

**CONTINUING DISCLOSURE ANNUAL REPORT  
FISCAL YEAR END DECEMBER 31, 2014  
(Filing Fiscal Year)**

**Cumberland County Municipal Authority Revenue Bonds  
(Presbyterian Homes, Inc. Project), Series A&B of 2008**

**Obligated Persons: Presbyterian Senior Living Obligated Group, by  
Presbyterian Homes, Inc., as the Obligated Group Representative (the “Obligated  
Group”)**

**CUSIP Numbers: 230614 DA4  
230614 DB2  
230614 DC0  
230614 DD8  
230614 DE6  
230614 DF3  
230614 DG1  
230614DH9  
230614DJ5  
230614DK2  
230614DL0  
230614DM8  
230614DN6  
230614DP1  
230614DQ9**

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APPENDIX A

Obligated Group Audited Financial Statements for Filing Fiscal Year  
and Certificate as to Defaults under Master Trust Indenture

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Combined Financial Statements

December 31, 2014 and 2013

(With Independent Auditor's Report Thereon)



# PRESBYTERIAN HOMES OBLIGATED GROUP

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## **Certification of Chief Executive and Chief Financial Officers**

We are responsible for the combined financial statements of the Presbyterian Homes Obligated Group as of December 31, 2014 and 2013, and attest that they are accurate, complete and fairly presented.

The accuracy and completeness of financial information depends on our systems, process, and most importantly our integrity. Our commitment to integrity is reflected in the code of conduct that the leadership of Presbyterian Senior Living has established as the standard for the entire organization. We believe that this commitment, our processes and internal controls produce financial information that can be trusted.

Combined financial statements report our financial positions and results using numbers and prescribed rules. They also include a significant amount of information that is required by financial reporting standards. We believe these combined financial statements disclose information that is important to create a complete picture of our stewardship of financial resources.

Combined financial statements alone can never reflect the breadth and depth of our stewardship of this ministry. They do not report on our most significant assets, our employees and volunteers. They also do not reflect our most important stewardship role; our commitment to provide Christian understanding and compassion to those seniors entrusted to our care. We believe that we continue to successfully fulfill the financial and non-financial aspects of our mission, extending a proud tradition of ministry that has served older persons in the name of Christ for the past 108 years.

Finally, we believe in openly and honestly sharing information. Please feel free to contact either of us if you have questions on any part of this report, or if we can be of further assistance in understanding Presbyterian Senior Living's mission.

Stephen E. Proctor  
Chief Executive Officer  
Presbyterian Senior Living

Jeffrey J. Davis  
Chief Financial Officer  
Presbyterian Senior Living

## **Independent Auditor's Report**

The Board of Trustees  
Presbyterian Homes Obligated Group

### **Report on the Combined Financial Statements**

We have audited the accompanying combined financial statements of the Presbyterian Homes Obligated Group (the Obligated Group) which comprise the combined statements of financial position as of December 31, 2014 and 2013, and the related combined statements of operations and changes in net assets, and cash flows for the years then ended, and the related notes to the combined financial statements.

### **Management's Responsibility for the Combined Financial Statements**

Management is responsible for the preparation and fair presentation of these combined 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 combined 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 combined 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 combined financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the combined 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 combined 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 combined 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 combined financial statements referred to above present fairly, in all material respects, the financial position of Presbyterian Homes Obligated Group as of December 31, 2014 and 2013, 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.

## **Basis of Combination**

We draw attention to Note 2(a) of the combined financial statements, which describes the basis of combination. The combined financial statements are prepared by the Presbyterian Homes Obligated Group to include only those entities set forth in the master trust indenture by and among BNY Mellon, dated May 1, 2008, as amended through the twenty-third supplemental indenture dated December 12, 2014. The consolidated financial statements of PHI, doing business as Presbyterian Senior Living, and affiliates, have been issued to its Board of Trustees as the consolidated financial statements of the primary reporting entity.

*Arnett Carbis Toothman LLP*

Arnett Carbis Toothman LLP  
New Castle, Pennsylvania  
April 8, 2015



**PRESBYTERIAN HOMES OBLIGATED GROUP**

Combined Statements of Financial Position

December 31, 2014 and 2013

<b>Assets</b>	<b>2014</b>	<b>2013</b>
Cash and cash equivalents	\$ 2,067,430	1,915,291
Investments	78,163,011	70,367,250
Statutory liquid reserves	8,593,338	5,567,996
Accounts receivable, net	21,635,230	17,989,593
Prepaid expenses and other current assets	3,118,266	2,111,822
Assets whose use is limited	11,511,690	10,275,363
Assets whose use is limited, construction funds	3,870,943	13,392,479
Pledges receivable, net	1,072,685	179,359
Assets held for sale	–	3,154,405
Property and equipment (net of accumulated depreciation of \$211,785,744 and \$198,849,866, respectively)	261,146,789	246,803,015
Assets under capital leases (net of accumulated amortization of \$515,699 and \$290,167, respectively)	490,722	434,676
Due from affiliates, net	57,455,739	64,568,178
Funds held in trust by others	15,273,801	15,113,651
Deferred financing costs (net of accumulated amortization of \$2,138,990 and \$1,958,707, respectively)	2,218,651	2,313,916
Other assets	24,182	744,318
Total assets	\$ <u>466,642,477</u>	<u>454,931,312</u>

See accompanying notes to combined financial statements.

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Combined Statements of Financial Position

December 31, 2014 and 2013

<b>Liabilities and Net Assets</b>	<u><b>2014</b></u>	<u><b>2013</b></u>
Accounts payable	\$ 9,078,556	9,123,365
Accrued expenses	13,095,288	15,363,390
Note payable	4,980,267	-
Lines of credit	15,561,035	11,420,443
Accrued interest	613,787	485,470
Resident deposits	1,183,678	2,734,618
Entrance fee payable	20,217,031	20,628,485
Deferred revenue - entrance fees	57,566,872	49,849,678
Fair value of interest rate swaps	277,664	714,302
Annuities payable	959,356	924,379
Long-term debt:		
Obligations under capital leases	500,001	445,847
Long-term debt	<u>201,627,519</u>	<u>210,490,113</u>
Total liabilities	<u>325,661,054</u>	<u>322,180,090</u>
Net assets:		
Unrestricted	117,137,839	109,888,654
Temporarily restricted	3,530,485	2,771,653
Permanently restricted	<u>20,313,099</u>	<u>20,090,915</u>
Total net assets	<u>140,981,423</u>	<u>132,751,222</u>
 Total liabilities and net assets	 <u>\$ 466,642,477</u>	 <u>454,931,312</u>

See accompanying notes to combined financial statements.

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Combined Statements of Operations and Changes in Net Assets

Years ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Operating revenues, gains, and other support:		
Resident services, including amortization of entrance fees of \$8,873,551 and \$8,466,312, respectively	\$ 168,149,017	163,673,960
Interest and dividend income	3,289,037	3,161,571
Realized gains on investments	1,590,581	3,014,004
Gain on sale of property and equipment and other assets	19,057	16,330
Contributions, gifts and bequests	725,837	663,976
Net assets released from restrictions	1,341,281	909,622
Total operating revenues, gains, and other support	<u>175,114,810</u>	<u>171,439,463</u>
Expenses:		
Nursing services	46,925,407	46,294,378
Rehabilitation	8,459,468	8,144,960
Recreation and special services	5,089,900	4,998,157
Pharmacy	2,899,161	2,727,679
Social services	720,780	654,825
Physician services	412,911	380,806
Food services	18,117,913	17,700,275
Building operations and maintenance	17,529,962	16,597,155
Housekeeping	3,645,640	3,519,091
Laundry and linen	1,273,640	1,315,713
General and administrative	26,027,945	25,463,092
Employee benefits	13,132,043	12,497,862
Interest	5,723,197	5,537,019
Depreciation	13,102,228	12,444,315
Amortization	170,601	184,211
Total expenses	<u>163,230,796</u>	<u>158,459,538</u>
Income from continuing operations	11,884,014	12,979,925
Discontinued operations:		
Discontinued operations, net of gain on sale of \$6,460,917 in 2014	6,123,325	399,820
Gain on discontinued operations	6,123,325	399,820
Operating income	18,007,339	13,379,745
Change in fair value of interest rate swaps	436,638	596,736
Loss on early extinguishment of debt	(108,203)	(938,303)
Excess of operating revenues, gains and other support over expenses	18,335,774	13,038,178
Other changes:		
Transfer (from) to parent	(247,286)	9,152
Reserve for related party receivable	(10,000,000)	-
Unrealized (losses) gains on investments	(839,303)	2,930,947
Total other changes	<u>(11,086,589)</u>	<u>2,940,099</u>
Increase in unrestricted net assets	7,249,185	15,978,277

See accompanying notes to combined financial statements.

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Combined Statements of Operations and Changes in Net Assets

Years ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Temporarily restricted net assets:		
Contributions, gifts and bequests	1,956,949	990,305
Interest and dividend income	71,044	208,357
Unrealized gain on investments	72,120	71,222
Net assets released from restrictions	<u>(1,341,281)</u>	<u>(909,622)</u>
Change in temporarily restricted net assets	<u>758,832</u>	<u>360,262</u>
Permanently restricted net assets:		
Contributions, gifts and bequests	153,856	110,269
Change in fair value of funds held in trust by others	<u>68,328</u>	<u>1,639,534</u>
Change in permanently restricted net assets	<u>222,184</u>	<u>1,749,803</u>
Change in net assets	8,230,201	18,088,342
Net assets, beginning of year	<u>132,751,222</u>	<u>114,662,880</u>
Net assets, end of year	<u>\$ 140,981,423</u>	<u>132,751,222</u>

See accompanying notes to combined financial statements.

