,525
Actual return on plan assets, net of expenses	8,385,742	4,570,710
Benefit payments	(4,551,099)	(4,338,091)
Fair value of plan assets at end of year	66,760,787	62,926,144
Funded status	$ (34,582,892)	(33,650,712)

Amounts recognized on the consolidated balance sheets as of December 31 consist of:

	2017	**2016**
Noncurrent liabilities	$ 34,582,892	33,650,712
Unrestricted net assets	(38,366,785)	(37,394,835)
Net amount recognized	$ (3,783,893)	(3,744,123)

Amounts recognized in unrestricted net assets but not yet included in net periodic benefit costs consist of:

	2017	**2016**
Net actuarial loss	$ (38,366,785)	(37,394,835)
	$ (38,366,785)	(37,394,835)

Other changes in plan assets and benefit obligations recognized directly in unrestricted net assets for the years ended December 31 are as follows:

		2017	2016
Net estimated gain (loss)	$	(971,950)	(52,497)
Total recognized in unrestricted net assets	$	(971,950)	(52,497)

The net loss for the defined benefit pension plan that will be amortized from unrestricted net assets into net periodic benefit cost over the next fiscal year is $1,129,297.

The following table summarizes the components of net periodic benefit cost (benefit) recognized for the years ended December 31:

		2017	2016
Interest cost	$	3,692,141	3,847,443
Expected return on plan assets		(4,817,888)	(4,964,135)
Amortization of net loss		1,085,986	987,406
Net periodic benefit cost (benefit)	$	(39,761)	(129,286)

		2017	2016
Benefit cost (benefit)	$	(39,761)	(129,286)
Benefits paid		4,551,099	4,338,091

Weighted average assumptions used to determine benefit obligations as of December 31 were as follows:

	2017	2016
Discount rate	3.43%	3.91%

Weighted average assumptions used to determine net periodic benefit cost for the years ended December 31 were as follows:

	2017	2016
Discount rate	3.91%	4.10%
Expected long-term rate of return on plan assets	8.00	8.25

(Continued)

The expected long-term rate of return is based on the expected sum of the returns on individual asset categories.

The Corporation's investment policies and strategies for the pension benefit plan use target allocations for the individual asset categories. The Corporation's investment goals are to generate returns that are sufficient to meet the plan's obligations while preserving capital. As part of this investment strategy, as of December 31, 2017 and 2016, the Corporation has invested approximately 22% of the pension plan assets into alternative investments, including a special situations master feeder fund (6%), a core property real estate fund (12%), and an energy debt fund (4%). The Corporation's risk management policies permit investments in mutual funds. The Corporation addresses diversification by the use of private mutual fund investments whose underlying investments are in domestic and international fixed income securities and domestic and international equity securities. These mutual funds are only available to institutional investors and are not traded on a public exchange; however, they can be sold to fund benefit payment obligations as they become payable without restriction.

The Corporation determines the fair value of the mutual funds based on quoted prices from the fund managers as of December 31. While these funds are not traded in active markets, there are no lock-ups or restrictions on redemptions related to mutual funds or the hedge fund of funds. The December 31 unit values reported by the fund managers approximate the exit price of the security.

The Corporation determines the fair value of alternative investments under the equity method of accounting using net asset value (NAV). The NAV of alternative investments is based on valuations provided by the administrators of the specific financial instrument. The underlying investments in these financial instruments may include marketable debt and equity securities, commodities, foreign currencies, derivatives, and private equity investments. The underlying investments themselves are subject to various risks, including market, credit, liquidity, and foreign exchange risk. The Corporation believes the NAV is a reasonable estimate of its ownership interest in the alternative investments. The Corporation's risk of alternative investments is limited to its carrying value. Alternative investments can be divested only at specific times in accordance with terms of the subscription agreements. The financial statements of all of the Corporation's alternative investments are audited annually.

The fair value of the Corporation’s plan assets as of December 31 by asset category are as follows:

	Fair value measurements as of December 31, 2017			
	Total	**Quoted prices in active markets for identical assets (Level 1)**	**Significant observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**
Asset category:				
Cash and short-term investments:				
SEI daily income prime obligation fund	$ 202	202	—	—
Equity funds:				
Large cap disciplined	12,177,867	—	12,177,867	—
Small/mid cap	4,757,511	—	4,757,511	—
World Equity Ex-U.S.	12,625,055	—	12,625,055	—
Dynamic asset allocation	5,254,605	—	5,254,605	—
Emerging markets equity fund	1,607,278	—	1,607,278	—
Fixed income funds:				
High yield bond fund	2,562,879	—	2,562,879	—
Limited duration bond fund	2,545,763	—	2,545,763	—
Emerging markets debt fund	2,608,472	—	2,608,472	—
Core fixed income fund	5,624,839	—	5,624,839	—
Opportunistic income fund	2,566,246	—	2,566,246	—
Plan assets valued at NAV				
Core property collective investment trust	8,256,869			
Special situations collective fund	3,904,848			
Energy debt fund	2,268,353			
Total	$ 66,760,787	202	52,330,515	—

