# Lutheran Child and Family Services of Illinois

Financial Report
June 30, 2017

**Contents**

RSM US LLP

## Independent Auditor's Report

To the Board of Trustees
Lutheran Child and Family Services of Illinois

**Report on the Financial Statements**
We have audited the accompanying consolidated financial statements of Lutheran Child and Family Services of Illinois (Agency) which comprise the consolidated statement of financial position as of June 30, 2017, and the related consolidated statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the consolidated financial statements (collectively, the financial statements).

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

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

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

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

**Opinion**
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Lutheran Child and Family Services of Illinois as of June 30, 2017, and the changes in its net assets and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

**Report on Summarized Comparative Information**

We have previously audited Lutheran Child and Family Services of Illinois' 2016 consolidated financial statements, and we expressed an unmodified audit opinion on those audited consolidated financial statements in our report dated April 24, 2017. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2016, is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

RSM US LLP

Chicago, Illinois
January 23, 2018

**Lutheran Child and Family Services of Illinois**

**Consolidated Statement of Financial Position**
**June 30, 2017 (With Comparative Totals for 2016)**

| | **2017** | 2016 |
|---|---|---|
| **Assets** | | |
| Cash and cash equivalents | **$ 159,731** | $ 582,435 |
| Accounts receivable, net | **7,230,639** | 4,832,198 |
| Contributions receivable, net | **471,198** | 554,296 |
| Prepaid expenses | **168,743** | 373,658 |
| Investments | **4,611,326** | 4,354,399 |
| Property and equipment, net | **4,832,615** | 5,176,216 |
| Other assets | **23,864** | 27,285 |
| Beneficial interest in perpetual trusts | **3,523,164** | 3,402,542 |
| | **$ 21,021,280** | $ 19,303,029 |
| **Liabilities and Net Assets** | | |
| Accounts payable | **$ 5,436,822** | $ 3,777,698 |
| Accrued expenses | **3,035,652** | 2,694,156 |
| Line of credit | **2,994,854** | 2,244,814 |
| Long-term debt | **4,418,023** | 4,540,008 |
| Accrued pension liability | **3,075,347** | 4,309,101 |
| Other liabilities | **490,912** | 559,363 |
| | **19,451,610** | 18,125,140 |
| Net assets: | | |
| Unrestricted: | | |
| Other | **306,720** | 803,129 |
| Net actuarial pension loss | **(3,906,806)** | (5,277,183) |
| | **(3,600,086)** | (4,474,054) |
| Temporarily restricted | **1,566,004** | 2,169,233 |
| Permanently restricted | **3,603,752** | 3,482,710 |
| | **1,569,670** | 1,177,889 |
| | **$ 21,021,280** | $ 19,303,029 |

See notes to consolidated financial statements.

**Lutheran Child and Family Services of Illinois**

**Consolidated Statement of Activities**
**Year Ended June 30, 2017 (With Comparative Totals for 2016)**

| | 2017 | | | | |
|---|---|---|---|---|---|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total | 2016 Total |
| Revenue: | | | | | |
| Contributions | $ 535,269 | $ 446,861 | $ - | $ 982,130 | $ 1,145,704 |
| Legacies and bequests | 803,551 | 4,993 | - | 808,544 | 1,156,961 |
| Contributions by associated congregations | 106,444 | - | - | 106,444 | 106,312 |
| In-kind contributions from food depositories | 558,472 | - | - | 558,472 | 576,978 |
| Allocations from federated fundraising organizations - United Way organizations | 128,552 | - | - | 128,552 | 189,329 |
| Fees and grants from governmental agencies | 30,084,290 | - | - | 30,084,290 | 28,893,122 |
| Other revenue: | | | | | |
| Program service fees | 1,778,476 | - | - | 1,778,476 | 1,944,086 |
| Program grants | 198,258 | - | - | 198,258 | 338,668 |
| Income from thrift shops | 375,716 | - | - | 375,716 | 368,917 |
| Miscellaneous | (20,735) | - | - | (20,735) | (20,806) |
| Rental income | 9,811 | - | - | 9,811 | 16,227 |
| Release of net assets arising from satisfaction of restrictions | 1,088,499 | (1,088,499) | - | - | - |
| | 35,646,603 | (636,645) | - | 35,009,958 | 34,715,498 |
| Expenses: | | | | | |
| Program services | 31,748,199 | - | - | 31,748,199 | 31,634,641 |
| Supporting services: | | | | | |
| Management and general expenses | 4,109,317 | - | - | 4,109,317 | 3,985,209 |
| Fundraising | 508,024 | - | - | 508,024 | 555,915 |
| Thrift shops | 81,227 | - | - | 81,227 | 86,818 |
| Investment fund | 44,929 | - | - | 44,929 | 48,908 |
| | 4,743,497 | - | - | 4,743,497 | 4,676,850 |
| Operating expenses | 36,491,696 | - | - | 36,491,696 | 36,311,491 |
| **Decrease in net assets before other changes in net assets** | (845,093) | (636,645) | - | (1,481,738) | (1,595,993) |

(Continued)

**Lutheran Child and Family Services of Illinois**

**Consolidated Statement of Activities (Continued)**
**Year Ended June 30, 2017 (With Comparative Totals for 2016)**

| | 2017 | | | | |
|---|---|---|---|---|---|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total | 2016 Total |
| Other changes in net assets: | | | | | |
| Investment income | $ 85,332 | $ - | $ 420 | $ 85,752 | $ 69,079 |
| Gains (losses) on investments | 263,352 | 33,416 | - | 296,768 | (1,797) |
| Change in value of perpetual trusts | - | - | 120,622 | 120,622 | (273,803) |
| Gain on sale of fixed assets | - | - | - | - | 254,635 |
| Pension-related changes other than net periodic benefit costs | 1,370,377 | - | - | 1,370,377 | (1,500,316) |
| | 1,719,061 | 33,416 | 121,042 | 1,873,519 | (1,452,202) |
| **Increase (decrease) in net assets** | 873,968 | (603,229) | 121,042 | 391,781 | (3,048,195) |
| Net assets: | | | | | |
| Beginning of year | (4,474,054) | 2,169,233 | 3,482,710 | 1,177,889 | 4,226,084 |
| End of year | $ (3,600,086) | $ 1,566,004 | $ 3,603,752 | $ 1,569,670 | $ 1,177,889 |

See notes to consolidated financial statements.

