

EXAMINATION WARRANT # 14-231405633-CP

REPORT OF EXAMINATION

OF THE

ALLEGHENY LUTHERAN SOCIAL MINISTRIES, INC.
ALTOONA, PENNSYLVANIA

AS OF

DECEMBER 31, 2014

For Informational Purposes Only

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For Informational Purposes Only

Harrisburg, Pennsylvania
December 7, 2015

Honorable Stephen J. Johnson, CPA
Deputy Insurance Commissioner
Office of Corporate and Financial Regulation
Pennsylvania Insurance Department
Harrisburg, Pennsylvania

Dear Sir:

In compliance with instructions contained in Examination Warrant 14-231405633-CP dated March 2, 2015, and in accordance with provisions of the Pennsylvania Continuing Care Provider Registration and Disclosure Act, 40 P.S. § 3219, an examination was conducted of the records and affairs of

ALLEGHENY LUTHERAN SOCIAL MINISTRIES, INC.

a continuing care retirement community hereafter referred to as the "Provider." This examination was conducted at the administrative office of the Provider located at 998 Logan Blvd., Altoona, Pennsylvania 16602.

The report of this examination is hereby respectfully submitted.

SCOPE OF EXAMINATION

This is the second examination of the Provider. This examination covered the period from January 1, 2010 through December 31, 2014, and consisted of a general survey of the Provider's business practices and management, and an evaluation of the Provider's financial condition, based upon the results of its annual audits. Material subsequent events were also reviewed.

Work programs employed in the performance of this examination were designed to comply with the standards promulgated by the Commonwealth of Pennsylvania Insurance Department ("Department").

The format of this report is consistent with the current practices of the Department and is limited to a description of the Provider, a discussion of key financial items that are of specific regulatory concern, and a disclosure of other significant regulatory information.

The objective of this examination was to determine the extent of the Provider's compliance with 40 P.S. §3202 and 31 Pa. Code §151.

For the years ending December 31, 2010 through December 31, 2013, the Certified Public Accounting firm of ParenteBeard, LLC of Pittsburgh, Pennsylvania, issued unmodified opinions on the Provider's financial statements based on generally accepted accounting principles.

For the year ending December 31, 2014, the Certified Public Accounting firm of Baker Tilly Virchow Krause, LLP of Pittsburgh, Pennsylvania issued an unmodified opinion on the Provider's financial statements based on generally accepted accounting principles.

HISTORY

The Provider was founded in 1948, and is a private, nonprofit organization, affiliated with the Evangelical Lutheran Church in America, which serves eight counties in central Pennsylvania. It is governed by a fourteen-member Board of Directors. Administrative offices are located at 998 Logan Boulevard, Altoona, PA. Other offices are located throughout the eight-county region.

The Provider has three campuses in Pennsylvania located in Hollidaysburg, Johnstown, and Pleasant Gap. The Hollidaysburg and Johnstown campuses include skilled nursing centers and assisted living facilities as part of the continuing care retirement community. The Pleasant Gap campus includes assisted living services. The Description of Facility that follows describes the campuses in more detail.

Allegheny Lutheran Social Ministries, Inc. provides other community services in addition to senior residential living. The Provider operates adult day care centers in Altoona, State College, and Somerset and also provides in-home personal care services in Blair, Cambria, and Somerset Counties. The Provider operates a federally-funded, home-based Head Start program in Bedford and Fulton Counties. Other programs include child day care centers and a center for children and families. The Provider employs 500 individuals in its eight-county service region.

The Provider has offered independent senior living since 1952. The Provider was issued a Certificate of Authority by the Department to operate as a continuing care retirement community on December 23, 2005.

The Provider is a tax exempt organization under Section 501(c) (3) of the Internal Revenue Code.

DESCRIPTION OF FACILITY

As of December 31, 2014, the Provider offered continuing care agreements at three campuses; the Oaks at Pleasant Gap, the Lutheran Home at Hollidaysburg, and the Lutheran Home at Johnstown. Continuing care residential living is available in cottages at the Hollidaysburg and Johnstown facilities. Both cottages and apartments are available for continuing care residential living at the Pleasant Gap facility.