	Fair value measurements as of December 31, 2016			
	Total	**Quoted prices in active markets for identical assets (Level 1)**	**Significant observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**
Asset category:				
Cash and short-term investments:				
SEI daily income prime obligation fund	$ 949	949	—	—
Equity funds:				
Large cap disciplined	13,147,223	—	13,147,223	—
Small/mid cap	5,328,845	—	5,328,845	—
World Equity Ex-U.S.	8,119,779	—	8,119,779	—
Dynamic asset allocation	5,125,201	—	5,125,201	—
Emerging markets equity fund	1,842,009	—	1,842,009	—
Fixed income funds:				
High yield bond fund	1,466,673	—	1,466,673	—
Limited duration bond fund	2,863,400	—	2,863,400	—
Emerging markets debt fund	1,824,112	—	1,824,112	—
Core fixed income fund	6,576,759	—	6,576,759	—
Opportunistic income fund	2,889,465	—	2,889,465	—
Plan assets valued at NAV				
Core property collective investment trust	7,603,180			
Collective fund escrow	365,327			
Special situations collective fund	3,621,975			
Energy debt fund	2,151,247			
Total	$ 62,926,144	949	49,183,466	—

Alternative investments measured at net asset value were excluded from the fair value hierarchy as of December 31, 2017 and 2016, as required by ASU 2015-07, *Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (or Its Equivalent).*

	Plan assets measured at fair value based on net asset value (NAVs) per share as of December 31, 2017			
	Fair Value	**Unfunded Commitments**	**Redemption Frequency (if currently eligible)**	**Redemption Notice Period**
Core property collective investment trust	$ 8,256,869	—	Daily	1 Day
Special situations collective fund	3,904,848	—	Daily	1 Day
Energy debt fund	2,268,353	—	Daily	1 Day
Total	$ 14,430,070	—		

	Plan assets measured at fair value based on net asset value (NAVs) per share as of December 31, 2016			
	Fair Value	**Unfunded Commitments**	**Redemption Frequency (if currently eligible)**	**Redemption Notice Period**
Core property collective investment trust	$ 7,603,180	—	Daily	1 Day
Collective fund excrow	365,327	—	Daily	1 Day
Special situations collective fund	3,621,975	—	Daily	1 Day
Energy debt fund	2,151,247	—	Daily	1 Day
Total	$ 13,741,729	—		

The special situations fund has an initial lock-up period of twenty-four months.

The actual asset allocations of the Corporation's plan assets as of December 31 are as follows and approximate the target allocations:

	2017	**2016**
Asset category:		
Equity funds	54%	53%
Fixed income funds	24	25
Alternative investments	22	22
Total	100%	100%

The Corporation does not expect to make any contributions to its pension plan in 2018.

The estimated benefit payments, which reflect expected future service, as appropriate, are as follows:

2018	$	5,155,662
2019		5,280,161
2020		5,345,617
2021		5,434,616
2022		5,555,770
2023 – 2027		28,158,422

The Corporation also has a defined contribution plan for certain employees. Contributions recognized as expense for this plan were $427,099 and $320,095 for the years ended December 31, 2017 and 2016, respectively.

The Corporation established a Supplemental Executive Retirement Plan (SERP), which was a nonqualified defined benefit plan under which the Corporation paid supplemental retirement benefits to key executives in addition to amounts received under the Corporation's pension plan. Executives received payments of their accrued benefit every five years. These amounts are not included in the determination of net periodic pension cost shown above. The SERP was not funded, and the liability for this plan was $0 and $753,300 as of December 31, 2017 and 2016, respectively. All payments for the SERP have been distributed as of December 31, 2017, and the plan was terminated.

(10) Temporarily Restricted Net Assets

Temporarily restricted net assets as of December 31 carry the following time or purpose restrictions:

		2017	2016
Beneficial interest in charitable remainder trusts and beneficial interest in trust	$	1,768,428	1,582,219
Charitable gift annuities		1,115,283	1,115,283
Capital additions		471,790	493,974
DLF – Support of DCFCM programs		2,615,746	2,245,017
Accumulated gains on endowment and other purposes		8,184,218	7,196,364
Total	$	14,155,465	12,632,857

Temporarily restricted net assets are released from donor restrictions by incurring expenses that satisfy the restrictions specified by donors related principally to specific programs or by the passage of time.

