MASONIC HOMES OF THE GRAND LODGE OF
FREE AND ACCEPTED MASONS OF PENNSYLVANIA

(D/B/A "Masonic Villages of the Grand Lodge of Pennsylvania")

CONSOLIDATED FINANCIAL REPORT

DECEMBER 31, 2012

INDEX

Smith Elliott Kearns & Company, LLC
Certified Public Accountants & Consultants

INDEPENDENT AUDITOR'S REPORT

Board of Directors
Masonic Villages of the
Grand Lodge of Pennsylvania
Elizabethtown, Pennsylvania

We have audited the accompanying consolidated financial statements of the Masonic Homes of the Grand Lodge of Free and Accepted Masons of Pennsylvania and subsidiaries,which comprise the consolidated balance sheets as of December 31, 2012 and 2011, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation of consolidated 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 consolidated financial statements based on our audits. We did not audit the financial statements of Pennsylvania Acacia Insurance Company, Ltd., a wholly-owned subsidiary, which statements reflect total assets of $ 7,860,045 and $ 6,853,890 as of December 31, 2012 and 2011, respectively, and total revenues of $ 646,038 and $ 660,302, respectively, for the years then ended. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Pennsylvania Acacia Insurance Company, Ltd., is based solely on the report of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

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

Board of Directors
Masonic Villages of the
Grand Lodge of Pennsylvania

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, based on our audits and the report of other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Masonic Homes of the Grand Lodge of Free and Accepted Masons of Pennsylvania and subsidiaries as of December 31, 2012 and 2011 and the results of their operations, changes in their net assets, and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis-of-Matter

As discussed in Note 2 to the financial statements, the Masonic Homes of the Grand Lodge of Free and Accepted Masons of Pennsylvania adopted Financial Accounting Standards Board, Accounting Standards Update No. 2012-01, "Health Care Entities (Topic 954) – Continuing Care Retirement Communities – Refundable Advance Fees" (ASU #2012-01) during 2012. Our opinion is not modified with respect to that matter.

Smith Elliott Kearns & Company, LLC

Carlisle, Pennsylvania
April 8, 2013

MASONIC HOMES OF THE GRAND LODGE OF
FREE AND ACCEPTED MASONS OF PENNSYLVANIA

CONSOLIDATED BALANCE SHEETS

December 31, 2012 and 2011

ASSETS	2012	Restated 2011
Current Assets:		
Cash and cash equivalents (Note 3)	$ 19,799,696	$ 20,802,538
Assets whose use is limited and that are required for current liabilities (Note 8)	2,418,773	2,331,391
Resident accounts receivable, net of estimated uncollectibles of $ 256,000 in 2012 and $ 231,000 in 2011 (Note 4)	6,315,043	7,044,314
Accounts receivable:		
Pennsylvania Masonic Youth Foundation	1,082	-
Grand Lodge	-	15,102
Masonic Charities Fund	29,304	31,794
The Masonic Library and Museum of Pennsylvania	224	1,254
Investment income receivable	1,658,006	1,992,651
Estimated third party settlements receivable (Note 18)	2,303,001	2,160,705
Inventory	1,650,219	1,644,125
Other current assets	1,263,042	1,097,192
Notes receivable (Note 6)	3,350,406	3,892,877
Contributions receivable (Note 5)	96,400	84,200
Total current assets	38,885,196	41,098,143
Contributions receivable, net of current portion (Note 5)	477,586	459,035
Loan receivable - Susquehanna-Wagman Associates, LLC	33,602	33,602
Assets whose use is limited, net of current portion (Note 8)	2,524,015	2,524,015
Minimum liquid reserve requirement (Notes 7, 24)	13,757,357	13,694,313
Investments (Note 7)	570,380,230	540,459,120
Property and equipment, net (Note 9)	305,416,460	285,954,775
Other Assets:		
Deferred costs, net (Note 10)	1,440,228	1,643,094
Other long-term assets	6,973	8,573
Total other assets	1,447,201	1,651,667
Collections (Note 1)	-	-
Total assets	$ 932,921,647	$ 885,874,670

LIABILITIES AND NET ASSETS	2012	Restated 2011
Current Liabilities:		
Current installments of long-term debt (Note 12)	$ 7,125,000	$ 6,835,000
Accrued expenses	12,518,572	13,369,822
Accounts payable:		
Trade	10,161,051	12,587,753
Pennsylvania Masonic Youth Foundation	-	709
Grand Lodge	16,683	-
Deferred revenue from estates and trusts	43,670	30,082
Deposits - Residents	874,368	909,830
Deposits on unoccupied units	1,287,142	2,069,648
Annuities payable	1,220,633	1,190,877
Total current liabilities	33,247,119	36,993,721
Accrued pension costs (Note 17)	31,973,234	27,887,130
Annuities payable, net of current portion	6,395,966	6,407,499
Deferred revenue from landfill settlement	67,500	77,500
Refundable fees	50,938,044	49,717,122
Deferred revenue from entrance fees	83,933,818	77,519,438
Interest rate swap agreements (Note 11)	34,912,253	35,834,510
Long-term debt, including unamortized premium of $ 915,456 in 2012 and $ 977,870 in 2011	164,420,456	171,607,870
Total liabilities	405,888,390	406,044,790
Net Assets:		
Unrestricted	269,931,520	244,498,692
Temporarily restricted	48,189,721	31,963,288
Permanently restricted	208,912,016	203,367,900
Total net assets	527,033,257	479,829,880
Total liabilities and net assets	$ 932,921,647	$ 885,874,670

The accompanying notes are an integral part of these consolidated financial statements.

