

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

Des Plaines, Illinois

CONSOLIDATED FINANCIAL STATEMENTS

Including Independent Auditors' Report

As of and for the Years Ended June 30, 2018 and 2017

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Lutheran Social Services of Illinois
Des Plaines, Illinois

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Lutheran Social Services of Illinois and Subsidiary Corporations (the "Organization"), which comprise the consolidated statements of financial position as of June 30, 2018 and 2017, and the related consolidated statements of activities, cash flows and functional expenses and directly related program services revenue for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Organization as of June 30, 2018 and 2017, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Report on Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying schedule of federal awards and supplemental information, as identified in the table of contents as required by *Title 2 U.S. Code of Federal Regulations Part 200*, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards, are presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated December 18, 2018 on our consideration of the Organization's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Organization's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Organization's internal control over financial reporting and compliance.

Baker Tilly Virchow Krause, LLP

Milwaukee, Wisconsin
December 18, 2018

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
As of June 30, 2018 and 2017

ASSETS	2018	2017
CURRENT ASSETS		
Cash and cash equivalents	\$ 1,180,571	\$ 3,290,060
Accounts receivable, net of allowance for doubtful accounts of \$2,486,359 and \$2,912,824 at June 30, 2018 and 2017, respectively	11,790,048	10,250,129
Current portion of unconditional promises to give, net of allowance for doubtful promises of \$0 at June 30, 2018 and 2017	197,225	167,323
Prepaid expenses and other assets	903,130	521,366
Short-term investments	6,831,726	5,576,888
Short-term investments - pledged as collateral	11,041,030	11,024,527
Assets held for sale	-	520,157
Total Current Assets	31,943,730	31,350,450
INVESTMENTS HELD FOR LONG-TERM PURPOSES	2,603,609	2,649,020
PROPERTY AND EQUIPMENT		
Land	4,187,671	4,187,671
Buildings and other improvements	105,249,416	101,945,025
Furniture and equipment	22,952,538	21,776,446
Construction in progress	-	181,922
Property and Equipment, at cost	132,389,625	128,091,064
Less allowance for depreciation	(70,744,192)	(66,520,424)
Property and Equipment, net	61,645,433	61,570,640
OTHER ASSETS		
Unconditional promises to give, less current portion above	59,970	186,347
Escrow deposit accounts	8,848,888	7,907,339
Tenant deposits in trust	107,994	107,994
Cash surrender value of life insurance contracts	285,361	320,902
Total Other Assets	9,302,213	8,522,582
TOTAL ASSETS	\$ 105,494,985	\$ 104,092,692

See accompanying notes to consolidated financial statements.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION (continued)
As of June 30, 2018 and 2017

LIABILITIES AND NET ASSETS		
	2018	2017
CURRENT LIABILITIES		
Line of credit	\$ 3,999,000	\$ 2,209,000
Current maturities of long-term debt:		
Mortgages payable	655,826	704,481
Capital lease obligations	359,294	77,106
Accounts payable and other accrued expenses	5,781,943	5,461,523
Cash advances for special purposes	58,239	263,636
Accrued interest payable	16,408	16,686
Accrued salaries and wages	3,782,017	4,498,340
Accrued and withheld taxes	684,381	746,406
Deferred gain on sale of property - current	323,272	-
Security deposits	-	4,004
Residents' special deposits	50,286	37,859
Total Current Liabilities	15,710,666	14,019,041
LONG-TERM LIABILITIES		
Long-term debt, less current maturities above:		
Mortgages payable	11,984,058	14,740,691
Capital lease obligations	2,232,799	52,572
Deferred grant revenue from capital advance agreements	41,113,110	42,753,558
Deferred grant revenue from assisted living conversion grant agreement	3,783,151	3,963,307
Deferred grant revenue from federal home loan agreements	78,676	91,348
Deferred gain on sale of property	1,697,177	-
Liability for split interest gift arrangements	631,581	673,951
Liability for pension benefits	10,228,972	13,629,822
Other long-term liabilities	553,042	576,599
Tenant security deposits held in trust	360,124	354,475
Due to HUD - residual receipts	605,820	695,470
Total Long-Term Liabilities	73,268,510	77,531,793
Total Liabilities	88,979,176	91,550,834
NET ASSETS		
Unrestricted	9,713,448	5,778,708
Temporarily restricted by donors	3,974,067	3,934,856
Permanently restricted by donors for endowment	2,828,294	2,828,294
Total Net Assets	16,515,809	12,541,858
TOTAL LIABILITIES AND NET ASSETS	\$ 105,494,985	\$ 104,092,692

See accompanying notes to consolidated financial statements.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

CONSOLIDATED STATEMENTS OF ACTIVITIES
For the Year Ended June 30, 2018

	2018			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
SUPPORT AND REVENUE				
Public Support:				
Lutheran church support	\$ 588,779	\$ -	\$ -	\$ 588,779
United Way	25,888	59,725	-	85,613
Contributions	2,795,954	164,345	-	2,960,299
Bequests	492,148	-	-	492,148
Total Public Support	<u>3,902,769</u>	<u>224,070</u>	<u>-</u>	<u>4,126,839</u>
Other Revenue:				
Fees and grants from government agencies	55,413,181	-	-	55,413,181
Program service fees	17,882,279	-	-	17,882,279
Grant revenue from deferred grant agreements	1,833,276	-	-	1,833,276
Public sales	59,490	-	-	59,490
Rents and investment return	710,594	87,052	-	797,646
Gain on disposal of property and equipment, net	227,966	-	-	227,966
Miscellaneous	185,548	-	-	185,548
Total Other Revenue	<u>76,312,334</u>	<u>87,052</u>	<u>-</u>	<u>76,399,386</u>
Net assets released from restrictions	<u>252,389</u>	<u>(252,389)</u>	<u>-</u>	<u>-</u>
Total Public Support and Revenue	<u>80,467,492</u>	<u>58,733</u>	<u>-</u>	<u>80,526,225</u>
EXPENSES				
Program Services	<u>72,226,588</u>	<u>-</u>	<u>-</u>	<u>72,226,588</u>
Supporting Services:				
Management and general	6,088,316	-	-	6,088,316
Fundraising	1,489,325	-	-	1,489,325
Total Supporting Services	<u>7,577,641</u>	<u>-</u>	<u>-</u>	<u>7,577,641</u>
Total Program and Supporting Services Expense	<u>79,804,229</u>	<u>-</u>	<u>-</u>	<u>79,804,229</u>
CHANGE IN NET ASSETS BEFORE OTHER ITEMS	663,263	58,733	-	721,996
OTHER ITEMS				
Actuarial loss on annuity obligations	-	(19,522)	-	(19,522)
Decrease in actuarial pension costs	<u>3,271,477</u>	<u>-</u>	<u>-</u>	<u>3,271,477</u>
CHANGE IN NET ASSETS	3,934,740	39,211	-	3,973,951
NET ASSETS - Beginning of Year	<u>5,778,708</u>	<u>3,934,856</u>	<u>2,828,294</u>	<u>12,541,858</u>
NET ASSETS - END OF YEAR	<u>\$ 9,713,448</u>	<u>\$ 3,974,067</u>	<u>\$ 2,828,294</u>	<u>\$ 16,515,809</u>

See accompanying notes to consolidated financial statements.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

CONSOLIDATED STATEMENTS OF ACTIVITIES (continued)
For the Year Ended June 30, 2017

	2017			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
SUPPORT AND REVENUE				
Public Support:				
Lutheran church support	\$ 960,640	\$ -	\$ -	\$ 960,640
United Way	32,687	61,251	-	93,938
Contributions	2,502,401	196,348	-	2,698,749
Bequests	873,883	-	-	873,883
Total Public Support	<u>4,369,611</u>	<u>257,599</u>	<u>-</u>	<u>4,627,210</u>
Other Revenue:				
Fees and grants from government agencies	52,719,529	-	-	52,719,529
Program service fees	16,441,795	-	-	16,441,795
Grant revenue from deferred grant agreements	1,833,276	-	-	1,833,276
Public sales	115,267	-	-	115,267
Rents and investment return	1,177,182	150,852	-	1,328,034
Gain on disposal of property and equipment, net	3,230,068	-	-	3,230,068
Miscellaneous	693,114	-	-	693,114
Total Other Revenue	<u>76,210,231</u>	<u>150,852</u>	<u>-</u>	<u>76,361,083</u>
Net assets released from restrictions	<u>365,655</u>	<u>(365,655)</u>	<u>-</u>	<u>-</u>
Total Public Support and Revenue	<u>80,945,497</u>	<u>42,796</u>	<u>-</u>	<u>80,988,293</u>
EXPENSES				
Program Services	<u>72,877,551</u>	<u>-</u>	<u>-</u>	<u>72,877,551</u>
Supporting Services:				
Management and general	5,656,168	-	-	5,656,168
Fundraising	1,537,124	-	-	1,537,124
Total Supporting Services	<u>7,193,292</u>	<u>-</u>	<u>-</u>	<u>7,193,292</u>
Total Program and Supporting Services Expense	<u>80,070,843</u>	<u>-</u>	<u>-</u>	<u>80,070,843</u>
CHANGE IN NET ASSETS BEFORE OTHER ITEMS	874,654	42,796	-	917,450
OTHER ITEMS				
Actuarial loss on annuity obligations	-	(69,303)	-	(69,303)
Decrease in actuarial pension costs	<u>5,542,165</u>	<u>-</u>	<u>-</u>	<u>5,542,165</u>
CHANGE IN NET ASSETS	6,416,819	(26,507)	-	6,390,312
NET ASSETS (DEFICIT) - Beginning of Year	<u>(638,111)</u>	<u>3,961,363</u>	<u>2,828,294</u>	<u>6,151,546</u>
NET ASSETS - END OF YEAR	<u>\$ 5,778,708</u>	<u>\$ 3,934,856</u>	<u>\$ 2,828,294</u>	<u>\$ 12,541,858</u>

See accompanying notes to consolidated financial statements.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended June 30, 2018 and 2017

	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in Net Assets	\$ 3,973,951	\$ 6,390,312
Adjustments to reconcile change in net assets to net cash flows from operating activities		
Depreciation	4,523,996	4,529,022
Change in value of liability for split interest gift arrangements (including charitable annuity lead trust)	19,522	69,303
Amortization of deferred grant revenue from various agreements	(1,833,276)	(1,833,276)
Recognition of income on split interest gift arrangements	(24,860)	(10,412)
Write off of unamortized prepaid bond issuance costs	-	251,764
Amortization of prepaid debt financing costs	12,810	13,749
Gain on disposal of property and equipment	(227,966)	(3,230,068)
Reinvestment of investment income	(162,446)	(155,286)
Net realized and unrealized gain on investments	(390,451)	(707,164)
Increase in cash surrender value of life insurance	(9,881)	(23,134)
Decrease in actuarial pension costs	(3,271,477)	(5,542,165)
Provision for bad debt	753,562	1,087,854
Changes in assets and liabilities:		
Accounts receivable	(2,293,481)	(1,600,112)
Unconditional promises to give	96,475	750,645
Other assets	(381,764)	(143,377)
Restricted deposit accounts	(87,305)	7,222
Accounts payable and other accrued expenses	446,549	(809,485)
Other current liabilities	(971,596)	1,195,668
Pension expense over (under) contributions	(129,373)	2,272,268
Other long-term liabilities	(17,908)	(44,873)
Due to HUD - residual receipts	(89,650)	(1,057,085)
Net Cash Flows from Operating Activities	(64,569)	1,411,370
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	(1,835,793)	(2,187,802)
Proceeds from disposal of property and equipment	435,989	3,633,459
Purchases of investments	(1,805,461)	(2,308,000)
Proceeds from sales of investments	936,944	192,663
Proceeds from surrendering life insurance policies	45,422	4,136
Net withdrawals (deposits to) from residual receipts, replacement reserve, and minimum capital investment	(854,244)	1,365,587
Net Cash Flows from Investing Activities	(3,077,143)	700,043

See accompanying notes to consolidated financial statements.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
Years Ended June 30, 2018 and 2017

	2018	2017
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from mortgage loan	\$ -	\$ 3,393,814
Proceeds from split interest gift arrangements	-	33,303
Proceeds from split interest agreements relinquished	245,164	-
Payments on split interest gift arrangements	(86,712)	(91,610)
Repayment of other debt	(916,229)	(981,166)
Net draws on (repayments under) line of credit	1,790,000	(5,938,000)
Payment of debt financing costs	-	(31,530)
Net Cash Flows from Financing Activities	1,032,223	(3,615,189)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(2,109,489)	(1,503,776)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	3,290,060	4,793,836
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 1,180,571	\$ 3,290,060
 Supplemental cash flow disclosures		
Cash paid for interest	\$ 429,692	\$ 650,399
 Noncash investing and financing activities		
Note payable, accrued interest and mortgage payable refinanced with mortgage payable	\$ -	\$ 2,292,381
Property and equipment purchases financed by capital leases, capital advances and accounts payable	\$ 2,837,498	\$ 60,014
Prepaid expenses financed with mortgage payable	\$ -	\$ 153,706
Escrow deposits transferred with refinance of mortgage payable, net	\$ -	\$ 2,430,608
Deferred gain on sale and leaseback of property	\$ 2,020,449	\$ -
Proceeds from sale used to settle mortgage payable	\$ 2,224,285	\$ 7,506,383
Accrued property taxes and rent settled with proceeds from sale	\$ 118,782	\$ -
Loan costs financed with mortgage payable	\$ -	\$ 218,651
Security deposits transferred with settlement of mortgage payable	\$ 4,004	\$ -

See accompanying notes to consolidated financial statements.