**Lutheran Child and Family Services of Illinois**

**Consolidated Statement of Functional Expenses**
**Year Ended June 30, 2017 (With Comparative Totals for 2016)**

| | 2017 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Core Programs | | | | | | |
| | Adoption | Family Counseling | Home-Based | Foster Care | Community Service | Residential | Total |
| Functional expenses: | | | | | | | |
| Salaries | $ 451,938 | $ 137,799 | $ 605,520 | $ 7,079,974 | $ 228,537 | $ 4,554,890 | $ 13,058,658 |
| Taxes and benefits | 93,555 | 35,836 | 157,540 | 1,836,775 | 57,511 | 978,041 | 3,159,258 |
| Salaries, taxes and benefits | 545,493 | 173,635 | 763,060 | 8,916,749 | 286,048 | 5,532,931 | 16,217,916 |
| Professional fees | 4,476 | 2,445 | 234,345 | 3,124,240 | - | 234,823 | 3,600,329 |
| Supplies | 1,267 | 798 | 10,471 | 96,699 | 576,403 | 338,753 | 1,024,391 |
| Telephone | 4,438 | 2,748 | 3,907 | 71,494 | 9,610 | 69,713 | 161,910 |
| Postage and shipping | 1,339 | - | 581 | 8,862 | 49 | 2,211 | 13,042 |
| Occupancy | 40,192 | 24,329 | 28,946 | 793,974 | 50,189 | 366,129 | 1,303,759 |
| Outside printing and artwork | - | 73 | 848 | 18,567 | - | 1,111 | 20,599 |
| Local transportation | 17,973 | 5,597 | 61,524 | 1,317,675 | 11,727 | 97,779 | 1,512,275 |
| Conferences and meetings | 160 | 2,943 | 218 | 11,936 | 5,479 | 27,977 | 48,713 |
| Specific assistance - foster board | - | - | - | 5,257,695 | - | 9,814 | 5,267,509 |
| Specific assistance - other | 407 | 298 | 38,966 | 369,173 | 4,484 | 68,181 | 481,509 |
| Membership dues | - | - | - | 126 | - | 3,854 | 3,980 |
| Equipment rental, repairs and maintenance | 1,820 | 188 | 611 | 12,386 | 2,458 | 59,795 | 77,258 |
| Insurance | 13,325 | 4,172 | 21,855 | 259,662 | 8,349 | 145,153 | 452,516 |
| Interest | - | - | - | 38 | (17,562) | 846 | (16,678) |
| Depreciation and amortization | 1,165 | 3,110 | 906 | 19,754 | 5,772 | 103,108 | 133,815 |
| Other | - | - | - | - | - | - | - |
| Total expenses before allocation of supporting expenses | 632,055 | 220,336 | 1,166,238 | 20,279,030 | 943,006 | 7,062,178 | 30,302,843 |
| Allocation of supporting services: | | | | | | | |
| Program administration | 257 | (6,772) | 1,208 | 4,528 | - | 779 | - |
| Management and general | 108,927 | 27,423 | 150,244 | 2,608,601 | 119,635 | 911,550 | 3,926,380 |
| Total program and supporting service expenses | $ 741,239 | $ 240,987 | $ 1,317,690 | $ 22,892,159 | $ 1,062,641 | $ 7,974,507 | $ 34,229,223 |

See notes to consolidated financial statements.

| 2017 | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Supporting | | | | Supporting | Other Programs | | | |
| Occupancy Allocation | Management and General | Nice Twice | Fund Raising | Total LCFS Operations | Investment Fund | Camp Wartburg | Lifelink | Total | 2016 Total |
| $ 223,725 | $ 1,779,142 | $ 46,252 | $ 294,089 | $ 15,401,866 | $ - | $ 484,874 | $ 99,824 | $ 15,986,564 | $ 16,311,218 |
| 51,972 | 456,165 | 12,029 | 76,482 | 3,755,906 | - | 126,099 | 23,978 | 3,905,983 | 3,671,486 |
| 275,697 | 2,235,307 | 58,281 | 370,571 | 19,157,772 | - | 610,973 | 123,802 | 19,892,547 | 19,982,704 |
| 720 | 1,032,436 | 1,828 | 21,706 | 4,657,019 | 37,538 | 12,856 | 24,105 | 4,731,518 | 4,010,192 |
| 58,965 | 29,211 | 1,544 | 63,275 | 1,177,386 | - | 175,294 | 481 | 1,353,161 | 1,446,585 |
| 117,149 | 53,988 | 1,022 | 118 | 334,187 | 727 | 8,351 | 1,710 | 344,975 | 327,932 |
| 26,813 | 13,705 | - | 6,851 | 60,411 | - | 3,522 | 1,413 | 65,346 | 84,539 |
| (564,429) | 132,553 | 11,748 | 22,452 | 906,083 | 6,619 | 148,480 | 8,712 | 1,069,894 | 1,095,091 |
| 1,991 | 40,019 | 515 | 2,512 | 65,636 | - | 13,626 | 365 | 79,627 | 117,089 |
| 12,113 | 78,189 | 774 | 5,168 | 1,608,519 | - | 13,968 | 2,819 | 1,625,306 | 1,634,799 |
| 1,233 | 73,195 | 1,071 | 2,774 | 126,986 | - | 4,352 | 241 | 131,579 | 93,107 |
| - | - | - | - | 5,267,509 | - | - | - | 5,267,509 | 5,538,373 |
| 1,261 | 1,924 | 1,830 | 309 | 486,833 | - | - | 1,419 | 488,252 | 457,817 |
| 105 | 63,045 | - | - | 67,130 | 45 | 4,285 | - | 71,460 | 82,180 |
| 103,992 | 11,825 | - | 1,778 | 194,853 | - | 4,796 | - | 199,649 | 207,396 |
| 16,264 | 70,057 | 1,068 | 10,140 | 550,045 | - | 22,118 | 3,317 | 575,480 | 679,445 |
| 33 | 250,333 | - | - | 233,688 | - | 31,515 | - | 265,203 | 193,132 |
| 53,150 | 21,535 | 96 | 370 | 208,966 | - | 117,779 | - | 326,745 | 361,110 |
| - | 1,995 | 1,450 | - | 3,445 | - | - | - | 3,445 | - |
| 105,057 | 4,109,317 | 81,227 | 508,024 | 35,106,468 | 44,929 | 1,171,915 | 168,384 | 36,491,696 | 36,311,491 |
| - | - | - | - | - | - | - | - | - | - |
| 6,923 | (4,091,816) | 10,448 | 65,370 | (82,695) | 12,262 | 35,633 | 34,800 | - | - |
| $ 111,980 | $ 17,501 | $ 91,675 | $ 573,394 | $ 35,023,773 | $ 57,191 | $ 1,207,548 | $ 203,184 | $ 36,491,696 | $ 36,311,491 |