(11) Permanently Restricted Net Assets

Permanently restricted net assets as of December 31 are held in perpetuity, the income from which is expendable for the following purposes:

	2017	2016
Funds held in trust by others – income restricted for:		
Support of programs	$ 26,770,887	24,730,141
Staff and resident programs	163,952	148,665
DLF	8,982,550	8,095,770
Endowment and other purposes	12,374,418	16,894,536
Charitable gift annuities	118,143	118,143
DLF – Support of DCFCM programs	376,007	394,684
	$ 48,785,957	50,381,939

The Corporation's endowment consists of approximately 25 individual funds established for a variety of purposes and consists of only donor-restricted endowment funds. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

The Corporation completed a significant process update over the course of 2017, involving its internal recordkeeping and tracking for the investment portfolio. Part of such effort was also to update the internal tracking and recordkeeping of the endowment component of the investment portfolio. In the course of such activities, Management identified a fund within the DLSM endowment portfolio without external donor designation, and for which the Corporation has not actively solicited new contributions. Additional research and inquiry resulted in Management concluding that such funds, including corpus and earnings, totaling $7,287,574 as of November 30, 2017, were a Board created quasi-endowment without an external restriction. A resolution was passed by the DLSM Board of Directors on November 1, 2017, approving the transfer of such funds from Permanently Restricted and Temporarily Restricted Net Assets to Unrestricted Net Assets.

The Corporation has interpreted the laws of the Commonwealth of Pennsylvania 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 Corporation classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment and the original value of subsequent gifts to the permanent endowment. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Corporation in a manner consistent with the laws of the Commonwealth of Pennsylvania. In accordance with the laws of the Commonwealth of Pennsylvania, the Corporation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

(1) The duration and preservation of the fund

(2) The purposes of the organization and the donor-restricted endowment fund

(3) General economic conditions

(4) The possible effect of inflation and deflation

(5) The expected total return from income and the appreciation of investments

(6) Other resources of the organization

(7) The investment policies of the organization

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 laws of the Commonwealth of Pennsylvania require the Corporation to retain as a fund of perpetual duration. No such deficiencies of this nature are reported in unrestricted net assets as of December 31, 2017 or 2016. The Corporation 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 in relation to inflation trends. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity.

To satisfy its long-term rate-of-return objectives, the Corporation 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 Corporation 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.

(12) Medical Malpractice Claims Coverage and Self Insurance

The Corporation purchases professional liability and umbrella liability coverage through a carrier, on a claims made basis. Management has evaluated claims incurred but not reported. Based on the Corporation’s claims history, management has not recorded a liability for claims incurred but not reported as of December 31, 2017 or 2016. The Corporation believes it has adequate insurance coverage or reserves for all asserted claims and unasserted claims.

The Corporation participates in a self-insured program for its workers’ compensation insurance. In the case of catastrophes or other events that would cause excessive workers’ compensation claims, the Corporation is reinsured for losses in excess of $600,000 per occurrence as of December 31, 2017 and 2016. Workers’ compensation costs are accrued based upon an estimated liability for reported claims and an estimated liability for claims incurred but not reported and approximated $1,990,000 and $2,716,000 as of December 31, 2017 and 2016, respectively, and are reported within accounts payable and accrued expenses and other long-term liabilities captions on the consolidated balance sheets. In addition, the Corporation maintains a $2,500,000 surety bond to secure future obligations under the terms of this self-insured program.

The Corporation's health insurance benefits program changed in January 2015 from a fully insured retrospectively rated cost plan whereby the Corporation's liability was subject to a range of potential exposure with an annual individual claim limitation to a self funded plan with a stop loss contract in place for catastrophic claims. Total health benefit accrued expenses approximated $365,000 and $298,000 as of December 31, 2017 and 2016, respectively, and are reported within the accounts payable and accrued expenses caption on the consolidated balance sheets.

(13) Functional Expenses

Expenses by functional classification for the years ended December 31 are as follows:

	2017	2016
Senior Living Services	$ 149,122,575	147,685,655
Services for Children, Family and Community	16,894,076	16,708,619
Statewide Adoption and Permanency Network	62,008,007	57,918,104
Ministry Support Services and Management	17,338,691	18,034,748
Fundraising	1,427,806	1,642,745
	$ 246,791,155	241,989,871

(14) Commitments and Contingencies

The Corporation has entered into various construction contracts related to campus repositioning activities at certain senior living communities. Contractual commitments as of December 31, 2017 totaled approximately $884,000.

From time to time, the Corporation is involved in claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Corporation's consolidated financial position or results of operations.

(15) Operating Leases

The Corporation has a number of leased facilities to conduct its operations, all of which are classified as operating leases, expiring over the next five years. The Corporation also has a number of leases covering certain equipment and vehicles, which are also classified operating leases.

