LUTHERAN SOCIAL SERVICE OF MINNESOTA
AND AFFILIATES

CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED SEPTEMBER 30, 2012 AND 2011

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CliftonLarsonAllen LLP
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INDEPENDENT AUDITORS' REPORT

Board of Directors
Lutheran Social Service of Minnesota and Affiliates
St. Paul, Minnesota

We have audited the accompanying consolidated statements of financial position of Lutheran Social Service of Minnesota and Affiliates (the Organization) as of September 30, 2012 and 2011, and the related consolidated statements of activities, functional expenses, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with U.S. generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Organization at September 30, 2012 and 2011, and the changes in their net assets and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

CliftonLarsonAllen LLP

CliftonLarsonAllen LLP

Minneapolis, Minnesota
January 29, 2013

LUTHERAN SOCIAL SERVICE OF MINNESOTA AND AFFILIATES
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
SEPTEMBER 30, 2012 AND 2011

	2012			
	Lutheran Social Service	LSS Park Avenue Apartments LP	LSS Park Avenue Apartments LP Eliminations	Lutheran Social Service Consolidated
ASSETS				
CURRENT ASSETS				
Cash and Cash Equivalents	$ 10,268,198	$ 154,272	$ -	$ 10,422,470
Pledges Receivable	384,857	-	-	384,857
Accounts Receivable, Net	9,173,724	2,238	(8,441)	9,167,521
Other Current Assets	439,034	1,553	-	440,587
Total Current Assets	20,265,813	158,063	(8,441)	20,415,435
Net Land, Buildings and Equipment	30,661,695	7,396,999	(152,000)	37,906,694
Investments	2,880,528	-	(86,000)	2,794,528
Intangible Assets: Goodwill	1,079,207	-	-	1,079,207
Long-Term Pledges Receivable	183,070	-	-	183,070
Other Assets Limited as to Use	39,423	80,973	-	120,396
Other Assets	1,296,738	314,333	-	1,611,071
Loan Receivable	11,100,529	-	(629,000)	10,471,529
Beneficial Interest in Perpetual Trust	2,574,870	-	-	2,574,870
Total Assets	$ 70,081,873	$ 7,950,368	$ (875,441)	$ 77,156,800
LIABILITIES AND NET ASSETS				
CURRENT LIABILITIES				
Accounts Payable, Accrued Liabilities and Deferred Income	$ 4,242,876	$ 75,721	$ (8,441)	$ 4,310,156
Conditional Grants, Current	109,354	-	-	109,354
Borrowing Under Line of Credit	180,335	-	-	180,335
Accrued Payroll, Benefits, Taxes, & Withholding	7,191,021	-	-	7,191,021
Current Portion of Long-Term Debt	808,489	-	-	808,489
Total Current Liabilities	12,532,075	75,721	(8,441)	12,599,355
Accrued Pension Liability	17,729,608	-	-	17,729,608
Obligation under Trust Agreement	947,883	-	-	947,883
Conditional Grants, Long Term	1,869,536	-	-	1,869,536
Asset Retirement Obligation	3,642	-	-	3,642
Long-Term Debt, Less Current Portion	16,914,704	1,697,901	(629,000)	17,983,605
Total Liabilities	49,997,448	1,773,622	(637,441)	51,133,629
NET ASSETS				
Unrestricted	(2,140,594)	6,176,746	(238,000)	3,798,152
Temporarily Restricted	18,312,319	-	-	18,312,319
Permanently Restricted	3,912,700	-	-	3,912,700
Total Net Assets	20,084,425	6,176,746	(238,000)	26,023,171
Total Liabilities and Net Assets	$ 70,081,873	$ 7,950,368	$ (875,441)	$ 77,156,800

2011			
Lutheran Social Service	LSS Park Avenue Apartments LP	LSS Park Avenue Apartments LP Eliminations	Lutheran Social Service Consolidated
$ 9,779,850	$ 180,651	$ -	$ 9,960,501
276,605	-	-	276,605
8,914,001	283	(18,804)	8,895,480
388,205	-	-	388,205
19,358,661	180,934	(18,804)	19,520,791
31,660,168	7,632,666	(152,000)	39,140,834
2,522,203	-	(86,000)	2,436,203
1,079,207	-	-	1,079,207
166,857	-	-	166,857
46,875	80,973	-	127,848
1,134,757	313,330	-	1,448,087
11,100,529	-	(629,000)	10,471,529
2,266,716	-	-	2,266,716
$ 69,335,973	$ 8,207,903	$ (885,804)	$ 76,658,072
$ 4,028,426	$ 95,004	$ (18,804)	$ 4,104,626
109,354	-	-	109,354
-	-	-	-
7,107,603	-	-	7,107,603
943,102	-	-	943,102
12,188,485	95,004	(18,804)	12,264,685
16,736,647	-	-	16,736,647
846,989	-	-	846,989
1,978,891	-	-	1,978,891
3,642	-	-	3,642
18,191,794	1,660,046	(629,000)	19,222,840
49,946,448	1,755,050	(647,804)	51,053,694
(1,983,407)	6,452,853	(238,000)	4,231,446
17,776,255	-	-	17,776,255
3,596,677	-	-	3,596,677
19,389,525	6,452,853	(238,000)	25,604,378
$ 69,335,973	$ 8,207,903	$ (885,804)	$ 76,658,072

LUTHERAN SOCIAL SERVICE OF MINNESOTA AND AFFILIATES
CONSOLIDATED STATEMENTS OF ACTIVITIES
SEPTEMBER 30, 2012 AND 2011

	2012			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
REVENUE AND PUBLIC SUPPORT				
Revenue:				
Government Fees and Grants	$ 77,491,513	$ 557,761	$ -	$ 78,049,274
Client Fees and Reimbursed Services	11,044,636	-	-	11,044,636
Investment Income	1,242	-	7,220	8,462
Others	553,064	1,360	-	554,424
Total Revenue	89,090,455	559,121	7,220	89,656,796
Public Support:				
Contributions	1,983,626	1,394,993	649	3,379,268
Grants (Nongovernmental)	852,298	2,116,563	-	2,968,861
Church	796,532	72,412	-	868,944
United Way	1,182,646	-	-	1,182,646
Total Public Support	4,815,102	3,583,968	649	8,399,719
Net Assets Released from Restrictions	3,763,242	(3,763,242)	-	-
Total Revenue and Public Support	97,668,799	379,847	7,869	98,056,515
EXPENSES				
Program Service:				
Services for Children / Youth / Family / CFCL	25,218,746	-	-	25,218,746
Services for Seniors	10,645,840	-	-	10,645,840
Services for People with Disabilities	49,197,958	-	-	49,197,958
Total Program Service Expenses	85,062,544	-	-	85,062,544
Support Service:				
Management and General	9,065,004	-	-	9,065,004
Fund Raising	1,938,301	-	-	1,938,301
Total Support Service Expenses	11,003,305	-	-	11,003,305
Total Expenses	96,065,849	-	-	96,065,849
CHANGE IN NET ASSETS - OPERATIONS	1,602,950	379,847	7,869	1,990,666
NON-OPERATING				
Pass-Through Revenues	5,300,299	-	-	5,300,299
Pass-Through Expenditures	(5,300,299)	-	-	(5,300,299)
	-	-	-	-
Additional Pension Increase:				
(Increase) Decrease:				
Current Period	(1,971,618)	-	-	(1,971,618)
Change in Value of Split Interest Agreements	9,113	(73,355)	-	(64,242)
Change in Value of Trusts	-	-	308,154	308,154
Change in Value of Investments	202,368	229,572	-	431,940
Noncontrolling Interest in LSS Park Avenue Apartments LP	(276,107)	-	-	(276,107)
Change in Net Assets Non-Operating	(2,036,244)	156,217	308,154	(1,571,873)
CHANGE IN NET ASSETS	(433,294)	536,064	316,023	418,793
Net Assets - Beginning of Year	4,231,446	17,776,255	3,596,677	25,604,378
NET ASSETS - END OF YEAR	$ 3,798,152	$ 18,312,319	$ 3,912,700	$ 26,023,171