The Oaks at Pleasant Gap provides a continuum of services on its 35-acre rural campus near State College, Pennsylvania. The facility is located at 200 Rachel Drive, Pleasant Gap,

Pennsylvania 16823. The campus includes 18 duplex cottages for independent living residents. A three story apartment building is occupied by personal care residents and independent living residents.

The Lutheran Home at Hollidaysburg includes an 89-bed skilled nursing facility. The suburban campus is located on approximately nine acres. The facility is located at 916 Hickory Street, Hollidaysburg, Pennsylvania 16648. The campus also includes 22 cottages for independent living residents and a four-floor apartment building known as "Hillcrest Apartments" which includes 39 independent living apartments. The continuing care residents reside in the cottages.

The Lutheran Home at Johnstown includes a 63-bed skilled nursing facility. The suburban campus is located on approximately 12 acres at 807 Goucher Street, Johnstown, Pennsylvania 15905. This campus also includes 18 cottages for independent living residents and a three story personal care facility.

FEES AND SERVICES

The entrance fees and monthly maintenance fees vary depending on the campus, the residential unit, and entrance fee option chosen by the resident. The Provider offers three entrance fee options: Under Option I, the entrance fee is 100% refundable and is only made available for apartment units at Pleasant Gap; under Option II, the entrance fee is 50% refundable; and under Option III, the entrance fee is non-refundable.

Under Option III, the entrance fee is fully earned upon occupancy. The monthly maintenance fee cannot be increased under this plan. Under Option II, half of the entrance fee is amortized at 1% per month for a period of 100 months. At the end of 100 months, the resident has the opportunity to receive a refund of 50% of the original entrance fee by switching to a monthly rental plan. If the resident does not choose to switch to the monthly rental plan, the original entrance fee continues to amortize until completely earned by the Provider.

The entrance fees and monthly fees as of December 31, 2014 are as follows:

The Oaks at Pleasant Gap

The entrance fees for cottage living range from \$50,000 to \$90,000, with monthly maintenance fees ranging from \$1,092 to \$2,177. The entrance fee for apartment living range from \$45,000 to \$165,000, with monthly maintenance fees ranging from \$786 per month to \$2,297 per month depending on the size of the apartment and the entrance fee refund option selected.

The Lutheran Home at Hollidaysburg

The entrance fee for a cottage at Hollidaysburg is \$50,000 for Option III or \$90,000 for Option II. Option I is not available for these units. The monthly maintenance fee ranges from \$742 per month to \$1,421 per month.

The Lutheran Home at Johnstown

The entrance fee for a cottage is \$10,000 for Option I, \$90,000 for Option II, and \$175,000 for Option III. There is no monthly maintenance fee for Option III. The monthly maintenance fee is \$575 for Option II and \$742 for Option I.

Services Provided to Continuing Care Residents

Living units are furnished with stove, dishwasher, refrigerator, and washer and dryer. The Provider is responsible for the maintenance, repair, and replacement of these furnishings. Real estate taxes are included in the monthly fee, and the Provider is responsible for the maintenance of the grounds. The Provider is also responsible for the payment of certain utilities in apartments, including gas, electricity, sewer and water, and refuse removal. Utilities are the responsibility of the residents of cottages.

REFUND POLICY

During the period of examination, four residents left the community and were entitled to a refund of a portion of the original entrance fee. In all cases, the refund was accurately determined and paid to the resident in accordance with the refund policy. The Provider's refund policy that follows complies with 40 P.S. §3214.

Refund during the Rescission Period

All payments, except the non-refundable application processing fee, shall be refunded to the resident if the residency agreement is rescinded within seven days of execution of the agreement by signing a Notice of Right to Rescind and delivering it to the Provider.