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Combined Statements of Cash Flows

Years ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Cash flows from operating activities:		
Change in net assets	\$ 8,230,201	18,088,342
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	13,102,228	12,444,315
Provision for bad debt	1,323,939	1,037,039
Reserve for related party receivable	10,000,000	-
Proceeds from entrance fees and deposits	17,832,494	15,637,518
Amortization of entrance fees	(8,873,551)	(8,466,312)
Loss on early extinguishment of debt	108,203	938,303
Change in fair value of interest rate swaps	(436,638)	(596,736)
Unrealized loss (gain) on investments and change in fair value of funds held in trust by others	698,855	(4,641,703)
Realized gains on investments	(1,590,581)	(3,014,004)
Gain on sale of property and equipment and other assets	(19,057)	(16,330)
Contributions restricted for long-term purposes	(153,856)	(110,269)
Gain on discontinued operations	(6,123,325)	(399,820)
Amortization of deferred costs	177,717	185,346
Amortization of bond discount	(7,116)	(1,135)
Changes in assets and liabilities:		
Increase in accounts receivable	(4,969,576)	(1,055,498)
(Increase) decrease in pledges receivable	(893,326)	59,018
(Increase) decrease in other assets	(283,743)	563,006
Decrease in accounts payable	(44,809)	(1,420,271)
(Decrease) increase in accrued expenses	(2,139,785)	2,088,192
Net cash provided by operating activities	<u>25,938,274</u>	<u>31,319,001</u>
Cash flows from investing activities:		
Acquisition of property and equipment	(27,515,261)	(33,877,994)
Net proceeds from sale of entity	9,310,000	-
Purchases of investments	(41,123,729)	(35,374,030)
Proceeds from sale of investments	39,319,412	39,245,430
Due from affiliates	(2,887,561)	(5,767,132)
Net cash used in investing activities	<u>(22,897,139)</u>	<u>(35,773,726)</u>
Cash flows from financing activities:		
Refunds of entrance fees and deposits	(2,792,690)	(3,532,757)
Change in entrance fee payable	(411,454)	(126,903)
Principal payments on and redemptions of long-term debt	(8,963,681)	(21,998,574)
Proceeds from issuance of long-term debt	-	31,595,427
Financing costs incurred	(85,017)	(369,601)
Net borrowings (repayments) of notes payable and lines of credit	9,120,859	(1,496,940)
Borrowings through capital leases	281,577	359,853
Repayments on capital leases	(227,423)	(164,558)
Contributions restricted for long-term purposes	153,856	110,269
Increase (decrease) in annuities payable	34,977	(107,080)
Net cash (used in) provided by financing activities	<u>(2,888,996)</u>	<u>4,269,136</u>
Net increase (decrease) in cash and cash equivalents	152,139	(185,589)
Cash and cash equivalents, beginning of year	<u>1,915,291</u>	<u>2,100,880</u>
Cash and cash equivalents, end of year	\$ <u><u>2,067,430</u></u>	<u><u>1,915,291</u></u>
Supplemental schedule of non-cash investing activities		
Decrease (increase) in assets held for sale by increase/decrease in property and equipment	\$ <u><u>-</u></u>	<u><u>(3,154,405)</u></u>

See accompanying notes to combined financial statements.

## PRESBYTERIAN HOMES OBLIGATED GROUP

Notes to Combined Financial Statements

December 31, 2014 and 2013

### (1) General Information

The Presbyterian Homes Obligated Group (the Obligated Group) consists of the following not-for-profit corporations: Presbyterian Homes, Inc., Presbyterian Homes in the Presbytery of Huntingdon (PHPH), Quincy Retirement Community (QRC), The Long Community Inc. (TLC), and PHI Investment Management Services, Inc. (PIMSI). Between all the members of the Obligated Group, they own, operate and manage twelve continuing care retirement communities, three stand-alone independent living facilities, and two stand-alone personal care homes.

The Obligated Group is governed by the Board of Trustees of PHI, doing business as Presbyterian Senior Living. Presbyterian Senior Living is the parent organization for the members of the Obligated Group.

During 2014, the PHI Board of Trustees approved the sale of Sycamore Manor Health Center, a stand-alone skilled nursing facility within Presbyterian Homes. On September 1, 2014, the Corporation sold Sycamore Manor Health Center to TL Management.

The following table details the number of beds/units that operate under each member of the Group:

	Total	Pres Homes	PHPH	QRC	TLC
Nursing beds	1,088	578	376	134	—
Personal care units	462	307	91	32	32
Independent living units	1,121	706	124	183	108
Total	2,671	1,591	591	349	140

### (2) Summary of Significant Accounting Policies

#### (a) Basis of Combination

These combined financial statements were prepared in accordance with accounting principles generally accepted in the United States of America, and only include those entities set forth in the master trust indenture by and among BNY Mellon, dated May 1, 2008, as amended through the twenty-third supplemental indenture dated December 12, 2014. Requirements of the master trust indenture preclude the consolidation of certain affiliates that are not members of the Obligated Group. All material intercompany transactions have been eliminated.

## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

**(b) Basis of Accounting**

These combined financial statements, which are presented on the accrual basis of accounting, have been prepared to focus on the Obligated Group as a whole and to 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.

**(c) Income Taxes**

The Obligated Group and all its members are not-for-profit organizations as described in Section 501(c)(3) of the Internal Revenue Code (Code) and have been recognized as tax exempt under Section 501(a) of the Code.

The Obligated Group follows the Financial Accounting Standards Board (FASB) accounting standard for accounting for uncertainty in income taxes. This standard clarifies the accounting for uncertainty in income taxes in a company's combined financial statements and prescribes a recognition threshold of more-likely-than-not to be sustained upon examination by the appropriate taxing authority. Measurement of the tax uncertainty occurs if the recognition threshold has been met. The standard also provides guidance on derecognition, classification, interest and penalties, and disclosure. Management has determined that this standard does not have a material impact on the combined financial statements.

The Obligated Group is part of a consolidated federal Exempt Organization Business Income Tax Return, for which the years ended December 31, 2011, 2012, and 2013 remain subject to examination by the Internal Revenue Service.

**(d) Use of Estimates**

The preparation of combined financial statements in accordance with accounting principles generally accepted in the United States of America as set forth in the master trust indenture 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 combined financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

(e) *Cash and Cash Equivalents*

The Obligated Group considers all liquid investments with a maturity of three months or less when purchased to be cash equivalents for the purposes of the combined statements of financial position and cash flows, except for those included in investments or assets whose use is limited. The Obligated Group's cash and cash equivalents are insured by the Federal Deposit Insurance Corporation (FDIC) for up to \$250,000. At times during 2014 and 2013, the Obligated Group's cash balances may have exceeded the FDIC coverage. The Obligated Group has not experienced any loss in these accounts.

(f) *Investments*

Investments in securities and mutual funds with readily determinable fair values and all investments in debt securities are measured at fair value, as determined by a national exchange in the combined statements of financial position. Alternative investments are not readily marketable and are presented at estimated fair value as determined by the investment managers. Alternative investments are held in private investment partnerships, which include publically traded securities, real estate and natural resources. Partnership agreements specify the type of investments held, liquidity, manager compensation, and other funding requirements. Management reviews, evaluates, and monitors the values provided and agrees with the valuation methods and assumptions used in determining the fair value of the alternative investments. Annual independent audits of each private investment partnership are provided and included in management's review.

A decline in market value of any investment below cost that is deemed to be other than temporary results in a reduction in carrying amount to fair value. The impairment is charged to realized loss and a new cost basis for the investment is established. For the years ended December 31, 2014 and 2013, no amounts were charged to realized loss for this purpose as management believes the decline in value is temporary due to general economic conditions and not an other than temporary decline in value.

Investment income consisted of the following:

	<u>2014</u>	<u>2013</u>
Interest and dividends	\$ 3,360,081	3,369,928
Realized gains on investments	1,590,581	3,014,004
Unrealized (losses) gains on investments and funds held in trust by others	<u>(698,855)</u>	<u>4,641,703</u>
	<u>\$ 4,251,807</u>	<u>11,025,635</u>

Investment expenses of \$321,857 and \$357,887 for the years ended December 31, 2014 and 2013, respectively, have been included in general and administrative expenses on the combined statements of operations and changes in net assets.



**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(g) Accounts Receivable**

Accounts receivable are shown net of an estimated allowance for doubtful accounts, as follows:

	<u>2014</u>	<u>2013</u>
Total accounts receivable	\$ 24,518,652	20,360,692
Less: allowance for doubtful accounts	<u>(2,883,422)</u>	<u>(2,371,099)</u>
Net accounts receivable	<u>\$ 21,635,230</u>	<u>17,989,593</u>

Receivables are considered past due when payments have not been received by the Obligated Group within 60 days of their contractually stated due date.

The allowance for doubtful accounts is established based on management's assessment of the collectability of specific customer accounts and the aging of the accounts receivable. Losses are charged against the allowance for doubtful accounts when management believes the uncollectability of a receivable is likely.

During 2014, the Obligated Group migrated to a new accounting software system. Under the old system, receivables were calculated as past due based on calendar days. The new system calculates the amounts due based on calendar months. This change in methodology from calendar days to calendar months has caused a decrease in the amount reported in the allowance for doubtful accounts of \$625,426.

**(h) Assets Whose Use is Limited**

Assets whose use is limited primarily include assets held by a trustee under the terms of various bond indentures and permanently restricted investments.

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(i) Pledges Receivable**

The Obligated Group records material pledges due in more than one year at the net present value less a discounted uncollectible amount.

	<u>2014</u>	<u>2013</u>
Pledges receivable	\$ 1,267,975	229,124
Less: unamortized discount	<u>(28,270)</u>	<u>—</u>
Subtotal	1,239,705	229,124
Less: allowance for uncollectibles	<u>(167,020)</u>	<u>(49,765)</u>
Net pledges receivable	<u>\$ 1,072,685</u>	<u>179,359</u>

Pledges receivable as of December 31, 2014 is as follows:

Amounts due in:	
Less than one year	\$ 868,068
One to five years	<u>399,907</u>
	<u>\$ 1,267,975</u>

**(j) Property and Equipment**

Property and equipment are stated at cost or, if donated, at fair market value on the date of donation. Depreciation is being provided on the straight-line method over the estimated useful lives of the assets. The Obligated Group's policy is to capitalize items in excess of \$3,000 or for a group of items that are the same or similar in nature or function as a group totaling \$3,000 or more.

Depreciable lives are determined as follows:

Land improvements	3-35 years
Buildings and improvements	5-75 years
Departmental equipment, furniture and fixtures	1-40 years
Furniture	5-25 years
Vehicles	4 years

**(k) Costs of Borrowing**

The average cost of capital during the period of construction of capital assets is capitalized as a component of construction-in-progress. Interest of \$1,096,780 and \$761,884 was capitalized in 2014 and 2013, respectively.

## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

**(l) Funds Held in Trust by Others**

The members of the Obligated Group have been named as a beneficiary of several trusts which are administered and controlled by independent trustees. The trusts are recorded as contribution revenue when the Obligated Group is notified of the trust's existence. The Obligated Group receives the earnings from these trusts whose principal is to be held in perpetuity. The earnings from the trust are reported as investment income, increasing unrestricted net assets.

Assets held in trust by others are valued based on the estimated fair value of the underlying investments. The change in the fair value of assets held in trust by others is reported as permanently restricted unrealized gains or losses on investments.

Also included in funds held in trust by others are gift annuities held by an independent trustee. Periodic payments are made until the death of the annuitant. These annuities are recorded at the present value of the annuity amount discounted at the contract rate over the estimated remaining life of the annuitant.

A summary of these funds at December 31 is as follows:

	<u>2014</u>	<u>2013</u>
Beneficial interest in perpetual trusts	\$ 14,607,755	14,494,504
Contributions receivable from remainder trusts	650,543	593,112
Gift annuities	<u>15,503</u>	<u>26,035</u>
	<u>\$ 15,273,801</u>	<u>15,113,651</u>

**(m) Derivatives and Hedging Activities**

The Obligated Group utilizes interest rate swap agreements to hedge variable interest rates but elected not to elect hedge accounting for these agreements.

The Obligated Group's interest rate swaps are carried as a liability as determined by a third party. Changes in fair value are reported in the combined statements of operations and changes in net assets as a component of the excess of operating revenues, gains and other support over expenses. For 2014 and 2013, an adjustment to the liability was recorded causing a gain each year of \$436,638 and \$596,736, respectively. These adjustments represent the decrease in the liability of the interest rate swaps.

## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

**(n) *Deferred Financing Costs***

The Obligated Group has deferred the costs incurred for obtaining the proceeds of its long-term debt arrangements. These costs are being amortized over the term of the related financings using the straight-line method which approximates the effective interest method. The Obligated Group incurred financing costs of \$85,017 and \$369,601, for the years ended 2014 and 2013, respectively. Amortization expense is expected to be \$198,096, \$169,346, \$162,743, \$155,020 and \$155,020 for the next five years.

**(o) *Workers' Compensation***

Accrued expenses include a provision for estimated self-insured workers' compensation claims for both reported claims not yet paid and claims incurred but not reported.

**(p) *Resident Deposits***

Entrance fees and waiting list deposits received from prospective residents prior to occupancy under Residence and Care Agreements are included in resident deposits in the combined statements of financial position. These deposits are transferred to deferred revenue upon occupancy of the related units.

**(q) *Deferred Revenue – Entrance Fees***

The Obligated Group follows the FASB accounting standards update regarding refundable entrance fees. This standard was issued to clarify the reporting for refundable advanced fees received by continuing care retirement communities. This guidance clarifies that an entity should classify an advance fee as deferred revenue when a continuing care retirement community has a resident contract that provides for payment of the refundable advanced fee upon reoccupancy by a subsequent resident, which is limited to the proceeds of reoccupancy. Refundable advance fees that are contingent upon reoccupancy by a subsequent resident but are not limited to the proceeds of reoccupancy should be accounted for and reported as a liability.

The Obligated Group does not amortize the guaranteed refundable portion of the entrance fees. This portion of the entrance fee is reflected as a liability on the combined statements of financial position.

The amount of entrance fees guaranteed refundable to residents at December 31, 2014 and 2013 under contractual refund provisions was approximately \$20,217,000 and \$20,628,000, respectively.

## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

(r) ***Statutory Liquid Reserves***

The Continuing Care Provider Registration and Disclosure Act in Pennsylvania requires a working capital reserve equivalent to the greater of the total debt service payments due during the next 12 months on account of any loan or long-term financing, or 10% of the projected annual operating expenses of the Obligated Group exclusive of depreciation. The reserve is computed on only the proportional share of financing or operating expenses that are applicable to Residence and Care Agreements.

In addition to the statutory liquid reserves, entrance fee payments in excess of 5% of the then existing entrance fee for the unit, received by the Obligated Group prior to the date the resident is permitted to occupy the living unit are included in the cash and cash equivalents and investments on the accompanying combined statements of financial position.

(s) ***Temporarily and Permanently Restricted Net Assets***

Temporarily restricted net assets are those whose use by the Obligated Group has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Obligated Group in perpetuity. The interest and dividend income from these restricted assets is used for the charitable purpose.

(t) ***Donor Restrictions***

The Obligated Group reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or the purpose to which the donation is restricted is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the combined statements of operations and changes in net assets as net assets released from restrictions. Donor restricted contributions whose restrictions are met within the same year as received are reflected as unrestricted contributions in the accompanying combined financial statements.

The Obligated Group reports non-cash gifts 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, the Obligated Group reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

Contributions, including unconditional promises to give, are recognized as revenues when the promise to give is first made. 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.

## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

**(u) Resident Service Revenue and Business Concentration**

Resident service revenue is reported at the estimated net realizable amount to be received from patients and others including Medicare, Medicaid, and other third-party payors for services rendered. The Obligated Group derives a portion of its revenues from federal and state reimbursement programs with a significant portion of state reimbursement from Pennsylvania's Department of Human Services (DHS).

The Obligated Group's nursing care facilities primarily derive their revenue from private pay, Medicare, and Medicaid. Private pay rates are established on the basis of the cost of delivering services and competitive consideration and, as such are essentially market driven. In contrast, Medicare and Medicaid payment rates are regulated by the federal and state governments. As a result, the industry is sensitive to related legislative changes and is affected by reductions in governmental spending for these programs.

Revenues from Medicare and Medicaid represent approximately 43% and 42% of revenues for 2014 and 2013, respectively. Medicare and Medicaid receivables represent approximately 50% and 48% of accounts receivable at December 31, 2014 and 2013, respectively.

Skilled nursing services provided to Medicare beneficiaries are paid under terms of a prospective payment system ("PPS") at pre determined rates based on clinical, diagnostic and other factors.

Nursing services provided to Pennsylvania Medicaid beneficiaries are paid at prospectively determined rates per day. These rates vary according to a resident classification system that is based on clinical diagnosis and other factors and the reimbursement methodology is subject to various limitations and adjustments. The Obligated Group's current concentration of skilled nursing facilities in Pennsylvania exposes it to the risk of changes in Medicaid reimbursement in this state. Rates are calculated by DHS on a quarterly basis. They are published in the Pennsylvania Bulletin prior to being finalized. Rates have been finalized through December 31, 2014.

In January 2005, the Centers for Medicare and Medicaid Services (CMS) approved a Pennsylvania State Plan amendment implementing a Nursing Home Assessment (the Assessment). The Assessment requires all Pennsylvania nursing homes, except for county homes, to pay a fee to 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. The supplemental and assessment amounts per day have been approved by CMS. For the years ended December 31, 2014 and 2013, the Obligated Group received or will receive approximately \$2,700,000 for each year, in additional revenue for the net effect of this assessment and supplement.

## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

(v) *Charity Care*

The Obligated Group follows the FASB accounting standards update that provides improved disclosure about charity care. The amount of charity care disclosed in the combined financial statements is measured based on the direct and indirect costs of providing charity care services. If the costs cannot be specifically attributed to services provided to charity care patients, reasonable techniques are used to estimate these costs, and these techniques are disclosed. Any funds received to offset or subsidize charity care services are also disclosed.

The Obligated Group's policy is to provide services without charge, or at amounts less than its established rates to residents who meet the certain need based criteria. These criteria consider resident income and expenses, financials resources, State and Federal government requirements, and other sources of payment for services which may be provided. The Obligated Group also receives donations and income from permanently restricted trusts and investments designated to the needs of its residents under this policy.

Amounts the Obligated Group provided and received for resident financial support are as follows:

	<u>2014</u>	<u>2013</u>
Charity care provided at the estimated cost thereof, net of amounts received from residents and third party payors	\$ 3,772,881	3,476,897
Additional benevolent care provided at amounts less than pre-established charges for private pay services	25,938,448	24,465,048
Giving and income designated for resident financial support	1,016,622	728,315

(w) *Advertising*

Advertising costs are expensed in the year incurred. Total advertising expense for the years ended December 31, 2014 and 2013 was \$441,688 and \$416,600, respectively.

## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

(x) *Classification of expenses*

	<u>2014</u>	<u>2013</u>
Program activities	\$ 137,202,851	132,996,446
General and administrative	25,359,065	25,053,014
Fundraising	<u>668,880</u>	<u>410,078</u>
	<u>\$ 163,230,796</u>	<u>158,459,538</u>

(y) *Fundraising Expense*

Fundraising expenses incurred by the Obligated Group are included in general and administrative on the combined statements of operations and changes in net assets.

(z) *Operating Income*

The combined statements of operations and changes in net assets include an intermediate measure of operations labeled as “operating income.” Changes in the performance indicator which are excluded from this measure include change in fair value of interest rate swaps and loss on the early extinguishment of debt.

(aa) *Performance Indicator*

The Obligated Group measures the performance of its operations using the combined statements of operations and changes in net assets, which includes a performance indicator of operations labeled as “excess of operating revenues, gains, and other support over expenses.” Changes in unrestricted net assets which are excluded from this measure are: transfer (from) to parent, reserve for related party receivable, and unrealized (losses) gains on investments.

(ab) *Combined Statements of Cash Flows*

Interest paid during the years ended December 31, 2014 and 2013 was \$6,756,878 and \$6,573,165, respectively.

(ac) *Reclassifications*

Certain reclassifications have been made to the 2013 combined financial statements to conform to the presentation of 2014.



## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

**(ad) Subsequent Events**

The Obligated Group has adopted the standard related to subsequent events. This standard provides guidance on accounting for and disclosure of events that occur after the combined statements of financial position date but before combined financial statements are issued or are available to be issued.

The Obligated Group has evaluated subsequent events through April 8, 2015, which is the date the combined financial statements were issued.

**(3) Investments**

The cost and fair value of investments at December 31 is as follows:

	2014		2013	
	Fair value	Cost	Fair value	Cost
Money market funds	\$ 23,388,778	23,388,778	23,609,025	23,609,025
Equity securities	38,794,503	36,228,673	41,038,873	36,068,036
Fixed income securities	18,130,749	18,462,793	17,798,902	18,010,658
Alternate investments	21,824,952	14,666,756	17,156,288	11,049,068
Totals	102,138,982	92,747,000	99,603,088	88,736,787
Less:				
Assets whose use is limited (note 5)	(15,382,633)		(23,667,842)	
Statutory liquid reserves	(8,593,338)		(5,567,996)	
Total investments	\$ 78,163,011		70,367,250	

The Obligated Group invests primarily in a diversified portfolio of mutual funds. The Obligated Group has twenty one mutual funds, nine alternative investments and several other fixed income securities as of December 31, 2014. The Obligated Group has twenty one mutual funds, eight alternative investments and several other fixed income securities as of December 31, 2013.

As of December 31, 2014, twelve mutual funds had a market value that had been below cost for less than a year. In total, its market value was less than two percent below cost. As of December 31, 2013, eighteen mutual funds had a market value that had been below cost for less than a year. In total, its market value was less than three percent below cost.

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(3) Investments (continued)**

Fourteen mutual funds had a market value that had been below cost for more than a year as of December 31, 2014. In total, its market value was less than six percent below cost. Seven mutual funds had a market value that had been below cost for more than a year as of December 31, 2013. In total, its market value was five percent below cost.

A summary of investments with fair values below cost as of December 31, 2014 follows:

	<u>Less than 12 Months</u>		<u>More than 12 Months</u>		<u>Total</u>	
	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>
Mutual funds	\$ 16,802,231	(344,922)	8,464,687	(505,171)	25,266,918	(850,093)
Total temporarily impaired investments	\$ 16,802,231	(344,922)	8,464,687	(505,171)	25,266,918	(850,093)

A summary of investments with fair values below cost as of December 31, 2013 follows:

	<u>Less than 12 Months</u>		<u>More than 12 Months</u>		<u>Total</u>	
	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>
Mutual funds	\$ 15,502,997	(406,884)	3,407,163	(174,306)	18,910,160	(581,190)
Total temporarily impaired investments	\$ 15,502,997	(406,884)	3,407,163	(174,306)	18,910,160	(581,190)

**(4) Related Party Transactions**

The Obligated Group members incur a management fee payable to their parent organization under a management agreement whereby Presbyterian Senior Living provides the Obligated Group with various management and administrative services to each of the Obligated Group's operating facilities. The Obligated Group members also incur certain operating expenses under the management agreement that are comprised primarily of the salaries and benefits of certain key management personnel provided to the Obligated Group by the parent organization. During the years ended December 31, 2014 and 2013, the Obligated Group incurred management fees and other expenses under the management agreement totaling \$14,101,397 and \$13,067,085, respectively, which is included in general and administrative expenses and discontinued operations on the combined statements of operations and changes in net assets.

## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

#### (4) Related Party Transactions (continued)

The Obligated Group is an irrevocable guarantor of all the debts of Presbyterian Senior Living Services, Inc. (Glen Meadows), an affiliate organization. As of December 31, 2014 and 2013, Glen Meadows had \$15,115,000 and \$15,685,000, respectively, in outstanding debt. In the event of a deficiency judgment from the sale of real property pledged as security for the purchase of a facility in Glen Arm, Maryland, the Obligated Group has guaranteed to repay all of the outstanding debt which matures through 2029.

The Obligated Group is an irrevocable guarantor of the Metro Bank Loan for PHI Stadium Place Senior Care Inc., an affiliate organization, for a maximum principal amount of \$10,000,000. As of December 31, 2014 and 2013, PHI Stadium Place Senior Care Inc. had \$9,918,419 and \$2,228,044, respectively, in outstanding debt. In the event of a deficiency judgment, the Obligated Group has guaranteed to repay all of this outstanding debt which matures through 2034.

Prelude Systems, Inc. (Prelude), is a joint venture between Presbyterian Senior Living and Diakon Lutheran Social Ministries (Diakon). Prelude is a technical information services organization with a wide range of programs designed to support the information systems needs of both Presbyterian Senior Living and Diakon as well as other healthcare and community service organizations. During 2014 and 2013, the Obligated Group incurred expenses related to Prelude amounting to \$1,811,896 and \$1,784,400, respectively, for information services provided by Prelude, of which \$27,683 and \$15,171 is included in accounts payable as of December 31, 2014 and 2013, respectively.

Amounts due from affiliate entities, principally Presbyterian Senior Living, as of December 31, 2014 and 2013 are \$57,455,739 and \$64,568,178, respectively.

The amounts receivable from the Obligated Group's affiliated organizations are unsecured, non-interest bearing and have no fixed repayment terms, except loans to the low income housing corporations. In 2014, the Obligated Group established a reserve of \$10,000,000 based on management's assessment of the collectability of specific receivables from an affiliate organization.

#### (5) Assets Whose Use is Limited

At December 31 assets whose use is limited consisted of the following:

	<u>2014</u>	<u>2013</u>
Permanently restricted investments	\$ 4,634,397	4,515,573
Bond fund	2,911,782	1,762,729
Debt service reserve fund	3,965,511	3,997,061
Held by trustee-for future projects	3,870,943	13,392,479
	<u>\$ 15,382,633</u>	<u>23,667,842</u>

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(6) Property and Equipment**

A summary of property and equipment and accumulated depreciation at December 31 is as follows:

	<b>2014</b>		<b>2013</b>	
	<b>Cost</b>	<b>Accumulated depreciation</b>	<b>Cost</b>	<b>Accumulated depreciation</b>
Land	\$ 27,314,909	–	27,189,272	–
Land improvements	18,041,907	14,520,534	17,902,279	14,079,108
Buildings and improvements	357,570,442	157,153,666	321,005,401	146,274,443
Departmental equipment, furniture and fixtures	42,753,193	35,142,856	39,941,844	33,721,550
Furniture	3,163,790	3,091,416	3,163,790	3,072,174
Vehicles	2,028,356	1,877,272	1,887,534	1,702,591
Construction-in-progress	22,059,936	–	34,562,761	–
	\$ 472,932,533	211,785,744	445,652,881	198,849,866
Net book value		\$ 261,146,789		246,803,015

As the Obligated Group undertakes expansion and improvement projects, costs are included in construction-in-progress. As projects are completed, the costs are transferred to buildings and building improvements. Ongoing improvement and expansion is anticipated in the normal course of operations.

As of December 31, 2014 and 2013 approximately \$13,500,000 and \$10,000,000, respectively, was committed for future renovations.

On September 1, 2014, the Corporation sold Sycamore Manor Health Center, a 133 bed nursing living facility for approximately \$9,310,000, and recognized a gain of \$6,460,917.

For the year ended December 31, 2013, Sycamore Manor Health Center's fixed assets were reclassified to assets held for sale on the combined statement of financial position in accordance with accounting standards related to discontinued operations.

For the years ended December 31, 2014 and 2013, Sycamore Manor Health Center's gain consisted of:

	<b>2014</b>	<b>2013</b>
Depreciation	\$ (200,231)	(299,890)
Interest	(65,219)	(103,549)
Amortization	(2,299)	(4,175)
Other expenditures, net of gain of \$6,460,917 in 2014	6,391,074	807,434
Total gain on discontinued operations	\$ 6,123,325	399,820

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(7) Long-term Debt**

Long-term debt of the group and of the amounts payable by the Obligated Group as of December 31, 2014 and 2013 consisted of the following:

	<b>2014</b>	<b>2013</b>
Cumberland County Municipal Authority Bonds Series 1993A, principal due in 2018, variable interest rate, 0.05% and 0.07% at December 31, 2014 and 2013, respectively, collateralized by irrevocable letter of credit and by property and equipment and gross revenues of the Obligated Group	\$ 6,000,000	6,000,000
Cumberland County Municipal Authority Revenue Bonds Series 2003B, tax exempt variable rate bonds, principal maturities in varying amounts from 2013 to 2032, interest converted to a fixed rate of 3.8% as of January 2, 2014, interest rate was 0.07% at December 31, 2013, collateralized by letter of credit	7,170,000	7,430,000
Kent County Delaware Economic Development Revenue Bond Series 2003B, principal and interest payable monthly on a 15-year amortization period, final principal payment due October 31, 2018, variable interest of 0.941% and 0.948% at December 31, 2014 and 2013, respectively, collateralized by property and equipment and gross revenues of the Obligated Group	3,115,363	3,856,634
Cumberland County Municipal Authority Revenue Bonds Series 2005A, tax exempt bonds, principal due in varying annual amounts from 2013 to 2021, interest rates ranging from 4% to 5%, insured by municipal bond insurance and collateralized by property and equipment and gross revenues of the Obligated Group	13,570,000	15,160,000
Cumberland County Municipal Authority Revenue Bonds Series 2008A, tax exempt bonds, principal due in varying annual amounts from 2013 to 2021, interest rates ranging from 5% to 5.45%, collateralized by property and equipment and gross revenues of the Obligated Group	6,660,000	7,810,000
Northampton County Industrial Development Authority Revenue Bonds Series 2014, tax exempt bonds, principal due on an annual basis of \$67,000 per year, interest payable monthly and is fixed at 3.24% until June 2024, collateralized by property and equipment and gross revenues of the Obligated Group	9,966,500	—

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(7) Long-term Debt (continued)**

	<u>2014</u>	<u>2013</u>
Blair County Hospital Authority Revenue Bonds Series 2014, tax exempt bonds, principal due on an annual basis of \$67,000 per year, interest payable monthly and is fixed at 3.24% until June 2024, collateralized by property and equipment and gross revenues of the Obligated Group	9,966,500	—
Cumberland County Municipal Authority Revenue Bonds Series 2008B, tax exempt bonds, principal due in varying annual amounts from 2022 to 2038, interest adjusted weekly, 0.03% and 0.07% at December 31, 2014 and 2013, respectively, collateralized by a letter of credit and by property and equipment and gross revenues of the Obligated Group	25,000,000	45,000,000
Cumberland County Municipal Authority Revenue Bonds Series 2008C, taxable variable rate bonds, converted to fixed rate bonds in 2013, principal maturities in varying amounts from 2013 to 2026, interest adjusted weekly, 0.05% and 0.07% at December 31, 2014 and 2013, respectively, collateralized by property and equipment and gross revenues of the Obligated Group	14,985,000	15,265,000
York County Industrial Development Authority Bonds Series 2010, tax exempt bank qualified debt, principal due in varying annual amounts from 2013 to 2033, interest was locked in 2013 and resets every 5 years, with interest at 2.75% at December 31, 2014 and 2013, collateralized by property and equipment and gross revenues of the Obligated Group	18,856,144	19,624,547
Bank of America taxable 5 year term loan, principal due in varying amounts, interest is fixed at 3.15%, and is collateralized by property and equipment and gross revenues of the Obligated Group, due in December 2016 with the option to extend all or a portion of the remaining balance of the 25-year amortization period	11,930,576	12,299,933
General Municipal Authority of the Township of Manheim Revenue Bonds Series 2011, principal maturities based on a twenty year repayment schedule, interest is fixed for the first 120 months, subsequent interest rates will be reset on a 10 year increment, interest was 3.48% at both December 31, 2014 and 2013, collateralized by property and equipment and gross revenues of the Obligated Group	8,899,370	9,272,913

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(7) Long-term Debt (continued)**

	<b>2014</b>	<b>2013</b>
1995 Series A revenue note to First National Bank of PA, payable in equal monthly installments of principal and interest sufficient to amortize the principal balance to July 10, 2026, the note bears a floating rate which was 2.054% at both December 31, 2014 and 2013, and is collateralized by property and equipment and gross revenues of the Obligated Group	1,930,727	2,097,988
1997 Series A Montgomery County Higher Education and Health Authority Demand Revenue Bonds, payable in monthly installments of principal and interest sufficient to amortize the principal balances to April 2017, the bonds bear a floating interest rate, which was 0.08% and 0.11% at December 31, 2014 and 2013, respectively, and are collateralized by a letter of credit and by property and equipment and gross revenues of the Obligated Group	2,630,000	3,425,000
Series 2002 Huntingdon County Industrial Development Authority, Mortgage Revenue Note, payable in equal monthly installments of principal and interest sufficient to amortize the principal balance to April 2023, the note bears a floating interest rate, interest will be reset in five year increments and was 0.9903% at both December 31, 2014 and 2013, and is collateralized by property and equipment and gross revenues of the Obligated Group	473,731	528,189
Series 2005 College Township Revenue Bonds, payable in equal monthly installments to include principal and interest through September 2026, the bonds bear a floating interest rate, which will reset in five year increments and was 3.83% at both December 31, 2014 and 2013, and are collateralized by property and equipment and gross revenues of the Obligated Group	2,635,598	2,809,204
Quincy Sewer Authority Revenue Bonds Series 2012, payable in equal monthly installments of principal and interest, due August 15, 2032, the note bears an interest rate of 3.35%, and is collateralized by property and equipment and gross revenues of the Obligated Group	9,143,517	9,513,907

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(7) Long-term Debt (continued)**

	<b>2014</b>	<b>2013</b>
Uwchlan Township Industrial Development Authority Revenue Note Series 2012, payable in equal monthly installments of principal and interest sufficient to amortize the principal balance to June 2032, interest fixed at 3.5% until June 2022, interest rates will be reset in 10 year increments, the note is collateralized by property and equipment and gross revenues of the Obligated Group	9,102,806	9,471,787
General Municipal Authority of the Township of Manheim Revenue Bond Series 2012, payable in equal monthly installments of principal and interest sufficient to amortize the principal balance to August 2032, a call option is available at the lender's discretion on August 2022, interest fixed at 2.75% until 2019, the note is collateralized by property and equipment and gross revenues of the Obligated Group	9,123,131	9,515,088
Cumberland County Municipal Authority Revenue Bonds Series 2013A, tax exempt bonds, principal due in varying annual amounts from 2013 to 2026, interest fixed at 3.11%, interest will be reset in 10 year increments, collateralized by property and equipment and gross revenues of the Obligated Group	6,525,790	6,548,707
Cumberland County Municipal Authority Revenue Bonds Series 2013B, tax exempt bonds, principal due in varying annual amounts from 2013 to 2022, interest fixed at 3.11%, collateralized by property and equipment and gross revenues of the Obligated Group	4,700,886	4,911,159
Indiana County Industrial Development Authority Revenue Bonds Series 2013, payable in equal monthly installments of principal and interest sufficient to amortize the principal balance to November 15, 2033, interest fixed at 3.48% until 2020, the note is collateralized by property and gross revenues of the Obligated Group	9,618,418	9,970,858



**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(7) Long-term Debt (continued)**

	<u>2014</u>	<u>2013</u>
Uwchlan Township Industrial Development Authority Revenue Bonds Series 2013, tax exempt bonds, payable in equal monthly installments of principal and interest sufficient to amortize the principal balance to June 2026, interest fixed at 3.6% until June 2023, interest rates will reset in 10 year increments, collateralized by property and equipment and gross revenues of the Obligated Group	9,503,184	9,851,640
	<u>201,507,241</u>	<u>210,362,554</u>
Less: Unamortized discount	(96,242)	(107,180)
Plus: Unamortized premium	<u>216,520</u>	<u>234,739</u>
	<u>\$ 201,627,519</u>	<u>210,490,113</u>

During 2013, \$225,000 of the Cumberland County 2008C bonds was repurchased. During 2014, \$10,000 of the Cumberland County 2005A bonds that were previously repurchased was sold. The bonds remaining are currently being held with the option to remarket at a future date.