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

CONSOLIDATED STATEMENTS OF FUNCTIONAL EXPENSES AND DIRECTLY RELATED PROGRAM SERVICES REVENUE For the Year Ended June 30, 2018

	2018							Subtotal Program Services
	PROGRAM SERVICES							
	Children's Community Services	Behavioral Health Services	Senior Community Services	Housing Services	Other Operating	Matins, Inc.	Vesper Mgmt Corporation	
FUNCTIONAL EXPENSES								
Salaries	\$ 15,931,528	\$ 12,234,918	\$ 458,897	\$ 4,403,779	\$ -	\$ -	\$ -	\$ 33,029,122
Employee health and retirement benefits, payroll taxes, etc.	<u>4,151,558</u>	<u>2,890,241</u>	<u>64,308</u>	<u>1,439,318</u>	-	-	-	<u>8,545,425</u>
Total salaries and related expenses	20,083,086	15,125,159	523,205	5,843,097	-	-	-	41,574,547
Professional fees and contract service payments	7,983,363	1,798,975	429	380,940	-	138	81,312	10,245,157
Supplies	270,419	754,349	619	387,199	-	-	3,229	1,415,815
Communications	432,658	540,745	5,497	388,002	-	-	2,944	1,369,846
Occupancy	2,495,648	1,174,575	3,547	3,869,739	-	-	116,715	7,660,224
Advertising and printing	86,007	37,448	4,187	123,777	-	-	-	251,419
Local transportation	1,708,547	438,659	11,741	120,416	-	-	-	2,279,363
Meetings, seminars and education	31,095	59,151	-	15,317	-	-	-	105,563
Specific assistance to individuals	510,227	135,446	-	4,648	-	-	-	650,321
Elderly and congregate expenses	-	-	-	142,533	-	-	-	142,533
Equipment rental and maintenance	180,783	333,207	10,743	40,036	-	-	-	564,769
Miscellaneous and other operating	27,410	240,565	3,062	1,277,813	-	115	100	1,549,065
Interest expense	39,778	53,139	345	287,913	-	-	32,159	413,334
Total functional expenses	<u>33,849,021</u>	<u>20,691,418</u>	<u>563,375</u>	<u>12,881,430</u>	-	253	236,459	<u>68,221,956</u>
Depreciation	230,125	408,071	20,955	2,951,941	-	-	393,540	4,004,632
Total Program and Supporting Services Expense	<u>\$ 34,079,146</u>	<u>\$ 21,099,489</u>	<u>\$ 584,330</u>	<u>\$ 15,833,371</u>	<u>\$ -</u>	<u>\$ 253</u>	<u>\$ 629,999</u>	<u>\$ 72,226,588</u>
DIRECTLY RELATED PROGRAM SERVICES REVENUE								
Fees and grants from governmental agencies	\$ 35,610,184	\$ 11,680,331	\$ 236,398	\$ 7,879,601	\$ -	\$ -	\$ -	\$ 55,406,514
Program service fees	194,598	9,997,114	278,672	7,411,895	-	-	-	17,882,279
Grant revenue from deferred grant agreements	-	-	-	1,833,276	-	-	-	1,833,276
Public sales	42,786	-	-	16,704	-	-	-	59,490
Rents and investment return	34,653	19,852	-	140,831	42,126	-	12,336	249,798
Loss on disposal of property and equipment, net	-	-	-	(137)	-	-	(14,351)	(14,488)
Miscellaneous	<u>4,303</u>	<u>101,348</u>	<u>255</u>	<u>36,484</u>	-	6,618	13,409	<u>162,417</u>
Total Directly Related Program Services Revenue	<u>\$ 35,886,524</u>	<u>\$ 21,798,645</u>	<u>\$ 515,325</u>	<u>\$ 17,318,654</u>	<u>\$ 42,126</u>	<u>\$ 6,618</u>	<u>\$ 11,394</u>	<u>\$ 75,579,286</u>

See accompanying notes to consolidated financial statements.

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

CONSOLIDATED STATEMENTS OF FUNCTIONAL EXPENSES AND DIRECTLY RELATED PROGRAM SERVICES REVENUE (continued)
For the Year Ended June 30, 2018

	2018				
	SUPPORTING SERVICES				
	Management and General	Resource Development	The Cornerstone Foundation, Inc.	Subtotal Fundraising	Total
FUNCTIONAL EXPENSES					
Salaries	\$ 2,727,222	\$ 868,507	\$ -	\$ 868,507	\$ 36,624,851
Employee health and retirement benefits, payroll taxes, etc.	703,046	206,071	-	206,071	9,454,542
Total salaries and related expenses	<u>3,430,268</u>	<u>1,074,578</u>	-	1,074,578	46,079,393
Professional fees and contract service payments	690,178	93,737	49,089	142,826	11,078,161
Supplies	50,870	42,993	-	42,993	1,509,678
Communications	141,892	14,518	2,391	16,909	1,528,647
Occupancy	451,848	1,891	-	1,891	8,113,963
Advertising and printing	9,903	94,730	639	95,369	356,691
Local transportation	87,097	27,671	927	28,598	2,395,058
Meetings, seminars and education	61,932	2,337	1,060	3,397	170,892
Specific assistance to individuals	-	-	-	-	650,321
Elderly and congregate expenses	-	-	-	-	142,533
Equipment rental and maintenance	334,376	1,688	-	1,688	900,833
Miscellaneous and other operating	238,765	25,908	52,727	78,635	1,866,465
Interest expense	74,264	-	-	-	487,598
Total functional expenses	<u>5,571,393</u>	<u>1,380,051</u>	<u>106,833</u>	<u>1,486,884</u>	<u>75,280,233</u>
Depreciation	516,923	2,441	-	2,441	4,523,996
Total Program and Supporting Services Expenses	<u>\$ 6,088,316</u>	<u>\$ 1,382,492</u>	<u>\$ 106,833</u>	<u>\$ 1,489,325</u>	<u>\$ 79,804,229</u>
DIRECTLY RELATED PROGRAM SERVICES REVENUE					
Fees and grants from governmental agencies	\$ -	\$ 6,667	\$ -	\$ 6,667	\$ 55,413,181
Program service fees	-	-	-	-	17,882,279
Grant revenue from deferred grant agreements	-	-	-	-	1,833,276
Public sales	-	-	-	-	59,490
Rents and investment return	4,749	-	543,099	543,099	797,646
Gain on disposal of property and equipment, net	242,454	-	-	-	227,966
Miscellaneous	23,131	-	-	-	185,548
Total Directly Related Program Services Revenue	<u>\$ 270,334</u>	<u>\$ 6,667</u>	<u>\$ 543,099</u>	<u>\$ 549,766</u>	<u>\$ 76,399,386</u>

See accompanying notes to consolidated financial statements.

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

CONSOLIDATED STATEMENTS OF FUNCTIONAL EXPENSES AND DIRECTLY RELATED PROGRAM SERVICES REVENUE (continued)
For the Year Ended June 30, 2017

	2017							
	PROGRAM SERVICES							
	Home and Community Services							Subtotal Program Services
Children's Community Services	Behavioral Health Services	Senior Community Services	Housing Services	Other Operating	Matins, Inc.	Vesper Mgmt Corporation		
FUNCTIONAL EXPENSES								
Salaries	\$ 16,097,533	\$ 11,765,220	\$ 413,109	\$ 4,930,653	\$ -	\$ -	\$ -	\$ 33,206,515
Employee health and retirement benefits, payroll taxes, etc.	<u>4,635,765</u>	<u>3,220,790</u>	<u>84,833</u>	<u>1,685,588</u>	-	-	-	<u>9,626,976</u>
Total salaries and related expenses	20,733,298	14,986,010	497,942	6,616,241	-	-	-	42,833,491
Professional fees and contract service payments	7,480,653	1,168,531	3,233	419,088	-	150	201,203	9,272,858
Supplies	282,828	654,112	2,640	421,863	-	-	9,688	1,371,131
Communications	409,479	344,453	5,731	467,708	-	-	8,641	1,236,012
Occupancy	2,142,529	1,102,163	6,634	4,008,719	-	-	502,330	7,762,375
Advertising and printing	48,916	35,494	474	151,175	-	-	-	236,059
Local transportation	1,570,389	383,661	27,652	120,745	-	-	-	2,102,447
Meetings, seminars and education	18,593	202,182	1,208	10,583	-	-	-	232,566
Specific assistance to individuals	368,541	41,924	-	5,365	-	-	-	415,830
Elderly and congregate expenses	-	-	-	128,278	-	-	-	128,278
Equipment rental and maintenance	186,890	279,047	10,310	51,803	-	-	-	528,050
Miscellaneous and other operating	40,807	252,850	3,196	1,486,045	6,291	15	15	1,789,219
Interest expense	17,419	45,621	6,604	587,902	-	-	79,939	737,485
Total functional expenses	<u>33,300,342</u>	<u>19,496,048</u>	<u>565,624</u>	<u>14,475,515</u>	<u>6,291</u>	<u>165</u>	<u>801,816</u>	<u>68,645,801</u>
Depreciation	<u>95,622</u>	<u>409,982</u>	<u>26,036</u>	<u>3,168,910</u>	-	-	<u>531,200</u>	<u>4,231,750</u>
Total Program and Supporting Services Expenses	<u>\$ 33,395,964</u>	<u>\$ 19,906,030</u>	<u>\$ 591,660</u>	<u>\$ 17,644,425</u>	<u>\$ 6,291</u>	<u>\$ 165</u>	<u>\$ 1,333,016</u>	<u>\$ 72,877,551</u>
DIRECTLY RELATED PROGRAM SERVICES REVENUE								
Fees and grants from governmental agencies	\$ 32,737,636	\$ 11,261,866	\$ 194,372	\$ 8,525,655	\$ -	\$ -	\$ -	\$ 52,719,529
Program service fees	346,585	7,643,722	330,459	8,121,029	-	-	-	16,441,795
Grant revenue from deferred grant agreements	-	-	-	1,833,276	-	-	-	1,833,276
Public sales	48,975	-	-	36,573	-	-	-	85,548
Rents and investment return	27,204	21,532	3,150	295,944	40,766	-	82,980	471,576
Gain (loss) on disposal of property and equipment, net	14,622	502,038	-	2,712,151	-	-	(3,143)	3,225,668
Miscellaneous	<u>24,654</u>	<u>371,719</u>	<u>120</u>	<u>219,202</u>	<u>19,744</u>	<u>-</u>	<u>(534)</u>	<u>634,905</u>
Total Directly Related Program Services Revenue	<u>\$ 33,199,676</u>	<u>\$ 19,800,877</u>	<u>\$ 528,101</u>	<u>\$ 21,743,830</u>	<u>\$ 60,510</u>	<u>\$ -</u>	<u>\$ 79,303</u>	<u>\$ 75,412,297</u>

See accompanying notes to consolidated financial statements.

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

CONSOLIDATED STATEMENTS OF FUNCTIONAL EXPENSES AND DIRECTLY RELATED PROGRAM SERVICES REVENUE (continued)
For the Year Ended June 30, 2017

	2017				
	SUPPORTING SERVICES				
	Management and General	Resource Development	The Cornerstone Foundation, Inc.	Subtotal Fundraising	Total
FUNCTIONAL EXPENSES					
Salaries	\$ 2,688,475	\$ 906,034	\$ -	\$ 906,034	\$ 36,801,024
Employee health and retirement benefits, payroll taxes, etc.	850,694	227,165	-	227,165	10,704,835
Total salaries and related expenses	<u>3,539,169</u>	<u>1,133,199</u>	-	<u>1,133,199</u>	<u>47,505,859</u>
Professional fees and contract service payments	695,316	18,887	43,901	62,788	10,030,962
Supplies	37,138	107,327	175	107,502	1,515,771
Communications	113,128	10,469	2,200	12,669	1,361,809
Occupancy	329,132	4,065	-	4,065	8,095,572
Advertising and printing	24,045	83,506	10,270	93,776	353,880
Local transportation	54,004	25,014	316	25,330	2,181,781
Meetings, seminars and education	44,257	1,478	26,655	28,133	304,956
Specific assistance to individuals	-	-	-	-	415,830
Elderly and congregate expenses	-	-	-	-	128,278
Equipment rental and maintenance	242,691	1,803	-	1,803	772,544
Miscellaneous and other operating	226,900	55,396	8,151	63,547	2,079,666
Interest expense	57,428	-	-	-	794,913
Total functional expenses	<u>5,363,208</u>	<u>1,441,144</u>	<u>91,668</u>	<u>1,532,812</u>	<u>75,541,821</u>
Depreciation	292,960	4,312	-	4,312	4,529,022
Total Program and Supporting Services Expenses	<u>\$ 5,656,168</u>	<u>\$ 1,445,456</u>	<u>\$ 91,668</u>	<u>\$ 1,537,124</u>	<u>\$ 80,070,843</u>
DIRECTLY RELATED PROGRAM SERVICES REVENUE					
Fees and grants from governmental agencies	\$ -	\$ -	\$ -	\$ -	\$ 52,719,529
Program service fees	-	-	-	-	16,441,795
Grant revenue from deferred grant agreements	-	-	-	-	1,833,276
Public sales	-	29,719	-	29,719	115,267
Rents and investment return	3,459	-	852,999	852,999	1,328,034
Gain on disposal of property and equipment, net	4,400	-	-	-	3,230,068
Miscellaneous	54,059	4,150	-	4,150	693,114
Total Directly Related Program Services Revenue	<u>\$ 61,918</u>	<u>\$ 33,869</u>	<u>\$ 852,999</u>	<u>\$ 886,868</u>	<u>\$ 76,361,083</u>

See accompanying notes to consolidated financial statements.