The future minimum annual lease payments under noncancelable operating leases in effect as of December 31, 2017, which have initial or remaining terms of more than one year, are as follows:

2018	$	1,218,960
2019		1,049,555
2020		741,758
2021		466,293
2022		407,134
	$	3,883,700

Total lease expense was $1,769,949 and $1,801,449 for the years ended December 31, 2017 and 2016, respectively.

(16) Subsequent Events

The Corporation has evaluated subsequent events through April 18, 2018, the date the consolidated financial statements were issued, and determined there were no additional subsequent events requiring disclosure or adjustment to the consolidated financial statements.

DIAKON
AND CONTROLLED AFFILIATES

Schedule of Consolidating Information, Balance Sheet

December 31, 2017

Assets	Diakon Lutheran Social Ministries	Diakon	Diakon Lutheran Fund	Diakon Lutheran Senior Living Maryland LLC	Diakon Child, Family & Community Ministries	Diakon Lutherwood Senior Housing, LLC	Diakon Lutheran Senior Housing at Luther Meadows	Diakon Lutheran Senior Housing at Heilman House	Diakon Frostburg Senior Housing LLC	Statewide Adoption Network (SWAN)	Diakon Medical Group	Old Main LLC	Consolidating entries	Total
Current assets:														
Cash and cash equivalents	$ 1,829,235	270,438	—	668,795	547,506	151,727	87,844	98,913	180,914	679,503	5,908	—	—	4,520,783
Assets limited as to use	9,608,001	—	—	—	—	—	—	—	—	—	—	—	—	9,608,001
Accounts receivable (net of allowance for doubtful accounts):														
Patients and residents	11,888,210	—	—	1,129,451	115,697	—	—	—	—	—	66,563	—	—	13,199,921
Statewide Adoption and Permanency Network	—	—	—	—	—	—	—	—	—	4,419,590	—	—	—	4,419,590
Other client services	626,151	—	—	—	2,545,942	—	—	—	—	—	—	—	(606,999)	2,565,094
Intercompany	(1,175,211)	(18,334)	454,082	(2,667,971)	590,197	(28,343)	(83,201)	(53,360)	(342,931)	—	(447,721)	3,772,793	—	—
Estimated third-party payor settlements	2,074,205	—	—	10,800	—	—	—	—	—	—	—	—	—	2,085,005
Lease receivable current	1,581,397	—	—	—	—	—	—	—	—	—	—	—	(1,581,397)	—
Prepaid expenses and other assets	2,149,599	—	—	170,394	57,298	15,346	6,556	7,236	36,237	10,325	—	—	—	2,452,991
Total current assets	28,581,587	252,104	454,082	(688,531)	3,856,640	138,730	11,199	52,789	(125,780)	5,109,418	(375,250)	3,772,793	(2,188,396)	38,851,385
Investments	109,766,044	1,271,366	18,907,420	3,122,102	—	—	—	—	—	—	—	—	—	133,066,932
Assets limited as to use, less current portion:														
Statutory minimum liquid reserves	7,122,163	—	—	—	—	—	—	—	—	—	—	—	—	7,122,163
Other	18,759,629	—	2,861,947	156,156	3,194,819	787,990	508,045	289,673	1,231,447	—	—	—	—	27,789,706
Investment in joint venture	868,587	89,950	—	—	—	—	—	—	—	—	—	—	—	958,537
Land, buildings and equipment, net	212,276,713	—	—	18,595,438	751,432	2,039,518	539,531	1,050,724	2,613,739	—	—	—	(7,674,516)	230,192,579
Other assets:														
Receivables from charitable gift annuities	1,233,426	—	—	—	—	—	—	—	—	—	—	—	—	1,233,426
Funds held in trust by others and beneficial interest in trust	28,703,267	—	8,982,550	—	—	—	—	—	—	—	—	—	—	37,685,817
Lease receivable long term	10,217,931	—	—	—	—	—	—	—	—	—	—	—	(10,217,931)	—
Other assets	4,773,238	—	—	—	—	—	—	—	—	—	—	—	—	4,773,238
Total assets	$ 422,302,585	1,613,420	31,205,999	21,185,165	7,802,891	2,966,238	1,058,775	1,393,186	3,719,406	5,109,418	(375,250)	3,772,793	(20,080,843)	481,673,783

(Continued)