2011			
Unrestricted	Temporarily Restricted	Permanently Restricted	Total
$ 77,309,541	$ 648,771	$ -	$ 77,958,312
11,488,129	-	-	11,488,129
7,153	-	-	7,153
563,227	2,495	-	565,722
89,368,050	651,266	-	90,019,316
1,915,391	1,205,745	165	3,121,301
1,315,700	1,877,236	-	3,192,936
942,719	79,705	-	1,022,424
1,271,476	-	-	1,271,476
5,445,286	3,162,686	165	8,608,137
3,485,234	(3,485,234)	-	-
98,298,570	328,718	165	98,627,453
26,644,933	-	-	26,644,933
12,941,772	-	-	12,941,772
46,672,008	-	-	46,672,008
86,258,713	-	-	86,258,713
8,992,351	-	-	8,992,351
1,803,695	-	-	1,803,695
10,796,046	-	-	10,796,046
97,054,759	-	-	97,054,759
1,243,811	328,718	165	1,572,694
5,221,576	-	-	5,221,576
(5,221,576)	-	-	(5,221,576)
-	-	-	-
(1,195,279)	-	-	(1,195,279)
13,018	-	-	13,018
-	-	(168,740)	(168,740)
(50,491)	1,410	-	(49,081)
(234,513)	-	-	(234,513)
(1,467,265)	1,410	(168,740)	(1,634,595)
(223,454)	330,128	(168,575)	(61,901)
4,454,900	17,446,127	3,765,252	25,666,279
$ 4,231,446	$ 17,776,255	$ 3,596,677	$ 25,604,378

LUTHERAN SOCIAL SERVICE OF MINNESOTA AND AFFILIATES
CONSOLIDATED STATEMENTS OF FUNCTIONAL EXPENSES
YEARS ENDED SEPTEMBER 30, 2012 AND 2011

	2012			
		Support Services		
	Program Services	Management and General	Fund Raising	Total
Salaries	$ 38,132,245	$ 5,020,073	$ 1,014,328	$ 44,166,646
Employee Benefits and Payroll Taxes	10,373,904	1,346,390	250,106	11,970,400
Total Personnel Costs	48,506,149	6,366,463	1,264,434	56,137,046
Professional Fees and Contract Services	1,451,711	850,854	109,255	2,411,820
Supplies	765,503	34,829	6,793	807,125
Communications	1,338,700	234,719	321,244	1,894,663
Occupancy	5,004,197	601,202	101,522	5,706,921
Equipment	527,352	203,934	31,914	763,200
Transportation	2,358,512	92,733	24,670	2,475,915
Staff Development	795,442	428,091	61,486	1,285,019
Client and Volunteer Expense	21,977,727	53,617	5,182	22,036,526
Other	628,364	117,486	11,801	757,651
Total Expense Before Depreciation	83,353,657	8,983,928	1,938,301	94,275,886
Depreciation	1,708,887	81,076	-	1,789,963
Total Expense	$ 85,062,544	$ 9,065,004	$ 1,938,301	$ 96,065,849

See accompanying Notes to Consolidated Financial Statements.

2011			
	Support Services		
Program Services	Management and General	Fund Raising	Total
$ 38,935,268	$ 4,910,765	$ 931,285	$ 44,777,318
10,691,129	1,291,025	247,497	12,229,651
49,626,397	6,201,790	1,178,782	57,006,969
1,985,622	853,904	77,114	2,916,640
805,306	28,684	66,823	900,813
1,308,972	289,747	246,439	1,845,158
4,937,560	590,972	103,689	5,632,221
616,299	160,987	35,250	812,536
2,390,652	75,126	29,640	2,495,418
706,101	516,695	46,616	1,269,412
21,695,935	43,357	6,245	21,745,537
284,600	165,048	13,097	462,745
84,357,444	8,926,310	1,803,695	95,087,449
1,901,269	66,041	-	1,967,310
$ 86,258,713	$ 8,992,351	$ 1,803,695	$ 97,054,759

LUTHERAN SOCIAL SERVICE OF MINNESOTA AND AFFILIATES
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED SEPTEMBER 30, 2012 AND 2011

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in Net Assets	$ 418,793	$ (61,901)
Adjustments to Reconcile Change in Net Assets to Cash and Cash Equivalents Provided by Operating Activities:		
Change in Value of Split Interest Agreements	66,958	(9,742)
Change in Value of Perpetual Trust	(472,361)	4,533
Asset Retirement Obligation	-	(111)
Adjustment for Pension Liability	992,961	769,069
Amortization of Deferred Gain from Tax Credit Financing	(463,690)	(463,691)
Noncash Donations of Low Interest Loans	(109,355)	(109,354)
Restricted Contributions for Long-Lived Assets, Including Increase in Accrued Interest	52,000	14,145
Bad Debt Expense and Change in Allowance	354,986	218,838
Realized and Unrealized (Gains) Losses on Investments	(315,575)	38,042
Depreciation	2,025,630	2,195,106
Amortization of Capital Lease Assets	188,699	159,704
Amortization - Other	39,726	81,285
Loss (Gain) on Sale of Land, Building and Equipment	2,763	(43,310)
Increase in Receivables	(751,493)	(746,681)
(Increase) Decrease in Other Assets	(199,760)	60,331
Increase (Decrease) in Current Liabilities	288,930	(313,090)
Net Cash Provided by Operating Activities	2,119,212	1,793,173
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of Investments	(511,511)	(37,723)
Proceeds from Sale of Investments	483,655	270,000
Proceeds from Sale of Property and Equipment	135,935	126,878
Capital Expenditures	(1,118,887)	(1,080,143)
Net Cash Used by Investing Activities	(1,010,808)	(720,988)
CASH FLOWS FROM FINANCING ACTIVITIES		
Long-Term Debt Payments	(990,978)	(753,461)
Proceeds from Line of Credit	180,335	-
Distribution from the Perpetual Trust	164,208	164,208
Net Cash Used by Financing Activities	(646,435)	(589,253)
NET INCREASE IN CASH AND CASH EQUIVALENTS	461,969	482,932
Cash and Cash Equivalents - Beginning of Year	9,960,501	9,477,569
CASH AND CASH EQUIVALENTS - END OF YEAR	$ 10,422,470	$ 9,960,501
SUPPLEMENTAL INFORMATION		
Cash Paid for Interest	$ 291,196	$ 293,020
NONCASH TRANSACTIONS		
Capital Assets Purchased with Capital Leases	$ -	$ 318,871