MASONIC HOMES OF THE GRAND LODGE OF FREE AND ACCEPTED MASONS OF PENNSYLVANIA

CONSOLIDATED STATEMENTS OF OPERATIONS

Years Ended December 31, 2012 and 2011

	2012	Restated 2011
Operating revenues:		
Resident service revenue (Note 18)	$ 116,381,949	$ 117,039,446
Provision for bad debts	(141,852)	(147,976)
Net resident service revenue	116,240,097	116,891,470
Amortization of entrance fees	9,478,109	8,670,406
Other operating revenue	3,075,193	2,370,035
Investment income	10,034,145	10,841,792
Unrealized appreciation (depreciation) on interest rate swap agreements	922,257	(11,318,749)
Total operating revenues	139,749,801	127,454,954
Operating expenses:		
Wages, salaries, and benefits	87,980,519	85,380,826
Supplies	15,534,502	15,186,768
Purchased services	13,261,192	12,856,965
Energy and utilities	7,737,516	7,918,308
Depreciation and amortization	16,458,514	15,994,517
Interest	5,895,404	7,139,313
Other operating expenses	6,961,575	6,336,561
Total operating expenses	153,829,222	150,813,258
Loss from operations	(14,079,421)	(23,358,304)
Nonoperating gains (losses):		
Contributions, gifts, and bequests	7,357,768	4,875,317
Contributions from Grand Lodge permanently restricted net assets	853,700	1,149,016
Income from perpetual trusts held by third parties	1,716,238	1,778,765
Realized gains on sale of investments	12,578,199	16,967,509
Adjustment of actuarial liabilities of split-interest agreements	(529,184)	(607,641)
Loss on disposal of property and equipment	(51,800)	(107,931)
Total nonoperating gains	21,924,921	24,055,035
Excess of revenues and gains over expenses and losses	7,845,500	696,731
Net assets released from restrictions:		
Satisfaction of program restrictions - Operations	4,909,303	5,436,375
Satisfaction of program restrictions - Purchase of property and equipment	680,292	4,147,362
Total net assets released from restrictions	5,589,595	9,583,737
Change in pension liability (Note 17)	(8,157,143)	(12,919,584)
Net unrealized appreciation (depreciation) on investments	20,154,876	(20,345,118)
Increase (decrease) in unrestricted net assets	$ 25,432,828	$ (22,984,234)

The accompanying notes are an integral part of these consolidated financial statements.

MASONIC HOMES OF THE GRAND LODGE OF
FREE AND ACCEPTED MASONS OF PENNSYLVANIA

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS

Years Ended December 31, 2012 and 2011

	2012				Restated 2011			
	Total	**Unrestricted**	**Temporarily Restricted**	**Permanently Restricted**	**Total**	**Unrestricted**	**Temporarily Restricted**	**Permanently Restricted**
Revenues and Gains:								
Total operating revenues	$ 139,749,801	$ 139,749,801	$ -	$ -	$ 127,454,954	$ 127,454,954	$ -	$ -
Nonoperating investment income	86,502	-	86,502	-	90,164	-	90,164	-
Realized gains on sale of investments	20,782,647	12,578,199	8,204,448	-	27,055,106	16,967,509	10,087,597	-
Contributions, gifts, and bequests	10,502,158	7,357,768	963,288	2,181,102	8,556,137	4,875,317	945,190	2,735,630
Contribution from Masonic Charities Fund	4,071	-	-	4,071	2,219	-	-	2,219
Contributions from Grand Lodge permanently restricted net assets	853,700	853,700	-	-	1,149,016	1,149,016	-	-
Income from perpetual trusts held by third parties	1,736,421	1,716,238	2,766	17,417	1,796,662	1,778,765	2,078	15,819
Total revenues and gains	173,715,300	162,255,706	9,257,004	2,202,590	166,104,258	152,225,561	11,125,029	2,753,668
Expenses and Losses:								
Unrestricted expenses	153,829,222	153,829,222	-	-	150,813,258	150,813,258	-	-
Loss on sale of property and equipment	51,800	51,800	-	-	107,931	107,931	-	-
Adjustment of actuarial assets and liabilities of split-interest agreements	501,672	529,184	(27,512)	-	588,943	607,641	(18,698)	-
Total expenses and losses	154,382,694	154,410,206	(27,512)	-	151,510,132	151,528,830	(18,698)	-
Excess of revenues and gains over expenses and losses	19,332,606	7,845,500	9,284,516	2,202,590	14,594,126	696,731	11,143,727	2,753,668
Net assets released from restrictions - Satisfaction of program restrictions	-	5,589,595	(5,594,595)	5,000	-	9,583,737	(9,748,834)	165,097
Change in pension liability (Note 17)	(8,157,143)	(8,157,143)	-	-	(12,919,584)	(12,919,584)	-	-
Net unrealized appreciation (depreciation) on investments	36,027,914	20,154,876	12,536,512	3,336,526	(32,849,055)	(20,345,118)	(12,109,484)	(394,453)
Increase (decrease) in net assets	47,203,377	25,432,828	16,226,433	5,544,116	(31,174,513)	(22,984,234)	(10,714,591)	2,524,312
Net assets at January 1, as originally reported	479,829,880	244,498,692	31,963,288	203,367,900	515,751,297	272,229,830	42,677,879	200,843,588
Prior period adjustment - restatement of amortization of entrance fees (Note 2)	-	-	-	-	(4,746,904)	(4,746,904)	-	-
Restated net assets at January 1	479,829,880	244,498,692	31,963,288	203,367,900	511,004,393	267,482,926	42,677,879	200,843,588
Net assets at December 31	$ 527,033,257	$ 269,931,520	$ 48,189,721	$ 208,912,016	$ 479,829,880	$ 244,498,692	$ 31,963,288	$ 203,367,900

The accompanying notes are an integral part of these consolidated financial statements.

MASONIC HOMES OF THE GRAND LODGE OF FREE AND ACCEPTED MASONS OF PENNSYLVANIA

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended December 31, 2012 and 2011

	2012	Restated 2011
Cash Flows from Operating Activities and Nonoperating Gains:		
Increase (decrease) in net assets	$ 47,203,377	$ (31,174,513)
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities and nonoperating gains:		
Depreciation and amortization	16,458,514	15,994,517
Bad debts	141,852	147,976
Bond premium amortization on 2006 bonds	(62,414)	(63,484)
Loss on disposal of property and equipment	51,800	107,931
Amortization of entrance fees	(9,478,109)	(8,670,406)
Initial contributions recognized from split-interest agreements	(621,200)	(405,002)
Actuarial adjustment for split-interest agreements	501,672	588,943
Contributions restricted for long-term investments	(2,202,590)	(2,753,668)
Net realized and unrealized (gains) losses on long-term investments	(56,810,561)	5,793,949
(Increase) decrease in fair value of interest rate swap agreements	(922,257)	11,318,749
Decrease in receivables	1,339,779	149,803
(Increase) decrease in other current assets and inventory	(171,944)	158,816
(Decrease) increase in accounts payable and accrued expenses	(3,261,978)	8,956,285
Increase in other current and noncurrent liabilities	3,281,724	7,509,059
Proceeds from entrance fees and deposits	24,909,559	22,088,530
Net cash provided by operating activities and nonoperating gains	20,357,224	29,747,485
Cash Flows from Investing Activities:		
Acquisition of property and equipment	(35,769,133)	(35,307,873)
Increase in assets whose use is limited	(87,382)	(78,586)
Proceeds from the sale of investments	44,445,955	28,730,380
Purchases of investments	(17,619,548)	(10,827,985)
Deferral of costs to upgrade Elizabethtown wastewater treatment plant	-	(1,056,000)
Decrease (increase) in other long-term assets	1,600	(2,300)
Net cash used in investing activities	(9,028,508)	(18,542,364)

The accompanying notes are an integral part of these consolidated financial statements.