Schedule 1

DIAKON
AND CONTROLLED AFFILIATES

Schedule of Consolidating Information, Balance Sheet

December 31, 2017

Liabilities and Net Assets (Deficit)	**Diakon Lutheran Social Ministries**	**Diakon**	**Diakon Lutheran Fund**	**Diakon Lutheran Senior Living Maryland LLC**	**Diakon Child, Family & Community Ministries**	**Diakon Lutherwood Senior Housing, LLC**	**Diakon Lutheran Senior Housing at Luther Meadows**	**Diakon Lutheran Senior Housing at Heilman House**	**Diakon Frostburg Senior Housing LLC**	**Statewide Adoption Network (SWAN)**	**Diakon Medical Group**	**Old Main LLC**	**Consolidating entries**	**Total**
Current liabilities:														
Line of credit	$ —	—	—	—	1,529,382	—	—	—	—	—	—	—	—	1,529,382
Accounts payable and accrued expenses	13,822,741	194,673	—	194,996	349,589	62,862	25,050	24,220	216,284	5,109,418	80,015	—	(687,383)	19,392,465
Deposits – patients and residents	537,001	968	—	8,000	—	39,362	17,843	18,524	40,265	—	—	—	—	661,963
Estimated third-party payor settlements	1,016,430	—	—	—	—	—	—	—	—	—	—	—	—	1,016,430
Current obligation under capital lease	—	—	—	430,633	—	—	—	—	—	—	—	—	(430,633)	—
Current maturities of long-term debt	6,409,000	—	—	—	—	116,808	41,252	44,414	57,241	—	—	—	—	6,668,715
Total current liabilities	21,785,172	195,641	—	633,629	1,878,971	219,032	84,145	87,158	313,790	5,109,418	80,015	—	(1,118,016)	29,268,955
Pension liability	34,582,892	—	—	—	—	—	—	—	—	—	—	—	—	34,582,892
Deferred revenue – entrance agreements	60,999,331	—	—	3,786,488	—	—	—	—	—	—	—	—	—	64,785,819
Refundable entrance fee liability	29,179,038	—	—	4,044,078	—	—	—	—	—	—	—	—	—	33,223,116
Other long-term liabilities	1,376,796	—	—	—	—	1,698	664	630	1,127	—	—	—	—	1,380,915
Long-term obligation under capital lease	—	—	—	20,389,197	—	—	—	—	—	—	—	—	(20,389,197)	—
Long-term debt, less current maturities and debt issuance costs	223,746,206	—	—	—	—	5,495,317	1,995,439	2,246,764	3,058,579	—	—	3,772,793	—	240,315,098
Total liabilities	371,669,435	195,641	—	28,853,392	1,878,971	5,716,047	2,080,248	2,334,552	3,373,496	5,109,418	80,015	3,772,793	(21,507,213)	403,556,795
Net assets (deficit):														
Unrestricted	2,580,504	1,417,779	19,231,694	(7,789,483)	3,130,705	(2,749,809)	(1,021,473)	(941,366)	345,910	—	(455,265)	—	1,426,370	15,175,566
Temporarily restricted	10,280,599	—	2,615,747	21,710	1,237,409	—	—	—	—	—	—	—	—	14,155,465
Permanently restricted	37,772,047	—	9,358,558	99,546	1,555,806	—	—	—	—	—	—	—	—	48,785,957
Total net assets (deficit)	50,633,150	1,417,779	31,205,999	(7,668,227)	5,923,920	(2,749,809)	(1,021,473)	(941,366)	345,910	—	(455,265)	—	1,426,370	78,116,988
Total liabilities and net assets (deficit)	$ 422,302,585	1,613,420	31,205,999	21,185,165	7,802,891	2,966,238	1,058,775	1,393,186	3,719,406	5,109,418	(375,250)	3,772,793	(20,080,843)	481,673,783

See accompanying independent auditor's report.

Schedule 2

DIAKON
AND CONTROLLED AFFILIATES

Schedule of Consolidating Information, Statement of Operations and Changes in Net Assets (Deficit)