See accompanying Notes to Consolidated Financial Statements.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Lutheran Social Service of Minnesota and Affiliates (the Organization) is the largest statewide private social service agency in Minnesota and is affiliated with the six Minnesota synods of the Evangelical Lutheran Church in America. The consolidated financial statements of the Organization include the following Affiliates:

- Lutheran Social Service of Minnesota Foundation
- Rezek House LLC
- LSS Townhomes LLC
- LSS Supportive Housing LLC
- Partners in Community Supports, Inc.
- CFCL Lending LLC
- CFCL LLC
- LSS Development LLC
- LSS Park Avenue Apartments LP

Program services are grouped into three service categories, which are:

- Children, Youth, Families and the Center for Changing Lives
- Seniors
- People with Disabilities.

The Organization has over 350 program units in over 300 locations in the State of Minnesota that provided services to more than 100,000 persons in 2012.

Basis of Presentation

Net assets and revenues, public support, and expenses are classified based on the existence or absence of donor-imposed restrictions. Net assets of the Organization and changes therein are classified into the following three categories:

Unrestricted – Resources over which the board of directors has discretionary control. Designated amounts represent those assets which the board has set aside for a particular purpose.

Temporarily Restricted – Those resources subject to donor imposed restrictions which will be satisfied by actions of the Organization or passage of time.

Permanently Restricted – Those resources subject to a donor imposed restriction that they be maintained permanently by the Organization. The donors of these resources permit the Organization to use all or part of the income earned, including capital appreciation, or related investments for unrestricted or temporarily restricted purposes. For endowments, the Organization classifies as permanently restricted net assets the original value of the gifts to the endowment and the value of subsequent gifts to the endowment.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of Presentation (Continued)

Revenues are reported as increase in unrestricted net assets unless use of the related asset is limited by donor-imposed restrictions. Expenses are reported as decrease in unrestricted net assets. The Organization has elected to present temporarily restricted contributions, which are fulfilled in the same time period, within the unrestricted net asset class.

Cash and Cash Equivalents

The Organization considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents. At times such deposits may be in excess of FDIC insurance limits. At times, the investment portfolio may contain cash and cash equivalents that are included in investments in the consolidated statement of financial position.

Investments

The Organization invests in a variety of investment vehicles. In general, investments are exposed to various risks, such as interest rate, credit and overall market volatility. Due to the level of risk associated with certain investments, changes in the values of investments will occur in the near term and such changes could materially affect the amounts reported.

Pledges Receivable

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received. Pledges that are expected to be collected within one year are recorded at their net realizable value. Pledges that are expected to be collected in future years are recorded at the present value of the amount expected to be collected. The discounts on those amounts are computed using an imputed interest rate applicable to the year in which the pledge is received. Conditional pledges are not included as support until such time as the conditions are substantially met.

Account Receivables

The Organization provides an allowance for uncollectible accounts based on the reserve method using management's judgment and the Organization's approved policy. Payment for services is required within 30 days of receipt of invoice. Accounts past due for more than 30 days are individually analyzed for collectability. In addition, an allowance is estimated for other accounts based on the Organization's policy as well as historical experience of the Organization. The Organization policy is based on determined percentages of outstanding receivables by age of the balance. When all collection efforts have been exhausted, the receivable is written off against the related reserve. At September 30, 2012 and 2011, the allowance for uncollectible accounts was $309,273 and $287,675, respectively.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Net Land, Buildings and Equipment

Property and equipment acquisitions are recorded at cost. Donated items are recorded at fair value on the date received. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method.

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Organization depreciates such assets over their estimates useful life, and releases such restrictions as to use by annually transferring amounts from temporarily restricted funds to unrestricted funds in equal to amounts annually.

Long-Lived Assets

The Organization reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. An impairment loss would be recognized when estimated future cash flows expected to result from the use of the asset and its eventual disposition is less than its carrying amount.

Deferred Financing Costs

Financing costs incurred in obtaining financing are being amortized by the straight-line method over the applicable terms of the bonds. Amortization expense was $10,906 for the years ended September 30, 2012 and 2011.

Intangible Assets: Goodwill

The Organization acquired controlling interest in Partners in Community Supports, Inc. (PICS) effective April 1, 2008 recognizing goodwill in the amount of $729,207.

During fiscal year 2010, the Organization purchased substantially all the assets, excluding real estate, of Empowerment Services Inc. (ESI), a Minnesota corporation, recognizing goodwill in the amount of $350,000.

The Organization does not amortize goodwill. Goodwill is tested for impairment using a qualitative assessment to determine whether it is more likely than not that the fair value is less than its carrying amount.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Split Interest Agreements

The Organization is named as a beneficiary in various gift annuities, charitable remainder trusts, and unitrusts. Upon notification of the gift an asset is recorded for the difference between the fair value of those assets and the liability under the gift contracts with donors. The amount expected to be received is established at the time of the contribution using life expectancy actuarial tables, expected investment returns and annuity payments, and is revalued at the end of each fiscal year. Actual gains and losses resulting from the annual revaluation of these obligations are reflected as temporarily or permanently restricted, consistent with the method used to initially record the contributions.

The value of these gifts was $1,040,224 and $976,684 at September 30, 2012 and 2011, respectively. The assets are recorded in the Beneficial Interest in Perpetual Trust on the Consolidated Statements of Financial Position.

The Organization became the trustee for the Pittman Trust in 2007. The trust is held for 20 years. The trust provides that the lower of 8% of trust assets or the total interest and dividends earned by the trust will be distributed to the remainders. At the end of 20 years, the trust will pay out to the Organization. The value of the trust, as of 2012, is booked at present value of $470,042 as an asset of $1,417,926 and an offsetting liability of $947,883 for the value of the future obligations under the trust. As of 2011, the value of the trust was booked at present value of $385,444 as an asset of $1,232,433 and an offsetting liability of $846,989 for the values of the future obligations under the trust. The assets are recorded in the Beneficial Interest in Perpetual Trust and the liability is recorded in the Obligation under Trust Agreement on the Consolidated Statements of Financial Position.

Conditional Grants

Forgivable loans have been recorded as conditional contributions. Revenue from these loans is being recognized evenly over the conditional use period. As such they are recorded as a long-term liability and included in Note 8, Long-Term Debt and Line of Credit.

Asset Retirement Obligation

A conditional asset retirement obligation is a legal obligation to perform an asset retirement activity in which the timing and/or settlement are conditional on a future event that may or may not be within the control of the entity. The Organization estimated the cost of any potential obligation to remove asbestos. The Organization used a future value rate assumption of 3% and a present value risk-free rate of 7% to determine the potential liability. The Organization has recorded a liability of $3,642 at September 30, 2012 and 2011.