MASONIC HOMES OF THE GRAND LODGE OF FREE AND ACCEPTED MASONS OF PENNSYLVANIA

CONSOLIDATED STATEMENTS OF CASH FLOWS - CONTINUED

Years Ended December 31, 2012 and 2011

	2012	Restated 2011
Cash Flows from Financing Activities:		
Refunds of entrance fees and deposits	$ (7,796,148)	$ (7,186,395)
Proceeds from contributions restricted for long-term investments	2,202,590	2,753,668
Proceeds from contributions under split-interest agreements	1,243,956	840,000
Net payments made on split-interest agreements	(1,136,956)	(1,134,951)
Decrease in deferred revenue from landfill settlement	(10,000)	(10,000)
Principal payment on long-term debt	(6,835,000)	(6,555,000)
Net cash used in financing activities	(12,331,558)	(11,292,678)
Net decrease in cash and cash equivalents	(1,002,842)	(87,557)
Cash and cash equivalents - Beginning of year	20,802,538	20,890,095
Cash and cash equivalents - End of year	$ 19,799,696	$ 20,802,538
Supplemental disclosure of cash flow information:		
Cash paid during the year for interest	$ 6,995,726	$ 7,218,753

The accompanying notes are an integral part of these consolidated financial statements.

NOTE 1: Summary of Significant Accounting Policies

Organization

The Masonic Homes of the Grand Lodge of Free and Accepted Masons of Pennsylvania (Masonic Homes) is a not-for-profit unit of the Grand Lodge of Free and Accepted Masons of Pennsylvania (Grand Lodge). Masonic Homes provides various services at its Elizabethtown, Pennsylvania, Warminster, Pennsylvania, Lafayette Hill, Pennsylvania, Sewickley, Pennsylvania, and Dallas, Pennsylvania campuses. These campuses are referred to, collectively and individually, as "Masonic Villages" for marketing and business purposes. Services provided at the Elizabethtown campus as of December 31, 2012 include:

1. a 436 bed nursing facility providing nursing care (Nursing Home)
2. 941 units of Retirement Living consisting of apartments and cottages
3. a 126 bed personal care facility (Personal Care)
4. a 40 bed home for disadvantaged children (Children's Home)
5. meeting and conference facilities
6. an Outreach program
7. an Adult Daily Living program
8. an 8 bed Residential care program (Residential Care) for developmentally disabled individuals
9. a farm.

As of December 31, 2012, services provided at the Warminster campus include a 28 bed nursing facility and 33 beds of personal care.

Services provided at the Sewickley campus include a 128 bed nursing facility, 61 beds of personal care, and 272 units of Retirement Living Apartments and Villas as of December 31, 2012.

As of December 31, 2012, services provided at the Lafayette Hill campus include a 60 bed nursing facility, 39 beds of personal care, and 98 units of Retirement Living Apartments.

Services provided at the Dallas campus include 83 units of Retirement Living Apartments and Cottages as of December 31, 2012.

Masonic Homes also provides significant financial support to the Pennsylvania Masonic Youth Foundation and The Masonic Library and Museum of Pennsylvania.

NOTE 1: Summary of Significant Accounting Policies – Continued

Principles of Consolidation

The consolidated financial statements include the financial statements of Masonic Homes and its wholly-owned subsidiaries, ILC Corp., Masonic Home of Pennsylvania, Inc., Pennsylvania Acacia Insurance Company, Ltd. (PAIC), and Acacia Services, LLC after elimination of all significant interrelated balances and transactions.

Assets Whose Use is Limited

Assets whose use is limited include assets held by trustees under an indenture agreement.

Resident Accounts Receivable

Accounts receivable for services provided to residents consists of amounts owed directly from residents on a private pay basis and amounts owed from third-party payors on behalf of residents. Receivables from third-party payors are recorded at established rates, net of contractual adjustments specific to each payor. Receivables from private pay residents are recorded at established rates. Receivables are considered to be past due when payments have not been received by Masonic Homes within 90 days of their contractually stated due date. The provision for uncollectible private pay resident accounts receivable is based on management's assessment of the collectability of individual receivables and the aggregate aging of all of the private pay resident accounts receivable. Losses are charged against the allowance for uncollectible private pay resident accounts receivable when management believes the un-collectability of a receivable is confirmed.

Inventory

Inventory consists of medical supplies and pharmaceutical products, livestock, and maintenance supplies and is valued at the lower of cost or market. Cost is determined on the first-in, first-out basis.

Notes Receivable and Allowance for Uncollectible Notes Receivable

Masonic Homes has provided short-term loans to residents entering its Retirement Living facilities. These loans are evidenced by a note which authorizes a judgment against the resident’s property to effect loan satisfaction, and are recorded at the gross amount of the loan proceeds, reduced by an allowance for uncollectible notes receivable. Interest income from notes receivable is accrued on the straight-line method. Notes are considered to be due one year from the date of the note.

Nonaccrual notes receivable are those on which accrual of interest has ceased and where all previously accrued but not collected interest is reversed. Notes are placed on nonaccrual status when, in the opinion of management, full collection is doubtful. Interest accrued but not collected as of the date of placement on nonaccrual status is reversed and charged against current income. While a note receivable is on nonaccrual status, subsequent cash payments received are either applied to outstanding principal balance or recorded as interest income, depending on management’s assessment of the ultimate collection of principal and interest.

The allowance for uncollectible notes receivable is evaluated on a regular basis by management and is based on historical experience, the nature and volume of the notes receivable portfolio, adverse conditions that may affect the borrower’s ability to repay, and prevailing economic conditions. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available. Notes are considered to be past due when principal and interest payments have not been received by Masonic Homes within 90 days of their contractually stated due date. Losses are charged against the allowance for uncollectible notes receivable when management believes the un-collectability of a note is confirmed.

Contributions Receivable

Contributions receivable recorded by Masonic Homes consist of charitable remainder unitrusts, charitable lead trusts, and promises to give.

Masonic Homes will be the recipient of specified funds over the terms of several charitable lead trusts and the remaining assets of several charitable remainder unitrusts upon the death of the beneficiaries. Contributions receivable are recorded at the net present value of the expected trust assets to be received based on the fair value of the trust assets, the contractual or risk-free rate of return (which ranges from 4.25% to 7.00%), and the life expectancy of the current beneficiary or term of the trust.

Unconditional promises to give that are expected to be collected within one year are recorded at net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of their estimated future cash flows. The discounts on those amounts are computed using risk-free interest rates applicable to the years in which the promises are received. Amortization of the discounts is included in contribution revenue. Conditional promises to give are not included as support until the conditions are substantially met.

Investments and Investment Income

The Masonic Homes carries investments at fair value. When available, fair value of the investments is determined using quoted market prices of a national securities exchange. In other instances fair value is determined using other observable market data or the Masonic Homes own assumptions. Contributed investments are initially valued at the quoted fair value on the date received, which is then treated as cost.