Under the terms of the Obligated Group's debt, the Obligated Group is required to maintain certain measures of financial performance as long as the notes are outstanding. These covenants have been met as of December 31, 2014 and 2013.

Several of the bonds are backed by letters of credit and subject to remarketing agreements. In the event that any or all of the bonds are tendered by the bondholder and are unable to be remarketed, the letter of credit would be drawn upon to repay the tendered bonds. Any drawings under the letters of credit are repayable on or before the first to occur of the following: the date on which the bonds purchased with the proceeds from a draw on the letter of credit are successfully remarketed by the remarketing agent, the date on which the bonds purchased with the proceeds from a draw on the letters of credit are redeemed or otherwise paid in full, the occurrence of an event of default, or the date the letters of credit expires. The letters of credit for the bonds will expire at various dates through November 2016.

In connection with the partial replacement of the Cumberland County 2008B bonds, in June 2014, the Obligated Group recorded a loss on the extinguishment of debt in the amount of \$108,203, representing the write-off of the unamortized debt issuance costs. In June 2013, the Obligated Group refunded and replaced the Cumberland County 2003A and 2008A bonds. A loss on the extinguishment of debt in the amount of \$938,303 was recorded in 2013, representing the write-off of the unamortized debt issuance costs and discount on the original purchase.

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(7) Long-term Debt (continued)**

Scheduled maturities for the five years subsequent to December 31, 2014 and thereafter are as follows:

<u>Years ended December 31,</u>	<u>Aggregate maturities</u>
2015	\$ 10,826,580
2016	11,178,798
2017	11,542,088
2018	10,809,099
2019	9,032,071
Thereafter	148,118,605
	<u>\$ 201,507,241</u>

The Obligated Group entered into several swap agreements with financial intermediaries, which fix the interest rates to be paid by the Obligated Group on the Cumberland County Series 2008B bonds and the Kent County 2003B bonds as follows:

<u>Amount Swapped</u>	<u>Basis</u>	<u>Counterparty</u>	<u>Effective Date</u>	<u>Expiration Date</u>	<u>Interest Rate</u>	<u>Underlying Issue</u>
\$10,000,000	SIFMA MSI	Wells Fargo	06/05/08	06/01/15	3.28%	Cumberland County 2008B
\$3,115,360	LIBOR	Bank of America	11/28/08	10/31/18	3.73%	Kent County 2003B

The fair value of the interest rate swap liabilities at December 31, 2014 and 2013 are as follows:

<u>Counterparty</u>	<u>Fair Value 12/31/2014</u>	<u>Fair Value 12/31/2013</u>
M&T	\$ -	\$ 55,431
Wells Fargo	134,015	439,013
Bank of America	143,649	219,858
Total	<u>\$ 277,664</u>	<u>\$ 714,302</u>

## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

#### (7) Long-term Debt (continued)

Pursuant to all these agreements the counterparty assumes the risk of varying interest rates, with the difference between the weekly variable rates and the fixed rates above being either paid by, or reimbursed to, the Obligated Group.

#### (8) Note Payable

In December 2014, the Obligated Group entered into a bank loan with Metro Bank for \$5,000,000. Interest on the loan is at a rate of 2.16%. Principal and interest are due in monthly payments and the remaining balance is due and payable on December 10, 2015. As of December 31, 2014, the Obligated Group had \$4,980,267 outstanding under this loan. The loan is collateralized by property and equipment and gross revenues of the Obligated Group.

#### (9) Lines of Credit

The Obligated Group has lines of credit with Bank of America and M&T Bank. Interest rates on these lines of credit are variable. The lines of credit are collateralized by property, plant and equipment of the Obligated Group. As of December 31, 2014 and 2013, under the line of credit agreements, the Obligated Group had available a total maximum of \$16,750,000 from the financial institutions. As of December 31, 2014 and 2013, the Obligated Group had \$15,561,035 and \$11,420,443, respectively, outstanding under these agreements at interest rates ranging from 0.25% to 2.94%.

#### (10) Leases

The Obligated Group is obligated under capital leases for equipment and vehicles that expire in 2018. At December 31, 2014 and 2013, the gross amounts of the equipment and related accumulated amortization recorded under capital leases were as follows:

	<u>2014</u>	<u>2013</u>
Office equipment and vehicles	\$ 1,006,421	724,843
Accumulated amortization	<u>(515,699)</u>	<u>(290,167)</u>
	<u>\$ 490,722</u>	<u>434,676</u>

Amortization expense of \$225,532 and \$157,394 for the years ended December 31, 2014 and 2013, respectively, for the assets held under capital leases is included in depreciation expense in the combined statements of operations and changes in net assets.

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(10) Leases (continued)**

A schedule of future minimum lease payments under the capital leases together with the present value of the net minimum lease payments as of December 31, 2014 follows:

2015	\$ 212,807
2016	175,659
2017	109,128
2018	<u>18,210</u>
	515,804
Amounts representing interest	<u>(15,803)</u>
	<u>\$ 500,001</u>

The Obligated Group leases certain equipment under operating leases, which expire at various dates through 2017. The future minimum lease payments under these operating leases are as follows:

2015	\$ 220,508
2016	116,126
2017	<u>25,552</u>
	<u>\$ 362,186</u>

Rental expense under operating leases was \$716,387 and \$802,030 for the years ended December 31, 2014 and 2013, respectively.

**(11) Annuities**

The Obligated Group has a gift annuity program. In return for their gifts, donors are paid a fixed annuity amount during the lifetime of the donor and/or the donor's beneficiary, which creates a liability of the Obligated Group. Total annuities payable were \$959,356 and \$924,379 at December 31, 2014 and 2013, respectively. The Obligated Group uses published mortality-rate tables adopted by the United States Internal Revenue Service and an assumed discount rate of approximately 4 to 6 percent to determine the present value of the actuarially determined liability. The Obligated Group has assets included in investments of \$1,418,854 and \$1,339,408 as of December 31, 2014 and 2013, respectively, to satisfy annuities.

## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

#### (12) Workers' Compensation Insurance

The Obligated Group has instituted a self-insured Workers' Compensation program as allowed by the Commonwealth of Pennsylvania Bureau of Workers' Compensation. This program provides for self-payment of work related injuries and illnesses as opposed to utilizing an insurance carrier. The Obligated Group has contracted with major insurance carriers for excess insurance coverage, loss control services, and administration. In 2014 and 2013, the Obligated Group maintained a letter of credit for \$3,000,000, in connection with this self-insurance program. At December 31, 2014 and 2013, the Obligated Group has recorded an accrued expense of approximately \$4.7 million and \$5.0 million, respectively, for workers' compensation claims which includes known case reserves and an estimate of the Obligated Group's liability for incurred but not reported claims.

#### (13) Medical Malpractice Claims Coverage

The Obligated Group maintains professional liability coverage on a claims-made basis through a commercial insurance carrier. Other than for premiums paid under this policy, no provision has been made for estimated losses. Management believes no incidents have occurred or will be asserted that will exceed the Obligated Group's insurance coverages or will have a material adverse effect on the combined financial statements.

#### (14) Temporarily Restricted Net Assets

Temporarily restricted net assets as of December 31 are available for the following purposes:

	<u>2014</u>	<u>2013</u>
Trust assets held for the benefit of The Easton Home	\$ 931,201	898,159
Charity care and/or equipment, including pledges receivable		
Endowment	87,260	62,340
Other	2,086,839	1,442,759
Gift annuities	348	880
Contributions receivable from remainder trusts	<u>424,837</u>	<u>367,515</u>
	<u>\$ 3,530,485</u>	<u>2,771,653</u>

Net assets of \$1,341,281 and \$909,622 were released from restriction during 2014 and 2013, respectively, in satisfaction of the above restrictions.

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(15) Permanently Restricted Net Assets**

Permanently restricted net assets are allocated for the following purposes at December 31:

	<u>2014</u>	<u>2013</u>
Trust assets held for the benefit of The Easton Home	\$ 830,086	830,086
Investments to be held in perpetuity, the income from which is expendable to support the following endowments:		
Operations	2,049,812	2,020,042
Scholarships	23,456	23,456
Charity care and/or equipment	2,561,129	2,472,075
Contributions receivable from remainder trusts	225,706	225,597
Gift annuities	15,155	25,155
Beneficial interest in perpetual trusts	<u>14,607,755</u>	<u>14,494,504</u>
	<u>\$ 20,313,099</u>	<u>20,090,915</u>

**(16) Endowment**

The endowments consist of donor restricted funds established for a variety of purposes supporting the Obligated Group. As required by accounting principles generally accepted in the United States of America, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

## **PRESBYTERIAN HOMES OBLIGATED GROUP**

### Notes to Combined Financial Statements

December 31, 2014 and 2013

#### **(16) Endowment (continued)**

##### **Interpretation of Relevant Law**

The Board of Trustees of the Obligated Group has interpreted the relevant state law as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Obligated Group classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as unrestricted and temporarily restricted net assets until those amounts are appropriated for expenditure by the organization in a manner consistent with the standard of prudence prescribed by the relevant state law and donor imposed stipulations. Unless specifically defined, a donor-restricted endowment fund that is required by donor stipulation to accumulate or appropriate endowment funds, the Obligated Group considers the following factors:

- (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 appreciation of investments
- (6) Other resources of the organization
- (7) The investment policies of the organization

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(16) Endowment (continued)**

The following schedule represents the changes in endowment net assets for the year ended December 31, 2014:

	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Endowment net assets, beginning of year	\$ 62,340	4,515,573	4,577,913
Investment return:			
Investment income	71,044	–	71,044
Contributions	–	118,824	118,824
Appropriation of endowment assets for expenditures	<u>(46,124)</u>	<u>–</u>	<u>(46,124)</u>
Endowment net assets, end of year	<u>\$ 87,260</u>	<u>4,634,397</u>	<u>4,721,657</u>

The following schedule represents the changes in endowment net assets for the year ended December 31, 2013:

	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Endowment net assets, beginning of year	\$ 110,726	4,449,998	4,560,724
Investment return:			
Investment income	69,995	–	69,995
Contributions	–	100,271	100,271
Appropriation of endowment assets for expenditures	<u>(118,381)</u>	<u>–</u>	<u>(118,381)</u>
Other changes			
Adjustments for prior year	<u>–</u>	<u>(34,696)</u>	<u>(34,696)</u>
Endowment net assets, end of year	<u>\$ 62,340</u>	<u>4,515,573</u>	<u>4,577,913</u>



## **PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

### **(16) Endowment (continued)**

#### **Funds with Deficiencies**

The fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or the relevant state law requires the Obligated Group to retain as a fund of perpetual duration. In accordance with accounting principles generally accepted in the United States of America, these deficiencies are reported as unrestricted net assets. There were no such deficiencies reported at December 31, 2014 or 2013.