Government Contracts

Government contracts are recorded as revenue when earned. The rates for the waivered service programs are determined each year through negotiations with various counties in the State of Minnesota. Revenue is earned when eligible expenditures, as defined in each grant or contract, are made. Funds received but not yet earned are shown as deferred revenue.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Government Contracts (Continued)

Expenditures under government contracts are subject to review by the granting authority. To the extent, if any, that such a review reduces expenditures allowable under these contracts, the Organization will record such disallowance at the time the final assessment is made.

The Organization receives a significant portion of its governmental service fees from Medicaid, Medical Assistance, Minnesota Supplemental Assistance, Social Security and Supplemental Security income which are subject to regulated rate increases.

Contributions

Contributions, unconditional promises to give, and other assets are recognized at fair values and are recorded as made. All contributions are available for unrestricted use unless specifically restricted by the donor.

The Organization reports gifts as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Adoption Fees

Revenue recognition of adoption fees occurs as follows: Half of the initial coordination fees are recognized at the initiation of the adoption process; the remaining portion is amortized over 18 months, management's estimated average length of time until an adoption is completed.

Advertising Expenses

Advertising expenditures are expensed as incurred. Advertising expense for the years ended September 30, 2012 and 2011 totaled $186,920 and $204,515, respectively.

Functional Expense Allocation

Expenses are allocated based on direct expenses whenever possible. Indirect expenses are allocated based on the best estimates of management.

Tax Exempt Status

Lutheran Social Service of Minnesota, Lutheran Social Service of Minnesota Foundation, and Partners In Community Supports, Inc. (PICS) have tax exempt status under Section 501(c)(3) of the Internal Revenue Code and Minnesota Statute. Rezek House LLC, LSS Townhomes LLC, LSS Supportive Housing LLC, CFCL Lending LLC, and CFCL LLC are single member limited liability companies, the activities of which are reported within the activities of the Organization as exempt activities. The Organization has been classified as an organization that is a public charity under the Internal Revenue Code and charitable contributions by the donors are tax deductible.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Tax Exempt Status (Continued)

LSS Park Avenue Apartments LP and LSS Development LLC are taxable entities formed as part of the financing of Park Avenue Apartments. The project provides low income individuals and families a quality place to live at below market rates. After the tax credit financing period ends in 2024, the Organization has the option to acquire the property at a bargain purchase price from their financing partner.

The Organization has adopted the income tax standard regarding the recognition and measurement of uncertain tax positions. The Organization has no current obligation for unrelated business income tax. The Organization's tax returns are subject to review and examination by federal and state authorities. The tax returns for the years 2009 to 2011 are open to examination by federal and state authorities.

Use of Estimates

The preparation of the consolidated financial statements in conformity with U.S. generally accepted accounting principles (GAAP) 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Subsequent Events

In preparing these financial statements, the Organization has evaluated events and transactions for potential recognition or disclosure through January 29, 2013, the date the consolidated financial statements were available to be issued.

NOTE 2 PLEDGES RECEIVABLE

Pledges receivable at September 30, 2012 and 2011 consist of commitments from various donors. The discount rate has been imputed at 3.5%, which approximates the Organization's risk free borrowing rate at September 30, 2012 and 2011. The allowance for uncollectible accounts was $43,099 and $51,791 for 2012 and 2011, respectively.

	2012	2011
Unconditional Pledges Receivable	$ 618,586	$ 505,892
Unamortized Discount	(7,560)	(10,639)
Allowance for Uncollectible Accounts	(43,099)	(51,791)
Total	$ 567,927	$ 443,462
Amounts Due in:		
Less Then One Year	$ 427,956	$ 328,396
One to Five Years	190,630	177,496
Total	$ 618,586	$ 505,892

NOTE 2 PLEDGES RECEIVABLE (CONTINUED)

Pledges receivable are recorded on the financial statements as follows:

	2012	2011
Current Pledges Receivable	$ 384,857	$ 276,605
Long-Term Pledges Receivable	183,070	166,857
	$ 567,927	$ 443,462

Pledges receivable from board members and employees totaled $178,147 and $97,701 at September 30, 2012 and 2011, respectively.

NOTE 3 FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amounts of cash and cash equivalents, accounts receivable and accounts payable approximate fair value because of the short maturity of these financial instruments. The fair value of pledges receivable, which is based on discounted cash flows using current interest rates, approximates the carrying value. The carrying values of investments and the beneficial interest in perpetual trust, which are the fair value, are based upon fair value measurements.

Fair Value Hierarchy

The Organization has categorized its financial instruments based on the priority of the inputs to the valuation technique, into a three-level 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). If the inputs used to measure the financial instruments fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value of the instrument.

Financial assets recorded on the statement of financial position are categorized based on the inputs to the valuation techniques as follows:

Level 1 – Financial assets and liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market that the Organization has the ability to access (examples include active exchange-traded equity securities, listed derivatives, and most U.S. Government and agency securities).

Level 2 – Financial assets and liabilities whose values are based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability.

NOTE 3 FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

Fair Value Hierarchy (Continued)

Level 2 inputs include the following:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in non-active markets (examples include corporate and municipal bonds, which trade infrequently);
- Pricing models whose inputs are observable for substantially the full term of the asset or liability (examples include most over-the-counter derivatives, including interest rate and currency swaps); and
- Pricing models whose inputs are derived principally from or corroborated by observable market data through correlation or other means for substantially the full term of the asset or liability (examples include certain residential and commercial mortgage related assets, including loans, securities, and derivatives).

Level 3 – Financial assets and liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect management's own assumptions about the assumptions a market participant would use in pricing the asset or liability (examples include certain private equity investments, long-term promises to give, split-interest agreements, and long-term grants payable).

The following table presents the Organization's value for those investments, excluding money market funds, measured at fair value on a recurring basis as of September 30:

	2012			
	Level 1	Level 2	Level 3	Total
INVESTMENTS				
Equities	$ 1,453,613	$ -	$ -	$ 1,453,613
Mutual Funds	843,665	-	-	843,665
Bonds	-	441,921	-	441,921
	$ 2,297,278	$ 441,921	$ -	$ 2,739,199
BENEFICIAL INTEREST IN PERPETUAL TRUST	$ -	$ -	$ 2,574,870	$ 2,574,870

	2011			
	Level 1	Level 2	Level 3	Total
INVESTMENTS				
Equities	$ 1,259,240	$ -	$ -	$ 1,259,240
Mutual Funds	725,332	-	-	725,332
Bonds	-	400,759	-	400,759
	$ 1,984,572	$ 400,759	$ -	$ 2,385,331
BENEFICIAL INTEREST IN PERPETUAL TRUST	$ -	$ -	$ 2,266,716	$ 2,266,716

NOTE 3 FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

Fair Value Hierarchy (Continued)

The totals above do not include certain amounts as they are not measured on a recurring basis at fair value. The table below reconciles total investments:

Total Investments	2012	2011
Investments Not Measured at Fair	$ 2,794,528	$ 2,436,203
Value on a Recurring Basis:		
Cash and Cash Equivalents	(55,329)	(50,872)
Total Investments Measured at Fair Value on a Recurring Basis	$ 2,739,199	$ 2,385,331

Fair Value Measurements

The Organization uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Additional information on how the Organization measures fair value is as follows:

Investments – Investments are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices. Securities valued using Level 1 inputs include those traded on an active exchange, such as the New York Stock Exchange, as well as U.S. Treasury and other U.S. government and agency mortgage-backed securities that are traded by dealers or brokers in active over-the-counter markets.