Investment income on borrowed funds held by a trustee and investment income from all other unrestricted investments are reported as operating revenues. Investment income and gains (losses) on investments of donor restricted funds are added to (deducted from) the appropriate donor restricted net assets.

Property and Equipment

Property and equipment are recorded at cost, or if donated, at fair value at the date of receipt. Masonic Homes reviews all disbursements greater than $ 1,000 for capitalization as property and equipment. Expenditures for repairs which extend the useful life of the assets are capitalized and routine maintenance and repair costs are expensed as incurred.

Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed on the straight-line method. Estimated useful lives are: land improvements - 10 to 20 years, buildings and improvements - 20 to 40 years, and equipment - 3 to 20 years.

NOTE 1: Summary of Significant Accounting Policies – Continued

Deferred Financing Costs

Deferred financing costs are amortized over the period the obligation is outstanding using the effective interest method.

Collections

Masonic Homes owns collections of Masonic memorabilia, paintings, antique furniture, farm equipment, and other artifacts related to the history of Masonic Homes. These collections are located at the Elizabethtown, Pennsylvania campus. The collections, which were primarily acquired through contributions since Masonic Homes' inception, are not recognized as assets on the consolidated balance sheets. Contributed collection items are not recognized as revenue in the consolidated statements of changes in net assets.

Retirement Living - Entrance Fee Units

Entrance Fees - Fees paid by a resident upon entering into a resident agreement for Retirement Living, net of the portion thereof that is expected to be refundable to the resident based on refundable contract choice (refundable fees), are recorded as deferred revenue and are amortized to revenue using the straight-line method over the estimated remaining life expectancy of the resident. Contingent contracts are those that provide a minimum refund percentage greater than zero and state that re-occupancy is required prior to the payment of a refund. The refundable portion of a contingent contract is not amortized to revenue but remains as a liability until withdrawal.

Contractually Refundable Fees - Masonic Homes offers two types of contracts at its Elizabethtown, Dallas, Sewickley, and Lafayette Hill campuses. Under the terms of the first contract type, amounts refundable equal the contract amount less 5.00% for the first month of occupancy and 1.00% for each month of occupancy thereafter. Under the terms of the second contract type, amounts refundable equal 90% of the original contract amount whenever the resident chooses to permanently leave retirement living or the facility. In addition, a variation of the refundable contract type is available at the Dallas campus providing an annual 1% increase in the refundable percentage. At December 31, 2012 and 2011, entrance fees of approximately $ 50,938,000 and $ 49,717,000, respectively, were refundable to residents (excluding deposits on unoccupied units) under the terms of the refundable contracts.

Obligation to Provide Future Services - Masonic Homes annually calculates the present value of the net cost of future services to be provided to Retirement Living residents. Costs of future services for Retirement Living residents at the Elizabethtown and Lafayette Hill campuses include the meals, housekeeping, maintenance, and facility costs that are provided under the terms of the Elizabethtown and Lafayette Hill contracts. Costs of future services for Retirement Living residents at the Sewickley campus include the healthcare services, meals, housekeeping, maintenance, and facility costs that are provided under the terms of the Sewickley contract. Costs of future services for Retirement Living residents at the Dallas campus include the housekeeping, maintenance and facility costs that are provided under the terms of the Dallas contract. The aggregate cost of future services is compared with the balance of deferred revenue from entrance fees and assets designated by Masonic Homes to pay the cost of healthcare services provided to Retirement Living residents at the Sewickley campus. If the present value of the net cost for future services and use of facilities exceeds the deferred revenue from entrance fees and designated assets, a liability will be recorded with a corresponding charge to expenses. Management's calculation resulted in an estimate of no liability for future services to be provided as of either December 31, 2012 or 2011, using discount rates of 7.00% each year.

These agreements are regulated by the Commonwealth of Pennsylvania Department of Insurance. Masonic Homes is required to maintain liquid reserves to cover the future costs associated with these agreements.

NOTE 1: Summary of Significant Accounting Policies – Continued

Resident Personal Funds

Masonic Homes receives and holds personal funds of certain residents as an agent of those residents. Cash and cash equivalents include resident personal funds totaling $ 874,368 and $ 909,830 as of December 31, 2012 and 2011, respectively.

Worker's Compensation Claims

For the years ended December 31, 2012 and 2011, Masonic Homes was insured for workers compensation claims in a large risk-large deductible program with a $ 350,000 deductible for each injury/disease and a $ 1,000,000 aggregate for each injury/disease. Premiums paid, net of any performance-based refunds, are recorded in wages, salaries, and benefits in the consolidated statements of operations.

Annuities Payable

Masonic Homes has several charitable gift annuity and charitable remainder unitrust arrangements with donors. Annuities payable are recorded at the net present value of the expected annuity payments based upon the amount of the contribution, the contractual rate of return (which ranges from 4.70% to 12.00%), and the life expectancy of the beneficiary of the annuity.

Bond Premium

Bond premium is amortized over the period the related long-term debt obligation is outstanding using the interest method.

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use by Masonic Homes has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by Masonic Homes in perpetuity.

Support

Contributions received are measured at their fair values and are reported as an increase in net assets. Masonic Homes reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets, or if they are designated as support for future periods. When a donor restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met in the same reporting period are reported as unrestricted support.

Gifts of goods and 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. Masonic Homes reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

Masonic Homes is the beneficiary under various wills and trust agreements. Amounts received from such sources are recorded when clear title is established and the proceeds are measurable.

NOTE 1: Summary of Significant Accounting Policies – Continued

Donated Services

A significant number of volunteers annually donate their services to Masonic Homes. Because the services provided do not require specialized skills, the value of these donated services is not reflected in the consolidated financial statements.

Resident Service Revenue

Masonic Homes' resident service revenue is earned from providing both healthcare and non-healthcare services. Health care programs include nursing care, personal care, hospice, medical supplies, and medical ancillary clinics. Non-health care programs include retirement living, the Children's Home, adult day care, the Residential Care program, home care, and wellness centers. Ordinary activities that are part of a resident's life at Masonic Homes also produce resident service revenue. These revenue producing activities include beauty and barber services, resident and guest meals, laundry, transportation, parking, and communications services.

Resident service revenue is recorded initially at the established rates. This amount is reduced by contractual adjustments and charity allowances to arrive at resident service revenue reported in the consolidated statement of operations.

Retroactively calculated contractual adjustments arising under reimbursement agreements with third-party payors are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. Adjustments related to final settlements with third-party payors are included in net resident service revenue in the year in which such adjustments become known.

Charity Care

Charity care is provided to residents who have demonstrated the inability to pay and are not eligible for third-party reimbursement. Certain residents qualify for charity care upon admission or when their financial resources are depleted. Because Masonic Homes provides charity care to residents who are unable to pay for these services, it is not reported as resident service revenue.