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 1 - Summary of Significant Accounting Policies

Nature of Activities

Lutheran Social Services of Illinois ("LSSI"), including the subsidiary corporations included herein (the "Organization"), is a multi-functional social service Organization which is the social ministry expression of the three Illinois Synods of the Evangelical Lutheran Church in America. It is a corporation organized under the laws of the State of Illinois pursuant to the provisions of the "General Not-For-Profit Corporation Act." It is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. The Organization qualifies for the charitable contribution deduction under Section 170(b)(1)(A) and is not a private foundation under Section 509(a)(2). The Organization receives a significant portion of its operating funds from public support, fees and grants from government agencies and program service fees. The Organization's fiscal year ends on June 30. Significant accounting policies followed by the Organization are presented below.

In accordance with authoritative accounting guidance related to reporting of related entities by not-for-profit organizations, twenty-two (22) affiliated not-for-profit corporations incorporated under the Illinois "General Not-For-Profit Corporation Act" are included as subsidiaries in the consolidated financial statements. These corporations are considered subsidiary corporations because LSSI has control over and an economic interest in these corporations. In addition, LSSI Rockford Property, Inc., which is a for-profit subsidiary, is also consolidated as the Organization owns 100 percent of that company. These subsidiary corporations are:

Assisi Homes-Downer Place, Inc.	Luther Center, Inc. **
Aurora Senior Housing, Inc.	Matins, Inc.
Batavia Council on Aging, Inc.	Northwest Chicago Group Homes, Inc.
The Cornerstone Foundation, Inc. ("Foundation")	Our Savior's Senior Housing
Deer Creek Manor, Inc.	Rochelle Senior Housing, Inc.
Dekalb Housing for the Handicapped, Inc.	Rolling Meadows Senior Living, Inc.
Forsberg Christian Retirement Center, Inc. ("Forsberg")*	Salem Village III, Inc.
Freeport Senior Housing, Inc.	Spring Ridge Housing for Seniors, Inc.
Freeport Senior Housing II, Inc.	Tabor Lutheran Senior Housing, Inc.
Fox Hill Senior Housing, Inc.	Vesper Management Corporation
LSSI Rockford Property, Inc.	Victorian Woods Senior Living, Inc.

* In 2016, the building that Forsberg operated from was sold and Forsberg did not have any activity after transferring the net proceeds to the Organization.

** In April 2017, the building Luther Center, Inc. operated was sold and Luther Center, Inc. did not have any activity after transferring the net proceeds to the Organization.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 1 - Summary of Significant Accounting Policies (cont.)

Nature of Activities (cont.)

Services that the Organization provides include:

Children's Community Services:

Child Care Services: child care and Head Start programs designed to develop students' social skills and school readiness.

Foster Care Services: foster care placement and case management for children who have been removed from their birth families due to abuse and/or neglect, to achieve permanency through reunification with families or through adoption.

Home and Community Services:

Behavioral Health Services: counseling, mental health and crisis intervention, drug and alcohol treatment for youth and adults, support and housing for adults with developmental disabilities, and services for formerly incarcerated individuals.

Senior Community and Housing Services: Non-medical assistance to older adults in their homes, and affordable housing for older adults and people over the age of 18 with disabilities.

Consolidated Financial Statement Presentation

The accompanying consolidated financial statements include the accounts of the Organization. All significant transactions among these corporations have been eliminated.

Basis of Accounting

The consolidated financial statements have been prepared using the accrual basis of accounting.

Cash and Cash Equivalents

The Organization considers all liquid investments with a maturity of three months or less when purchased to be cash and cash equivalents.

Receivables

Accounts receivable are uncollateralized funding source obligations, which generally are payable within 30 days from the invoice or billing date. Accounts receivable are stated at the invoice amount.

Payments of accounts receivable are applied to the specific invoices identified on the funding source's remittance advice or, if unspecified, to the earliest unpaid invoices.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 1 - Summary of Significant Accounting Policies (cont.)

Receivables (cont.)

The carrying amount of accounts receivable is reduced by a valuation allowance that reflects management's best estimate of amounts that will not be collected. The allowance for doubtful accounts is based on management's assessment of the collectibility of specific funding source accounts and the aging of accounts receivable. If actual write-offs are higher than the historical experience, management's estimates of the recoverability of amounts due to the Organization could be adversely affected. All accounts or portions thereof deemed to be uncollectible or require an excessive collection cost are written off to the allowance for doubtful accounts.

Unconditional Promises to Give

Unconditional promises to give are recognized as revenue in the period received and as assets or decreases in liabilities, depending on the form of the benefits to be received.

The carrying amount of unconditional promises to give is reduced by a valuation allowance that reflects management's best estimate of amounts that will not be collected. Amounts that are expected to be collected after one year have been discounted at the time the pledge is recorded. The allowance for uncollectible amounts is based on management's assessment of the collectibility of specific promises to give. All accounts or portions thereof deemed to be uncollectible or to require an excessive collection cost are written off to the allowance for doubtful promises to give. The Organization believes unconditional promises to give are fully collectible at June 30, 2018 and 2017 and no allowance has been established.

Conditional promises to give are recognized only when the conditions on which they depend are substantially met and the promises become unconditional. There were no conditional promises to give as of June 30, 2018 and 2017.

Income Taxes

The Organization is recognized by the Internal Revenue Service as a tax exempt organization under Section 501(c)(3) of the Internal Revenue Code and, except for taxes pertaining to unrelated business income, is exempt from federal and state income taxes.

The Organization follows current accounting guidance which addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the consolidated financial statements. Under this guidance, the Organization may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by taxing authorities, based on the technical merits of the position. Examples of tax positions include the tax-exempt status of the Organization and various positions related to the potential sources of unrelated business income. The tax benefits recognized in the consolidated financial statements from such a position are measured based on the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement. The guidance on accounting for uncertainty in income taxes also addresses de-recognition, classification, interest and penalties on income taxes.

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 1 - Summary of Significant Accounting Policies (cont.)

Income Taxes (cont.)

With few exceptions, the Organization is no longer subject to U.S. federal, state or local income tax examinations by tax authorities for the years before 2014. The Organization is not currently under examination by any taxing jurisdiction. It is the Organization's policy to recognize interest and penalties related to unrecognized tax expense when paid.

LSSI Rockford Property, Inc. has a tax year ending December 31. During 2010, LSSI Rockford Property, Inc. completed a sale that was treated for income tax purposes as an installment sale. The deferred tax liability of \$520,475 was included in other long-term liabilities as of June 30, 2018 and 2017 in the consolidated statements of financial position.

Investments

Investments are generally recorded at fair value based upon quoted market prices, when available, or estimates of fair value with gains and losses included in the consolidated statements of activities. Donated securities are recorded at fair value on the date received or at nominal value when the fair value is not readily available. Investments in partnerships that the Organization does not control are recorded based on the equity method.

The Organization's external investment advisors are engaged to monitor and report on portfolio performance and to make recommendations to the Foundation's investment committee as to investment manager selection and or replacement, and asset allocations. Once those recommendations are approved, Organization management executes the necessary transactions to cause the investment portfolio to conform to the use of investment managers and the asset allocation percentages as approved. Monitoring and rebalancing of the investment portfolio is conducted on an on-going basis by management subject to the tolerances within the approved investment policy.

Property and Equipment

Property and equipment are stated at cost, if purchased, or fair value at the date of the gift, if donated. All acquisitions of property and equipment generally in excess of \$1,000 and all expenditures for repairs, maintenance, improvements and betterments that materially prolong the useful lives of assets are capitalized. Maintenance, repairs, and minor improvements are expensed as incurred. When assets are retired or otherwise disposed of, their costs and related accumulated depreciation are removed from the accounts and resulting gains or losses are included in the change in net assets.

Property and equipment are depreciated using the straight-line method over their estimated useful lives as follows:

Buildings	25 - 40 years
Other improvements	5 - 25 years
Furniture and equipment	3 - 7 years

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 1 - Summary of Significant Accounting Policies (cont.)

Impairment of Long-Lived Assets

The Organization reviews long-lived assets for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or the fair value less costs to sell. To date, there have been no such losses recorded due to impairment.

Sale and Lease-back of Property

In September 2017, the Organization entered an agreement to sell one of its properties and lease that property from the purchaser through September 2024. At June 30, 2017, the property is reported in the consolidated statements of financial position as assets held for sale at its net book value of \$520,157. The property was held as collateral on the note payable to the Mission Investment Fund (Note 8) and the note was paid in full at the time of the sale. The lease of the property met the criteria for capitalization and is included in property on the consolidated statements of financial position at June 30, 2018. The capitalized cost, accumulated depreciation, future minimum lease payments and interest are included in Note 8.

The sale price was \$3,000,000 and resulted in a deferred gain of \$2,262,902 at the time of the sale. The gain is recognized in proportion to the amortization of the leased asset. During 2018, \$242,454 was recognized in gain on sale of property on the consolidated statements of activities. The total remaining deferred gain of \$2,020,449 is reported as a liability on the consolidated statements of financial position at June 30, 2018.

Escrow Deposit Accounts

At June 30, 2018 and 2017, the Organization had restricted cash totaling \$8,848,888 and \$7,907,339, respectively, mainly related to replacement reserves, tenant security deposits, residual receipts and minimum capital investments required by the U.S. Department of Housing and Urban Development ("HUD"). HUD regulations require these funds be held in segregated accounts. HUD has provided guidance to the Organization and other housing units on the repayment terms of residual receipts reserve balances. All amounts greater than \$250 per unit, totaling \$605,820 and \$695,470 at June 30, 2018 and 2017, respectively, are reflected as a liability.

Advertising

Non-direct advertising and promotion costs are charged to operations when incurred and for the years ended June 30, 2018 and 2017 the amounts included in operations were \$99,877 and \$116,818, respectively.

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 1 - Summary of Significant Accounting Policies (cont.)

Capital Advance and Assisted Living Conversion Grant Agreements

The deferred grant revenue from the capital advance and assisted living conversion agreements with HUD are being amortized over the terms of the agreements using the straight-line method.

Split Interest Gift Arrangements

The Organization has entered into split interest gift arrangements that are mainly comprised of gift annuities and charitable trusts. Gift annuities provide that the annuitants will receive payments for life. The payments will continue even if related assets have been exhausted. At the death of the annuitants, all remaining assets, if any, are directed in accordance with the related agreements.

Charitable trusts provide that the income beneficiaries will receive payments for life, so long as there are assets available in the trust. At the death of the income beneficiaries, all remaining assets are directed in accordance with the related agreements.

At June 30, 2018 and 2017, the Organization held investments of \$1,734,297 and \$1,840,882, respectively, associated with these split interest agreements, which are recorded as investments held for long-term purposes on the consolidated statements of financial position.

The liability for split interest gift arrangements represents the present value of these obligations due to the annuitants and income beneficiaries. The present value was calculated based upon life expectancies using discount factors determined at the date of the gift that range from 1.2% to 10.6%.

Net Assets

Net assets, revenues, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Organization are classified and reported as follows:

Unrestricted Net Assets - Net assets that are not subject to donor-imposed stipulations.

Temporarily Restricted Net Assets - Net assets subject to donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the Organization pursuant to those stipulations.

Permanently Restricted Net Assets - Net assets subject to donor-imposed stipulations that they be maintained permanently by the Organization.

Distributions

The Organization's regulatory agreements with HUD stipulate among other things, that the Organization will not make distributions of assets or income to any of its officers or directors.

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 1 - Summary of Significant Accounting Policies (cont.)

Support and Revenues

Revenue is presented on the consolidated statements of activities net of billing adjustments.

The Organization receives a significant portion of its operating funds from grants and awards. These funds are reported as unrestricted support as the grants reimburse the Organization for services provided.

The Organization records contributions in accordance with current authoritative accounting guidance relating to accounting for contributions received and contributions made. The Organization receives contributions through pledges, bequests, in-kind gifts, life insurance premium payments, split interest gift arrangements and outright cash gifts. Contributions are classified as unrestricted, temporarily restricted or permanently restricted based on donor restrictions. Split interest gift arrangement receipts are classified partially as contributions and partially as a liability for the present value of the obligation. Upon the death of the annuitants or income beneficiaries, the remaining amount is classified as unrestricted or temporarily restricted based on donor directions.