Beneficial interest in Perpetual Trusts – Perpetual Trusts are recorded at fair value on a recurring basis. Fair value measurement is estimated based upon the Organization's percentage interest in the fair value of the trust's assets, and, accordingly, are classified using Level 3 inputs. The underlying assets in the trusts are valued based upon quoted prices.

Level 3 Assets

The following table provides a summary of changes in fair value of the Organization's Level 3 financial assets for the years ended September 30, 2012 and 2011:

	Beneficial Interest in Perpetual Trust
Balance as of October 1, 2011	$ 2,266,716
Distribution	(164,208)
Change in Value of Undistributed Trust Assets	472,362
Balance as of September 30, 2012	$ 2,574,870
Balance as of October 1, 2010	$ 2,435,456
Distribution	(164,208)
Change in Value of Undistributed Trust Assets	(4,532)
Balance as of September 30, 2011	$ 2,266,716

NOTE 3 FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

Level 3 Assets

The fair value of long-term debt is estimated based on current rates offered to the Organization for debt of similar terms and maturities. Under this method, the Organization's fair value of long-term debt was approximately $4.9 million more than the carrying value at September 30, 2012 and 2011.

NOTE 4 LAND, BUILDINGS, AND EQUIPMENT

Cost and related accumulated depreciation at September 30, 2012 and 2011 were:

	2012		2011	
	Cost	Accumulated Depreciation	Cost	Accumulated Depreciation
Land	$ 3,481,707	$ -	$ 3,536,707	$ -
Land Improvements	940,108	563,546	920,844	516,655
Construction in Process	261,535	-	10,324	-
Buildings and Building Improvements	44,507,402	13,054,388	44,415,530	11,611,980
Equipment	7,355,093	5,794,407	6,891,548	5,460,557
Vehicles	180,170	151,372	159,538	137,556
Capital Leases - Vehicles	1,320,896	576,504	1,320,896	387,805
	58,046,911	$ 20,140,217	57,255,387	$ 18,114,553
Net Land, Buildings and Equipment	$ 37,906,694		$ 39,140,834	

NOTE 5 PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS

Defined Benefit Pension Plan

The Organization has a noncontributory defined benefit pension plan. The Organization froze its defined benefit pension plan for all participants. The plan provided for 100% vesting after five years of service or attainment of the normal retirement age of 65, with reduced compensation in cases of early retirement. Benefits are based on credited years of service and the average of the employee's highest compensation over a consecutive 36-month period during the 10 years prior to retirement.

The measurement dates used for the Plan disclosures are as of September 30, 2012 and 2011 and for the years then ended.

NOTE 5 PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS (CONTINUED)

Defined Benefit Pension Plan (Continued)

The changes in the projected benefit obligation are as follows:

	2012	2011
Change in Projected Benefit Obligation		
Projected Benefit Obligation at Beginning of Year	$ 32,027,141	$ 31,756,002
Service Cost	-	-
Interest Cost	1,654,884	1,678,646
Amendment (Curtailment)	-	-
Assumption changes	-	-
Actuarial (Gain)/Loss	4,058,433	(182,270)
Benefits Paid	(1,552,802)	(1,225,237)
Projected Benefit Obligation at End of Year	$ 36,187,656	$ 32,027,141

	2012	2011
Change in Plan Assets:		
Fair Value of Plan Assets at Beginning of Year	$ 15,290,494	$ 15,788,424
Actual Return on Plan Assets	3,048,536	(346,516)
Employer Contribution	1,800,000	1,200,000
Expenses	(128,180)	(126,177)
Benefits Paid	(1,552,802)	(1,225,237)
Fair Value of Plan Assets at End of Year	$ 18,458,048	$ 15,290,494
Funded Status of the Plan:		
Benefit Obligation	$ 36,187,656	$ 32,027,141
Fair Value of Plan Assets	18,458,048	15,290,494
Excess of Benefit Obligation Over Fair Value of Plan Assets	$ (17,729,608)	$ (16,736,647)
Components of Net Periodic Benefit Costs:		
Service Cost	$ -	$ -
Interest Cost	1,654,884	1,678,646
Expected Return on Plan Assets	(1,214,181)	(1,262,064)
Amortization of Net Loss	380,640	357,208
Net Periodic Pension Cost	$ 821,343	$ 773,790
Underfunded Plan Information:		
Projected Benefit Obligation at End of Year	$ 36,187,656	$ 32,027,141
Accumulated Benefit Obligation at End of Year	36,187,656	32,027,141
Fair Value of Assets at End of Year	18,458,048	15,290,494

NOTE 5 PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS (CONTINUED)

Defined Benefit Pension Plan (Continued)

Weighted average assumptions used to determine net periodic benefit cost are as follows:

	2012	2011
Actuarial Assumptions		
Assumptions Used to Determine Benefit Obligations at September 30:		
Assumed Discount Rate	4.50%	5.25%
Assumed Annual Increase in Salaries	-	-
Assumptions Used to Determine Net Periodic Benefit Cost for Years Ended September 30:		
Assumed Discount Rate	5.25%	5.75%
Expected Long-Term Return on Plan Assets	8.00%	8.00%
Assumed Annual Increase in Salaries	-	-

Investment Allocation/Basis Used to Determine Expected Long-Term Rate of Return

This investment policy is to enhance the value of Defined Benefit Plan funds held in the portfolio(s) and at the same time provide a dependable, increasing source of income, which will be used to support benefit distributions of the Plan. The portfolio shall be composed of diversified assets, including both equities and fixed-income investments. The equities are designed to provide current income, growth of income and appreciation of principal. The fixed-income investments are intended to provide a predictable and reliable source of interest income while reducing the volatility of the portfolio. As a long-term policy guideline, equity investments will constitute 65% of Plan assets and fixed income (bonds and cash) 35% of the portfolio.

The percentage of the fair value of total plan assets held as of September 30, 2012 and 2011 (the measurement date) by asset category is as follows:

	2012	2011
The Plan Assets are invested as follows:		
Equity Securities	77%	72%
Debt Securities	23%	28%

NOTE 5 PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS (CONTINUED)

Investment Allocation/Basis Used to Determine Expected Long-Term Rate of Return (Continued)

The Plan uses fair value measurement to record fair value adjustments to certain assets and to determine fair value disclosures. The following table presents the fair value hierarchy for the balances of the assets of the Plan measured at fair value on a recurring basis as of September 30:

	2012			
	Level 1	Level 2	Level 3	Total
INVESTMENTS				
Equities	$ 4,872,479	$ -	$ -	$ 4,872,479
Mutual Funds	-	9,285,856	-	9,285,856
Bonds	-	4,220,048	-	4,220,048
	$ 4,872,479	$ 13,505,904	$ -	$18,378,383

	2011			
	Level 1	Level 2	Level 3	Total
INVESTMENTS				
Equities	$ 3,928,426	$ -	$ -	$ 3,928,426
Mutual Funds	-	7,119,113	-	7,119,113
Bonds	-	4,201,461	-	4,201,461
	$ 3,928,426	$ 11,320,574	$ -	$15,249,000

The totals above do not include certain amounts as they are not measured on a recurring basis at fair value. The table below reconciles total investments:

	2012	2011
Total Investments	$ 18,458,048	$ 15,290,494
Investments Not Measured at Fair Value on a Recurring Basis:		
Cash and Cash Equivalents	(79,665)	(41,494)
Total Investments Measured at Fair Value on a Recurring Basis	$ 18,378,383	$ 15,249,000

The Organization provided funding to the plan of $1,800,000 during fiscal year 2012. Additional funding of $1,200,000 annually is expected.