Refund after Rescission Period but Prior to Occupancy

In the event of termination of the agreement due to the resident's death before the designated occupancy date, or in the event resident is precluded from taking occupancy because of illness, injury, or incapacity prior to the designated occupancy date, a full refund less the application processing fee and any amounts deducted to cover expenses incurred by the Provider for any upgrades or improvements as requested by the resident will be made.

If the resident does not terminate the agreement within the seven day rescission period but does terminate prior to the occupancy date, while not precluded from taking occupancy due to illness, injury, incapacity, or death; a full refund will be made, less the application processing fee, reservation fee, and any amounts deducted to cover expenses incurred by the Provider.

Refund after Occupancy

In the event of termination for any reason after occupancy, the following refund provisions shall apply depending on the entrance fee option selected by resident.

Option I

Upon termination of the resident agreement, the resident is entitled to a full refund of the original entrance fee paid. This is reduced by the amount of any financial assistance subsidy provided to the resident by the Provider, and any amounts necessary to refurbish, restore or repair

the living unit in the event of unreasonable wear and tear. In addition, any cost incurred at the specific request of resident, or any unpaid charges will also be deducted from the refund.

Option II

In the event of termination for any reason during the amortization period, the resident will be entitled to a refund of unamortized portion of the entrance fee. All refunds are subject to deductions for the amount of financial assistance subsidy provided to resident by the Provider, and any amounts necessary to cover costs incurred by the Provider to refurbish, restore or repair the residential unit in the event of unreasonable wear and tear, and or costs incurred at the specific request of resident, and or any unpaid charges.

Option III

The resident is not entitled to a refund of any portion of the entrance fee following termination of the agreement. The entrance fee is deemed to be earned in full by the Provider as of the date of occupancy or the designated occupancy date, whichever is earlier.

Conditions and Due Date for Refunds

Prior to occupancy, any refund due is made within 30 days of termination. After occupancy, any refund due is made within 30 days of re-occupancy of the same unit. If a resident converts to a monthly rental plan at the end of the 100-month amortization period under Option II, the refund will be made within 30 days of converting to the monthly plan.

The Provider may pay the resident a refund prior to re-occupancy at the Provider's sole discretion, however 6% of the original entrance fee will be deducted from any refund due.

MANAGEMENT AND CONTROL

Board of Directors

The business and affairs of the Provider are managed by its fourteen member Board of Directors ("Board"). As of December 31, 2014, there were 13 members on the Board and one vacancy. During 2015, the Board had filled the vacancy and maintained a fourteen member Board. As of December 31, 2014, the Board included the following members:

Name and Address

Principal Occupation

Thomas Bradley
Altoona, PA

Retired Teacher

Helen Brennerman
Port Matilda, PA

Retired College Administrator

William Thompson
Hollidaysburg, PA

Pharmacist
Thompson Pharmacy

Allegheny Lutheran Social Ministries, Inc.

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|--|--------------------------------------|
| Amy Mearkle Johnstown, PA | Director of Marketing Delgrosso's |
| Gregory Pile Davidsville, PA | Retired Bishop |
| Dr. Tanya Holsopple Duncansville, PA | Physician |
| Michael Settimio Altoona, PA | Banker S & T Bank |
| David Cobaugh Johnstown, PA | Retired |
| Thomas Dixon Johnstown, PA | Funeral Director |
| William Lloyd Somerset, PA | Retired |
| Richard Whipkey Somerset, PA | Retired |
| Susan Williamson State College, PA | Pastor |
| Katherine Douglass Silver Springs, MD | Retired |

Officers

The following officers were serving as of December 31, 2014:

| Name | Title |
|-------------------------|-----------------------------------|
| Patricia Werner Savage | President and CEO |
| Christopher J. Reighard | Vice-President of Finance and CFO |
| Rebecca Young | Vice-President of Human Resources |
| Lori Adams | Assistant Secretary |

CORPORATE RECORDS

Articles of Incorporation

During the period covered by this examination, there were no amendments made to the Provider's Articles of Incorporation which were material in nature relative to the overall operations.

By-Laws

During the period covered by this examination, there were no amendments made to the Provider's By-Laws which were material in nature relative to the overall operations.