Contributions that are restricted by the donor are reported as contributions in temporarily restricted or permanently restricted net assets, as appropriate. When a restriction expires, the temporarily restricted net assets are reclassified to unrestricted net assets. Investment income and realized and unrealized gains (losses) resulting from contributions are reported as unrestricted or temporarily restricted net assets, as designated by the donor. Investment income and realized and unrealized gains (losses) restricted by a donor are reported as increases (decreases) in temporarily restricted net assets and released when the restrictions are met.

Donated Services, Materials and Property

The Organization uses the services of volunteers who contribute their time and materials to provide services to the various programs. Volunteer hours utilized in 2018 and 2017 are not reflected in the consolidated financial statements as they generally do not require specialized skills.

Donations of property and equipment are recorded as support at their estimated fair value at the date of donation. Such donations are reported as unrestricted support unless the donor has restricted the donated asset to a specific purpose. Assets donated with explicit restrictions regarding their use and contributions of cash that must be used to acquire property and equipment are reported as restricted support. Absent donor stipulations regarding how long those donated assets must be maintained, the Organization reports expirations of donor restrictions when the donated or acquired assets are placed in service as instructed by the donor.

Functional Allocation of Costs

Certain costs have been allocated among the programs and supporting services benefited.

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 1 - Summary of Significant Accounting Policies (cont.)

Operations

Operating results in the consolidated statements of activities reflect all transactions increasing or decreasing net assets except those items of a long-term nature, that is, those associated with:

Actuarial gains or losses on annuity obligations
Increase or decrease in actuarial pension costs

Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

New Accounting Pronouncements

The Financial Accounting Standards Board ("FASB") has issued Accounting Standards Update ("ASU") 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities* ("ASU 2016-14"). ASU 2016-14 is intended to simplify and improve current net asset classification requirements and the information presented in financial statements and notes about a not-for-profit entity's liquidity, financial performance, expense classifications and cash flows. ASU 2016-14 is effective for fiscal years beginning after December 15, 2017 (fiscal year 2019). Management is currently evaluating the impact of ASU 2016-14 on the Organization's consolidated financial statements.

FASB issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)* ("ASU 2014-09"). ASU 2014-09 establishes principles for recognizing revenue upon the transfer of promised goods or services to customers, in an amount that reflects the expected consideration received in exchange for those goods or services. Amendments defer the effective date of ASU 2014-09, clarify the implementation guidance on principal versus agent considerations, and clarify the identification of performance obligations and the licensing implementation guidance. Topic 606 (as amended) is effective for fiscal years ending after December 15, 2018 (fiscal year 2020). The amendments may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of initial application. The Organization is currently assessing the effect that Topic 606 (as amended) will have on its results of operations, financial position and cash flows.

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 1 - Summary of Significant Accounting Policies (cont.)

New Accounting Pronouncements (cont.)

During June 2018, FASB issued ASU 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. The new guidance is intended to clarify and improve accounting guidance for contributions received and contributions made. The amendments in this ASU should assist entities in (1) evaluating whether transactions should be accounted for as contributions (nonreciprocal transactions) or as exchange (reciprocal) transactions subject to other guidance and (2) determining whether a contribution is conditional. For not-for-profit entities that have conduit debt, ASU 2018-08 is effective for fiscal years beginning after June 15, 2018. All other entities should apply the amendments for fiscal years beginning after December 15, 2018 (fiscal year 2020). The Organization is currently assessing the impact that ASU 2018-08 will have on its results of operations, financial position and cash flows.

In February 2016, FASB issued ASU 2016-02, *Leases (Topic 842)* ("ASU 2016-02") that amends the treatment for leases. The new accounting model for leases capitalizes all leases greater than twelve months, both capital and operating, as assets and liabilities on the statement of financial position. The Organization will be required to apply the standard for fiscal years and reporting periods beginning after December 15, 2019 (fiscal year 2021). Early adoption is permitted. Management is currently evaluating the impact of ASU 2016-02 on the Organization's consolidated financial statements.

FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash* ("ASU 2016-18"). This standard will require cash flow statements to explain the change during a reporting period of the totals for cash, cash equivalents, restricted cash, and restricted cash equivalents. Amounts reported as restricted cash should be included with cash and cash equivalents when reconciling the beginning of period and end of period total amounts shown on the statement of cash flows. The update also includes a requirement that the footnotes to the financial statements explain the nature of the restrictions. The Organization will be required to apply the standard for fiscal years beginning after December 15, 2018 (fiscal year 2020). Early adoption will be permitted and the standard should be applied retrospectively upon adoption. Management is currently evaluating the impact of ASU 2016-18 on the Organization's consolidated financial statements.

FASB issued Accounting Standards Update 2017-07, *Compensation Retirement Benefits (Topic 715) Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost* ("ASU 2017-07"). The standard requires that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered during the period. Other components of the net benefit cost, as defined, are required to be presented in the statement of activities separately from the service cost component and outside a subtotal of income from operations, if one is presented. It must be clear where the other components are reported. The Organization will be required to apply the standard for fiscal years beginning after December 15, 2018 (fiscal year 2020). Early adoption is permitted and the standard should be applied retrospectively. Management is currently evaluating the impact of ASU 2017-07 on the Organization's consolidated financial statements.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 2 - Management's Plan

In 2016 and 2017, the Organization terminated programs that were operating at deficits as a result of negative changes in net assets in fiscal years ended June 30, 2016 and 2015. Additionally, the Organization incurred startup costs in 2016 and 2017 to grow behavioral health services and generate additional revenues.

For the fiscal year ended June 30, 2017, the Organization experienced a positive change in net assets as well as positive net cash flows from operating activities, and disposals of property and equipment. As a result, line-of-credit use was reduced during the year.

The Organization also experienced a positive change in net assets during fiscal year ended June 30, 2018. Management is continuously evaluating other changes in operations to improve financial performance and will adjust its plan accordingly.

NOTE 3 - Unconditional Promises To Give

Unconditional promises to give at June 30 consist of the following:

	<u>2018</u>	<u>2017</u>
Receivable in less than one year	\$ 197,225	\$ 167,323
Receivable in one to five years	<u>75,000</u>	<u>224,352</u>
Total unconditional promises to give	272,225	391,675
Less unamortized discount	<u>(15,030)</u>	<u>(38,005)</u>
Net unconditional promises to give	<u>\$ 257,195</u>	<u>\$ 353,670</u>

NOTE 4 - Fair Value Measurements

The Organization follows authoritative accounting guidance relating to fair value measurements, which provides a framework for measuring, reporting and disclosing fair value under generally accepted accounting principles. This guidance applies to all assets and liabilities that are measured, reported and/or disclosed on a fair value basis.

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NOTE 4 - Fair Value Measurements (cont.)

As defined in current authoritative guidance, fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, the Organization uses various valuation methods including the market, income and cost approaches. The assumptions used in the application of these valuation methods are developed from the perspective of market participants pricing the asset or liability. Inputs used in the valuation methods can be either readily observable, market corroborated, or generally unobservable inputs. Whenever possible the Organization attempts to utilize valuation methods that maximize the use of observable inputs and minimize the use of unobservable inputs. Based on the observability of the inputs used in the valuation methods the Organization is required to provide the following information according to the fair value hierarchy. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values. Assets and liabilities measured, reported and/or disclosed at fair value will be classified and disclosed in one of the following three categories:

Level 1 - Quoted market prices in active markets for identical assets or liabilities.

Level 2 - Observable market based inputs or unobservable inputs that are corroborated by market data.

Level 3 - Unobservable inputs that are not corroborated by market data.

The table below presents the balances of assets measured at fair value on a recurring basis by level within the hierarchy.

	June 30, 2018			
	Level 1	Level 2	Level 3	Total
Cash and money market trust funds	\$ -	\$ 801,067	\$ -	\$ 801,067
Mutual funds	6,030,710	-	-	6,030,710
Beneficial interest in funds held in trust	-	-	829,261	829,261
Investments - restricted for collateral	-	11,041,030	-	11,041,030
Investments - trust accounts for split interest gift arrangements	929,938	804,359	-	1,734,297
Other investment	-	-	40,000	40,000
Total	<u>\$ 6,960,648</u>	<u>\$ 12,646,456</u>	<u>\$ 869,261</u>	<u>\$ 20,476,365</u>

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NOTE 4 - Fair Value Measurements (cont.)

	June 30, 2017			
	Level 1	Level 2	Level 3	Total
Cash and money market trust funds	\$ -	\$ 961	\$ -	\$ 961
Mutual funds	5,575,978	-	-	5,575,978
Beneficial interest in funds held in trust	-	-	808,087	808,087
Investments - restricted for collateral	-	11,024,527	-	11,024,527
Investments - trust accounts for split interest gift arrangements	1,015,734	825,148	-	1,840,882
Total	\$ 6,591,712	\$ 11,850,636	\$ 808,087	\$ 19,250,435

Mutual funds and a majority of the investments - trust accounts for split interest gift arrangements - are measured at fair value using quoted market prices. They are classified as Level 1 as they are traded in an active market.

Cash and money market trust funds, investments - restricted for collateral, and portions of the Charitable Bond mutual funds, Charitable Equity mutual funds, and Tangible Assets mutual funds included within investments - trust accounts for split interest gift arrangements - are measured at fair value using multiple sources of information that are corroborated by market data and are considered Level 2 items.

Beneficial interest in funds held in trust - trusts that the Organization is named as the beneficiary in which they are not the trustee of the assets are considered Level 3 items as the valuation is based on significant unobservable inputs that are not corroborated by market data.

Other investment - consists of ownership of a non-publicly traded company and is considered a Level 3 item as the valuation is based on significant unobservable inputs that are not corroborated by market data.

A determination to classify a financial instrument within Level 3 of the valuation hierarchy is based upon the significance of the unobservable factors to the overall fair value measurement. However, Level 3 financial instruments typically include, in addition to the unobservable or Level 3 components, observable components; accordingly, the gains and losses in the table below include changes in fair value due in part to observable factors that are included within the valuation methodology.

The changes in level 3 assets measured at fair value on a recurring basis are summarized below for the year ended June 30, 2018:

	Beneficial interest in funds held in trust	Other investment
Balance at June 30, 2017	\$ 808,087	\$ -
Net realized and unrealized gains included in the change in net assets	21,174	-
Purchases	-	40,000
Balance at June 30, 2018	\$ 829,261	\$ 40,000

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NOTE 4 - Fair Value Measurements (cont.)

The changes in level 3 assets measured at fair value on a recurring basis are summarized below for the year ended June 30, 2017:

	Beneficial interest in funds held in trust
Balance at June 30, 2016	\$ 850,284
Net realized and unrealized gains included in the change in net assets	52,571
Distributions to LSSI	(94,768)
Balance at June 30, 2017	\$ 808,087

The Organization's financial instruments, excluding investments, consist principally of cash, accounts receivable, unconditional promises to give, other assets, cash surrender value of life insurance, accounts payable, line of credit, a note payable and other liabilities, all whose carrying value approximates fair value as they are short term in nature. Due to the special terms of the agreements, it is not practical to estimate the fair value of the HUD related long-term debt including mortgages payable, capital advances and assisted living conversion agreements.

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NOTE 5 - Short-Term Investments and Investments Pledged as Collateral

Investments and related unrealized appreciation (depreciation) as of June 30, 2018 are summarized as follows:

	<u>Cost or Gift Value</u>	<u>Unrealized Appreciation (Depreciation)</u>	<u>Total Investments at Fair Value</u>
LSSI Funds:			
Mainstay Marketfield Fund	\$ 250,648	\$ 156,308	\$ 406,956
Foundation Funds:			
Schwab Money Market Fund	801,067	-	801,067
MaxSafe Money Market Fund - restricted for collateral	11,041,030	-	11,041,030
Dodge and Cox Fund	862,680	150,693	1,013,373
DFA Emerging Market Fund	209,303	62,774	272,077
Vanguard Short Term Bond	1,819,795	(61,654)	1,758,141
Vanguard Total Stock Market Fund	<u>1,923,916</u>	<u>656,196</u>	<u>2,580,112</u>
Subtotal Foundation funds	<u>16,657,791</u>	<u>808,009</u>	<u>17,465,800</u>
Total short-term investments and short-term investments pledged as collateral	<u>\$ 16,908,439</u>	<u>\$ 964,317</u>	<u>\$ 17,872,756</u>

Investments and related unrealized appreciation (depreciation) as of June 30, 2017 are summarized as follows:

	<u>Cost or Gift Value</u>	<u>Unrealized Appreciation (Depreciation)</u>	<u>Total Investments at Fair Value</u>
LSSI Funds:			
Mainstay Marketfield Fund	\$ 66,000	\$ 234,903	\$ 300,903
Foundation Funds:			
Schwab Money Market Fund	961	-	961
MaxSafe Money Market Fund - restricted for collateral	11,024,527	-	11,024,527
Dodge and Cox Fund	842,065	166,265	1,008,330
DFA Emerging Market Fund	202,841	54,465	257,306
Vanguard Short Term Bond	1,788,221	(25,973)	1,762,248
Vanguard Total Stock Market Fund	<u>1,880,373</u>	<u>366,767</u>	<u>2,247,140</u>
Subtotal Foundation funds	<u>15,738,988</u>	<u>561,524</u>	<u>16,300,512</u>
Total short-term investments and short-term investments pledged as collateral	<u>\$ 15,804,988</u>	<u>\$ 796,427</u>	<u>\$ 16,601,415</u>

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NOTE 5 - Short-Term Investments and Investments Pledged as Collateral (cont.)