**Lutheran Child and Family Services of Illinois**

**Consolidated Statement of Cash Flows**
**Year Ended June 30, 2017 (With Comparative Totals for 2016)**

| | | **2017** | | 2016 |
|---|---|---|---|---|
| Cash flows from operating activities: | | | | |
| Increase (decrease) in net assets | **$** | **391,781** | $ | (3,048,195) |
| Adjustments to reconcile increase (decrease) in net assets to net cash used in operating activities: | | | | |
| Depreciation and amortization | | **326,745** | | 361,110 |
| Allowance for doubtful accounts | | **(383,823)** | | 328,965 |
| (Gains) losses on investments | | **(296,768)** | | 1,797 |
| Change in value of perpetual trusts | | **(120,622)** | | 273,803 |
| Pension-related changes other than net periodic benefit costs | | **(1,370,377)** | | 1,500,316 |
| Changes in: | | | | |
| Accounts/contributions receivable | | **(1,931,520)** | | (656,899) |
| Prepaid expenses | | **204,915** | | 109,955 |
| Other assets | | **3,421** | | 9,281 |
| Accounts payable and accrued expenses | | **2,000,620** | | 957,261 |
| Other liabilities | | **68,172** | | 160,411 |
| **Net cash used in operating activities** | | **(1,107,456)** | | (2,195) |
| Cash flows from investing activities: | | | | |
| Purchases of property and equipment | | **16,856** | | (229,153) |
| Proceeds from sales of investments | | **1,903,443** | | 1,192,439 |
| Purchases of investments | | **(1,863,602)** | | (2,192,545) |
| **Net cash provided by (used in) investing activities** | | **56,697** | | (1,229,259) |
| Cash flows from financing activities: | | | | |
| Proceeds of long-term debt | | **-** | | 4,526,442 |
| Payments of long-term debt | | **(121,985)** | | (3,209,147) |
| Net proceeds from (payments on) line of credit | | **750,040** | | (562,779) |
| **Net cash provided by financing activities** | | **628,055** | | 754,516 |
| **Decrease in cash and cash equivalents** | | **(422,704)** | | (476,938) |
| Cash and cash equivalents: | | | | |
| Beginning of year | | **582,435** | | 1,059,373 |
| End of year | **$** | **159,731** | $ | 582,435 |
| Supplemental disclosure of cash flow information: | | | | |
| Interest paid | **$** | **265,966** | $ | 180,345 |

See notes to consolidated financial statements.

## Note 1. Nature of Activities and Significant Accounting Policies

Lutheran Child and Family Services of Illinois (the Agency or LCFS) is a nonprofit statewide social service agency whose mission is to attract, develop, mobilize, and provide resources to improve the well-being of children, individuals, families, congregations, and communities so that their lives are improved. Its corporate office is in River Forest, Illinois.

The Agency confronts neglect, abuse, isolation and poverty by providing safe homes for children, fostering self-reliance in families, strengthening connectivity in communities and promoting the dignity of all people. The Agency accomplishes its mission through the following services and programs:

Children Placement Services, including international and domestic adoption, foster care and licensing, and Regenerations – foster care for incarcerated youth.

Youth Residential Services, including Lutherbrook Child and Adolescent Center, Southern Thirty Adolescent Center, and Lutherbrook Academy therapeutic day school.

Clinical Services, including individual, marital and family counseling, preventive workshops and seminars, crisis counseling, and information and referral services.

Community Services, including disaster response services, food and clothing distribution, "Nice Twice" Thrift Stores, and youth camp and retreat center at Camp Wartburg.

**Financial condition and management's plans**: For the fiscal year ended June 30, 2016, the agency reported that it had been experiencing liquidity pressures due to a combination of persistent operating losses, disputed billings with the State of Illinois and insufficient borrowing capacity. During the course of the fiscal year which ended June 30, 2017, the Agency embarked on a turnaround plan to remediate operating losses, secure additional financing and sell major real estate. Execution of the plan began in the later stages of the fiscal year. The Agency was able to secure an additional $2,500,000 line of credit borrowing capacity. That borrowing capacity is being used to provide temporary working capital, while full execution of the corrective action plan proceeds. Concurrently, steady improvements have been made in the pursuit of accounts receivable collections.

At the end of fiscal year 2017, LCFS closed its community programs, Lutherbrook residential center, and academy program resulting in a significant reduction of the overall agency workforce. With regard to the remaining programs, substantial cost management initiatives have been and continue to be implemented. LCFS also began marketing the sale of its major properties. The proceeds of these sales will be used to pay down the balances on the lines of credit thereby providing improved short term borrowing capacity. One major property, the River Forest corporate office, and other smaller properties were sold within the first half of fiscal year 2018. Efforts to sell the remaining properties will continue through the rest of fiscal year 2018. In addition, efforts to continuously review and reduce operating expenses and enhance operating revenue will be a priority.

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

A summary of significant accounting policies is summarized below:

**Basis of presentation**: The consolidated financial statements have been prepared in accordance with accounting principles applicable to nonprofit organizations in conformity with accounting principles generally accepted in the United States of America. Therefore, the Agency classifies its activities as unrestricted, temporarily, or permanently restricted based on the existence or absence of donor-imposed restrictions. The consolidated financial statements include the accounts of the following separate entities for which the Agency is the sole member:

Camp Wartburg in Waterloo, Illinois
Lutheran Child and Family Services of Illinois Foundation in River Forest, Illinois (Investment Fund)
Lifelink International Adoption

The Agency is the sole member of Lifelink International Adoption, which provides international adoption services. Lifelink International Adoption dissolved in January 2017.

All significant intercompany accounts and transactions are eliminated in consolidation.