#### **Return Objectives and Risk Parameters**

The Obligated Group has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowments while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Obligated Group must hold in perpetuity for donor-specified purposes. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of a composite of public market indexes based on the mix of investments held, while assuming a moderate level of investment risk. The Obligated Group expects its endowment funds, over time, to provide an average rate of return of approximately the consumer price index plus the investment spending percentage plus one percent annually. Actual returns in any given year may vary from this amount.

#### **Strategies Employed for Achieving Objectives**

The Obligated Group relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Obligated Group targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

## **PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

### **(16) Endowment (continued)**

#### **Endowment Spending Policy and How the Investment Objectives Relate to the Spending Policy**

The Obligated Group has a total return policy for calculating the amounts available for distribution each year. It is a percent of its endowment fund's average fair value over the prior three calendar year ends. This percentage was 3.0% for both 2014 and 2013. Actual distributions are to satisfy donor restrictions. If the total return amount exceeds the actual earnings of the Endowment Funds in any one year, then the amount needed to fund such excess will first be taken from the accumulated excess earnings from prior years, then from the accumulated net capital gains of Endowment Funds and, conversely, any undistributed income after the allocation of the total return distribution is added back to the unrestricted or temporarily restricted fund balance. In establishing this policy, the Obligated Group considered the long-term expected return on its endowment. Accordingly, over the long term, the Obligated Group expects the current spending policy to allow its endowment to grow at an average of inflation plus one percent annually. For 2014 and 2013 an allocation of three percent, of the prior year's balance was used to calculate restricted funds available balance. This is consistent with the Obligated Group's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

### **(17) Retirement Plan**

The Obligated Group has a defined-contribution retirement plan covering all employees that have completed one year of service and have reached the age of 21. Vesting occurs after three years of service. Contributions to the plan are at the discretion of the Board of Trustees of PHI and employees have the ability to direct how their contributions are invested. For the years ended December 31, 2014 and 2013, retirement plan expense totaled approximately \$1,356,138 and \$1,274,031, respectively.

### **(18) Commitments and Contingencies**

The Obligated Group is involved in several legal proceedings arising from its activities in the health care industry. Although it is not possible to presently determine the final outcome of these matters, management believes the aggregate liability, if any, resulting from such proceedings will not have a material adverse effect on the Obligated Group's assets, liabilities, net assets, operations or cash flows.

## PRESBYTERIAN HOMES OBLIGATED GROUP

### Notes to Combined Financial Statements

December 31, 2014 and 2013

#### (19) Financial Instruments

##### (a) *Fair Values of Financial Instruments*

The following valuation techniques were used to measure the fair value of each class of financial instruments:

Money market funds, certificates of deposit and equity and fixed income securities: Fair value of money market funds, certificates of deposit and equity and fixed income securities is based on quoted market prices for the identical security.

Alternative investments: Alternative investments are held in private investment partnerships, which include publically traded securities, real estate and natural resources. Partnership agreements specify the type of investments held, liquidity, manager compensation, and other funding requirements. Management reviews, evaluates and monitors the values provided and agrees with the valuation methods and assumptions used in determining the fair value of the alternative investments. Annual independent audits of each private investment partnership are provided and included in management's review.

Beneficial interest in perpetual trusts and net assets of foundation: Fair value of the beneficial interest in perpetual trusts and net assets of foundation was based on the Obligated Group's percent ownership of the underlying trust assets, which approximate the value of estimated future cash flows to be received from the trust.

Contributions receivable from remainder trusts: Fair value of the contributions receivable from remainder trusts was based on the present value of future cash inflows.

Interest rate swaps: Fair value of the interest rate swaps are based on the net present value of expected future cash flows of the difference between the fixed interest rate of the interest rate swap and the counterparty's forward yield curve. The forward yield curve is readily available in public markets or can be derived from information available in publicly quoted markets.

Long-term debt and notes payable: Long-term debt and notes payable are carried at cost in the combined statements of financial position for notes payable, bonds payable and mortgages payable at December 31, 2014 and 2013. Fair value is based on quoted market prices for the same or similar issues. The totals outstanding were \$206,607,786 and \$210,490,113 at December 31, 2014 and 2013, respectively, and its fair values at December 31, 2014 and 2013 approximates \$210,727,247 and \$216,121,599, respectively.

## **PRESBYTERIAN HOMES OBLIGATED GROUP**

### Notes to Combined Financial Statements

December 31, 2014 and 2013

#### **(19) Financial Instruments (continued)**

The Obligated Group has a number of other financial instruments, none of which are held for investment purposes. The Obligated Group estimates that the fair value of all financial instruments at December 31, 2014 and 2013 does not differ materially from the aggregate carrying values of its financial instruments recorded in the accompanying combined statements of financial position.

The standards for accounting for fair value measurements established a fair value hierarchy that prioritizes the inputs to valuation methods 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 unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities.
- Level 2: Quoted prices in markets that are not active, or inputs that are observable either directly or indirectly for substantially the full term of the asset or liability.
- Level 3: Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported with little or no market activity).

An asset's or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. There have been no changes to the fair value methodologies used to measure fair value at December 31, 2014 or 2013.

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(19) Financial Instruments (continued)**

For assets and liabilities measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2014 are as follows:

<u>Description</u>	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Money market funds	\$ 23,388,778	23,388,778	–	–
Equity securities	38,794,503	38,794,503	–	–
Fixed income securities	18,130,749	18,130,749	–	–
Alternate investments	21,824,952	–	–	21,824,952
Total investments	102,138,982	80,314,030	–	21,824,952
Beneficial interest in perpetual trusts	14,607,755	–	–	14,607,755
Contributions receivable from remainder trusts	650,543	–	–	650,543
Gift annuities	15,503	–	–	15,503
Total assets	\$ 117,412,783	80,314,030	–	37,098,753
Interest rate swaps	\$ (277,664)	–	(277,664)	–

For assets and liabilities measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2013 are as follows:

<u>Description</u>	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Money market funds	\$ 23,609,025	23,609,025	–	–
Equity securities	41,038,873	41,038,873	–	–
Fixed income securities	17,798,902	17,798,902	–	–
Alternate investments	17,156,288	–	–	17,156,288
Total investments	99,603,088	82,446,800	–	17,156,288
Beneficial interest in perpetual trusts	14,494,504	–	–	14,494,504
Contributions receivable from remainder trusts	593,112	–	–	593,112
Gift annuities	26,035	–	–	26,035
Total assets	\$ 114,716,739	82,446,800	–	32,269,939
Interest rate swaps	\$ (714,302)	–	(714,302)	–

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined Financial Statements

December 31, 2014 and 2013

**(19) Financial Instruments (continued)**

For investments falling within Level 3 in the fair value hierarchy, the activity recognized during the year ended December 31, 2014 is as follows:

Description	<u>Alternative Investments</u>	<u>Contributions Receivable from Remainder Trusts</u>	<u>Beneficial Interest in Perpetual Trusts</u>	<u>Gift Annuities</u>
Balance at				
December 31, 2012	\$ 15,665,634	597,391	12,800,949	28,401
Unrealized gains (losses)	1,443,141	(4,279)	1,693,555	(12,366)
Distributions	(3,486,606)	-	-	-
Contributions	3,399,000	-	-	10,000
Realized gains	<u>135,119</u>	<u>-</u>	<u>-</u>	<u>-</u>
Balance at				
December 31, 2013	\$ 17,156,288	593,112	14,494,504	26,035
Unrealized gains (losses)	1,885,529	57,431	113,251	(10,532)
Distributions	(3,821,525)	-	-	-
Contributions	6,553,005	-	-	-
Realized gains	<u>51,655</u>	<u>-</u>	<u>-</u>	<u>-</u>
Balance at				
December 31, 2014	<u>\$ 21,824,952</u>	<u>650,543</u>	<u>14,607,755</u>	<u>15,503</u>

Unrealized and realized gains (losses) on alternative investments are reported as unrestricted and remainder trusts, gift annuities and beneficial interest in perpetual trusts are permanently restricted in the combined statements of operations and changes in net assets.

**(b) Financial Instruments with Off-Balance-Sheet Risk**

Financial instruments with off-balance-sheet risk to the Obligated Group consist of certain financial guarantees of its affiliates and letters of credit obtained from various financial institutions. The Obligated Group's exposure to credit loss in the event of nonperformance by the other party to the financial instrument is represented by the contractual amount of those obligations.

## **PRESBYTERIAN HOMES OBLIGATED GROUP**

Notes to Combined financial statements

December 31, 2014 and 2013

### **(20) Subsequent Events**

On February 12, 2015, the PHI Board of Trustees agreed to enter into an affiliation agreement with Cathedral Village, a Pennsylvania non-profit corporation in Philadelphia. Under the agreement, Cathedral Village will become an affiliated organization.

In March 2015, the Obligated Group entered into an asset purchase agreement with an unrelated third party to sell the assets of the Woodland Retirement Community for \$11,000,000. The terms of the agreement call for the closing to occur within 90 days after the execution of the asset purchase agreement, which occurred on March 9, 2015.

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## Independent Auditor's Report on Supplementary Information

To the Board of Trustees  
Presbyterian Homes Obligated Group

Our audits were made for the purpose of forming an opinion on the combined financial statements taken as a whole. The following supplementary information accompanying the combined financial statements is presented for the purpose of additional analysis and is not a required part of the basic combined financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the combined financial statements. The supplementary information has been subjected to the auditing procedures applied in the audits of the combined financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the combined financial statements 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 basic combined financial statements taken as a whole.