Estimated future benefit payments, which reflect expected future services, are as follows:

Year Ending September 30,	Amount
2013	$ 1,685,351
2014	1,751,253
2015	1,834,043
2016	1,933,330
2017	2,006,146
2018-2022	11,260,532

NOTE 5 PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS (CONTINUED)

Other Post Retirement Benefits

The Organization also has a defined contribution 403(b) retirement savings plan that covers substantially all employees. Employees can elect to contribute a portion of their pretax earnings to the plan. Employees are eligible for participation in the plan upon employment. In 2012 and 2011, the Organization matched participant contributions by 50% up to the first 4% of eligible compensation. The plan was amended in fiscal 2005 to allow for Employer discretionary contributions to be determined annually by the Organization's management. The discretionary contribution in 2012 and 2011 was 2% of eligible compensation. Employees become fully vested in the Employer match and discretionary contribution after five years of service. Expenses charged to the Organization's financial statements for this plan was $1,808,613 and $1,769,337 for the years ended September 30, 2012 and 2011, respectively.

NOTE 6 BENEFICIAL INTEREST IN PERPETUAL TRUST

The Anderson Trust, a perpetual trust in the amount of $2,574,870 and $2,266,716 at September 30, 2012 and 2011, respectively, is included in permanently restricted net assets. The Organization has the irrevocable right to receive the income on these trust assets, subject to certain limitations, but will never receive the assets held in trust. The unrealized gains and the undistributed earnings on the trusts are reported as additions to the permanently restricted net asset balance. The distributed income from these trusts is to be used for the maintenance and operation of a facility for needy children. This restriction was expanded by the Minnesota District Court of Hennepin County in 2009 to include adults with disabilities and enlarged the area to within a 50-mile radius from the present location. Income distributions from the trust were $164,208 for the years ended September 30, 2012 and 2011.

NOTE 7 SELF-INSURED BENEFIT LIABILITIES

In 1992, a benefit fund was established for the Organization's self-funded employee medical, dental, and short-term disability plans. Under the plans, which are administered by the trust, contributions are made by the Organization and employees to pay claims, administrative costs, and commercial insurance premiums. The commercial insurance premiums (stop-loss insurance) cover individual medical claims in excess of $200,000 and aggregate claims over 120% of annual expected claims or $6,344,400. The self-insured medical, dental, and short-term disability expense recorded in the Organization's financial statements was $6,502,796 and $5,587,196 in 2012 and 2011, respectively. The Organization has recorded liabilities of $1,554,856 and $1,431,635 for claims incurred but not yet paid as of September 30, 2012 and 2011, respectively. The trust is a separate entity which is excluded from the Organization's consolidated financial statements

NOTE 7 SELF-INSURED BENEFIT LIABILITIES (CONTINUED)

The Organization became self-insured for workers' compensation on April 1, 1994. As of September 30, 2012 and 2011, the Organization has recorded liabilities of $329,150 and $399,810, respectively, for claims incurred but not yet reported. In addition, the Organization has a $1,291,953 surety bond to secure amounts potentially required to be paid for workers' compensation. Consulting actuaries assist the Organization in determining its liability for self-insured claims.

NOTE 8 LONG-TERM DEBT AND LINE OF CREDIT

		2012		2011	
Description	Security	Face Value	Current Value	Face Value	Current Value
4.31% to 4.50% City of Grand Rapids, Minnesota, Tax-Exempt Series 2003A and B Bonds, Due through 2015	Houses, Computers and Motor Vehicles	$ 167,389	$ 167,389	$ 503,660	$ 503,660
4.92% to 5.70% City of Brainerd, Minnesota, Tax-Exempt Series 2001A, B and C Bonds, Due through 2016	Houses, Computers and Motor Vehicles	196,158	196,158	284,287	284,287
4.91% to 6.41% Minnesota Agricultural and Economic Development Board, Tax-Exempt Series 1999A Bonds, Due through 2014	Houses, Computers and Motor Vehicles	64,107	64,107	104,061	104,061
Note Payable to American National Bank of Minnesota, Interest at 6.75%, Due through March 1, 2014	Land and Buildings	195,279	195,279	223,100	223,100
Note Payable to Minnesota Housing Finance Agency, Non-Interest Bearing, Forgivable in 2020 *	Safe House Land and Building	40,439	14,659	40,439	16,681
Thrivent PRI Loan, 2% Interest; Due through July 31, 2014		533,334	533,334	666,667	666,667
Lutheran Community Foundation PRI Loan, 2% Interest; Due through July 31, 2014		66,666	66,666	83,333	83,333
US Bank Short Term Bank Note, Interest at LIBOR plus two basis points, Due through April 30, 2013	Accounts Receivable and Inventory	135,604	135,604	158,463	158,463
Note Payable to Hennepin County Housing and Redevelopment Authority Affordable Housing Incentive Fund, Non-Interest Bearing, Forgivable in 2037 *	Land and Buildings	600,000	501,668	600,000	521,667
Capital Leases	Vehicles	760,423	760,426	942,366	942,366
Subtotal for Lutheran Social Service of Minnesota		2,759,399	2,635,289	3,606,376	3,504,285

NOTE 8 LONG-TERM DEBT AND LINE OF CREDIT (CONTINUED)

Description	Security	2012 Face Value	2012 Current Value	2011 Face Value	2011 Current Value
Note Payable to Minnesota Housing Finance Agency, Non-Interest Bearing, Forgivable in 2020 *	Land and Buildings	521,674	191,281	521,674	217,364
Note Payable to City of St. Paul Housing and Redevelopment Authority, Interest at 2.00%, Principal and Interest Due through December 31, 2026	Land and Buildings	372,500	228,664	366,500	217,777
Subtotal for Rezek House LLC		894,174	419,945	888,174	435,141
Note Payable to Minnesota Housing Finance Agency, Non-Interest Bearing, Forgivable May 16, 2033 *	Land and Buildings	1,720,580	1,199,339	1,720,580	1,257,254
Note Payable to Minnesota Housing Finance Agency, Non-Interest Bearing, Due May 16, 2033	Land and Buildings	119,420	64,194	119,420	62,324
Note Payable to Family Housing Fund, Non-Interest Bearing, Due May 16, 2033	Land and Buildings	130,000	70,654	130,000	68,596
Note Payable to Minnesota Community Development Authority, Interest at 1.00%, Principal and Interest Due May 16, 2033	Land and Buildings	328,000	211,514	325,000	205,354
Subtotal for LSS Townhomes LLC		2,298,000	1,545,701	2,295,000	1,593,528
Note Payable to Family Housing Fund, Non-Interest Bearing, Due May 19, 2034	Land and Buildings	126,000	63,103	126,000	61,117
Note Payable to Hennepin County Housing and Redevelopment Authority, Interest at 1.00%, Principal and Interest Due May 19, 2034	Land and Buildings	281,778	169,229	279,175	163,901
Note Payable to City of Minneapolis, Interest at 1.00%, Principal and Interest Due May 19, 2034	Land and Buildings	275,814	165,695	273,269	160,480