Consolidated Statements of Operations Earnings Measurement

Masonic Homes' income (loss) from operations includes all unrestricted revenue from the provision of health care and residential services, operating revenue from incidental activities such as the farm, investment income, changes in the fair value of derivative instruments, and expenses incurred in the performance of these activities. Non-operating gains and losses are excluded from the loss from operations.

Consolidated Statements of Changes in Net Assets Earnings Measurement

Masonic Homes utilizes the excess (deficiency) of revenues and gains over expenses and losses to measure its annual earnings. The excess of revenues and gains over expenses and losses includes revenues and expenses from program activities, contributions, investment income, realized gains (losses) from the sale of investments, and changes in the fair value of derivative instruments. The net unrealized appreciation (depreciation) on investments and changes in the minimum pension obligation are excluded from the excess (deficiency) of revenues and gains over expenses and losses.

Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid debt instruments (i.e. money market funds) with original maturities of three months or less, excluding amounts classified as assets whose use is limited.

NOTE 1: Summary of Significant Accounting Policies – Continued

Income Taxes

Masonic Homes is a not-for-profit entity as described in Section 501(c)(3) of the Internal Revenue Code and is exempt from federal income taxes on related income pursuant to Section 509(a) of the Code.

Generally accepted accounting principles require organizations to disclose significant tax positions that are subject to uncertainty about the merits of the position taken or the amount of the position that may ultimately be sustained upon examination by the taxing authorities. The effects of tax positions are recognized in financial statements if, in the opinion of management, the tax position would more likely than not be sustained upon an examination by the taxing authorities, including the resolution of any applicable appeals or litigation. Masonic Homes' most significant tax position is that it is exempt from payment of federal and state income taxes. Accordingly, Masonic Homes has not reported any income tax expense in the statement of operations and the statement of changes in net assets for the years ended December 31, 2012 and 2011. Masonic Homes has not recorded liabilities for income taxes or unrecognized income tax benefits in the balance sheets as of December 31, 2012 and 2011. The tax years subsequent to 2008 may be subject to review by federal, state, and local taxing authorities.

Use of Estimates

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

Derivative Financial Instruments

Derivative financial instruments used by Masonic Homes consist of pay-fixed, receive variable interest rate swap agreements. The purpose of these interest rate swap agreements is to limit Masonic Homes' exposure to interest rate changes on its variable-rate debt.

Disclosure about Fair Value of Financial Instruments

Financial instruments include cash and cash equivalents, short-term investments, investment securities, resident accounts receivable, notes receivable, deposits, long-term debt, and interest rate swaps.

The fair value of cash and cash equivalents are deemed to be the same as their carrying value. The fair value of resident accounts receivable equals their carrying value, since they are stated net of estimated uncollectible amounts. The fair value of the long-term debt is determined based on the quoted market price of the long-term debt at the consolidated balance sheet date. The fair values of interest rate swap agreements are based on quoted market prices if available or valuation techniques which consider the present value of estimated expected future cash flows. Disclosure of additional fair values is contained in the following notes.

NOTE 2: Adoption of New Accounting Standard

In July of 2012, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2012-01, "Health Care Entities (Topic 954) – Continuing Care Retirement Communities – Refundable Advance Fees" (ASU #2012-01). The objective of ASU #2012-01 is to clarify the reporting for refundable entrance fees received by continuing care retirement communities. The new standard requires that a continuing care retirement community recognize a deferral of revenue when a contract between the continuing care retirement community and a resident stipulates that (1) a portion of the entrance fee is refundable if the contract-holder's unit is re-occupied by a subsequent resident, (2) the refund is limited to the proceeds of re-occupancy, and (3) the legal environment and the entity's management policy and practice support the withholding of refunds under condition (2). ASU #2012-01 also implies that if a continuing care retirement community's practices do not support treating refundable entrance fees as deferred revenue, the liability for refundable entrance fees should not be used as an offset to a continuing care retirement community's estimated obligation to provide future services. ASU #2012-01 must be implemented for annual financial statements of public entities for fiscal years beginning after December 15, 2012. Early adoption of ASU #2012-01 is permitted.

Masonic Homes offers retirement living services at four locations in Pennsylvania. Most of these retirement living services are based on contracts with refund provisions for the entrance fees paid by residents. Prior to 2011, Masonic Homes' practice was to issue contractually-determined refunds to residents withdrawing from their retirement living unit in accordance with the applicable contract terms. A portion of these contractually-refundable fees were included in deferred revenue from entrance fees on Masonic Homes' balance sheet. This approach resulted in the annual recognition of amortization of a portion of these contractually-refundable fees on the statement of operations. Masonic Homes also used the year-end liability for refundable fees to offset the present value of future services to be provided to Retirement Living residents. Since the combination of deferred revenue from entrance fees and refundable entrance fees annually exceeded the present value of future services to be provided to Retirement Living services, this approach resulted in an estimate of no liability for future services to be provided. Application of the new provisions of ASU #2012-01 to Masonic Homes' practices for entrance fees will result in a reduction in the annual revenue from the amortization of entrance fees. However, the proscribed revisions to deferred revenue from entrance fees were not sufficient to require Masonic Homes to recognize an estimated obligation to provide future services under the new provisions of ASU #2012-01.

Masonic Homes has adopted the provisions of ASU #2012-01 for the year ended December 31, 2012. During the application of the new accounting standard, it was determined that Masonic Homes had understated deferred revenue from entrance fees and overstated refundable entrance fees for 2011 and previously reported periods. Although this situation did not result in any changes to Masonic Homes' unrestricted net assets for 2011 and previously reported periods, the effect of correctly stating these amounts combined with implementation of ASU #2012-01 produced increases in deferred revenue from entrance fees and decreases in refundable entrance fees as of December 31, 2011 and 2010.

The financial statements for the year ended December 31, 2011 have been restated to conform to the new requirements of ASU #2012-01. Unrestricted net assets as of January 1, 2011 have been reduced by $ 4,746,904 to reflect the impact of adopting the provisions of ASU #2012-01. The accompanying financial statements have been restated to reflect the recalculated estimate of refundable fees, deferred revenue from entrance fees, and unrestricted net assets for the year ended December 31, 2011. The restatements occurred as follows:

NOTE 2: Adoption of New Accounting Standard - Continued

	Refundable Fees	Deferred Revenue from Entrance Fees	Unrestricted Net Assets	Change in Net Assets
January 1, 2011 as originally reported	$ 53,206,411	$ 63,051,516	$ 272,229,830	
Prior period adjustment	(7,229,563)	11,976,467	(4,746,904)	
January 1, 2011, as restated	$ 45,976,848	$ 75,027,983	$ 267,482,926	
December 31, 2011, as originally reported	$ 56,391,048	$ 65,212,389	$ 250,131,815	$ (30,288,294)
Prior period adjustment	(6,673,926)	12,307,049	(5,633,123)	(886,219)
December 31, 2011 as restated	$ 49,717,122	$ 77,519,438	$ 244,498,692	$ (31,174,513)