For the investments held within the Foundation, interest and dividend income and net realized and unrealized gains (losses) are allocated monthly to unrestricted and temporarily restricted net assets based on the relationship of the net assets of each fund to the total net assets, as adjusted for additions to or deductions from those funds. All other investment earnings are recorded as increases (decreases) in unrestricted net assets.

NOTE 6 - Investments - Held for Long-Term Purposes

Investments related to life annuity contracts and for the Andrew E. Seaver Trust Fund are stated at fair value. Investments and unrealized appreciation (depreciation) at June 30, 2018 are summarized as follows:

	<u>Cost</u>	<u>Unrealized Appreciation (Depreciation)</u>	<u>Fair Value</u>
Foundation investments related to life annuity contracts			
Money Market funds	\$ 67,925	\$ -	\$ 67,925
Charitable Bond mutual funds	555,300	(7,001)	548,299
Charitable Equity mutual funds	735,354	106,536	841,890
Tangible Assets mutual funds	75,318	(6,667)	68,651
Other funds	<u>207,205</u>	<u>327</u>	<u>207,532</u>
Subtotal	<u>1,641,102</u>	<u>93,195</u>	<u>1,734,297</u>
 ELCA Endowment Fund	 <u>621,728</u>	 <u>207,533</u>	 <u>829,261</u>
Unrestricted investments			
Investment in partnership	40,000	-	40,000
Other mutual fund	51	-	51
Subtotal	<u>40,051</u>	<u>-</u>	<u>40,051</u>
Total Investments Held for Long-Term Purposes	<u>\$ 2,302,881</u>	<u>\$ 300,728</u>	<u>\$ 2,603,609</u>

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NOTE 6 - Investments - Held for Long-Term Purposes (cont.)

Investments and unrealized appreciation at June 30, 2017 are summarized as follows:

	<u>Cost</u>	<u>Unrealized Appreciation (Depreciation)</u>	<u>Fair Value</u>
Foundation Investments related to life annuity contracts			
Money Market funds	\$ 45,324	\$ -	\$ 45,324
Charitable Bond mutual funds	635,555	1,844	637,399
Charitable Equity mutual funds	830,593	110,137	940,730
Tangible Assets mutual funds	50,402	(15,982)	34,420
Other funds	<u>178,687</u>	<u>4,322</u>	<u>183,009</u>
Subtotal	1,740,561	100,321	1,840,882
 ELCA Endowment Fund	 621,728	 186,359	 808,087
 Unrestricted investments			
Other mutual fund	<u>51</u>	<u>-</u>	<u>51</u>
Total Investments Held for Long-Term Purposes	<u>\$ 2,362,340</u>	<u>\$ 286,680</u>	<u>\$ 2,649,020</u>

The following schedules summarize the investment return, which includes interest on cash and cash equivalents, short-term and long-term investments, and its classification in the consolidated statements of activities:

	<u>2018</u>		
	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
Interest and dividend income	\$ 165,717	\$ 29,686	\$ 195,403
Net realized and unrealized gains	<u>333,085</u>	<u>57,366</u>	<u>390,451</u>
Total investment return	<u>\$ 498,802</u>	<u>\$ 87,052</u>	<u>\$ 585,854</u>
	 <u>2017</u>		
	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
Interest and dividend income	\$ 315,462	\$ 29,380	\$ 344,842
Net realized and unrealized gains	<u>585,692</u>	<u>121,472</u>	<u>707,164</u>
Total investment return	<u>\$ 901,154</u>	<u>\$ 150,852</u>	<u>\$ 1,052,006</u>

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NOTE 7 - Line of Credit

The Organization has a revolving line of credit agreement with Wintrust Bank for borrowings up to \$11,000,000 which expires on December 18, 2018. The line of credit is secured by a Foundation guaranty in a pledged asset account at Wintrust in a MaxSafe TM account. As of June 30, 2018 and 2017, the fair value of the assets in the pledged account was \$11,041,030 and \$11,024,527, respectively. As of June 30, 2018 and 2017, the Organization's borrowing under the line was \$3,999,000 and \$2,209,000, respectively.

Interest expense on the line of credit was \$108,405 and \$110,119 in 2018 and 2017, respectively.

The Organization and the Foundation are subject to certain covenants. The Organization and the Foundation were in compliance as of June 30, 2018.

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NOTE 8 - Long-Term Debt

Long-term debt at June 30 consists of the following:

	2018	2017
Mortgages Payable:		
P/R Mortgage & Investment Corp. with monthly payments of \$64,828 including interest at 3.38%, until September 1, 2019. Starting October 1, 2019 payments are reduced to monthly payment of \$30,697 including interest at 3.38%. Any remaining principal or interest is due July 1, 2052. The property is secured by a mortgage on the Project's building and land and insured by HUD under Section 223(f) of the National Housing Act. The Project also has a FHA interest subsidy which offsets interest expense until the subsidy expires June 1, 2019. (Salem Village III, Inc.)	\$ 7,916,794	\$ 8,376,800
Mission Investment Fund ("MIF") with monthly payments of \$11,825, including interest at 3.75% adjusted every 3 years to MIF's current rate, due March 31, 2041 secured by land and building. This mortgage was paid in full in September 2017 when the collateral of land and building was sold.	-	2,227,601
Mortgage Payable with P/R Mortgage & Investment Corp. in the amount of \$5,368,000. Monthly payments of \$23,607, including interest at 3.95% were required beginning September 1, 2013, balance due August 1, 2048. The mortgage payable is secured by a mortgage on the rental property and insured by HUD under Section 223(f) of the National Housing Act. (Batavia Council on Aging, Inc.)	4,989,224	5,073,645
HUD with monthly payments of \$5,056, including interest at 7.63%, due July 1, 2021, secured by land and building and cannot be prepaid. (DeKalb Housing for the Handicapped, Inc.)	166,216	212,286
Total Mortgages Payable	13,072,234	15,890,332
Less: Current Maturities	(655,826)	(704,481)
Long-Term Portion of Mortgages Payable	12,416,408	15,185,851
Less: loan costs, net of accumulated amortization	(432,350)	(445,160)
Total Long-Term Portion of Mortgages Payable, Net	\$ 11,984,058	\$ 14,740,691

Legal and accounting fees, printing costs, and other expenses associated with the issuance of debt held by the Organization are included in mortgages payable and are amortized over the term of the mortgages on a straight line basis. Amortization included in interest expense charged to the consolidated statements of activities for the years ended June 30, 2018 and 2017 was \$12,810 and \$13,749, respectively. At June 30, 2018 and 2017, the remaining net amount of debt issuance costs was \$432,350 and \$445,160, respectively.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 8 - Long-Term Debt (cont.)

The following annual principal maturities of the above mortgages for the next five years are as follows:

2019	\$	655,826
2020		335,411
2021		279,549
2022		234,860
2023		238,325
Thereafter		<u>11,328,263</u>
Total	\$	<u>13,072,234</u>

The Organization leases a building and certain equipment that qualify as capital leases during 2018 and 2017. At June 30, 2018 and 2017, the gross value of these assets was \$3,335,171 and \$510,454, respectively, and the related accumulated amortization was \$781,225 and \$372,309, respectively. The assets are included in property and equipment in the consolidated statements of financial position.

The following is a schedule of future minimum lease payments under the capital leases together with the present value of the net minimum lease payments as of June 30, 2018:

2019	\$	463,622
2020		465,662
2021		467,081
2022		469,010
2023		480,736
Thereafter		<u>616,711</u>
Total Future Minimum Lease Payments		2,962,822
Less: Interest		<u>(370,729)</u>
Present Value of Future Minimum Lease Payments		2,592,093
Less: Current Portion		<u>(359,294)</u>
Long-Term Capital Lease Obligations	\$	<u>2,232,799</u>

Total interest expense including amortization of debt issuance costs and other bank fees was \$487,598 and \$794,913 in 2018 and 2017, respectively.

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NOTE 9 - Capital Advance Agreements

The Organization has funded the construction of various housing projects through capital advance agreements with HUD, which provided for borrowings not to exceed \$64,779,300 at June 30, 2018 and 2017. The agreements are given to the HUD Projects in the form of mortgage notes and bear no interest and require no repayment provided that the housing to which it relates remains available for low-income elderly or developmentally disabled persons in accordance with the appropriate regulations. The amount drawn at June 30, 2018 and 2017 was \$64,779,300. Grant revenue from the capital advance agreements is being recognized over the terms of the agreements on a straight-line basis. During the years ended June 30, 2018 and 2017, the Organization recognized revenue of \$1,640,448 on these agreements.

The deferred grant revenue recorded at June 30 consists of capital advance agreements for the following HUD Projects:

	2018			
	Year of Expiration	Amount Drawn to Date	Grant Revenue Recognized to Date	Deferred Grant Revenue
Assisi Homes-Downer Place, Inc.	2039	\$ 7,057,900	\$ 3,224,733	\$ 3,833,167
Our Savior's Senior Housing, Inc.	2035	6,059,600	3,471,600	2,588,000
Tabor Lutheran Senior Housing, Inc.	2038	5,884,600	2,747,944	3,136,656
Rochelle Senior Housing, Inc.	2036	3,531,400	1,916,720	1,614,680
Freeport Senior Housing, Inc.	2033	3,197,300	1,974,798	1,222,502
Northwest Chicago Group Homes, Inc.	2034	1,483,800	900,813	582,987
Freeport Senior Housing II, Inc.	2042	3,039,200	1,185,006	1,854,194
Aurora Senior Housing, Inc.	2040	3,895,500	1,655,082	2,240,418
Victorian Woods Senior Living, Inc.	2046	6,524,200	1,951,807	4,572,393
Spring Ridge Housing for Seniors, Inc.	2048	7,759,800	1,984,696	5,775,104
Rolling Meadows Senior Living, Inc.	2049	3,290,600	734,157	2,556,443
Deer Creek Manor, Inc.	2049	3,568,300	772,464	2,795,836
Fox Hill Senior Housing, Inc.	2053	9,487,100	1,146,370	8,340,730
Total		\$ 64,779,300	\$ 23,666,190	\$ 41,113,110

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NOTE 9 - Capital Advance Agreements (cont.)

	2017			
	Year of Expiration	Amount Drawn to Date	Grant Revenue Recognized to Date	Deferred Grant Revenue
Assisi Homes-Downer Place, Inc.	2039	\$ 7,057,900	\$ 3,042,201	\$ 4,015,699
Our Savior's Senior Housing, Inc.	2035	6,059,600	3,320,112	2,739,488
Tabor Lutheran Senior Housing, Inc.	2038	5,884,600	2,592,400	3,292,200
Rochelle Senior Housing, Inc.	2036	3,531,400	1,828,256	1,703,144
Freeport Senior Housing, Inc.	2033	3,197,300	1,894,194	1,303,106
Northwest Chicago Group Homes, Inc.	2034	1,483,800	863,409	620,391
Freeport Senior Housing II, Inc.	2042	3,039,200	1,108,554	1,930,646
Aurora Senior Housing, Inc.	2040	3,895,500	1,554,774	2,340,726
Victorian Woods Senior Living, Inc.	2046	6,524,200	1,788,019	4,736,181
Spring Ridge Housing for Seniors, Inc.	2048	7,759,800	1,789,480	5,970,320
Rolling Meadows Senior Living, Inc.	2049	3,290,600	651,225	2,639,375
Deer Creek Manor, Inc.	2049	3,568,300	683,928	2,884,372
Fox Hill Senior Housing, Inc.	2053	9,487,100	909,190	8,577,910
Total		<u>\$ 64,779,300</u>	<u>\$ 22,025,742</u>	<u>\$ 42,753,558</u>

NOTE 10 - Federal Home Loan Grant Agreements

The Organization received grants totaling \$190,000 from One Mortgage Partners Corporation, a member of the Federal Home Loan Bank of Chicago, to partially fund the construction of two housing projects. The grants are in the form of mortgage notes which bear no interest and require no repayment provided that the housing to which they relate remains available for low-income elderly persons in accordance with the appropriate regulations and other grant requirements. Grant revenue from the agreements is being recognized over the terms of the agreements on a straight-line basis. During the years ended June 30, 2018 and 2017, the Organization recognized revenue of \$12,672 on these agreements. The deferred revenue recorded at June 30, 2018 and 2017 is \$78,676 and \$91,348, respectively.

NOTE 11 - Assisted Living Conversion Grant Agreement

The Organization has funded the conversion of 56 units at Salem Village III, Inc. ("Salem Village") housing project to assisted living units through an Assisted Living Conversion Grant Agreement with HUD, which provided for borrowings not to exceed \$6,339,159. This agreement provides funding for physical costs of the conversion, legal, architectural and consulting fees, and temporary relocation costs, including vacancy losses. The agreement requires no principal and interest payments as long as Salem Village is used for approved purposes until July 1, 2039. The agreement is secured by the related building. If the Project does not comply with the terms of the agreement, the entire assisted living conversion grant amount would be required to be paid back to HUD.