NOTE 8 LONG-TERM DEBT AND LINE OF CREDIT (CONTINUED)

		2012		2011	
Description	Security	Face Value	Current Value	Face Value	Current Value
Note Payable to Minnesota Housing Finance Agency, Non-Interest Bearing, Due May 19, 2034	Land and Buildings	600,000	300,489	600,000	291,032
Note Payable to City of Minneapolis, Non-Interest Bearing, Forgivable May 19, 2034 *	Land and Buildings	100,000	71,945	100,000	75,277
Total for LSS Supportive Housing LLC		1,383,592	770,462	1,378,444	751,807
Note Payable to Wells Fargo, N.A.; Interest at 1.9 plus LIBOR Rate, Due through December 31, 2017	Center For Changing Lives Building and improvements	2,815,853	2,815,853	2,959,855	2,959,855
Note Payable to New Markets Investment XXVIII, LLC, Interest at 5.81%, Principal payments from 2014 through January 24, 2038 **	Center For Changing Lives Building and improvements	13,717,365	11,514,834	13,717,365	11,978,524
Total for LSS Center for Changing Lives		16,533,218	14,330,687	16,677,220	14,938,379
Note Payable to Hennepin County AHTF, Interest at 5.50%, Principal and Interest Due January 24, 2038	Park Avenue Apartments	649,397	649,397	615,542	615,542
Note Payable to City of Minneapolis AHIF, Interest at 1%, Principal and Interest Due December 31, 2037	Park Avenue Apartments	419,504	419,504	415,504	415,504
Total for Park Avenue Apartments		1,068,901	1,068,901	1,031,046	1,031,046
Total Long-Term Debt and Conditional Grants		24,937,284	20,770,984	25,876,260	22,254,186
Less: Conditional Grants		2,982,693	1,978,891	2,982,693	2,088,244
Total Debt		21,954,591	18,792,094	22,893,567	20,165,942
Less: Current Maturities of Long-Term Debt		808,489	808,489	943,102	943,102
Long-Term Debt, Excluding Current Maturities and Conditional Grants		$ 21,146,102	$ 17,983,605	$ 21,950,465	$ 19,222,840

* Conditional Grants

** There is a loan receivable in the amount of $10,471,529 with an interest rate of 7.4% associated with the Center for Changing Lives project. Interest payments received from this loan offset interest expense paid on the Note Payable, in the amount of $11,514,834, to New Markets XXVIII LLC.

NOTE 8 LONG-TERM DEBT AND LINE OF CREDIT (CONTINUED)

For below market loans the present value discount is imputed using rates between 3% and 5% depending on the year the loan was initiated.

Principal maturities for long-term debt are as follows:

Year Ending September 30,		Amount
2013		$ 808,489
2014		995,976
2015	**	11,902,077
2016		298,302
2017		158,051
Thereafter		4,629,199
Total		$ 18,792,094

*** A majority of the amount payable in 2015 is offset by an incoming loan receivable in the amount of $10,471,529.

Land and buildings with a net book value of $11,217,194 and $11,586,387 are pledged as collateral at September 30, 2012 and 2011, respectively, primarily on MHFA mortgage notes.

At September 30, 2012, the Organization was not in compliance with the liabilities to net assets ratio for its Brainerd Series 2001 bonds and received a waiver subsequent to year-end. The Organization received a waiver dated January 7, 2013. The balance is scheduled to be paid in full by December 31, 2016.

Line of Credit

The Organization has a total of $3,000,000 of working capital lines of credit with U.S. Bank. The lines bear interest on outstanding borrowings at the bank's reference rate (3.25% at September 30, 2012) and mature on March 31, 2013. At September 30, 2012 and 2011, the amount outstanding was $-0-. In addition, there is a short-term loan of $210,000 that will be renewed on April 30, 2013. The interest rate is 30 day LIBOR + 290 basis points, and $1,750 in principal is paid each month. The balance outstanding at end of the year ended September 30, 2012 and 2011 was $135,604 and $158,463, respectively.

On July 10, 2012, the Organization entered into a line of credit with Park Midway Bank for $3,000,000. This line bears interest on outstanding borrowings at the bank's reference rate (3.25% at September 30, 2012) and matures on July 10, 2013. At September 30, 2012, the amount outstanding was $180,335.

NOTE 8 LONG-TERM DEBT AND LINE OF CREDIT (CONTINUED)

Center for Changing Lives

The Organization established a construction loan of up to $6.4 million for the Center for Changing Lives Project. The balance outstanding at end of the year ended September 30, 2012 and 2011 was $2,815,853 and $2,959,855, respectively For the first four years, quarterly payments of interest were required at a rate equal to LIBOR plus 1.9%. All funds received for the Capital Campaign must be used to pay down the loan; there are outstanding pledges receivable in the amount of $75,693 and $139,741 as of September 30, 2012 and 2011, respectively.

The schedule of principal amortization during this four year period provided that the outstanding principal at the end of each year may not exceed a specified maximum amount:

December 31, 2008	$6,800,000
December 31, 2009	$5,600,000
December 31, 2010	$4,400,000
December 31, 2011	$3,200,000
2012 to 2017	15 Year Amortization of 2011 Balance
December 31, 2017	Balance Due in Full

At the end of the four year initial period (January 24, 2012), the loan (a maximum of $3,200,000) converted to a fixed rate based on the five-year treasury rate plus 1.05%. The loan matures December 31, 2017.

There is a loan receivable from CFCL Investment Fund, LLC in the amount of $10,471,529 and a loan payable to the New Market Investment XXVIII, LLC in the amount of $13,717,365 from the Center for Changing Lives Project. There will be quarterly interest payments due on these amounts until 2014. Principal payments will be made starting April 2014, with a loan maturity date of January 24, 2038.

NOTE 9 LEASES

The Organization has operating lease agreements for office space, residential facilities and vehicles. The majority of these leases expire throughout the next five years. In most instances, office space lease terms are renewable.

As of September 30, 2012, future minimum rental payments required under operating leases that have initial or remaining non-cancelable lease terms in excess of one year were:

Year Ending September 30,	Amount
2013	$ 2,628,475
2014	1,716,099
2015	1,260,722
2016	933,747
2017	387,587
Thereafter	344,220
Total	$ 7,270,850

Rental expense for all operating leases was $2,690,305 and $2,606,197 for the years ended September 30, 2012 and 2011, respectively.