	Amortization of Entrance Fees
Year ended December 31, 2011, as originally reported	$ 9,556,625
Prior period adjustment	(886,219)
Year ended December 31, 2011, as restated	$ 8,670,406

NOTE 3: Cash and Cash Equivalents

Masonic Homes holds cash and cash equivalents that have been restricted by donors for certain purposes. Masonic Homes is not permitted to use restricted cash and cash equivalents for general operations. The components of Masonic Homes' cash and cash equivalents as of December 31, 2012 and 2011 are as follows:

	2012	2011
Available for operations	$ 16,084,899	$ 15,067,264
Retirement living escrow funds	2,106,663	3,896,750
Held for residents deposits	874,368	909,830
Total unrestricted	19,065,930	19,873,844
Temporarily restricted	733,766	928,694
	$ 19,799,696	$ 20,802,538

NOTE 4: Resident Accounts Receivable

Masonic Homes' resident accounts receivable consists of amounts owed from individuals, insurance companies, and government agencies. As of December 31, 2012 and 2011, Masonic Homes' aggregate resident accounts receivable over 90 days past due totaled $ 493,736 and $ 636,822, respectively.

Masonic Homes’ resident accounts receivable are reduced by an allowance for uncollectible accounts. In evaluating the collectability of resident accounts receivable, Masonic Homes evaluates its past history and identifies trends for each of its major sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payor sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts. For receivables associated with private pay residents (which

NOTE 4: Resident Accounts Receivable – Continued

includes both residents without insurance and residents with deductible and copayment balances due for which third-party coverage exists for part of the bill), Masonic Homes records a provision for bad debts in the period of service on the basis of past experience, which indicates that many private pay residents are unable or unwilling to pay the portion of the bill for which they are financially responsible. The difference between the standard rates and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for uncollectible accounts.

The changes in the allowance for uncollectible accounts receivable for the years ended December 31, 2012 and 2011 were as follows:

	2012	2011
Allowance at January 1	$ 231,000	$ 269,000
Provision for bad debts	141,852	147,976
Accounts receivable written off, net of recoveries	(116,852)	(185,976)
Allowance at December 31	$ 256,000	$ 231,000

NOTE 5: Contributions Receivable

Contributions receivable consisted of the following as of December 31, 2012 and 2011:

	2012	2011
Charitable remainder unitrusts	$ 32,020	$ 22,286
Charitable lead annuity trusts	416,623	442,844
Promises to give	125,343	78,105
Total contributions receivable	573,986	543,235
Less:		
Current portion of charitable lead annuity trusts	44,000	44,000
Current portion of promises to give	52,400	40,200
Noncurrent portion	$ 477,586	$ 459,035

Promises to give consist of the following as of December 31, 2012 and 2011:

	2012	2011
Promises to give before unamortized discount and allowance for uncollectibles	$ 130,400	$ 82,200
Unamortized discount	(5,057)	(4,095)
Allowance for uncollectibles	-	-
Net promises to give	$ 125,343	$ 78,105

NOTE 5: Contributions Receivable - Continued

The schedule of payments to be received from promises to give as of December 31, 2012 is as follows:

2013	$	52,400
2014		39,000
2015		39,000
2016		-
2017		-
	$	130,400

The discount rates used for promises to give received during the years ended December 31, 2012 and 2011 were 1.84% and 1.89%, respectively.

NOTE 6: Notes Receivable

Notes receivable with Masonic Homes' Retirement Living residents totaled $ 3,350,406 and $ 3,892,877, as of December 31, 2012 and 2011, respectively. Interest was charged at rates ranging from 0% to 5% per annum. Notes receivable over 90 days past due totaled $ 263,130 and $ 511,680 as of December 31, 2012 and 2011, respectively. There was no notes receivable on nonaccrual status as of December 31, 2012 and 2011. Based on management's evaluation of the notes receivable portfolio, no provision for uncollectible notes receivable is required.

NOTE 7: Investments

Certain investments are pooled with related organizations and are referred to as "Consolidated Fund" investments. Consolidated Fund investments and certain short-term investments are administered by twelve different investment management firms and held in safekeeping by JPMorgan Chase Bank, N. A. Approximately 90% of the pooled investments are attributable to the Masonic Homes.

The following table summarizes total Consolidated Fund investments held in safekeeping at JPMorgan Chase Bank, N. A.:

At December 31, 2012	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Domestic stocks	$ 94,525,391	$ 27,393,389	$ 2,649,407	$ 119,269,373
International stocks	22,571,791	3,700,588	1,118,072	25,154,307
U.S. Government and Agency bonds	12,991,261	199,568	145,891	13,044,938
Domestic corporate bonds	101,586,192	4,216,474	156,517	105,646,149
Municipal bonds	8,273,547	472,794	25,297	8,721,044
Mutual funds - Equity securities	138,524,330	21,673,013	6,528	160,190,815
Collective investment fund - Hedge funds	375,229	-	26,697	348,532
Exchange traded funds	49,247,968	404,149	1,800,747	47,851,370
Limited partnership - International investments	18,502,952	6,082,205	25,823	24,559,334
Mortgage backed securities	28,012,201	1,236,191	55,831	29,192,561
Asset backed securities	27,292,876	1,898,320	8,759	29,182,437
Demand notes	865,674	21,680	12,275	875,079
Real estate investment trusts	691,182	136,617	54,821	772,978
Money market funds	37,664,527	32	12	37,664,547
Total Consolidated Fund	$ 541,125,121	$ 67,435,020	$ 6,086,677	$ 602,473,464

NOTE 7: Investments – Continued

At December 31, 2011	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Domestic stocks	$ 110,270,470	$ 21,071,241	$ 6,735,756	$ 124,605,955
International stocks	43,875,124	3,198,205	7,426,570	39,646,759
U.S. Government and Agency bonds	12,320,532	742,862	2,364	13,061,030
Domestic corporate bonds	100,927,769	4,297,924	908,723	104,316,970
Municipal bonds	10,480,115	410,294	96,220	10,794,189
Mutual funds - Equity securities	103,741,109	10,416,277	1,576,725	112,580,661
Collective investment fund - Hedge funds	375,229	-	26,697	348,532
Exchange traded funds	38,295,283	-	6,368,493	31,926,790
Limited partnership - International investments	27,290,335	6,242,765	24,365	33,508,735
Mortgage backed securities	40,516,814	1,444,514	136,321	41,825,007
Asset backed securities	22,235,807	394,124	548,592	22,081,339
Real estate investment trusts	1,166,430	48,652	165,187	1,049,895
Money market funds	34,984,718	2	24	34,984,696
Total Consolidated Fund	$ 546,479,735	$ 48,266,860	$ 24,016,037	$ 570,730,558