**Classification of net assets**

*Unrestricted*: Net assets available for support of the Agency's operations and are not subject to donor-imposed restrictions. The Agency's unrestricted fund accounts for all resources over which the Board of Trustees has control for use in carrying out the Agency's activities or for such other purposes as the Board may direct.

*Temporarily restricted*: Net assets available for support, with donor-imposed restrictions, that may or will be met either by actions of the Agency or the passage of time. Temporarily restricted net assets are reclassified to unrestricted net assets when the restrictions are met or have expired. These reclassifications are reported in the consolidated statement of activities as net assets released from restrictions. Donor-restricted contributions whose restrictions are met in the same reporting period are reported as unrestricted support.

*Permanently restricted*: Net assets for which the principal must remain intact per donor restriction and the earnings can be used for specified purposes or general operations to the extent of its investment income. Included in this category is the Agency’s interest in perpetual trusts.

**Accounting policies**: The Agency follows accounting standards established by the Financial Accounting Standards Board (the FASB) to ensure consistent reporting of financial condition, results of activities, and cash flows. References to Generally Accepted Accounting Principles (GAAP) in these footnotes are to the *FASB Accounting Standards Codification,* sometimes referred to as the Codification or ASC.

**Revenue recognition**: The majority of funding for the Agency’s operations is provided by governmental agencies. Revenue from government grants is recognized as it is earned. Revenue is considered earned when services are performed and it is expended in accordance with the agreement. Program service fees are recognized as the services are provided. The Agency recognizes donors' unconditional promises to give cash and other assets as revenue in the period the promises are made. Contributions receivable have been recorded for amounts expected to be collected in the future. Donors' promises to give cash and other assets that are conditional are not recognized until the conditions on which they depend are substantially met.

**Donated materials and services**: Donated materials and equipment are reflected as contributions at their estimated fair values at date of receipt. A substantial number of volunteers have donated their time to the Agency's program services and fundraising campaigns, but none of these amounts have been recorded as contributions because the services do not meet the criteria for recognition in the consolidated financial statements.

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

**Agency transactions**: The Agency has a contractual relationship with an unrelated organization that performs marketing and advertising services for adoptive families whereby the Agency acts as a fiscal intermediary between this organization and the organization’s clients due to a State of Illinois requirement. The Agency considers their relationship with the organization to meet the accounting definition of an agent and therefore does not recognize these transactions in the consolidated statement of activities. Funds collected on behalf of the organization and not yet remitted back to the organization are recorded as a liability. At June 30, 2017, the Agency had a debit balance of approximately $23,000 within other liabilities on the consolidated statement of financial position related to these transactions as a result of overpayment.

**Cash and cash equivalents**: The Agency considers all liquid investments with maturities of three months or less at date of acquisition to be cash and cash equivalents, except for certain cash equivalents that are included with investment funds because these amounts are used for investment purposes. The Agency maintains its cash in bank accounts which, at times, may exceed the federally insured limits. The Agency has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash.

**Accounts receivable**: Receivables are valued at management's estimate of the amount that will ultimately be collected. The allowance for doubtful accounts is based on specific identification of uncollectible accounts and the Agency's historical collection experience.

**Investments**: Investments are presented in the consolidated financial statements at fair value in accordance with accounting principles generally accepted in the United States of America. Investment income, realized gains (losses), and change in unrealized gains (losses) are reflected in the consolidated statement of activities. Investments received as contributions are recorded at fair value at the date of receipt.

The Agency's investment portfolio is subject to various risks, such as interest rate, credit and overall market volatility. Because of these risks, it is possible that changes in the fair value of investments may occur and that such changes could materially affect the Agency's consolidated financial statements.

**Property and equipment**: Property and equipment are recorded at cost. Additions and improvements to existing property over $500 during the year are capitalized, while general maintenance and repairs are charged to expense. The cost and accumulated depreciation of items sold or retired are removed from the property and equipment account and any gain or loss upon disposition is recognized at that time.

Provisions for depreciation of buildings and equipment have been computed using the straight-line method over the estimated useful lives of the assets, as follows:

| | Years |
|---|---|
| Description: | |
| Buildings and land improvements | 15 - 40 |
| Building improvements | 10 - 15 |
| Furniture and equipment | 3 - 10 |
| Vehicles | 5 |
| Curriculum materials | 5 |

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

The Agency 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 carrying amount or the fair value less costs to sell.

**Functional allocation of expenses**: The costs of providing programs and other activities have been presented on a functional basis in the consolidated statement of functional expenses. Accordingly, certain costs have been allocated among the programs and supporting services benefited. Operating expenses directly identified with a functional core program are charged to that program and, where these expenses affect more than one program, they are allocated on the basis of ratios estimated by management.

**Use of estimates**: In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, management makes estimates and assumptions affecting the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements, as well as the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

**Income taxes**: The accounting standard on accounting for uncertainty in income taxes 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 Agency 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 Agency and various positions related to the potential sources of unrelated business taxable income. For the reporting periods presented in these consolidated financial statements, there were no unrecognized tax benefits identified or recorded as liabilities.

The Agency files forms 990 in the U.S. federal jurisdiction and the State of Illinois. The Agency is generally no longer subject to examination by the Internal Revenue Service for years before fiscal 2014.

**Current and pending accounting pronouncements**: In 2017, the Agency adopted Accounting Standards Update (ASU) 2014-15, *Presentation of Financial Statements – Going Concern (Subtopic 205-40)*. The update provides guidance on management's responsibility in evaluating whether there is substantial doubt about an organization's ability to continue as a going concern and about related footnote disclosures. For each reporting period, management will be required to evaluate whether there are conditions or events that raise substantial doubt about an organization's ability to continue as a going concern within one year from the date the financial statements are issued. Accordingly, the Agency has performed this evaluation over its financial statements for the year ended June 30, 2017.

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*, requiring an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The updated standard will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective and permits the use of either a full retrospective or retrospective with cumulative effect transition method. The updated standard will be effective for the Agency's June 30, 2020 financial statements. The Agency has not yet selected a transition method and is currently evaluating the effect that the updated standard will have on the consolidated financial statements.