The Organization leases certain vehicles under long-term lease agreements. The leases, which are accounted for as capital leases, expire at various dates. The cost of vehicles recorded under capital leases was $1,320,896 at September 30, 2012 and 2011. Accumulated depreciation was $576,504 and $387,805 at September 30, 2012 and 2011, respectively. Future minimum lease payments are as follows:

Year Ending September 30,	Amount
2013	$ 228,967
2014	221,989
2015	175,608
2016	131,097
2017	105,828
Total Lease Payments	863,489
Less Interest Expense	(103,063)
Total Minimum Lease Payments	$ 760,426

NOTE 10 NET ASSETS

Temporarily Restricted

Temporarily restricted net assets are available for the following purposes at September 30, 2012 and 2011:

	2012	2011
Split Interest Deferred Gifts / Trusts	$ 1,558,650	$ 1,361,329
Donations and Forgivable Loan Interest for Property	13,653,176	13,712,933
Cash Restricted by Donors for Specific Program Use	3,100,493	2,701,993
Total	$ 18,312,319	$ 17,776,255

Permanently Restricted

Permanently restricted net assets with investment return restricted for the following purposes at September 30, 2012 and 2011 are as follows:

	2012	2011
Perpetual Trust for VASA Lutheran Home	$ 2,574,870	$ 2,266,716
Endowment Investments	1,084,240	1,084,089
Camp Knutson	44,768	57,664
Other	208,822	188,208
Total	$ 3,912,700	$ 3,596,677

Net Assets Released from Restrictions

The net assets released from restrictions as of September 30, 2012 and 2011 consist of the following:

	2012	2011
Time and Purpose Releases	$ 2,804,212	$ 2,527,709
Building Releases	959,030	957,525
Total	$ 3,763,242	$ 3,485,234

NOTE 11 COMMITMENTS AND CONTINGENCIES

A land lease between Luther Seminary and the organization commenced in 1992 at the site of the new administrative office facility. The lease term is 50 years, with the option to extend the lease for an additional 25 years. Annual rent is $13,911 adjusted every five years for the percentage change in the Consumer Price Index for Urban Wage Earners and Clerical Workers.

NOTE 11 COMMITMENTS AND CONTINGENCIES (CONTINUED)

The Organization provides Guardianship and Conservatorship services for vulnerable adults throughout the state of Minnesota. For these services, the court orders the appointment of a person or agency to act as a substitute decision maker for a person. The Organization follows the National Guardianship Association and the Minnesota Association for Guardianship Conservatorship standards. As of September 30, 2012 and 2011, the Organization was the guardianship or conservator of estates totaling $32,470,519 and $30,620,295, respectively.

The Organization is involved in legal action in regards to normal business activities. Management does not feel that these actions are material and pose a financial threat to the organization and, accordingly, no liability is accrued at September 30, 2012 and 2011.

NOTE 12 ENDOWMENTS

The Organization has donor restricted endowment funds established for the purpose of securing the Organization's long-term financial viability and continuing to meet the needs of the Organization. As required by GAAP, net assets of the endowment fund are classified and reported based on the existence or absence of donor-imposed restrictions. The Board of Directors of the Organization has interpreted the state's 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 Organization classifies as permanently restricted net assets the original value of the gifts to the permanent endowment and the value of subsequent gifts to the permanent endowment. The remaining portion of the donor restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the organization in a manner consistent with the standard of prudence prescribed by UPMIFA.

<u>Funds with Deficiencies</u>

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 were $202,367 as of September 30, 2011. These deficiencies resulted from unfavorable market fluctuations in the endowment fund's investments.

NOTE 12 ENDOWMENTS (CONTINUED)

Return Objectives and Risk Parameters, Investment and Spending Policies for the Organization's Foundation

The Organization's Foundation Board of Directors has adopted an Investment and Distribution Policy for its endowments assets. The policy seeks to maintain the purchasing power of the endowment assets while providing a predictable funding stream to its programs. In addition, the organization has hired an outside investment manager to oversee the investment of the endowment funds. Endowment assets include those assets of donor-restricted funds that the Organization must hold in perpetuity or for a donor-specified period(s).

The investment policy provides a targeted mix of equity and income investments. Investment performance is benchmarked quarterly against the performance of the S&P 500 and the applicable bond fund indexes.

Annual distributions from the Endowment funds are targeted at 5% of its endowment fund's average fair value over the prior 12 quarters through the calendar year-end based upon the preceding the fiscal year in which the distribution is planned. In addition, actual investment performance is considered in the distribution decision.

Endowment net asset composition by type and changes in endowment net assets for the years ended September 30 is as follows:

	2012			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment Fund Balance, September 30, 2011	$ (202,367)	$ -	$ 1,329,460	$ 1,127,093
Contributions	-	-	291	291
Investment Return:				
Investment Income	19,869	8,079	-	27,948
Investment Expenses	(11,359)	-	-	(11,359)
Realized Gains (Losses)	(11,759)	-	-	(11,759)
Unrealized Gains (Losses)	205,616	-	-	205,616
Total Investment Return	202,367	8,079	-	210,446
Endowment Fund Balance, September 30, 2012	$ -	$ 8,079	$ 1,329,751	$ 1,337,830

	2011			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment Fund Balance, September 30, 2010	$ (155,889)	$ -	$ 1,329,295	$ 1,173,406
Contributions	-	-	165	165
Investment Return:				
Investment Income	23,126	-	-	23,126
Investment Expenses	(10,762)	-	-	(10,762)
Realized Gains (Losses)	-	-	-	-
Unrealized Gains (Losses)	(58,842)	-	-	(58,842)
Total Investment Return	(46,478)	-	-	(46,478)
Endowment Fund Balance, September 30, 2011	$ (202,367)	$ -	$ 1,329,460	$ 1,127,093

NOTE 13 AGREEMENT WITH CHILDREN'S HOME SOCIETY & FAMILY SERVICES

Effective July 1, 2012, the Organization entered into a management services agreement with Children's Home Society & Family Services (CHSFS). The agreement continues through June 30, 2018 and automatically renews for additional one-year terms thereafter unless terminated pursuant to terms of the agreement. The President/CEO of the Organization will serve concurrently as the chief executive officer of CHSFS and report to the Board of Directors of CHSFS. Under this agreement, the Organization provides management and administrative services for CHSFS in exchange for a management fee which is calculated based on the operating revenues of CHSFS. At September 30, 2012, the Organization had a receivable from CHSFS totaling approximately $85,000 for management fees. In addition, the organization secured a $3 million line of credit for the use of CHSFS. At September 30, 2012, the Organization had a receivable from CHSFS for approximately $5,000 which was advanced for cash flow purposes. During the duration of the agreement, interest on the line of credit shall neither accrue nor be payable to the Organization. Principal repayment from CHSFS to the Organization shall be made to the extent funds are available in the timing and amount determined by the Organization. The loan is secured by a mortgage on real property owned by CHSFS. In conjunction with this management agreement, the Organization and CHSFS also signed a lease whereby the Organization will lease space from CHSFS from July 1, 2012, through June 30, 2018. The lease provides for annual rental payments to CHSFS of approximately $240,000.