ANNUAL DISCLOSURE STATEMENT

The Provider prepares a separate disclosure statement for each campus. A review was made of the 2014 annual disclosure statements for compliance with the Pennsylvania Continuing Care Provider Registration and Disclosure Act ("Act"), 40 P.S. §3207 and the Pennsylvania Insurance Regulations ("Regulations"), 31 Pa. Code § 151.7 and § 151.9. The 2014 disclosure statements contained all information required by the Act and the Regulations.

RESIDENT AGREEMENT

The 2014 resident agreement was reviewed for compliance with the Pennsylvania Continuing Care Provider Registration and Disclosure Act ("Act"), 40 P.S. § 3214, and the Pennsylvania Insurance Regulations ("Regulations"), 31 Pa. Code § 151.8 and § 151.9. The 2014 resident agreement was found to contain all information required by the Act and the Regulations.

PENDING LITIGATION

There was no known pending legal action or any known potential legal action which could have a materially adverse effect on the Provider's financial condition as of the date of this examination report.

FINANCIAL STATEMENTS

The financial condition of the Provider, as of December 31, 2014, and the results of its operations for the last two years under examination are reflected in the following statements:

- Comparative Balance Sheet
- Comparative Statement of Operations
- Comparative Statement of Changes in Net Assets
- Comparative Statement of Cash Flows

The financial information used to compile the following financial statements was presented in the audited financial statements as of December 31, 2014. There were no changes made to the financial statements as a result of this examination.

**Comparative Balance Sheet
as of December 31,**

| <u>Assets</u> | <u>2014</u> | <u>2013</u> |
|--|-----------------------------|-----------------------------|
| Current assets | | |
| Cash and cash equivalents | \$ 3,084,478 | \$ 2,099,371 |
| Accounts receivable, residents | 1,795,949 | 2,337,993 |
| Other accounts receivable | 1,100,929 | 1,290,027 |
| Current portion of assets whose use is limited | 833,954 | - |
| Prepaid expenses | 460,401 | 361,558 |
| Resident trust funds | 50,887 | 49,897 |
| Total current assets | <u>7,326,598</u> | <u>6,138,846</u> |
| Assets whose use is limited: | 33,366,789 | 26,219,098 |
| Act 82 reserves | 312,989 | 247,111 |
| Property and equipment, net | 22,233,517 | 20,522,533 |
| Deferred financing costs, net | 232,336 | 133,513 |
| Other assets | 114,388 | 114,388 |
| Beneficial interest in perpetual trusts | 3,987,635 | 3,932,437 |
| Total assets | <u><u>67,574,252</u></u> | <u><u>57,307,926</u></u> |
| <u>Liabilities and net assets</u> | | |
| Current liabilities | | |
| Current maturities of long-term debt | 1,618,082 | 1,478,208 |
| Accounts payable, trade | 700,258 | 1,114,378 |
| Accrued expenses | 1,125,053 | 1,063,827 |
| Accrued payable, construction | 833,954 | - |
| Resident trust funds | 50,887 | 49,897 |
| Total current liabilities | <u>4,328,234</u> | <u>3,706,310</u> |
| Long-term debt | 16,652,693 | 9,768,527 |
| Refundable advance fees and deposits | 2,543,706 | 2,245,552 |
| Deferred revenues from advance fees | 1,545,468 | 1,305,399 |
| Other liabilities | 77,557 | 74,834 |
| Total liabilities | <u>25,147,658</u> | <u>17,100,622</u> |
| Net assets | | |
| Unrestricted | 36,526,566 | 34,388,461 |
| Temporarily restricted | 535,601 | 509,614 |
| Permanently restricted | 5,364,427 | 5,309,229 |
| Total net assets | <u>42,426,594</u> | <u>40,207,304</u> |
| Total liabilities and net assets | <u><u>\$ 67,574,252</u></u> | <u><u>\$ 57,307,926</u></u> |