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

In May 2015, FASB issued ASU 2015-07, *Fair Value Measurement (Topic 850*): *Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*, which removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient. ASU 2015-07 also limits certain disclosures to investments for which the entity has elected to measure the fair value using the practical expedient. This ASU will be effective for the Agency for its fiscal year ending June 30, 2018. Early adoption is permitted and the amendments in ASU 2015-07 should be applied retrospectively to all periods presented. As ASU 2015-07 only amends and eliminates certain disclosures, the Agency does not anticipate its adoption will have a material impact on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. The guidance in this ASU supersedes the leasing guidance in Topic 840, *Leases*. Under the new guidance, lessees are required to recognize lease assets and lease liabilities on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for the Agency for its fiscal year ending June 30, 2021. The Agency is currently evaluating the effect that the updated standard will have on the consolidated financial statements.

In August 2016, the FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*, which simplifies and improves how a not-for-profit organization classifies its net assets, as well as the information it presents in financial statements and notes about its liquidity, financial performance, and cash flows. Among other changes, the ASU replaces the three current classes of net assets with two new classes, “net assets with donor restrictions” and “net assets without donor restrictions”, and expands disclosures about the nature and amount of any donor restrictions. The new standard is effective for the Agency for its fiscal year ending June 30, 2019, with early adoption permitted. The Agency is currently evaluating the impact the adoption of this guidance will have on its consolidated financial statements.

In March 2017, the FASB issued ASU 2017-07*–Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Benefit Cost.* The amendments in this ASU require that the service cost component of net benefit cost be presented on the statement of activities in the same line item(s) as other compensation costs for services rendered during the period. All remaining components of net benefit cost must be reported outside the subtotal for income from operations. The new standard will be effective for the Agency’s 2020 financial statements. The Agency is currently evaluating the effect that the updated standard will have on the consolidated financial statements.

### Note 2. Accounts Receivable

Accounts receivable at June 30, 2017, consisted of:

| | |
|---|---|
| Due from governmental agencies, net of allowance for doubtful accounts of $1,618,355 | $ 7,088,591 |
| Other | 142,048 |
| | $ 7,230,639 |

## Note 3. Contributions Receivable

Contributions receivable as of June 30, 2017, net of allowance of $7,775, are $471,198. An allowance for uncollectible contributions has been provided based upon management's analysis of various factors including prior collection history, type of contribution, and nature of fundraising activities. At June 30, 2017, $388,746 in contributions receivable are multiyear pledges and are included in temporarily restricted net assets as time restricted until the point in time that collections are received from the donor. All other contributions receivable are expected to be collected in less than one year.

Multiyear pledges at June 30, 2017, consist of the following:

| | |
|---|---|
| Receivable in less than one year | $ 114,618 |
| Receivable in one to five years | 274,128 |
| | $ 388,746 |

## Note 4. Investments

Investments at June 30, 2017, consisted of:

| | Cost | Fair Value |
|---|---|---|
| Cash equivalents | $ 334,835 | $ 334,835 |
| | 334,835 | 334,835 |
| Equity securities: | | |
| U.S. large cap | 1,872,380 | 2,337,666 |
| U.S. mid-cap | 131,900 | 153,912 |
| EAFE equity | 331,061 | 409,750 |
| Non U.S. equity | 1,528 | 1,621 |
| Global equity | 188,938 | 194,964 |
| Emerging markets | 15,133 | 17,087 |
| | 2,540,940 | 3,115,000 |
| Fixed income securities: | | |
| U.S. fixed income funds | 1,157,380 | 1,161,491 |
| | $ 4,033,155 | $ 4,611,326 |

Included in professional fees for the year ended June 30, 2017, in the consolidated statement of functional expenses is $67,996 of investment fees.

## Note 5. Fair Value Disclosures

### *Fair Value Measurements*

The Agency follows the accounting guidance on fair value measurements and disclosures, which defines fair value as 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 and sets out a fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). Inputs are broadly defined under the Topic as assumptions market participants would use in pricing an asset or liability. The three levels of the fair value hierarchy are described below:

Level 1. Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2. Inputs other than quoted prices within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3. Inputs are unobservable for the asset or liability and include situations where there is little, if any, market activity for the asset or liability. The inputs into the determination of fair value are based upon the best information in the circumstances and may require significant management judgment or estimation.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, an investment's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The Agency's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the investment.

For the fiscal year ended June 30, 2017, the application of valuation techniques applied to similar assets and liabilities has been consistent with techniques used in previous years. The Agency assesses levels of investments at each measurement date and transfers between levels are recognized on the accrual date of the event or change in circumstances that caused the transfer. For the year ended June 30, 2017, there were no such transfers. The following is a description of the valuation methodologies used for instruments at fair value:

**Investment securities**: Equity securities, fixed income securities and other securities classified as Level 1 in the fair value hierarchy are recorded at fair value based on quoted market prices in an active market. Securities classified as Level 2 represent securities whose fair value is estimated using recently executed transactions, market price quotations (where observable) or bond spreads. Changes in the fair value of securities are recorded as unrealized gains and losses.

**Beneficial interest in perpetual trusts and gifts held by LCMS Foundation**: The fair value of beneficial interest in trusts and gifts held by LCMS Foundation were provided by the respective trustees. The trustees determine fair value based on readily available pricing sources for market transactions involving identical assets for securities and based on an outside appraisal for farmland.

## Note 5. Fair Value Disclosures (Continued)

The table below presents the balances of assets measured at fair value on a recurring basis:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Investments: | | | | |
| Cash equivalents | $ 334,160 | $ 675 | $ - | $ 334,835 |
| Equity securities: | | | | |
| U.S. large cap | 2,337,666 | - | - | 2,337,666 |
| U.S. mid cap | 153,912 | - | - | 153,912 |
| EAFE equity | 409,750 | - | - | 409,750 |
| Non U.S. equity | 1,621 | - | - | 1,621 |
| Global equity | 97,640 | 97,324 | - | 194,964 |
| Emerging markets | 17,087 | - | - | 17,087 |
| Fixed income securities: | | | | |
| U.S. fixed income funds | 1,161,491 | - | - | 1,161,491 |
| | $ 4,513,327 | $ 97,999 | $ - | $ 4,611,326 |

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Beneficial interest in perpetual trusts | $ - | $ - | $ 3,523,164 | $ 3,523,164 |
| Gifts held by LCMS Foundation | - | - | 90,228 | 90,228 |
| | $ - | $ - | $ 3,613,392 | $ 3,613,392 |

The activity of the Agency's Level 3 assets for the year ended June 30, 2017, is as follows:

| | Gifts held by LCMS Foundation | Beneficial Interest in Perpetual Trusts |
|---|---|---|
| Balance, July 1, 2016 | $ 90,228 | $ 3,402,542 |
| Net change in value of perpetual trusts | - | 120,622 |
| Balance, June 30, 2017 | $ 90,228 | $ 3,523,164 |

## Note 6. Property and Equipment

Property and equipment at June 30, 2017, consisted of:

| | |
|---|---|
| Land | $ 1,339,687 |
| Buildings and improvements | 9,646,155 |
| Furniture and equipment | 2,216,402 |
| Vehicles | 297,449 |
| Curriculum materials | 165,967 |
| Construction in progress | - |
| | 13,665,660 |
| Accumulated depreciation | (8,833,045) |
| | $ 4,832,615 |

Depreciation and amortization expense in fiscal 2017 was $326,745.