At December 31, 2012 and 2011, Masonic Homes' investments consisted of the following:

	2012		2011	
	Cost	Fair Value	Cost	Fair Value
Money Market Funds	$ 8,532,477	$ 8,532,477	$ 11,740,545	$ 11,740,545
Consolidated Fund	298,771,572	319,514,538	307,900,420	308,490,830
Other investments	258,473	230,966	92,616	85,407
Real estate	420,000	320,000	420,000	320,000
State Street Bank & Trust	70,939	70,939	-	-
Charles Schwab Institutional	197,322	183,631	206,760	177,354
Wells Fargo Bank Common Trust Funds	404,447	434,929	414,139	438,961
Total Unrestricted	308,655,230	329,287,480	320,774,480	321,253,097
Money Market Funds	2,284,515	2,284,515	2,919,827	2,919,827
Consolidated Fund	184,781,998	209,625,993	178,069,953	190,388,758
Other investments	97,418	124,474	97,418	113,152
BNY Mellon Financial Dreyfus Money Market Fund	60,157	60,157	60,157	60,157
Perpetual Trusts Held by Third Parties	24,243,066	42,754,968	24,243,066	39,418,442
Total Restricted	211,467,154	254,850,107	205,390,421	232,900,336
	$ 520,122,384	$ 584,137,587	$ 526,164,901	$ 554,153,433

NOTE 7: Investments – Continued

Masonic Homes' investments are presented on the balance sheet in the following categories as of December 31, 2012 and 2011:

	2012	2011
Minimum liquid reserve requirement	$ 13,757,357	$ 13,694,313
Investments at fair value	570,380,230	540,459,120
	$ 584,137,587	$ 554,153,433

Total return on Masonic Homes' investments for the years ended December 31, 2012 and 2011 consisted of the following:

	2012	2011
Operating investment income - Unrestricted	$ 10,034,145	$ 10,841,792
Nonoperating investment income - Temporarily restricted	86,502	90,164
Total investment income	10,120,647	10,931,956
Realized gains on sale of investments	20,782,647	27,055,106
Net unrealized appreciation (depreciation) on investments	36,027,914	(32,849,055)
	$ 66,931,208	$ 5,138,007

Masonic Homes has designated portions of its unrestricted Consolidated Fund investments to use for specific programs or functions. The composition of Masonic Homes' designated investments as of December 31, 2012 and 2011 is as follows:

	2012		2011	
	Cost	Fair Value	Cost	Fair Value
Masonic Homes Reserve Fund	$ 176,627,357	$ 193,028,588	$ 186,786,808	$ 192,165,764
Masonic Homes Memorial Fund	-	-	10,830,975	9,951,536
Masonic Temple Preservation Fund	10,295,547	10,929,742	-	-
Children's Home Fund	6,573,618	6,714,973	8,182,231	7,824,659
Charitable Gift Annuity Reserve Fund	11,971,651	12,621,008	11,510,234	11,434,598
Masonic Eastern Star Homes Building and Improvement Fund	775,860	649,337	752,572	585,673
Warminster Building and Improvement Fund	2,529,486	2,165,263	2,402,733	1,906,757
Masonic Eastern Star Endowment Fund	1,200,307	1,003,105	1,164,332	904,755
Dallas Retirement Living Fund	1,538,467	1,559,051	1,454,731	1,380,076
Sewickley General Fund	-	-	5,450,231	5,450,231
Sewickley Lifecare Fund	2,711,176	2,791,550	2,569,208	2,488,139
Sewickley Retirement Living Fund	76,575,955	79,191,870	72,322,617	70,100,870
Lafayette Hill General Fund	8,035,268	8,225,040	7,492,565	7,184,596
Lafayette Hill Minimum Reserve Fund	1,563,800	1,584,860	1,506,961	1,429,473
Pennsylvania Acacia Insurance Company	7,161,335	7,810,899	6,588,861	6,783,029
	$ 307,559,827	$ 328,275,286	$ 319,015,059	$ 319,590,156

NOTE 7: Investments – Continued

The Consolidated Fund investment policy includes specific guidance on the maximum amount that each organization participating in the Consolidated Fund may withdraw from its Consolidated Fund investments each year. The maximum amount that may be withdrawn and spent is equal to a percentage of the three-year average fair value of a participating organization's Consolidated Fund investments. The investment policy permits withdrawals from unrestricted investments in excess of the spending maximum. For the years ended December 31, 2012 and 2011, the spending percentage recommended by the Grand Lodge Committee on Finance and elected by the Trustees of the Consolidated Fund was 5.00%. Masonic Homes reports the cumulative excess of the restricted spending maximum over amounts withdrawn from restricted Consolidated Fund investments as temporarily restricted net assets.

Masonic Homes' performance in comparison with the spending maximum amounts is summarized in the following table:

	Unrestricted	Permanently Restricted	Total
Masonic Homes' Consolidated Fund spending maximum amount for 2012	$ 14,525,129	$ 9,170,745	$ 23,695,874
Amounts withdrawn from Consolidated Fund	35,468,732	8,977,223	44,445,955
Excess (deficiency) of spending maximum amount over amounts withdrawn	$ (20,943,603)	$ 193,522	$ (20,750,081)

	Unrestricted	Permanently Restricted	Total
Masonic Homes' Consolidated Fund spending maximum amount for 2011	$ 14,394,898	$ 9,530,260	$ 23,925,158
Amounts withdrawn from Consolidated Fund	19,384,369	9,346,011	28,730,380
Excess of spending maximum amount over amounts withdrawn	$ (4,989,471)	$ 184,249	$ (4,805,222)

NOTE 8: Assets Whose Use is Limited

Assets whose use is limited that are required for obligations classified as current liabilities are reported in current assets. The composition of assets whose use is limited at December 31, 2012 and 2011, is set forth below.

	2012		2011	
	Cost	Fair Value	Cost	Fair Value
Under indenture agreement held by trustee - Cash and short-term investments	$ 4,942,788	$ 4,942,788	$ 4,855,406	$ 4,855,406
Less current portion	2,418,773	2,418,773	2,331,391	2,331,391
	$ 2,524,015	$ 2,524,015	$ 2,524,015	$ 2,524,015

NOTE 9: Property and Equipment

A summary of property and equipment at December 31, 2012 and 2011 follows:

	2012	2011
Land	$ 4,835,865	$ 4,742,310
Land improvements	14,350,252	12,570,753
Buildings and improvements	339,389,410	317,792,619
Equipment	178,339,612	157,249,017
	536,915,139	492,354,699
Less accumulated depreciation	244,538,896	228,648,386
	292,376,243	263,706,313
Construction in progress	13,040,217	22,248,462
Property and equipment, net	$ 305,416,460	$ 285,954,775

Depreciation expense for the years ended December 31, 2012 and 2011 was $ 16,255,648 and $ 15,435,444, respectively.