**Comparative Statement of Operations
for the Year Ended December 31,**

| | <u>2014</u> | <u>2013</u> |
|--|---------------------|---------------------|
| Operating revenues: | | |
| Net program service revenues | \$ 23,672,469 | \$ 23,247,690 |
| Pennsylvania nursing home assessment | 635,925 | 639,381 |
| Other operating revenues | 298,483 | 389,366 |
| Net assets released from restrictions | 48,631 | 27,864 |
| Total operating revenues | <u>24,655,508</u> | <u>24,304,301</u> |
| Operating expenses | | |
| Salaries and wages | 11,199,481 | 11,061,635 |
| Other expenses | 7,641,303 | 7,466,567 |
| Employee benefits | 2,640,954 | 2,642,370 |
| Depreciation | 1,916,159 | 2,063,401 |
| Interest | 442,648 | 655,067 |
| Pennsylvania nursing home assessment | 359,639 | 337,520 |
| Amortization | 21,135 | 20,316 |
| Total operating expenses | <u>24,221,319</u> | <u>24,246,876</u> |
| Operating income | <u>434,189</u> | <u>57,425</u> |
| Non-operating revenues (expense) | | |
| Investment income | 1,189,898 | 2,910,334 |
| Contributions | 536,242 | 313,104 |
| Loss on disposal of deferred financing costs | (22,224) | - |
| Total non-operating revenues, net | <u>1,703,916</u> | <u>3,223,438</u> |
| Revenues in excess of expenses | 2,138,105 | 3,280,863 |
| Other changes in net assets | | |
| Net assets released from restrictions used for purchase of property and equipment | - | 20,000 |
| Increase in unrestricted net assets | <u>\$ 2,138,105</u> | <u>\$ 3,300,863</u> |

**Comparative Statement of Changes in Net Assets
for the Year Ended December 31,**

| | <u>2014</u> | <u>2013</u> |
|--|---------------------|---------------------|
| <u>Unrestricted net assets</u> | | |
| Revenues in excess of expenses | \$ 2,138,105 | \$ 3,280,863 |
| Net assets released from restrictions used for purchase of property and equipment | - | 20,000 |
| Increase in unrestricted net deficit | <u>2,138,105</u> | <u>3,300,863</u> |
| <u>Temporarily restricted net assets</u> | | |
| Contributions | 56,938 | 50,406 |
| Investment income | 17,680 | 4,689 |
| Net assets released from restrictions | (48,631) | (47,864) |
| Increase in temporarily restricted net assets | <u>25,987</u> | <u>7,231</u> |
| <u>Permanently restricted net assets</u> | | |
| Valuation gain, beneficial interest in perpetual trusts | 55,198 | 275,131 |
| Increase in permanently restricted net assets | <u>55,198</u> | <u>275,131</u> |
| Increase in net assets | 2,219,290 | 3,583,225 |
| Net assets, beginning of year | <u>40,207,304</u> | <u>36,624,079</u> |
| Net assets, end of year | <u>\$42,426,594</u> | <u>\$40,207,304</u> |

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**Comparative Statement of Cash Flows
for the Year Ended December 31,**