## Note 7. Line of Credit

The Agency has a $3,000,000 revolving line of credit (line) with the Mission Investment Fund of The Evangelical Lutheran Church in America, Inc. (Mission Investment Fund). The line with the Mission Investment Fund has a maturity date of May 1, 2018, and the Agency and Mission Investment Fund both anticipate an extension of this credit facility prior to that date. Outstanding borrowings bear interest, payable monthly, at 3.75 percent. The line is secured by a blanket lien on all Agency assets. The Agency had outstanding borrowings of $2,994,854 on the line as of June 30, 2017.

## Note 8. Long-Term Debt

Long-term debt at June 30, 2017, consisted of:

| | |
|---|---|
| Ally Financial, payable in equal monthly installments of $374 including interest at 7.10%, due in November 2019; secured by the vehicle purchased with this loan. | $ 9,928 |
| Mission Investment Fund of The Evangelical Lutheran Church in America, payable in equal monthly installments of $24,591 including interest at initial rate of 3.875%, due in May 2041; secured by certain of the Agency's buildings. Interest rate resets every 5 years at a current rate determined by the lender. | 4,408,095 |
| | $ 4,418,023 |

## Note 8. Long-Term Debt (Continued)

Future maturities of long-term debt as of June 30, 2017, are as follows for the respective fiscal years:

| | |
|---|---|
| 2018 | $ 130,353 |
| 2019 | 135,627 |
| 2020 | 138,454 |
| 2021 | 142,010 |
| 2022 | 147,611 |
| Thereafter | 3,723,968 |
| | $ 4,418,023 |

## Note 9. Employee Benefit Plans

The Agency administers the 403(b) Thrift Plan of Lutheran Child and Family Services, a defined contribution plan. All employees become eligible to participate in the Thrift Plan upon achieving service level and age requirements. Employees are fully vested after 3 years of service. Full vesting also occurs at retirement age 65 or upon death or disability. Effective July 1, 2013, the Plan was amended as follows: 1) the Agency's base contribution was discontinued, 2) the Agency's matching contribution was changed to an annual discretionary contribution for eligible participants employed by the Agency at year-end, 3) prior service with any other employer will not be recognized for eligibility and 4) forfeited nonvested accounts are used to reduce plan expenses and the remainder will be allocated to eligible participants. Forfeited nonvested accounts are no longer available to reduce future Agency contributions. The Agency made no contributions to the Thrift Plan in the year ended June 30, 2017.

The Agency also has a defined benefit pension plan (Plan), which covers all eligible full-time staff and provides for monthly pension payments to eligible employees upon retirement. Benefits are based upon earnings and eligible years of service. The Agency's funding policy is to contribute amounts necessary to maintain the long-term stability of the Plan. Effective September 30, 2004, the Agency froze the Plan for future benefit accruals. No further benefits will accrue under the Plan after this date. This action will not affect benefits accrued prior to September 30, 2004 or participants' vesting in benefits accrued prior to that date. Participants will receive benefits based on their final average salary as of September 30, 2004.

The following sets forth the Agency's postretirement plan's funded status and amounts recognized at June 30, 2017, using a measurement date of June 30, 2017, in the Agency's consolidated financial statements:

| | |
|---|---|
| Projected benefit obligation | $ 12,955,341 |
| Plan assets at fair value | 9,879,994 |
| Funded status deficit | $ 3,075,347 |
| Accumulated benefit obligation | $ 12,955,341 |
| Liability recognized in the consolidated statement of financial position | $ 3,075,347 |
| Unrecognized actuarial loss not yet recognized in net periodic benefit cost, but included as a separate component of unrestricted net assets at June 30, 2017 | $ 3,906,806 |

## Note 9. Employee Benefit Plans (Continued)

Net periodic benefit cost and other amounts recognized in unrestricted net assets for the year ended June 30, 2017, are as follows:

| | | |
|---|---|---|
| Net periodic benefit cost | $ | 136,623 |
| Other amounts recognized in unrestricted net assets: | | |
| Net actuarial gain reclassified from unrestricted net assets to net periodic benefit cost | $ | 342,775 |
| Current year net gain | | 1,027,602 |
| Total recognized in unrestricted net assets | $ | 1,370,377 |

It is estimated that $216,523 of the net actuarial loss will be recognized as a component of net periodic benefit cost for the year ending June 30, 2018.

The table below sets forth the weighted average assumptions used to determine the benefit obligation at June 30, 2017, and the net periodic benefit cost for the year ended June 30, 2017. These rates were selected based upon current market conditions, the Agency's experience and future expectations.

| | Benefit Obligation | Net Periodic Benefit Cost |
|---|---|---|
| Discount rate | 3.70% | 3.40% |
| Expected rate of return on plan assets | 7.50% | 7.50% |
| Rate of increase in future compensation | N/A | N/A |

The Agency determines the long-term expected rate of return on plan assets by examining historical capital market returns, correlations between asset classes, and the plan’s normal asset allocation. Current and near-term market factors, such as inflation and interest rates, are then evaluated to arrive at the expected return on plan assets.

Plan assets at June 30, 2017, were comprised of:

| | |
|---|---|
| Equity funds | 67.15% |
| Fixed income funds | 26.65% |
| General account | 6.20% |
| | 100.00% |

The Agency’s overall investment strategy is to maintain a diversified investment allocation containing both equities and fixed income. The established target allocation is 65 percent equities and 35 percent fixed income. The Plan investment allocation is intended to provide current income to pay benefits when due while also providing opportunity for long-term growth.