Period ended December 31, 2017

	Diakon Lutheran Social Ministries	Diakon	Diakon Lutheran Fund	Diakon Lutheran Senior Living Maryland LLC	Diakon Child, Family & Community Ministries	Diakon Lutherwood Senior Housing, LLC	Diakon Lutheran Senior Housing at Luther Meadows	Diakon Lutheran Senior Housing at Heilman House	Diakon Frostburg Senior Housing LLC	Statewide Adoption Network (SWAN)	Diakon Medical Group	Old Main LLC	Consolidating entries	Total
Operating revenues, gains and other support:														
Patient and resident service revenue, net of contractual allowances	$ 127,999,168	—	—	14,735,730	11,302	—	—	—	—	—	71,976	—	—	142,818,176
Patient and resident service revenue, nursing home assessment	3,868,169	—	—	—	—	—	—	—	—	—	—	—	—	3,868,169
Amortization of entrance fees	9,495,277	—	—	440,014	—	—	—	—	—	—	—	—	—	9,935,291
Contract revenue	22,654	—	—	—	10,494,437	760,040	247,402	254,094	423,627	—	—	—	—	12,202,254
Grants from intercompanies	—	—	—	—	1,545,000	—	—	—	—	—	—	31,795	(1,576,795)	—
Other fees and services	7,017,005	182,638	—	57,570	8,181,945	471,298	201,339	224,074	460,481	—	58,900	—	(5,647,476)	11,207,774
Statewide Adoption and Permanency Network revenue	—	—	—	—	—	—	—	—	—	62,008,007	—	—	—	62,008,007
Investment income, net of expenses	6,458,179	42,934	1,666,529	74,394	9,695	467	180	136	168	—	—	—	(936,904)	7,315,778
Income from trusts	1,295,250	—	322,190	—	—	—	—	—	—	—	—	—	—	1,617,440
Contributions and bequests	589,668	—	5,874	2,104	225,783	—	—	211	1,346	—	—	—	—	824,986
Net assets released from restrictions – operations	999,149	—	91,765	1,183	546,306	—	—	—	—	—	—	—	—	1,638,403
Gain on disposal of assets	3,502,725	—	—	—	—	—	—	—	—	—	—	—	—	3,502,725
Total operating revenues, gains and other support	161,247,244	225,572	2,086,358	15,310,995	21,014,468	1,231,805	448,921	478,515	885,622	62,008,007	130,876	31,795	(8,161,175)	256,939,003
Expenses:														
Salaries and wages	52,440,567	—	—	5,108,708	8,538,797	222,008	82,157	90,014	155,663	756,242	334,472	—	—	67,728,628
Employee benefits	10,473,655	—	—	921,009	1,839,985	33,530	17,227	17,057	31,545	173,606	26,083	—	—	13,533,697
Other expenses	62,380,676	182,638	1,306,094	7,766,633	8,879,600	484,084	173,605	161,625	459,954	—	225,586	—	(6,485,064)	75,535,431
Other expenses – Statewide Adoption and Permanency Network	—	—	—	—	—	—	—	—	—	61,078,159	—	—	(739,217)	60,338,942
Nursing home assessment	2,060,071	—	—	—	—	—	—	—	—	—	—	—	—	2,060,071
Interest	9,165,391	—	—	1,171,499	34,185	267,371	95,605	107,652	113,766	—	—	31,795	(1,171,499)	9,815,765
Depreciation and amortization	16,113,067	—	—	774,813	29,061	283,536	83,650	114,070	153,332	—	—	—	227,092	17,778,621
Total expenses	152,633,427	182,638	1,306,094	15,742,662	19,321,628	1,290,529	452,244	490,418	914,260	62,008,007	586,141	31,795	(8,168,688)	246,791,155
Operating income (loss)	8,613,817	42,934	780,264	(431,667)	1,692,840	(58,724)	(3,323)	(11,903)	(28,638)	—	(455,265)	—	7,513	10,147,848
Equity in gains of joint venture and subsidiaries	362,128	—	—	—	—	—	—	—	—	—	—	—	—	362,128
Excess (deficit) of operating revenues, gains and other support over expenses	8,975,945	42,934	780,264	(431,667)	1,692,840	(58,724)	(3,323)	(11,903)	(28,638)	—	(455,265)	—	7,513	10,509,976
Other changes:														
Pension-related changes other than net periodic pension costs	(971,950)	—	—	—	—	—	—	—	—	—	—	—	—	(971,950)
Unrealized gains on investments	7,260,744	27,583	1,260,535	347,395	14,004	—	—	—	—	—	—	—	—	8,910,261
Net assets released from restrictions – capital	7,038	—	—	—	2,034	—	—	—	—	—	—	—	—	9,072
Equity transfer	7,287,574	—	—	—	—	—	—	—	—	—	—	—	—	7,287,574
Total other changes	13,583,406	27,583	1,260,535	347,395	16,038	—	—	—	—	—	—	—	—	15,234,957
Increase (decrease) in unrestricted net assets (deficit)	22,559,351	70,517	2,040,799	(84,272)	1,708,878	(58,724)	(3,323)	(11,903)	(28,638)	—	(455,265)	—	7,513	25,744,933

(Continued)

Schedule 2

DIAKON
AND CONTROLLED AFFILIATES

Schedule of Consolidating Information, Statement of Operations and Changes in Net Assets (Deficit)