*Arnett Carbis Toothman LLP*

Arnett Carbis Toothman LLP  
New Castle, Pennsylvania  
April 8, 2015



**Presbyterian Homes Obligated Group**

**Combining Schedule of Financial Position**

**December 31, 2014**

<b>Assets</b>	<b>Presbyterian Homes, Inc.</b>	<b>Presbyterian Homes in the Presbytery of Huntingdon</b>	<b>PHI Management Services Corporation</b>	<b>The Long Community</b>	<b>Quincy United Methodist Home</b>	<b>Obligated Group Subtotal</b>	<b>Eliminating Entries</b>	<b>Obligated Group Total</b>
Cash and cash equivalents	\$ 1,748,433	41,354	–	244,030	33,613	2,067,430	–	2,067,430
Investments	9,478,525	8,278,027	47,708,494	8,777,568	3,920,397	78,163,011	–	78,163,011
Statutory liquid reserves	6,992,389	800,407	–	–	800,542	8,593,338	–	8,593,338
Accounts receivable, net	13,047,393	5,593,634	–	26,921	2,967,282	21,635,230	–	21,635,230
Prepaid expenses and other current assets	1,927,166	472,971	11,397	146,254	560,478	3,118,266	–	3,118,266
Assets whose use is limited	6,712,644	2,214,461	2,334,913	–	249,672	11,511,690	–	11,511,690
Assets whose use is limited, construction funds	3,870,943	–	–	–	–	3,870,943	–	3,870,943
Pledges receivable, net	1,066,285	6,400	–	–	–	1,072,685	–	1,072,685
Property and equipment, net	169,678,965	36,494,941	–	41,640,084	13,332,799	261,146,789	–	261,146,789
Assets under capital lease, net	281,129	105,847	–	34,709	69,037	490,722	–	490,722
Due from (to) affiliates, net	50,269,620	4,160,782	12,796,806	(11,055,430)	1,283,961	57,455,739	–	57,455,739
Funds held in trust by others	7,857,399	634,296	–	917,327	5,864,779	15,273,801	–	15,273,801
Beneficial interest in assets of affiliate	1,761,286	–	–	–	–	1,761,286	(1,761,286)	–
Unamortized deferred costs: Deferred financing costs, net	1,750,953	115,861	–	307,366	44,471	2,218,651	–	2,218,651
Other assets	24,182	–	–	–	–	24,182	–	24,182
<b>Total assets</b>	<b>\$ 276,467,312</b>	<b>58,918,981</b>	<b>62,851,610</b>	<b>41,038,829</b>	<b>29,127,031</b>	<b>468,403,763</b>	<b>(1,761,286)</b>	<b>466,642,477</b>

See independent auditor's report on supplementary information.

**Presbyterian Homes Obligated Group**  
**Combining Schedule of Financial Position**  
**December 31, 2014**

<b>Liabilities and Net Assets</b>	<b>Presbyterian Homes, Inc.</b>	<b>Presbyterian Homes in the Presbytery of Huntingdon</b>	<b>PHI Management Services Corporation</b>	<b>The Long Community</b>	<b>Quincy United Methodist Home</b>	<b>Obligated Group Subtotal</b>	<b>Eliminating Entries</b>	<b>Obligated Group Total</b>
Accounts payable	\$ 6,440,384	1,816,971	–	101,419	719,782	9,078,556	–	9,078,556
Accrued expenses - other	8,406,753	3,357,562	22,950	415,331	892,692	13,095,288	–	13,095,288
Notes payable	4,980,267	–	–	–	–	4,980,267	–	4,980,267
Lines of credit	15,561,035	–	–	–	–	15,561,035	–	15,561,035
Accrued interest	597,623	16,164	–	–	–	613,787	–	613,787
Resident deposits	947,118	166,560	–	16,900	53,100	1,183,678	–	1,183,678
Entrance fee payable	17,507,316	1,543,470	–	–	1,166,245	20,217,031	–	20,217,031
Deferred revenue – entrance fees	41,284,422	7,975,233	–	–	8,307,217	57,566,872	–	57,566,872
Fair value of interest rate SWAPS	269,240	8,424	–	–	–	277,664	–	277,664
Annuities payable	819,436	18,728	–	80,578	40,614	959,356	–	959,356
Long-term debt:								
Obligations on capital leases	285,764	107,981	–	34,830	71,426	500,001	–	500,001
Long-term debt	150,358,396	11,047,025	–	34,050,224	6,171,874	201,627,519	–	201,627,519
<b>Total liabilities</b>	<b>247,457,754</b>	<b>26,058,118</b>	<b>22,950</b>	<b>34,699,282</b>	<b>17,422,950</b>	<b>325,661,054</b>	<b>–</b>	<b>325,661,054</b>
Net assets:								
Unrestricted	15,109,525	30,029,151	61,067,374	5,419,877	5,511,912	117,137,839	–	117,137,839
Temporarily restricted	3,179,659	270,764	–	2,343	77,719	3,530,485	–	3,530,485
Permanently restricted	10,720,374	2,560,948	1,761,286	917,327	6,114,450	22,074,385	(1,761,286)	20,313,099
<b>Total net assets</b>	<b>29,009,558</b>	<b>32,860,863</b>	<b>62,828,660</b>	<b>6,339,547</b>	<b>11,704,081</b>	<b>142,742,709</b>	<b>(1,761,286)</b>	<b>140,981,423</b>
<b>Total liabilities and net assets</b>	<b>\$ 276,467,312</b>	<b>58,918,981</b>	<b>62,851,610</b>	<b>41,038,829</b>	<b>29,127,031</b>	<b>468,403,763</b>	<b>(1,761,286)</b>	<b>466,642,477</b>

See independent auditor's report on supplementary information.

Presbyterian Homes Obligated Group  
Combining Schedule of Operations and Changes in Net Assets  
Period ended December 31, 2014

	Presbyterian Homes, Inc.	Presbyterian Homes in the Presbytery of Huntingdon	PHI Management Services Corporation	The Long Community	Quincy United Methodist Home	Obligated Group Subtotal	Eliminating Entries	Obligated Group Total
Operating revenues, gains, and other support:								
Resident services	\$ 105,536,570	39,747,053	-	4,501,185	18,371,159	168,155,967	(6,950)	168,149,017
Interest and dividend income	588,049	401,186	1,478,930	443,428	456,188	3,367,781	(78,744)	3,289,037
Realized gains on investments	(39,305)	190,307	1,304,248	108,625	40,304	1,604,179	(13,598)	1,590,581
Gain on sale of property and equipment and other assets	3,829	-	-	-	15,228	19,057	-	19,057
Contributions, gifts and bequests	218,866	279,899	-	69,840	157,232	725,837	-	725,837
Net assets released from restrictions	1,100,932	137,674	-	21,546	81,129	1,341,281	-	1,341,281
Total operating revenues, gains, and other support	107,408,941	40,756,119	2,783,178	5,144,624	19,121,240	175,214,102	(99,292)	175,114,810
Expenses:								
Nursing services	27,970,985	12,709,613	-	629,421	5,615,388	46,925,407	-	46,925,407
Rehabilitation	4,633,777	2,831,429	-	-	994,262	8,459,468	-	8,459,468
Recreation and special services	3,283,518	1,148,165	-	66,014	592,203	5,089,900	-	5,089,900
Pharmacy	1,614,654	960,217	-	10,614	313,676	2,899,161	-	2,899,161
Social services	439,850	204,155	-	-	76,775	720,780	-	720,780
Physician services	204,132	140,356	-	9,000	59,423	412,911	-	412,911
Food services	11,393,624	4,486,811	-	538,379	1,699,099	18,117,913	-	18,117,913
Building operations and maintenance	11,435,277	3,091,882	-	1,001,591	2,001,212	17,529,962	-	17,529,962
Housekeeping	2,454,800	871,661	-	50,241	268,938	3,645,640	-	3,645,640
Laundry and linen	681,275	413,889	-	327	185,099	1,280,590	(6,950)	1,273,640
General and administrative	16,142,686	5,938,089	248,536	822,326	2,882,606	26,034,243	(6,298)	26,027,945
Employee benefits	7,871,382	3,615,377	-	199,130	1,446,154	13,132,043	-	13,132,043
Interest	3,871,943	418,622	-	1,174,933	257,699	5,723,197	-	5,723,197
Depreciation	8,373,197	2,281,137	-	1,103,842	1,344,052	13,102,228	-	13,102,228
Amortization	126,030	21,521	-	20,545	2,505	170,601	-	170,601
Total expenses	100,497,130	39,132,924	248,536	5,626,363	17,739,091	163,244,044	(13,248)	163,230,796
Income (loss) from continuing operations	6,911,811	1,623,195	2,534,642	(481,739)	1,382,149	11,970,058	(86,044)	11,884,014
Discontinued operations:								
Discontinued operations, net of gain of \$6,460,917 in 2014	6,123,325	-	-	-	-	6,123,325	-	6,123,325
Gain on discontinued operations	6,123,325	-	-	-	-	6,123,325	-	6,123,325
Change in fair value of interest rate swap	413,981	22,657	-	-	-	436,638	-	436,638
Loss on early extinguishment of debt	(108,203)	-	-	-	-	(108,203)	-	(108,203)
Excess of operating revenues, gains and other support over expenses	13,340,914	1,645,852	2,534,642	(481,739)	1,382,149	18,421,818	(86,044)	18,335,774
Other changes:								
Transfer (from) to parent	198,876	-	(446,162)	-	-	(247,286)	-	(247,286)
Reserve for related party receivable	(10,000,000)	-	-	-	-	(10,000,000)	-	(10,000,000)
Unrealized losses on investments	(124,506)	(163,849)	(127,643)	(373,038)	(136,311)	(925,347)	86,044	(839,303)
Total other changes	(9,925,630)	(163,849)	(573,805)	(373,038)	(136,311)	(11,172,633)	86,044	(11,086,589)
Increase (decrease) in unrestricted net assets	3,415,284	1,482,003	1,960,837	(854,777)	1,245,838	7,249,185	-	7,249,185
Temporarily restricted net assets:								
Contributions, gifts and bequests	1,702,101	133,023	-	11,179	110,646	1,956,949	-	1,956,949
Interest and dividend income	71,044	-	-	-	-	71,044	-	71,044
Unrealized gain on investments	63,803	8,317	-	-	-	72,120	-	72,120
Net assets released from restriction	(1,100,932)	(137,674)	-	(21,546)	(81,129)	(1,341,281)	-	(1,341,281)
Change in temporarily restricted net assets	736,016	3,666	-	(10,367)	29,517	758,832	-	758,832
Permanently restricted net assets:								
Contributions, gifts and bequests	124,086	29,770	-	-	-	153,856	-	153,856
Change in fair value of funds held in trust by others	138,809	4,742	33,041	(26,249)	(48,974)	101,369	(33,041)	68,328
Change in permanently restricted net assets	262,895	34,512	33,041	(26,249)	(48,974)	255,225	(33,041)	222,184
Change in net assets	4,414,195	1,520,181	1,993,878	(891,393)	1,226,381	8,263,242	(33,041)	8,230,201
Net assets, beginning of year	24,595,363	31,340,682	60,834,782	7,230,940	10,477,700	134,479,467	(1,728,245)	132,751,222
Net assets, end of year	\$ 29,009,558	32,860,863	62,828,660	6,339,547	11,704,081	142,742,709	(1,761,286)	140,981,423

See independent auditor's report on supplementary information.