## Note 9. Employee Benefit Plans (Continued)

Following is a description of the valuation methodologies used for assets measured at fair value.

**General account**: Valued at fair value by discounting the related cash flows based on current yields of similar instruments with comparable durations considering the credit-worthiness of the issuer.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Plan believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

**Pooled separate accounts**: Valued at the total of the net asset value of the shares of mutual funds and cash held by the account at year-end. The Plan's interest in the pooled separate accounts is valued based on information reported by the investment advisor.

The following table presents the Plan's assets using the fair value hierarchy, described previously in Note 5, as of June 30, 2017:

| Asset Category | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| General account | $ - | $ - | $ 612,066 | $ 612,066 |
| Pooled separate accounts: | | | | |
| Equity index fund | - | 1,401,143 | - | 1,401,143 |
| Mid-cap equity index fund | - | 675,601 | - | 675,601 |
| Small cap value fund | - | 405,861 | - | 405,861 |
| Small cap growth fund | - | 259,646 | - | 259,646 |
| Fixed income funds | - | 2,633,534 | - | 2,633,534 |
| Vanguard diversified fund | - | 652,563 | - | 652,563 |
| Pension deutsche growth VIP | - | 649,470 | - | 649,470 |
| Vanguard international fund | - | 1,375,241 | - | 1,375,241 |
| Fidelity VIP mid-cap fund | - | 663,556 | - | 663,556 |
| Vanguard VIF REIT index | - | 551,313 | - | 551,313 |
| Total | $ - | $ 9,267,928 | $ 612,066 | $ 9,879,994 |

The table below sets forth a summary of changes in the fair value of the Plan's Level 3 assets for the year ended June 30, 2017:

| | General Account |
|---|---|
| Balance, beginning of the year | $ 451,450 |
| Interest | 5,170 |
| Purchases | 725,000 |
| Sales | (569,554) |
| Balance, end of the year | $ 612,066 |

## Note 9. Employee Benefit Plans (Continued)

The following table represents the Plan's Level 3 financial instruments, the valuation techniques used to measure the fair value of those financial instruments, and the significant unobservable inputs and the ranges of values for those inputs as of June 30, 2017:

| Instrument | Fair Value as of June 30, 2017 | Principal Valuation Technique | Unobservable Inputs | Range of Significant Input Values | Weighted Average |
|---|---|---|---|---|---|
| Mutual of America Life Insurance Company General Account | $ 612,066 | Market Approach | 1) Discount Rate<br>2) Credit Rating of Issuer | 1) 1.00%<br>2) A+ | 1.00% |

In estimating fair value of the investments in Level 3, the Plan Sponsor's Investment Committee may use third-party pricing sources or appraisers. In substantiating the reasonableness of the pricing data provided by third parties, the Plan's Investment Committee evaluates a variety of factors including review of methods and assumptions used by external sources, recently executed transactions, existing contracts, economic conditions, industry and market developments, and overall credit ratings.

The following table below sets forth additional disclosures of the Plan's investments whose fair value is estimated using net asset value per share (or its equivalent) as of June 30, 2017:

| Investment | Fair Value | Redemption Frequency | Redemption Notice Period |
|---|---|---|---|
| Pooled separate accounts: | | | |
| Equity index fund (a) | $ 1,401,143 | Monthly | 30 days |
| Mid-cap equity index fund (a) | 675,601 | Monthly | 30 days |
| Small cap value fund (a) | 405,861 | Monthly | 30 days |
| Small cap growth fund (a) | 259,646 | Monthly | 30 days |
| Fixed income funds (b) | 2,633,534 | Monthly | 30 days |
| Vanguard diversified fund (a) | 652,563 | Monthly | 30 days |
| Pension deutsche growth VIP (a) | 649,470 | Monthly | 30 days |
| Vanguard international fund (a) | 1,375,241 | Monthly | 30 days |
| Fidelity VIP mid-cap fund (b) | 663,556 | Monthly | 30 days |
| Vanguard VIF REIT index (c) | 551,313 | Monthly | 30 days |
| | $ 9,267,928 | | |

(a) This category invests mainly in domestic and international stocks. Investments in this category are withdrawn in 30 days or less from the date of the withdrawal notice. In the event of contract discontinuance, the withdrawal will be made no later than 120 days after the later of the date of discontinuance or the date of receipt of notification. The fair value of investments in this category has been determined using the net asset value per share of the investments.

(b) This category invests in corporate, U.S. government agency and mortgage-backed securities. Investments in this category are withdrawn in 30 days or less from the date of the withdrawal notice. In the event of contract discontinuance, the withdrawal will be made no later than 120 days after the later of the date of discontinuance or the date of receipt of notification. The fair value of investments in this category has been determined using the net asset value per share of the investments.

(c) This category invests in publicly traded equity real estate investment trusts. Investments in this category are withdrawn 30 days or less from the date of the withdrawal notice. The fair value of investments in this category has been determined using the net asset value per share of the investments.

## Note 9. Employee Benefit Plans (Continued)

There are no unfunded commitments related to any of the above funds at June 30, 2017.

| | | |
|---|---|---|
| Employer contributions for the year ended June 30, 2017 | $ | - |
| Benefits paid during the year ended June 30, 2017 | $ | 569,555 |

The Agency does not plan to contribute to the Plan in the year ending June 30, 2018.

The benefits expected to be paid for 10 years, assuming that all participants retire at their normal retirement age, are approximately as follows:

| | | |
|---|---|---|
| 2018 | $ | 678,000 |
| 2019 | | 675,000 |
| 2020 | | 686,000 |
| 2021 | | 695,000 |
| 2022 | | 705,000 |
| 2023-2027 | | 3,507,000 |

## Note 10. Lease Commitments

The Agency is obligated under various occupancy and equipment leases expiring in various years through fiscal 2022. Several of these rental arrangements have no formal written leases and are payable on a month-to-month basis and are not included in the schedule below. Future minimum payments under non-cancellable leases are approximately as follows:

| | | |
|---|---|---|
| 2018 | $ | 392,962 |
| 2019 | | 436,137 |
| 2020 | | 348,819 |
| 2021 | | 278,821 |
| 2022 | | 180,416 |
| | $ | 1,637,155 |

Total occupancy rental expense for the year ended June 30, 2017, was $366,894.