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NOTE 11 - Assisted Living Conversion Grant Agreement (cont.)

Funding of \$514,240 was recognized in prior years relating to vacancy losses. Remaining grant revenue of \$5,824,919 from this agreement is being recognized over the term of the agreement on a straight-line basis, beginning with the in-service dates of all of the converted units. Revenue realized from the conversion costs for the years ended June 30, 2018 and 2017 was \$180,156. The deferred revenue recorded at June 30, 2018 and 2017 was \$3,783,151 and \$3,963,307, respectively.

NOTE 12 - Pension Plan

Prior to January 1, 2010 the Organization was a participant in the retirement plan for employees of the United Way of Metropolitan Chicago and participating agencies, which covered substantially all employees hired prior to July 1, 2006. As of January 1, 2010, the Pension Equity Plan for employees of Lutheran Social Services of Illinois was separated from the United Way plan. This change had no effect on plan assets, liabilities, employee benefits or Organization funding requirements. The Organization uses a June 30 measurement date for the plan.

As of July 1, 2006, entry by new employees into the Organization's pension plan was frozen. All Organization employees who were hired prior to July 1, 2006 became eligible to participate in the pension plan in accordance with the terms of the plan, and all employees who were participants in the plan on July 1, 2006 shall continue as participants until their benefits are distributed in accordance with the terms of the plan.

During the year ended June 30, 2009, the Organization froze additional benefit accruals under the plan, resulting in a plan curtailment. Participants in the Organization's defined benefit plan became eligible for employer contributions under the Organization's defined contribution plan effective January 1, 2009.

Included in unrestricted net assets at June 30, 2018 and 2017 are the following amounts that have not yet been recognized in net periodic pension cost: unrecognized actuarial net losses of \$10,858,429 and \$14,129,906, respectively. The actuarial loss included in unrestricted net assets and expected to be recognized in net periodic pension costs during the fiscal year ending June 30, 2019 is \$1,322,222.

The table below presents details about the Organization plan including the changes in accumulated benefit obligations, the fair value of plan assets, and funded status for the years ended June 30 (actuarial values of the benefit obligation were calculated as of June 30, 2018 and 2017, respectively).

	<u>2018</u>	<u>2017</u>
Change in benefit obligation		
Accumulated benefit obligation at beginning of year	\$ 39,821,444	\$ 45,749,803
Provision for expenses	500,000	400,000
Interest cost	1,383,396	1,394,661
Actuarial gain	(2,612,317)	(2,770,527)
Settlements**	-	(2,085,914)
Benefits paid	(2,653,030)	(2,866,579)
Administrative expenses paid	<u>(637,973)</u>	<u>-</u>
Accumulated benefit obligation at end of year	<u>\$ 35,801,520</u>	<u>\$ 39,821,444</u>

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NOTE 12 - Pension Plan (cont.)

Since benefit accruals have been frozen, the projected benefit obligation is equal to the accumulated benefit obligation at June 30, 2018 and 2017.

	2018	2017
Change in plan assets		
Fair value of plan assets at beginning of year	\$ 26,191,622	\$ 28,850,084
Actual return on assets	1,283,929	2,144,031
Employer contribution	1,388,000	150,000
Settlements**	-	(2,085,914)
Benefits paid	(2,653,030)	(2,866,579)
Administrative expenses paid	(637,973)	-
	<u>\$ 25,572,548</u>	<u>\$ 26,191,622</u>
Fair value of plan assets at end of year		
Funded status of the plan	<u>\$ (10,228,972)</u>	<u>\$ (13,629,822)</u>
	2018	2017
Components of benefit cost		
Provision for expense	\$ 500,000	\$ 400,000
Interest cost	1,383,396	1,394,661
Expected return on plan assets	(1,773,724)	(1,814,183)
Recognized actuarial loss	<u>1,148,955</u>	<u>1,574,532</u>
Net periodic benefit costs	1,258,627	1,555,010
Cost for settlements**	-	<u>867,258</u>
Total benefit cost	<u>\$ 1,258,627</u>	<u>\$ 2,422,268</u>

** Settlements occurred during 2017 due to the amount of lump sum payments provided to plan participants exceeding the service and interest costs. In 2017 the settlement costs were \$2,085,914. There were no settlement costs in 2018.

The underfunded status of the plan of \$10,228,972 and \$13,629,822 at June 30, 2018 and 2017, respectively, is recognized in the accompanying consolidated statements of financial position as long-term liability for pension benefits.

The following are weighted average assumptions used to determine benefit obligations at June 30:

	2018	2017
Discount rate	4.00%	3.60%

There were no participant contributions made to the plan during the years ended June 30, 2018 and 2017.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 12 - Pension Plan (cont.)

The following are weighted-average assumptions used to determine net periodic benefit cost for the years ended June 30:

	2018	2017
Discount rate	3.60%	3.30%
Expected return on plan assets	6.50%	6.50%

The Organization's expected long-term return on plan assets assumption is based on a periodic review and modeling of the plan's asset allocation over a long-term horizon. Expectations of returns for each asset class are the most important of the assumptions used in the review and modeling and are based on comprehensive reviews of historical data and economic/financial market theory. The expected long-term rate of return on assets was selected from within the reasonable range of rates determined by historical real returns for the asset classes covered by the investment policy.

The Organization's plan assets at June 30, 2018, by asset category are as follows:

	Level 1	Level 2	Level 3	Total
Cash and money market funds	\$ -	\$ 1,492,984	\$ -	\$ 1,492,984
Mutual funds	21,132,751	2,946,813	-	24,079,564
Total	\$ 21,132,751	\$ 4,439,797	\$ -	\$ 25,572,548

The Organization's plan assets at June 30, 2017, by asset category are as follows:

	Level 1	Level 2	Level 3	Total
Cash and money market funds	\$ -	\$ 350,000	\$ -	\$ 350,000
Mutual funds	17,609,817	8,231,805	-	25,841,622
Total	\$ 17,609,817	\$ 8,581,805	\$ -	\$ 26,191,622

Cash and money market funds - These investments are measured at fair value using multiple sources of information that are corroborated by market data and are considered Level 2 items.

Mutual funds - These investments consist of Vanguard Long-Term Investment Grade Fund, Vanguard Intermediate Term Corporate Fund, Dodge and Cox Stock Fund, American Funds Euro Pacific Growth Fund, Harbor International Fund Institutional Class and DFA Emerging Markets Value Fund, and are measured at fair value using quoted market prices. They are classified as Level 1 as they are traded in an active market. In addition, the Organization is invested in the Comerica S&P Composite 1500 Index Fund, which is not actively traded and is considered a Level 2 item.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 12 - Pension Plan (cont.)

The hedge fund was sold in 2017. The hedge fund held at June 30, 2016 consisted of Grosvenor Capital Management LP which is a multi-strategy hedge fund-of-fund. The fund was diversified through various sectors of investments including equity long/short, event driven, multi-strategy, credit, macro, and tail risk managers. Allocations by sector range from 10% to 40% with no individual manager having an allocation greater than 4%. The return objective was between equity and fixed income returns with volatility at half of the equity market.

Hedge funds - Investments in hedge funds have no readily determinable fair value and are classified as Level 3 as the valuation is based on significant unobservable inputs that are not corroborated by market data. The valuation was determined by the investment managers.

The changes in level 3 assets measured at fair value on a recurring basis are summarized below for the year ended June 30, 2017:

	Hedge funds
Balance at June 30, 2016	\$ 3,582,644
Net realized and unrealized gains	182,653
Purchases, sales, issuances and settlements, net	(3,765,297)
Balance at June 30, 2017	\$ -

The Organization's investment policy includes various guidelines and procedures designed to ensure assets are invested in a manner necessary to meet expected future benefits earned by participants. The investment guidelines consider a broad range of economic conditions.

The objectives of the target allocations are to maintain investment portfolios that diversify risk through prudent asset allocation parameters, achieve asset returns that meet or exceed the plan's actuarial assumptions, and achieve asset returns that are competitive with like institutions employing similar investment strategies.

The investment policy is periodically reviewed by the Organization. The policy is established and administered in a manner so as to comply at all times with applicable government regulations.

The estimated net periodic benefit cost for 2019 is:

Provision for expense	\$ 600,000
Interest cost	1,365,895
Expected return on assets	(1,451,355)
Amortization of net loss	807,682
Estimated net periodic benefit cost	\$ 1,322,222

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 12 - Pension Plan (cont.)

The following pension benefit payments are expected to be paid:

2019	\$ 3,308,300
2020	2,453,796
2021	2,560,539
2022	2,553,453
2023	2,409,331
2024-2027	11,926,036

The Organization plans to make contributions of \$8,088,000 to the plan in fiscal year 2019.

The discount rate and expected rate of return on plan assets are critical assumptions which significantly affect pension accounting. Even relatively small changes in these rates would significantly change the recorded pension expense and accrued liability. The expected return on plan assets is computed based on an asset valuation method which recognizes gains/losses over a period of five years. Management believes the discount rate and expected rate of return on plan assets used in determining its year-end pension accounting are reasonable based on currently available information. However, it is at least reasonably possible that these assumed rates will be revised in the near term, based on future events and changes in circumstances.

NOTE 13 - Defined Contribution Retirement Plan

The Organization has adopted a defined contribution retirement plan ("Plan") under Internal Revenue code section 403(b). All Organization employees (except temporary employees) who have completed one year of service are eligible to participate in the Plan. All such eligible employees, who are at least age 21, may elect to make contributions to the Plan through salary deductions. There is no minimum service requirement to make employee contributions to the Plan. Under the Plan, the Organization may make a discretionary annual employer contribution to eligible participants. There was no Organization contribution to the Plan for the years ending June 30, 2018 and 2017.

NOTE 14 - Worker's Compensation Trust

The Organization has a self-funded Worker's Compensation Trust (the "Trust") which is organized and operated under the provisions of the Illinois Religious and Charitable Risk Pooling Trust Act. The trustees of the Trust are appointed by the Organization.

The Organization makes monthly contributions to the Trust. The Organization has recorded a liability for unpaid contributions, which includes unpaid claims and claims incurred but not reported, of \$1,103,353 and \$1,013,802 at June 30, 2018 and 2017, respectively. The estimated liability is classified as accounts payable and other accrued expenses on the consolidated statements of financial position.

The Organization has established a cash reserve account for the worker's compensation trust with a balance of \$1,387,022 and \$1,384,949 at June 30, 2018 and 2017, respectively, which is included in cash and cash equivalents.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 15 - Accrued Salaries and Wages

Accrued salaries and wages include accrued vacation pay of \$1,797,939 and \$1,819,017 at June 30, 2018 and 2017, respectively.

NOTE 16 - Accrued Unemployment

The Organization pays for Illinois unemployment compensation on a claims-made basis. At June 30, 2018 and 2017, \$23,105 and \$200,000, respectively, was accrued as the estimated liability for these claims. These amounts are classified as accounts payable and other accrued expenses on the consolidated statements of financial position.

NOTE 17 - Net Assets

Net assets have been received to be held in perpetuity for several programs. The amounts of these net assets as of June 30 are shown below by program and purpose:

	2018	2017
Adoption services	\$ 131,736	\$ 131,736
Behavioral health	16,248	16,248
Child and adolescent	203,223	203,223
Children and disabled individuals	302,802	302,802
Children and older adults	1,191,190	1,191,190
Endowment for general use	546,194	546,194
Leadership and awards	116,090	116,090
Older adults	267,875	267,875
Other programs	5,575	5,575
Services outside metropolitan Chicago	47,361	47,361
Total Permanently Restricted Net Assets	\$ 2,828,294	\$ 2,828,294

The income from these assets must be used in support of the aforementioned programs and purposes.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 17 - Net Assets (cont.)

Temporarily restricted net assets are available for the following programs, purposes and periods as directed by the donors as of June 30:

	2018	2017
Adoption services	\$ 48,894	\$ 45,588
Administration	306,793	306,793
Behavioral health	256,345	156,956
Child and adolescent	310,164	360,082
Children and disabled individuals	604,232	587,636
Children and older adults	541,231	514,439
Disaster relief	975,809	1,058,088
Leadership and awards	111,106	107,216
Older adults	178,624	147,720
Other programs	<u>640,869</u>	<u>650,338</u>
Total Temporarily Restricted Net Assets	<u>\$ 3,974,067</u>	<u>\$ 3,934,856</u>

Net assets were released from temporary donor restrictions by expending funds for the following purposes during the years ended June 30:

	2018	2017
Behavioral health	34,916	66,000
Child and adolescent	61,435	111,336
Prisoner and family ministry	-	95,934
Transfer for split interest gift arrangements and charitable trusts between unrestricted net assets and net assets temporarily restricted	112,338	24,108
Expiration of time restrictions	<u>43,700</u>	<u>68,277</u>
Total Net Assets Released from Restriction	<u>\$ 252,389</u>	<u>\$ 365,655</u>

NOTE 18 - Endowment Funds

The Organization follows current authoritative accounting guidance relating to endowments of not-for-profit organizations and enhanced disclosures for all endowment funds. Guidance is provided on classifying net assets associated with donor-restricted endowment funds held by organizations that are subject to an enacted version of Uniform Prudent Management of Institutional Funds Act ("UPMIFA"). A key component of the guidance and UPMIFA is a requirement to classify the portion of a donor-restricted endowment fund that is not classified as permanently restricted net assets as temporarily restricted net assets until appropriated for expenditure. Another key component of the guidance is a requirement for expanded disclosures about all endowment funds.