**PRESBYTERIAN HOMES OBLIGATED GROUP**

Statutory Minimum Liquid Reserves  
(See Independent Auditor's Report on Supplementary Information)

As of December 31, 2014

	Presbyterian Homes, Inc.	Presbyterian Homes in the Presbytery of Huntingdon	PHI Management Services Corporation	The Long Community	Quincy United Methodist Home	Obligated Group
2015 Budgeted Operating Expenses	\$ 105,275,686	39,465,832	285,125	5,749,987	17,638,892	168,415,522
Less: depreciation expense	(9,095,034)	(2,192,915)	-	(1,100,097)	(1,201,400)	(13,589,446)
Expenses subject to minimum liquid reserve requirement	96,180,652	37,272,917	285,125	4,649,890	16,437,492	154,826,076
Percentage of residents subject to residence and care arrangements at December 31, 2014	39%	20%	0%	0%	46%	
	37,510,454	7,454,583	-	-	7,561,246	52,526,284
Statutory requirement	10%	10%	10%	10%	10%	10%
Statutory minimum liquid reserve requirement	\$ 3,751,045	745,458	0	0	756,125	5,252,628 (a)
Next 12 months debt service payments:						
Total debt service for next 12 months	\$ 10,603,296	1,700,744		2,617,721	500,537	15,422,298
Percentage of residents subject to residence and care arrangements at December 31, 2014	39%	20%	0%	0%	46%	
Statutory minimum liquid reserve requirement	\$ 4,135,285	340,149	-	-	230,247	4,705,681 (b)
Statutory minimum liquid reserve, greater of (a) or (b)	\$ 4,135,285	745,458	-	-	756,125	5,636,868
Total per Bank Statements as of 12/31/2014	\$ 6,992,389	800,407	-	-	800,543	8,593,338
Assets in excess of statutory minimum liquid reserve requirement	\$ 2,857,103	54,949	-	-	44,418	2,956,470

## APPENDIX B

### Calculation of Obligated Group's Debt Service Coverage Ratio and Reserve Ratio

**PHI Obligated Group  
The Bank of New York/Mellon**

<b>Debt Service Coverage Ratio</b>	<u><b>1/1-12/31/14</b></u>	
Excess of Operating Revenues, Gains and Other Support over Expenses	18,335,775	
+/- (Gain)/Loss on sale of property and equipment	(19,057)	
+/- Loss(Gain) on Abandoned Project	-	
+/- Loss(Gain) on Early Extinguishment of debt	108,203	
+/- Revenue/Exp from Discontinued Operations	(6,123,325)	
+/- (Increase)Decrease in fair value of interest rate	<u>(436,638)</u>	
Net Income	11,864,958	
+ Interest Expense (total per AFS format does not include ca	5,723,197	
- Interest Expense on Line of Credit (included in Interest Exp	(339,340)	
+ Depreciation	13,102,228	
+ Amortization Expense	170,601	
+ Entrance fees received in cash during the period (net of ref	14,628,350	
+/- (Increase)Decrease in A/R-RIF 1140-1010-00	(1,737,323)	
- Amortization of entrance fees for the period	<u>(8,873,551)</u>	
<b>Funds Available for Debt Service</b>	<b>34,539,120</b>	
 <b>Maximum Annual Debt Service Requirement (Incl. 20% debt svc on guaranteed debt)</b>	 <b>17,361,424</b>	<b>MADS</b>
Cash Flow coverage as calculated	199%	
Required cash flow coverage	125%	
 <b>Maximum Annual Debt Service Requirement (Incl. 100% debt svc on guaranteed debt)</b>	 <b>18,663,732</b>	<b>MADS</b>
Cash Flow coverage as calculated	185%	
Required cash flow coverage	125%	

The Obligated Group meets its debt service coverage requirement for the 12 month period ending December 31, 2014

PHI Obligated Group  
 The Bank of New York/Mellon

Reserve Ratio covenant shall be tested semiannually as of each June 30th and December 31st (per Section 7.4 of Master Trust Agreement)

**Reserve Ratio:** means, as of any date of calculation, the ratio of (x) the Obligated Group's (i) unrestricted and unencumbered cash and investments and (ii) cash and investments pledged to secure (A) Obligations issued under this Indenture, or (B) bonds, notes or other obligations under any indenture loan agreement, reimbursement agreement or any other agreement that are secured by Obligations, including all moneys held in any debt service reserve fund or other funds or accounts thereunder, notwithstanding that such funds may be pledged to secure specific Obligations or other Indebtedness (excluding amounts in a debt service fund held for payment of interest) but only to the extent that the moneys in such accounts may be used for payment of operating expenses or Debt Service Requirements without third-party consent, to (y) the aggregate principal amount of Long Term Indebtedness of the Obligated Group Outstanding on such date (Definition - p11 of Master Trust Agreement)

Cash and Cash Equivalents		2,067,430	
+ Statutory Minimum Liquid Reserve		8,593,338	
+ Investments		78,163,011	
+ Cash and Investments Pledged to secure debt (incl Debt Serv. Reserve Fund)		3,965,478	
		<u>92,789,257</u>	(x)
Current + Non-current Portion of Long-term Debt	Ob Group	201,627,519	
Current + Non-current Portion Obligation on Capital Leases		500,001	
Current + Non-current Portion Annuities Payable		959,356	
Current + Non-current Portion of Long-term Debt	GMRC	15,115,000	
Current + Non-current Portion of Long-term Debt	Stadium Place	9,918,419	
		<u>228,120,295</u>	(y)
<b>Long Term Indebtedness</b>			
Reserve Ratio as calculated			41% (x)/(y)
Required reserve ratio (1)			25%

The Obligated Group meets its covenant for the period ending December 31, 2014

PHI Obligated Group  
Radian  
Debt Covenant Calculations  
12/31/2014

12/31/2014

**Debt Service Coverage Ratio (Section 704)**

Excess of Operating Revenues, Gains and Other Support over Expenses	18,335,775
Less Gain on sale of assets	(19,057)
Add Loss on Abandoned Project	-
Add Loss on Early Extinguishment of debt	108,203
Plus depreciation and amortization	13,272,829
Less unrealized gain on swap	(436,638)
Plus interest expense, including capitalized interest & interest on lines of credit	5,723,197 <sup>(1)</sup>
	36,984,309
Cash flow	36,984,309
Plus net entrance fees received	12,891,027
Less entrance fee amortization	(8,873,551)
	41,001,785
Net Revenues Available for Debt Service	41,001,785
Maximum annual debt service	17,361,424
Actual Ratio	2.36
Required Ratio	1.20

*Note: Pledges made by donors but not actually collected during the period are immaterial*

Measured on a fiscal year basis only

**Reserve Ratio (Section 705)**

Cash	2,067,430	
Assets whose use is limited	3,965,478	
Investments	78,163,011	
Statutory Liquid Reserves	8,593,338	
Total cash	92,789,257	
Long Term Indebtedness	228,120,295	Incl. GMRC & SP Guarantees
Outstanding long term debt with guarantees	228,120,295	
Actual ratio	0.41	
Required Ratio Effective 12/31/05 and Thereafter	0.30	

Tested Semi-Annually on 6/30 & 12/31

**Short Term Debt (Section 707d)**

Short term debt	20,541,302	B
Operating Revenues from Prior Fiscal Year (i.e., 2013)	163,673,960	A
15% of Net service revenue	24,551,094	
Within requirement by (out of requirement)	4,009,792	A-B=C
AND		

Must be met on an on-going basis

During the fiscal year, short term debt must be reduced to \$0 for a period of seven consecutive days or reduced to an amount not greater than 5% of the total operating revenues for the prior fiscal year for a period of thirty consecutive days. Satisfied requirement from 1/2/2014 through 1/31/2014

Debt Service Coverage is measured on a fiscal year basis only  
Reserve ratio is tested semi-annually on 6/30 and 12/31.



APPENDIX C

Obligated Group Mortgaged Facilities Occupancy Statistics for Filing Fiscal Year

PHI Obligated Group

Section 7.14 of the Master Trust Agreement -

(b) within 45 days after close of each fiscal quarter, quarterly consolidated statements of the Obligated Group's operations

(d) within 30 days of the end of each quarter, marketing and occupancy reports indicating the actual occupancy of the Facilities as a percentage of capacity

(see (a), (c), and (e) for other annual or misc requirements)

	4th Quarter %	12/31/2014 YTD %
<b>Occupancy - NURSING</b>		
Green Ridge Village	92.9%	93.7%
Kirkland Village	93.1%	90.8%
St. Andrew's Village	86.8%	87.1%
Ware Presbyterian Village	95.8%	96.9%
Westminster Village / Allentown	96.6%	96.7%
Westminster Village / Dover	93.1%	92.2%
Subtotal - Presbyterian Homes, Inc.	93.0%	92.2%
The Presbyterian Village at Hollidaysburg	91.9%	92.6%
Westminster Woods at Huntingdon	96.4%	94.4%
Windy Hill Village	97.8%	97.5%
Woodland Retirement Community	81.8%	86.0%
Subtotal - PHPH	91.2%	92.3%
Glen Meadows Retirement Community	97.4%	97.8%
Quincy Village	95.7%	96.7%
Grand Total - NURSING	92.8%	92.8%

	4th Quarter %	12/31/2014 YTD %
<b>Occupancy - PERSONAL CARE (Based on Units)</b>		
The Easton Home	77.0%	87.7%
Green Ridge Village	87.5%	90.1%
Kirkland Village	93.3%	93.4%
St. Andrew's Village	95.6%	97.7%
Ware Presbyterian Village	88.8%	94.1%
Westminster Village / Dover	93.5%	92.6%
Presbyterian Home at Williamsport	74.1%	78.6%
Subtotal - Presbyterian Homes, Inc.	87.1%	90.8%
The Presbyterian Village at Hollidaysburg	89.3%	91.8%
Westminster Woods at Huntingdon	98.3%	97.7%
Windy Hill Village	92.5%	96.8%
Subtotal - PHPH	92.9%	94.7%
Glen Meadows Retirement Community	78.3%	79.1%
Quincy Village	91.5%	95.1%
The Long Community, Inc.	97.7%	96.0%
Grand Total - PERSONAL CARE	88.5%	91.2%

	4th Quarter %	12/31/2014 YTD %
<b>Occupancy - INDEPENDENT LIVING (Based on Units)</b>		
Green Ridge Village	90.5%	84.8%
Kirkland Village	94.8%	94.7%
Mark Kennedy Park	96.9%	98.0%
Moyer House	97.8%	98.8%
St. Andrew's Village (Includes Grace Manor)	98.3%	95.8%
Ware Presbyterian Village	85.7%	86.6%
Westminster Village / Allentown	84.4%	88.8%
Westminster Village / Dover	87.1%	91.3%
Subtotal - Presbyterian Homes, Inc.	90.8%	91.0%
The Presbyterian Village at Hollidaysburg	95.5%	98.6%
Westminster Woods at Huntingdon	92.6%	93.1%
Windy Hill Village	73.3%	86.7%
Woodland Retirement Community	94.3%	96.7%
Subtotal - PHPH	92.6%	94.4%
Glen Meadows Retirement Community	91.8%	90.8%
Quincy Village	97.0%	96.0%
The Long Community, Inc.	99.7%	99.0%
Grand Total - INDEPENDENT LIVING	92.7%	92.7%