Period ended December 31, 2017

	Diakon Lutheran Social Ministries	Diakon	Diakon Lutheran Fund	Diakon Lutheran Senior Living Maryland LLC	Diakon Child, Family & Community Ministries	Diakon Lutherwood Senior Housing, LLC	Diakon Lutheran Senior Housing at Luther Meadows	Diakon Lutheran Senior Housing at Heilman House	Diakon Frostburg Senior Housing LLC	Statewide Adoption Network (SWAN)	Diakon Medical Group	Old Main LLC	Consolidating entries	Total
Temporarily restricted net assets:														
Contributions and bequests	$ 134,979	—	—	241	489,454	—	—	—	—	—	—	—	—	624,674
Investment gains, net of expenses	1,685,427	—	258,470	10,555	211,422	—	—	—	—	—	—	—	—	2,165,874
Unrealized gains on investments	2,279,311	—	204,025	5,235	216,229	—	—	—	—	—	—	—	—	2,704,800
Net assets released from restrictions – operations	(999,149)	—	(91,765)	(1,183)	(546,306)	—	—	—	—	—	—	—	—	(1,638,403)
Net assets released from restrictions – capital	(7,038)	—	—	—	(2,034)	—	—	—	—	—	—	—	—	(9,072)
Change in beneficial interest in trust	186,209	—	—	—	—	—	—	—	—	—	—	—	—	186,209
Equity transfer	(2,539,627)	—	—	—	28,153	—	—	—	—	—	—	—	—	(2,511,474)
Increase in temporarily restricted net assets	740,112	—	370,730	14,848	396,918	—	—	—	—	—	—	—	—	1,522,608
Permanently restricted net assets:														
Contributions and bequests	234,619	—	(18,677)	21,363	—	—	—	—	—	—	—	—	—	237,305
Increase in fair value of funds held in trust by others	2,056,033	—	886,780	—	—	—	—	—	—	—	—	—	—	2,942,813
Equity transfer	(4,747,947)	—	—	—	(28,153)	—	—	—	—	—	—	—	—	(4,776,100)
(Decrease) increase in permanently restricted net assets	(2,457,295)	—	868,103	21,363	(28,153)	—	—	—	—	—	—	—	—	(1,595,982)
Increase (decrease) in net assets (deficit)	20,842,168	70,517	3,279,632	(48,061)	2,077,643	(58,724)	(3,323)	(11,903)	(28,638)	—	(455,265)	—	7,513	25,671,559
Net assets (deficit), beginning of year	29,790,982	1,347,262	27,926,367	(7,620,166)	3,846,277	(2,691,085)	(1,018,150)	(929,463)	374,548	—	—	—	1,418,857	52,445,429
Net assets (deficit), end of year	$ 50,633,150	1,417,779	31,205,999	(7,668,227)	5,923,920	(2,749,809)	(1,021,473)	(941,366)	345,910	—	(455,265)	—	1,426,370	78,116,988

See accompanying independent auditor's report.