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS As of and for the Years Ended June 30, 2018 and 2017

NOTE 18 - Endowment Funds (cont.)

The Organization's endowment consists of approximately 40 individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees of the Foundation to function as endowment. Any permanently restricted contributions received from donors are included in the donor restricted endowment fund. Any other named fund or special purpose fund that donors have established are included in board-designated endowment and any restrictions are reflected in the endowment. As required by accounting principles generally accepted in the United States of America ("GAAP"), net assets associated with endowment funds, including funds designated by the Foundation's Board of Trustees to function as endowment, are classified and reported based on the existence or absence of donor-imposed restrictions.

The Foundation considers a portion of the funds due from LSSI to be a part of the endowment. The Foundation has advanced LSSI a significant portion of the "Board-designated" endowment funds without interest, during the years ended June 30, 2018 and 2017. The amount loaned to LSSI was \$1,026,581 and \$1,943,827 at June 30, 2018 and 2017, respectively, and the balance is eliminated on the consolidated financial statements. A significant portion of the Foundation's investments are pledged as collateral on the Organization's line of credit (Note 7).

Interpretation of Relevant Law -The Organization classifies as permanently restricted net assets (a) the original value of the gifts donated to the permanent endowment and (b) the original value of subsequent gifts to the permanent endowment.

The remaining portion of the donor-restricted endowment fund that is not classified as permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Organization in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Organization considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund
2. The purposes of the Organization and the donor-restricted endowment fund
3. General economic conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of the Organization
7. The investment policies of the Organization

The following description of the endowment represents the activity at the Foundation. The Foundation guarantees the line of credit which has covenants that include investment limitations. Management of LSSI intends to improve the financial position of the Organization to obtain net asset balances to meet the obligations of the endowment and invest the endowment assets according to its policy.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 18 - Endowment Funds (cont.)

Endowment net asset composition by type of fund consists of the following as of June 30, 2018:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ -	\$ 993,134	\$ 2,828,294	\$ 3,821,428
Board-designated endowment funds	<u>13,579,004</u>	<u>2,030,330</u>	<u>-</u>	<u>15,609,334</u>
Total endowment funds	<u>\$ 13,579,004</u>	<u>\$ 3,023,464</u>	<u>\$ 2,828,294</u>	<u>\$ 19,430,762</u>

Endowment net asset composition by type of fund consists of the following as of June 30, 2017:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ -	\$ 943,298	\$ 2,828,294	\$ 3,771,592
Board-designated endowment funds	<u>13,721,271</u>	<u>2,100,114</u>	<u>-</u>	<u>15,821,385</u>
Total endowment funds	<u>\$ 13,721,271</u>	<u>\$ 3,043,412</u>	<u>\$ 2,828,294</u>	<u>\$ 19,592,977</u>

Changes in endowment net assets for the years ended June 30 are as follows:

	<u>2018</u>			
	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, June 30, 2017	<u>\$ 13,721,271</u>	<u>\$ 3,043,412</u>	<u>\$ 2,828,294</u>	<u>\$ 19,592,977</u>
Investment return				
Investment income	119,823	29,686	-	149,509
Net appreciation realized and unrealized	<u>210,292</u>	<u>57,366</u>	<u>-</u>	<u>267,658</u>
Total investment return	330,115	87,052	-	417,167
Contributions*	482,281	-	-	482,281
Appropriation for expenditure	<u>(954,663)</u>	<u>(107,000)</u>	<u>-</u>	<u>(1,061,663)</u>
Endowment net assets, June 30, 2018	<u>\$ 13,579,004</u>	<u>\$ 3,023,464</u>	<u>\$ 2,828,294</u>	<u>\$ 19,430,762</u>

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 18 - Endowment Funds (cont.)

	2017			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, June 30, 2016	\$ 13,659,361	\$ 2,975,560	\$ 2,828,294	\$ 19,463,215
Investment return				
Investment income	117,579	29,380	-	146,959
Net appreciation realized and unrealized	<u>454,479</u>	<u>121,472</u>	-	<u>575,951</u>
Total investment return	572,058	150,852	-	722,910
Contributions*	359,095	-	-	359,095
Appropriation for expenditure	<u>(869,243)</u>	<u>(83,000)</u>	-	<u>(952,243)</u>
Endowment net assets, June 30, 2017	<u>\$ 13,721,271</u>	<u>\$ 3,043,412</u>	<u>\$ 2,828,294</u>	<u>\$ 19,592,977</u>

*Contributions include other deposits into the Board-designated endowment funds of \$328,294 and \$80,538 in 2018 and 2017, respectively.

Funds with Deficiencies - From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Organization to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature that are reported in unrestricted net assets was \$0 as of both June 30, 2018 and 2017. These deficiencies resulted from unfavorable market fluctuations that occurred after the investment of new permanently restricted contributions. Subsequent gains that restore the fair value of the assets of the endowment fund to the required level will be classified as an increase in unrestricted net assets.

Return Objectives and Risk Parameters - The Organization has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to Organization programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Organization must hold in perpetuity or for a donor-specified period(s) as part of board-designated funds. Under this policy, as approved by the governing board, the endowment assets are invested in a manner that is intended to produce results that exceed 5% annually while assuming a moderate level of investment risk.

Strategies Employed for Achieving Objectives - To satisfy its long-term rate-of-return objectives, the Organization relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Organization targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 18 - Endowment Funds (cont.)

Spending Policy and How the Investment Objectives Relate to Spending Policy - The Organization has a policy of appropriating for distribution each year 4-5% of its endowment fund's average fair value of applicable assets over the lower of the prior 4 or 12 quarters through the calendar year-end preceding the fiscal year in which the distribution is appropriated. In establishing this policy, the Organization considered the long-term expected return on its endowment. Accordingly, over the long term, the Organization expects the current spending policy to allow its endowment to grow at an average of approximately 3% annually. This is consistent with the Organization'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.

NOTE 19 - Lease Agreements

The Organization has entered into lease agreements for land and buildings, under which rental expense for 2018 and 2017 was \$1,556,971 and \$1,287,111, respectively.

Minimum future rental commitments for all operating leases in effect as of June 30, 2018 are summarized as follows:

2019	\$ 1,418,874
2020	1,378,896
2021	1,348,277
2022	991,103
2023	495,623
Thereafter	<u>138,779</u>
Total	<u>\$ 5,771,552</u>

Significant clauses contained in the lease agreements include the following:

- Escalation clauses not exceeding 5% on any given lease,
- Sharing of operation and maintenance costs,
- Ability to cancel a lease if funding for the related program is insufficient,
- Various options to extend the lease term, and
- Liability insurance requirements.

Minimum lease payments exclude rentals under renewal options which, as of June 30, 2018, are not reasonably assured of being exercised.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 20 - Contingencies

The Organization is a defendant in various lawsuits. The final results of such litigation cannot be determined at this time. In the opinion of management, any ultimate liability in these lawsuits would either be within insurance limits or would have no adverse effect on the consolidated financial statements.

As an employer, the Organization is subject to allegations of violation of various laws relating to employment. The Organization's attorneys have advised management that, relative to currently pending complaints, no judgment can be formed as to the likelihood of an unfavorable outcome. Management expects no material liability will be incurred as a result of these complaints.

The grants received by the Organization are subject to audit, and the Organization could become liable for any expenditures disallowed upon audit. Management believes, however, that such disallowance, if any, would not be material.

NOTE 21 - Certain Concentrations

Receivables

As of June 30, the Organization's accounts receivable include amounts due from all sources as follows:

	2018	2017
Illinois Department of Public Aid	\$ 1,015,584	\$ 2,189,275
Illinois Department of Children and Family Services	4,623,921	3,173,196
Illinois Department on Aging	73,815	26,403
Illinois Department of Human Services	1,792,574	2,540,818
Chicago Department of Human Services	252,899	478,304
Managed HUD Projects	437,465	360,434
Medicare	136,359	83,402
Private Pay - Other Client Fees	708,863	690,963
Insurance - Managed Care	5,030,354	3,295,488
Other	204,573	324,670
Total	14,276,407	13,162,953
Less: Allowance for doubtful accounts	(2,486,359)	(2,912,824)
Accounts receivable, net of allowance	\$ 11,790,048	\$ 10,250,129

The Organization receives a significant portion of its revenue and other support from several government units. If these government units terminated their support of the Organization, the Organization's ability to provide the services described in Note 1 could be significantly reduced.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended June 30, 2018 and 2017

NOTE 21 - Certain Concentrations (cont.)

Concentrations of Credit

The Organization maintains its cash deposits at several financial institutions which, at times, may exceed federally insured limits of \$250,000. The Organization has not experienced any losses in such accounts and management believes it is not exposed to any significant credit risk on these deposits.

NOTE 22 - Subsequent Events

In September 2018, a contribution for \$6 million was made to LSSI's pension plan. As part of the transaction, the Foundation advanced \$2 million of its "Board-designated" endowment funds without interest to LSSI. The remainder of the contribution was funded by LSSI by borrowing an additional \$4 million on the line of credit. The amounts advanced to LSSI from the Foundation as of June 30, 2018 and 2017 are disclosed in Note 18. The funds advanced are expected to be reimbursed over a period of years through the Foundation's annual distribution to LSSI and/or through other cash resources.

The Organization has evaluated subsequent events through December 18, 2018, which is the date that the consolidated financial statements were available to be issued, for events requiring disclosure or recording in the consolidated financial statements.

OTHER INDEPENDENT AUDITORS' REPORTS

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER
MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS

INDEPENDENT AUDITORS' REPORT

Board of Directors
Lutheran Social Services of Illinois
Des Plaines, Illinois

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the consolidated financial statements of Lutheran Social Services of Illinois (the "Organization"), which comprise the consolidated statement of financial position as of June 30, 2018, and the related consolidated statements of activities, cash flows and functional expenses and directly related program services revenue for the year then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated December 18, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered the Organization's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Organization's consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Baker Tilly Virchow Krause, LLP

Milwaukee, Wisconsin
December 18, 2018

REPORT ON COMPLIANCE FOR THE MAJOR FEDERAL PROGRAM AND REPORT ON INTERNAL
CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE

INDEPENDENT AUDITORS' REPORT

Board of Directors
Lutheran Social Services of Illinois
Des Plaines, Illinois

Report on Compliance for the Major Federal Program

We have audited Lutheran Social Services of Illinois' (the "Organization") compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on the Organization's major federal program for the year ended June 30, 2018. The Organization's major federal program is identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

The Organization's basic consolidated financial statements include the operations of subsidiaries of the Organization, as identified in the notes to the schedule of expenditures of federal awards, which received federal awards that are not included in the Organization's schedule of expenditures of federal awards during the year ended June 30, 2018. Our audit, described below, did not include the operations of those entities because they have separate audits under the Uniform Guidance or do not require an audit under the Uniform Guidance.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal program.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for the Organization's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Organization's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of the Organization's compliance.

Opinion on the Major Federal Program

In our opinion, the Organization complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2018.

Other Matters

The results of our auditing procedures disclosed an instance of noncompliance, which is required to be reported in accordance with the Uniform Guidance and which is described in the accompanying schedule of findings and questioned costs as item 2018-001. Our opinion on the major federal program is not modified with respect to this matter.

The Organization's response to the noncompliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. The Organization's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control Over Compliance

Management of the Organization is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Organization's internal control over compliance with the types of requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we did identify a certain deficiency in internal control over compliance, described in the accompanying schedule of findings and questioned costs as item 2018-002, that we consider to be a significant deficiency.