## Note 11. Contingencies

Purchase of service contracts from the State of Illinois are subject to audit and the Agency could become liable for any expenditures disallowed upon any such audit. Management believes, however, any possible disallowance would not be material to the consolidated financial statements.

In the normal course of its activities, the Agency may be named in lawsuits filed by its clients or their representatives. As an employer, the Agency is from time-to-time subject to allegations of violations of various laws related to employment. The Agency does not believe that any current claims will result in a material impact on the consolidated financial statements.

## Note 12. Endowment Funds

The Agency's endowment consists of beneficial interests in perpetual trusts, certain permanently restricted endowments, as well as unrestricted funds designated by the Board of Trustees to function as endowments established for a variety of purposes. The board-designated endowment represents the investment portfolio held by the LCFS Foundation. These funds are intended to be retained and invested for the long-term benefit of the Agency, but can be appropriated through action by the Board of Trustees.

As required by accounting principles generally accepted in the United States of America, net assets associated with endowment funds, including funds designated by the Board to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

*Interpretation of Relevant Law*

The Agency's management has interpreted the Illinois Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Agency classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Agency in a manner consistent with the standard of prudence prescribed by UPMIFA.

In accordance with UPMIFA, the Agency considers the following factors in making a determination to appropriate or accumulate earnings on donor-restricted endowment funds:

1. The duration and preservation of the fund;
2. The purpose of the Agency 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 Agency; and
7. The investment policies of the Agency.

The Agency's endowment net asset composition by type of fund is as follows for the year ended June 30, 2017:

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---|---|---|---|---|
| Donor-restricted | $ - | $ 17,922 | $ 3,603,752 | $ 3,621,674 |
| Board-designated | 3,814,806 | - | - | 3,814,806 |
| Total funds | $ 3,814,806 | $ 17,922 | $ 3,603,752 | $ 7,436,480 |

**Note 12. Endowment Funds (Continued)**

The changes in endowment net assets for the Agency were as follows for the year ended June 30, 2017:

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---|---|---|---|---|
| Endowment net assets, beginning of year | $ 3,516,243 | $ 9,034 | $ 3,482,710 | $ 7,007,987 |
| Investment return: | | | | |
| Investment income | 113,697 | 3,917 | - | 117,614 |
| Net appreciation (realized and unrealized) | 232,802 | 4,971 | 120,622 | 358,395 |
| Total investment return | 346,499 | 8,888 | 120,622 | 476,009 |
| Contributions | 228,275 | - | 420 | 228,695 |
| Appropriation for expenditure | (276,211) | - | - | (276,211) |
| Endowment net assets, end of year | $ 3,814,806 | $ 17,922 | $ 3,603,752 | $ 7,436,480 |

*Return Objectives and Risk Parameters*

The Agency has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Agency must hold in perpetuity or for a donor-specified period(s), as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the long-term return objective is to maintain the endowment fund's purchasing power while covering the annual payout and investment expenses.

*Strategies Employed for Achieving Objectives*

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

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

The Agency has a policy of appropriating for distribution each year a percentage of its unrestricted board-designated endowment fund's fair value calculated off of the prior fiscal year-end balance for use in the current year. In establishing distribution rates, the Agency considers the long-term expected return on its endowment. This policy is consistent with the Agency 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. The Agency's spending policy related to the beneficial interest in perpetual trusts is to utilize any income distributed for operating purposes.

## Note 13. Temporarily Restricted Net Assets

Temporarily restricted net assets at June 30, 2017, consisted of:

| | | |
|---|---|---|
| Lutherbrook capital improvement | $ | 178,598 |
| Time restricted | | 388,746 |
| Camp | | 790,887 |
| Community | | 38,044 |
| Foster care | | 41,699 |
| LCMS Foundation | | 90,228 |
| Other | | 37,802 |
| | $ | 1,566,004 |

## Note 14. Permanently Restricted Net Assets

Permanently restricted net assets at June 30, 2017, consisted of:

| | | |
|---|---|---|
| Camp Wartburg endowment | $ | 75,000 |
| Alumni endowment | | 5,588 |
| Beneficial interest in perpetual trusts | | 3,523,164 |
| | $ | 3,603,752 |

## Note 15. Beneficial Interest in Perpetual Trusts

The Agency is the income beneficiary of the Arthur D. Day and Armilda A. Day Memorial Trust, which is a perpetual trust. The fair value of the trust assets is included in the Agency's permanently restricted fund as a beneficial interest in perpetual trust. The trust's assets consist of approximately $1,117,000 of securities and investable cash, and 224 acres of farm land and buildings with an approximated fair market value of $2,239,500. The income from the trust is to be paid quarterly. During fiscal year 2017, the Agency received $63,264 of income from the trust and this amount is recorded within unrestricted investment income on the consolidated statement of activities, as the use of the income is not restricted.

The Agency is one of the income beneficiaries of two other perpetual trusts with assets of $410,441 and $843,259, respectively, at June 30, 2017, consisting of marketable securities. The Agency's proportionate share of trusts' assets was approximately $55,000 and $112,000, respectively. The income from the trusts is to be paid quarterly. During fiscal year 2017, the Agency received $860 and $6,064 of income, respectively, from the trusts and these amounts are included within unrestricted investment income on the consolidated statement of activities, as the use of the income is not restricted.

## Note 16. Comparative Totals for Prior Year

The consolidated financial statements include certain prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with GAAP. Accordingly, such information should be read in conjunction with the Agency's financial statements for the fiscal year ended June 30, 2016, from which the summarized information was derived.

## Note 17. Subsequent Events

The Agency has evaluated subsequent events for potential recognition and/or disclosure through January 23, 2018, the date the consolidated financial statements were available to be issued.

On July 6, 2017, the Agency entered into a line of credit promissory note with Mission Investment Fund of Evangelical Lutheran Church in America, Inc. The terms of this line of credit promissory note call for a 3.75 percent fixed interest rate and is a 1-year term. The Agency can draw a maximum of $2,500,000 under this line of credit promissory note. On July 7, 2017, the Agency drew down $750,000 on this line of credit promissory note.

In July 2017, the Agency classified the following properties for sale: the Corporate office, Lutherbrook campus, Chicago Uptown office, Springfield office, Mt. Vernon office, Camp Wartburg, and the Hardin office. As of January 23, 2018, the Hardin office had been sold, and all other properties besides Lutherbrook were under contract.

Additionally, Lutherbrook formally ceased operations in August 2017.