Schedule 3

DIAKON
AND CONTROLLED AFFILIATES

Schedule of Consolidating Information, Statement of Cash Flows

Year ended December 31, 2017

	Diakon Lutheran Social Ministries	Diakon	Diakon Lutheran Fund	Diakon Lutheran Senior Living Maryland LLC	Diakon Child, Family and Community Ministries	Diakon Lutherwood Senior Housing, LLC	Diakon Lutheran Senior Housing at Luther Meadows	Diakon Lutheran Senior Housing at Heilman House	Diakon Lutheran Senior Housing at Frostburg	Statewide Adoption Network (SWAN)	Diakon Medical Group	Old Main LLC	Elimination entries	Total
Cash flows from operating activities:														
Increase (decrease) in net assets (deficit)	$ 20,842,177	70,517	3,279,632	(48,061)	2,077,643	(58,724)	(3,323)	(11,903)	(28,638)	—	(455,265)	—	7,504	25,671,559
Adjustments to reconcile increase (decrease) in net assets (deficit) to net cash provided by (used in) operating activities:														
Net realized gains on investments	(1,776,386)	—	(890,663)	(1,556)	(58,279)	—	—	—	—	—	—	—	—	(2,726,884)
Net unrealized gains on investments	(9,540,055)	(27,583)	(1,464,560)	(352,630)	(230,233)	—	—	—	—	—	—	—	—	(11,615,061)
Depreciation and amortization	16,113,067	—	—	774,813	29,061	283,536	83,650	114,070	153,332	—	—	—	227,092	17,778,621
Amortization of debt issuance costs	129,936	—	—	—	—	16,308	5,476	4,536	7,182	—	—	6,476	—	169,914
Increase in pension liability	932,180	—	—	—	—	—	—	—	—	—	—	—	—	932,180
Amortization of entrance fees	(9,495,277)	—	—	(440,014)	—	—	—	—	—	—	—	—	—	(9,935,291)
Proceeds from entrance fees	13,459,329	—	—	557,774	—	—	—	—	—	—	—	—	—	14,017,103
Change in funds held in trust by others and beneficial interest in trust	(2,242,242)	—	(886,780)	—	—	—	—	—	—	—	—	—	—	(3,129,022)
Equity in gains of joint venture	(362,128)	—	—	—	—	—	—	—	—	—	—	—	—	(362,128)
Gain on disposal of assets	(3,502,725)	—	—	—	—	—	—	—	—	—	—	—	—	(3,502,725)
Provision for bad debts	1,941,724	—	—	352,080	133,183	—	—	—	—	—	—	—	—	2,426,987
Restricted contributions and investment income	(1,055,876)	—	(148,028)	(30,976)	(154,570)	—	—	—	—	—	—	—	—	(1,389,450)
Changes in assets and liabilities:														
Accounts receivable	3,134,239	(39,443)	(204,088)	288,844	(1,149,542)	(50,338)	16,497	(9,569)	51,879	(76,525)	381,158	(3,772,793)	22,491	(1,407,190)
Prepaid expenses and other current assets	1,424,988	—	—	(8,374)	(36,300)	(3,755)	119	128	1,619		—	—	—	1,378,425
Other Assets	418,612	—	—	—	—	—	—	—	—	—	—	—	—	418,612
Accounts payable, accrued expenses, and other liabilities	(3,102,009)	42,651	—	(13,506)	(211,263)	(48,565)	(192)	(905)	154,861	45,203	80,015	—	(21,006)	(3,074,716)
Deposits – patients and residents	34,640	—	—	1,000	—	514	402	(189)	315	—	—	—	—	36,682
Net cash provided by (used in) operating activities	27,354,194	46,142	(314,487)	1,079,394	399,700	138,976	102,629	96,168	340,550	(31,322)	5,908	(3,766,317)	236,081	25,687,616
Cash flows from investing activities:														
Purchase of investments and assets limited as to use	(26,439,026)	(46,693)	(1,085,080)	(225,063)	(178,523)	(73,979)	(25,159)	(23,950)	1,371,444	—	—	—	—	(26,726,029)
Proceeds from sales of investments and assets limited as to use	22,541,104	249,681	1,251,539	1,339	300,235	—	—	—	—	—	—	—	—	24,343,898
Purchase of property and equipment	(18,687,129)	—	—	—	(671,582)	(50,582)	(11,600)	(10,361)	(1,655,832)	—	—	—	(236,081)	(21,323,167)
Proceeds from sale of property and equipment	6,200,000	—	—	—	—	—	—	—	—	—	—	—	—	6,200,000
Proceeds from capital lease	408,412	—	—	—	—	—	—	—	—	—	—	—	(408,412)	—
Net cash (used in) provided by investing activities	(15,976,639)	202,988	166,459	(223,724)	(549,870)	(124,561)	(36,759)	(34,311)	(284,388)	—	—	—	(644,493)	(17,505,298)
Cash flows from financing activities:														
Payment of long-term debt	(10,623,617)	—	—	—	—	(112,166)	(39,631)	(42,559)	(50,951)	—	—	—	—	(10,868,924)
Proceeds from debt re-financing	—	—	—	—	—	—	—	—	—	—	—	3,842,181	—	3,842,181
Net proceeds on line of credit	—	—	—	—	542,144	—	—	—	—	—	—	—	—	542,144
Payment of debt issuance costs	(21,583)	—	—	—	—	—	—	—	14,283	—	—	(75,864)	—	(83,164)
Proceeds from restricted contributions and investment income	1,055,876	—	148,028	30,976	154,570	—	—	—	—	—	—	—	—	1,389,450
Proceeds from entrance fees	2,692,416	—	—	244,859	—	—	—	—	—	—	—	—	—	2,937,275
Refunds of entrance fees	(4,940,225)	—	—	(523,929)	—	—	—	—	—	—	—	—	—	(5,464,154)
Principal payments under capital lease obligation	—	—	—	(408,412)	—	—	—	—	—	—	—	—	408,412	—
Net cash (used in) provided by financing activities	(11,837,133)	—	148,028	(656,506)	696,714	(112,166)	(39,631)	(42,559)	(36,668)	—	—	3,766,317	408,412	(7,705,192)
Net (decrease) increase in cash and cash equivalents	(459,578)	249,130	—	199,164	546,544	(97,751)	26,239	19,298	19,494	(31,322)	5,908	—	—	477,126
Cash and cash equivalents, beginning of year	2,288,813	21,308	—	469,631	962	249,478	61,605	79,615	161,420	710,825	—	—	—	4,043,657
Cash and cash equivalents, end of year	$ 1,829,235	270,438	—	668,795	547,506	151,727	87,844	98,913	180,914	679,503	5,908	—	—	4,520,783

Schedule of noncash investment and financing activities:

A capital lease obligation of $236,566 was incurred by DLSL-MD when it entered into a lease with DLSM for property and equipment.

DLSM recorded leased property under capital lease and a lease receivable of $686,566 at the net book value of the assets.

See accompanying independent auditor's report.