| | <u>2014</u> | <u>2013</u> |
|---|---------------------|---------------------|
| <u>Cash flows from operating activities:</u> | | |
| Increase in net assets | \$ 2,219,290 | \$ 3,583,225 |
| Adjustments to reconcile increase in net assets to net cash provided by operating activities: | | |
| Depreciation and amortization | 1,937,294 | 2,083,717 |
| Loss on disposal of deferred financing costs | 22,224 | - |
| Provision for doubtful collections | 234,478 | 200,500 |
| Proceeds from nonrefundable advance fees, and deposits, existing units | 272,500 | 740,105 |
| Amortization of advance fees | (302,431) | (164,983) |
| Net realized and unrealized gain on investments | (548,307) | (2,267,240) |
| Contributions and grants restricted for long-term purpose | (5,826) | (26,893) |
| Investment income restricted for long-term purposes | (17,680) | (4,689) |
| Valuation gain, beneficial interest in perpetual trusts | (55,198) | (275,131) |
| Change in assets and liabilities: | | |
| Accounts receivable, residents and other | 496,664 | (620,346) |
| Prepaid expenses | (98,843) | (53,331) |
| Accounts payable, trade | (414,120) | 38,147 |
| Accrued expenses | 61,226 | 44,291 |
| Other liabilities | 2,723 | (5,565) |
| Net cash provided by operating activities | <u>3,803,994</u> | <u>3,271,807</u> |
| <u>Cash flows from investing activities</u> | | |
| Net purchases of assets whose use is limited | (7,499,216) | (580,213) |
| Purchases of property and equipment | (2,793,189) | (1,549,192) |
| Increase in other assets | - | (1,805) |
| Net cash used in investing activities | <u>(10,292,405)</u> | <u>(2,131,210)</u> |
| <u>Cash flows from financing activities</u> | | |
| Proceeds from long-term debt | 10,000,000 | - |
| Proceeds from advance fees, new units | 540,000 | 280,000 |
| Proceeds from refundable advance fees | 328,588 | - |
| Proceeds from investment income restricted for long-term purposes | 17,680 | 4,689 |
| Proceeds of contributions and grants restricted for long-term purposes | 5,826 | 26,893 |
| Repayment of long-term debt | (2,975,960) | (1,410,335) |
| Refunds of advance fees | (300,434) | (242,573) |
| Payment of deferred financing costs | (142,182) | - |
| Net cash provided by (used in) financing activities | <u>7,473,518</u> | <u>(1,341,326)</u> |
| Net increase (decrease) in cash and cash equivalents | 985,107 | (200,729) |
| Cash and cash equivalents, at beginning of year | 2,099,371 | 2,300,100 |
| Cash and cash equivalents, at end of year | <u>\$ 3,084,478</u> | <u>\$ 2,099,371</u> |

NOTES TO THE FINANCIAL STATEMENTS

Statutory Minimum Liquid Reserves

\$312,989

The Pennsylvania Continuing Care Provider Registration and Disclosure Act, 40 P.S. §3209, requires the Provider to establish and maintain a statutory liquid reserve in an amount equal to or exceeding the greater of:

- (1) The total of all principal and interest payments due during the next 12 months on account of any mortgage loan or other long-term financing of the facility; or
- (2) Ten percent of the projected annual operating expenses of the facility exclusive of depreciation.

Of the above two requirements, number (1) is \$312,989 and number (2) is \$206,503. As of December 31, 2014, the Provider had established and reported a reserve of \$312,989 for this purpose.

Escrow Requirements

The Provider has established an escrow account with a financial institution, but the Provider does not accept deposits in advance of the occupancy date. Should the Provider accept a deposit from any prospective resident prior to the occupancy date, then the deposit must be placed into escrow until such time as the resident is permitted to take occupancy in accordance with 40 P.S. §3212 (1).

SUBSEQUENT EVENTS

The examination team was not made aware of any events that could have a significant effect on the solvency of the Provider through the date of this examination report.

RECOMMENDATIONS

This is the second examination of the Provider.

Prior Examination Recommendations

No recommendations were made in the prior examination.

Current Examination Recommendations

There are no recommendations as a result of this examination.

Allegheny Lutheran Social Ministries, Inc.

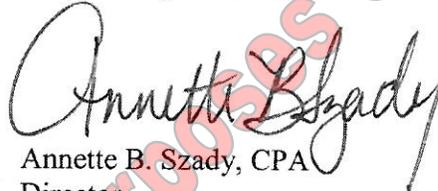
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CONCLUSION

As a result of our examination, we conclude that Allegheny Lutheran Social Ministries, Inc. is in compliance with applicable Pennsylvania laws and regulations as they pertain to continuing care retirement communities as of December 31, 2014.

This examination was conducted by Joseph P. Monaco and James Minder, with the latter completing field work.

Respectfully submitted,



Annette B. Szady, CPA
Director
Bureau of Financial Examinations



James Minder, CPA
Examination Manager
Bureau of Financial Examinations

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