The Organization's response to the internal control over compliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. The Organization's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Baker Tilly Virchow Krause, LLP

Milwaukee, Wisconsin
March 25, 2019

SUPPLEMENTARY INFORMATION

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended June 30, 2018

Federal Awards Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Pass-Through Grantor's Number	Federal Expenditures	Subrecipient Awards
U.S. DEPARTMENT OF AGRICULTURE				
Passed through the Illinois State Board of Education				
School Breakfast Program	10.553	05-016-120P-00	\$ 6,556	\$ -
National School Lunch Program	10.555	05-016-120P-00	10,797	-
Total of Child Nutrition Cluster			<u>17,353</u>	
Passed through the Illinois State Board of Education				
Child and Adult Care Food Program	10.558	05-016-120P-00	94,391	-
Total U.S. Department of Agriculture			<u>111,744</u>	-
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES				
Passed through the Illinois Department of Children and Family Services				
Promoting Safe & Stable Families	93.556	013005-804-7	3,446	-
Promoting Safe & Stable Families	93.556	013005-804-8	6,081	-
Promoting Safe & Stable Families	93.556	013005-905-8	211,645	-
Total of CFDA 93.556			<u>221,172</u>	-
Passed through the Illinois Department of Human Services				
Child Care Development Block Grant	93.575	80408490-W	7,549	-
Total of CCDF Cluster			<u>7,549</u>	-
Passed through City of Chicago Department of Family and Support Services				
Head Start**	93.600	32008	157,055	-
Head Start**	93.600	33351	732,768	-
Total of CFDA 93.600			<u>889,823</u>	-
Passed through the Illinois Department of Human Services				
Social Services Block Grant	93.667	FCSWR01028	217,970	-
Block Grants for Community Mental Health Services	93.958	45CWB00426 & 45CWB00425	150,387	-
Passed through the Illinois Department of Human Services - Office of Alcoholism and Substance Abuse				
Block Grants for Prevention and Treatment of Substance Abuse	93.959	43CWC00181	1,106,334	-
Block Grants for Prevention and Treatment of Substance Abuse	93.959	43CWZ03220	171,451	-
Total of CFDA 93.959			<u>1,277,785</u>	-
Total U.S. Department of Health and Human Services			<u>\$ 2,764,686</u>	<u>\$ -</u>

See accompanying notes to schedule of expenditures of federal awards.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (continued)
For the Year Ended June 30, 2018

Federal Awards Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Pass-Through Grantor's Number	Federal Expenditures	Subrecipient Awards
CORPORATION FOR NATIONAL AND COMMUNITY SERVICE				
Direct				
Retired and Senior Volunteer Program	94.002	N/A	\$ 143,787	\$ -
Passed through the Illinois Department of Public Health				
AmeriCorps	94.006	87380011F	<u>54,590</u>	<u>-</u>
Total Corporation for National and Community Service			<u>198,377</u>	<u>-</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 3,074,807</u>	<u>\$ -</u>

** Indicates program tested as a major program in 2018.

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS For the Year Ended June 30, 2018

Basis of Presentation

The accompanying schedule of expenditures of federal awards (the "schedule") includes the federal award activity of the Organization, except as noted below, under programs of the federal government for the year ended June 30, 2018. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* ("Uniform Guidance"). Because the schedule presents only a selected portion of the operations of the Organization, it is not intended to and does not present the financial position, changes in net assets or cash flows of the Organization.

Expenditures for the following consolidated subsidiaries of the Organization are not included to meet the requirements of the cost principles contained in the Uniform Guidance because they have separate audits or are not required to have an audit under Uniform Guidance:

Assisi Homes - Downer Place, Inc.	Northwest Chicago Group Homes, Inc.
Aurora Senior Housing, Inc.	Our Savior's Senior Housing
Batavia Council on Aging, Inc.	Rochelle Senior Housing, Inc.
Deer Creek Manor, Inc.	Rolling Meadows Senior Living, Inc.
Dekalb Housing for the Handicapped, Inc.	Salem Village III, Inc.
Fox Hill Senior Housing, Inc.	Spring Ridge Housing for Seniors, Inc.
Freeport Senior Housing, Inc.	Tabor Lutheran Senior Housing, Inc.
Freeport Senior Housing II, Inc.	Victorian Woods Senior Living

Summary of Significant Accounting Policies

Expenditures reported on the schedule are reported on the cash basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Negative amounts shown on the schedule represent adjustments or credits made in the normal course of business to amounts reported as expenditures in prior years. Pass-through entity identifying numbers are presented where available.

Indirect Cost Rate

The Organization has not elected to use the 10-percent de minimis indirect cost rate allowed under the Uniform Guidance.

Subrecipients

The Organization provided no federal awards to subrecipients.

Federal Loan Programs

The awards presented in the schedule do not include any federal loans administered by the Organization.

Non-Cash Assistance

The Organization did not receive any non-cash federal awards.

Federal Insurance

The awards presented in the schedule do not include any federal insurance in effect during 2018.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
For the Year Ended June 30, 2018

Section I: Summary of Auditors' Results

Financial Statements

Type of report the auditors issued on whether the financial statements audited were prepared in accordance with GAAP:	unmodified		
Internal control over financial reporting:			
Material weakness(es) identified?	_____ yes	_____ <u>X</u> _____ no	none reported
Significant deficiency(ies) identified?	_____ yes	_____ <u>X</u> _____	reported
Noncompliance material to financial statements noted?	_____ yes	_____ <u>X</u> _____	no

Federal Awards

Internal control over major federal programs:			
Material weakness(es) identified?	_____ yes	_____ <u>X</u> _____	no none reported
Significant deficiency(ies) identified	_____ <u>X</u> _____	_____ yes _____	reported
Type of auditors' report issued on compliance for major federal programs:	unmodified		
Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?	_____ <u>X</u> _____	_____ yes _____	no

Identification of major federal programs:

CFDA Number	Name of Federal Program or Cluster
93.600	Headstart

Dollar threshold used to distinguish between Type A and Type B programs	\$ 750,000
Auditee qualified as low-risk auditee?	_____ <u>X</u> _____ yes _____ no

LUTHERAN SOCIAL SERVICES OF ILLINOIS AND SUBSIDIARY CORPORATIONS

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued) For the Year Ended June 30, 2018

Section II: Financial Statement Findings

There were no findings.

Section III: Federal Award Findings and Questioned Costs

2018-001

Agency: U.S. Department of Health and Human Services passed through City of Chicago Department of Family and Support Services

CFDA Number and Program Name: 93.600 - Head Start

Criteria: The grantor requires the Organization to comply with the requirements of the program which include the requirement that 10% of funded Head Start enrollment be provided to children with disabilities.

Statement of Condition: The Organization did not comply with the requirement that 10% of funded Head Start enrollment must be provided to children with disabilities for the period July 2017 through November 2017. In December, the contract was amended and the Organization did exceed the 10% requirement for the period December 2017 through June 2018.

Questioned Costs: The amount of questioned costs cannot be determined.

Context: Management identified that the Organization was not in compliance. As a result, management submitted reports to the funder communicating that the requirement was not met and amended the contract during year which led to the Organization being in compliance.

Effect: The Organization was not in compliance with the earmarking requirement of the grant for a portion of the fiscal year.

Cause: The Organization was not able to enroll enough participants with disabilities to meet the 10% requirement for a portion of the year.

This is a repeat finding (prior years 2017-001 and 2016-001).

Recommendation: We recommend management continue to monitor its compliance with the requirement of the contract.

Management's Response: The Organization's Head Start program is committed to providing care and services to all eligible families and children, including those with disabilities. Management has corrected this finding but will continue the following plan to maintain compliance:

- LSSI staff will continue to work with the Chicago Public Schools (CPS) and families to identify children in need.
- LSSI's Quality and Compliance Manager will continue to monitor screening, referral and submission process of all enrolled children.
- LSSI will continue contracted services with a translation company to support children and families with diverse languages.
- LSSI will continue to use recruitment letters to reach out to organizations and schools with families of special needs children to develop partnerships.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
For the Year Ended June 30, 2018

Section III: Federal Award Findings and Questioned Costs (continued)

2018-002

Agency: U.S. Department of Health and Human Services passed through City of Chicago Department of Family and Support Services

CFDA Number and Program Name: 93.600 - Head Start

Criteria: The Uniform Guidance requires that the Organization have controls over the period of performance compliance requirement to ensure expenditures are recorded and charged to the funder in the proper period.

Statement of Condition: The Organization has controls over payroll and other expenditures to ensure allowable costs are recorded in the proper period of performance. We found the controls surrounding non-payroll expenses not occurring as designed to confirm costs were charged in the correct period.

Questioned Costs: There were no questioned costs.

Context: Not applicable.

Effect: We identified certain areas within the control system surrounding compliance that could lead to noncompliance not being immediately identified.

Cause: Employee turnover and lack of training led to certain oversight controls not consistently occurring at the beginning of the contract period.

Recommendation: We recommend that management review current internal controls surrounding month end close to accurately capture and record expenditures in the correct period. Additional training could also be advisable.

Management's Response: LSSI management will review current internal controls related to recording expenses in correct financial and contractual periods. LSSI management will refresh program and business staff on the importance of reviewing expenses prior to the close of financial and contractual periods, follow up with vendors for timely submission of invoices, and accrue expenses when invoices are not submitted timely.

**LUTHERAN SOCIAL SERVICES OF ILLINOIS
AND SUBSIDIARY CORPORATIONS**

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
For the Year Ended June 30, 2018

2017-001

Agency: U.S. Department of Health and Human Services passed through City of Chicago Department of Family and Support Services

CFDA Number and Program Name: 93.600 - Head Start

Criteria: The grantor requires the Organization to comply with the requirements of the program which include the requirement that 10% of funded Head Start enrollment be provided to children with disabilities.

Statement of Condition: The Organization did not comply with the requirement that 10% of funded Head Start enrollment must be provided to children with disabilities.

Questioned Costs: The amount of questioned costs cannot be determined.

Context: Management identified that the Organization was not in compliance. As a result, management submitted reports to the funder communicating that the requirement was not met and is implementing plans to correct the condition.

Effect: The Organization is not in compliance with the earmarking requirement of the grant.

Cause: The Organization was not able to enroll enough participants with disabilities to meet the 10% requirement.

This is a repeat finding (prior year 2016-001).

Recommendation: We recommend management continue to work with their funders to amend the contract requirements and continue to advertise and promote the program to those with disabilities.

Management's Response: The Organization's Head Start program is committed to providing care and services to all eligible families and children, including those with disabilities. The plan to address the 10% of funding to be provided to children with disabilities is as follows:

- LSSI has an ongoing implementation plan to meet the federal mandate of having 10% of children with disabilities.
- LSSI staff work with the Chicago Public Schools (CPS) and families to identify children in need. Some of these children, after screenings, are determined not eligible for services and some families also decline further evaluations. For the upcoming year, we will work more diligently with parents to understand the value of early intervention and ensure we have strong referral for and individual education plan (IEP) that CPS will not deem unqualified for services.
- Staff were trained in August 2017 and February 2018 regarding timely observing and screening of children and how to interpret the screenings and working with families.
- A translation company was contracted to support children and families with diverse languages.
- Recruitment letters were sent out in September 2017 and January 2018 to reach out to other organizations and schools with families with special needs children to develop partnerships.

This finding has been repeated as finding 2018-001.



1001 E. Touhy Avenue, Suite 50
Des Plaines, Illinois 60018
LSSI.org
PHONE 847.635.4600
FAX 847.635.6764

Summary Schedule of Audit Findings
For Year Ended June 30, 2018

Finding 2018-001

93.600 Head Start

– The organization did not comply with requirement that 10% of funded Head Start enrollment must be provided to children with disabilities from July 1, 2017 – November 30 2017.

Status – Correction Action in Progress

Corrective Action – the program is committed to meeting our compliance obligations. The action plan is as follows

Lutheran Social Services of Illinois' Head Start program is committed to providing care and services to all eligible families and children, including those with disabilities. The plan to address the 10% of funding to be provided to children with disabilities is as follows:

- LSSI has an ongoing implementation plan to meet the federal mandate of having 10% of children with disabilities. The number of children with disabilities that LSSI was responsible for during July 1, 2017 through November 30, 2017 was 14. This was reduced to 9 from December 1, 2017 through June 30, 2018 based on a city-wide slot reduction. Between 9/6/17 – 8/2/18 LSSI had 9 children evaluated by CPS, with 6 additional IEPs received, bringing the program year total to 12.
- LSSI staff will continue to work with the Chicago Public Schools (CPS) and families to identify children in need. Some of these children, after screenings, are determined not eligible for services and some families also decline further evaluations. For the upcoming year, we will continue to work diligently with parents to understand the value of early intervention and ensure we have strong referral for and individual education plan (IEP) that CPS will not deem unqualified for services.
- Continued staff training will occur to keep staff focused on timely observing and screening of children and how to interpret the screenings and working with families.
- LSSI continues to work with a translation company to support children and families with diverse languages.
- Recruitment letters continue to be sent out to reach other organizations and schools to develop partnerships connecting LSSI with families of special needs children.
- The Quality and Compliance Manager continues to monitor screening, the referral and submission process of all enrolled children.

Prepared by:

Norma Moore/Program Director

Lutheran Social Services of Illinois/Community Child Care

1001 E Touhy Ave, Des Plaines, IL 60018

847-635-4445

Norma.Moore@lssi.org

LSSI.org



Lutheran Social Services of Illinois

1001 E. Touhy Avenue, Suite 50
Des Plaines, Illinois 60018
LSSI.org
PHONE 847.635.4600
FAX 847.635.6764

Summary Schedule of Audit Findings For Year Ended June 30, 2018

Finding 2018-002

93.600 Head Start

– The Organization did not comply with the Uniform Guidance requirement to have controls over the period of performance compliance requirement to ensure expenditures are recorded and charged to the funder in the proper period.

Status – Correction Action in Progress

Corrective Action – the Organization is committed to meeting our compliance obligations. The action plan is as follows:

- LSSI management will review current internal controls related to recording expenses in correct financial and contractual periods.
- LSSI management will refresh program and business staff on the importance of reviewing expenses prior to the close of financial and contractual periods, follow up with vendors for timely submission of invoices, and accrual of expenses when invoices are not submitted timely.

Prepared by:
Elizabeth Winke/Controller
Lutheran Social Services of Illinois/Community Child Care
1001 E Touhy Ave, Des Plaines, IL 60018
847-390-1401
Elizabeth.Winke@lssi.org
LSSI.org