NOTE 10: Deferred Costs

A summary of deferred costs at December 31, 2012 and 2011 follows:

	2012	2011
Financing costs for various long-term debt issues	$ 1,525,527	$ 1,689,887
Costs to upgrade Elizabethtown Borough wastewater treatment plant	1,056,000	1,056,000
	2,581,527	2,745,887
Less accumulated amortization	(1,141,299)	(1,102,793)
	$ 1,440,228	$ 1,643,094

Amortization expense related to deferred costs totaled $ 202,866 and $ 559,073 for the years ended December 31, 2012 and 2011, respectively.

NOTE 11: Interest Rate Swap Agreements

On July 1, 1999, Masonic Homes entered into an interest rate swap agreement on the 1999 Bonds with Wells Fargo Bank, NA (formerly known as Wachovia Bank NA). This agreement expires on July 1, 2034. Wells Fargo Bank, NA exchanged a fixed rate of 4.5925% on the outstanding principal of the 1999 Bonds for the variable interest rate Masonic Homes would have paid. Masonic Homes entered into this agreement to limit the exposure to interest rate changes on the 1999 Bonds.

On September 7, 2001, Masonic Homes entered into an interest rate swap agreement on the 2001 Bonds with Wells Fargo Bank, NA (formerly known as Wachovia Bank NA). This agreement expires September 7, 2031. Wells Fargo Bank, NA exchanged a fixed rate of 4.085% on the outstanding principal of the 2001 Bonds for the variable interest rate Masonic Homes would have paid. Masonic Homes entered into this agreement to limit the exposure to interest rate changes on the 2001 Bonds.

NOTE 11: Interest Rate Swap Agreements – Continued

On September 7, 2001, Masonic Homes entered into a forward interest rate swap agreement with Wells Fargo Bank, NA (formerly known as Wachovia Bank NA) on variable rate bonds that were issued during 2002 (2002 Bonds). This agreement expires May 1, 2032. Wells Fargo Bank, NA exchanged a fixed rate of 4.190% on the outstanding principal of the 2002 Bonds for the variable interest rate Masonic Homes would have paid. Masonic Homes entered into this agreement to limit the exposure to interest rate changes on the 2002 Bonds.

On May 22, 2003, the Masonic Homes entered into an interest rate swap agreement on the 2004 Bonds with Wells Fargo Bank, NA (formerly known as Wachovia Bank NA). This agreement expires on November 19, 2019. Wells Fargo Bank, NA exchanged a fixed rate of 3.75% on the outstanding principal of the 2004 Bonds for the variable interest rate Masonic Homes would have paid. Masonic Homes entered into this agreement to limit the exposure to interest rate changes on the 2004 Bonds.

The variable interest rates on all four of Masonic Homes' interest rate swap agreements are determined using 67% of the London Interbank Offered Rate (LIBOR). The variable interest rates on the 1999 Bonds, the 2001 Bonds, the 2002 Bonds, and the 2004 Bonds are determined by the remarketing agent based on the Securities Industry and Financial Markets Association (SIFMA) index, adjusted for market demand.

On April 1, 2008, the Lancaster County Hospital Authority issued Variable Rate Demand/Fixed Rate Health Center Revenue bonds (Masonic Homes Project), Series 2008 (2008 Bonds) for $ 144,950,000. The proceeds of the 2008 Bonds were used to completely refund the outstanding principal of the 1999 Bonds, the 2001 Bonds, the 2002 Bonds, and the 2004 Bonds. Masonic Homes received the proceeds of the 2008 Bonds in four separate series that corresponded to the outstanding principal amount and repayment schedules of each of the refunded bond series. Series A of the 2008 Bonds ($ 37,420,000) replaced the 2001 Bonds. Series B of the 2008 Bonds ($ 34,725,000) replaced the 2002 bonds. Series C of the 2008 Bonds ($ 29,550,000) replaced the 2004 Bonds. Series D of the 2008 Bonds ($ 43,255,000) replaced the 1999 Bonds. The new bonds were structured in four separate series to correspond to outstanding principal amounts and repayment schedules of the four refunded bond issues. This approach enabled the interest rate swap agreements to continue to be used with the new variable rate demand bonds.

The interest rate swaps are recognized as an asset or liability on the consolidated balance sheets at their fair value. Changes in fair value are recorded as a change in unrealized appreciation or depreciation on the consolidated statements of operations and the consolidated statements of changes in net assets. As of December 31, 2012 and 2011, the fair values of Masonic Homes' interest rate swap agreements were as follows:

	2012	2011
Liabilities:		
1999 Bonds / 2008 Bonds (Series D) interest rate swap agreement	$ (14,716,089)	$ (15,000,121)
2001 Bonds / 2008 Bonds (Series A) interest rate swap agreement	(8,932,589)	(9,087,670)
2002 Bonds / 2008 Bonds (Series B) interest rate swap agreement	(8,778,699)	(8,941,144)
2004 Bonds / 2008 Bonds (Series C) interest rate swap agreement	(2,484,876)	(2,805,575)
	$ (34,912,253)	$ (35,834,510)

NOTE 11: Interest Rate Swap Agreements – Continued

At both December 31, 2012 and 2011, the accumulated derivative loss which had been reported outside of the performance indicator was:

	2012	2011
1999 Bonds / 2008 Bonds (Series D) interest rate swap agreement	$ (7,215,803)	$ (7,215,803)
2001 Bonds / 2008 Bonds (Series A) interest rate swap agreement	(3,359,207)	(3,359,207)
2002 Bonds / 2008 Bonds (Series B) interest rate swap agreement	(3,510,225)	(3,510,225)
	$ (14,085,235)	$ (14,085,235)

By using derivative instruments, Masonic Homes is exposed to credit and market risk. If the counterparty fails to perform, credit risk is equal to the extent of the fair value gain in a derivative. When the fair value of a derivative contract is positive, this generally indicates that the counterparty owes Masonic Homes and, therefore, creates a repayment risk for Masonic Homes. When the fair value of a derivative contract is negative, Masonic Homes owes the counterparty and, therefore, it has no repayment risk. Masonic Homes minimizes the credit (or repayment) risk in derivative instruments by entering into transactions with high quality counterparties that are reviewed periodically by Masonic Homes' management.

At December 31, 2012 and 2011, the net payments associated with the terms of the swap agreements totaled:

Fixed rate payments	2012	2011
1999 Bonds / 2008 Bonds (Series D) interest rate swap agreement	$ 1,806,804	$ 1,850,089
2001 Bonds / 2008 Bonds (Series A) interest rate swap agreement	1,354,314	1,397,410
2002 Bonds / 2008 Bonds (Series B) interest rate swap agreement	1,285,352	1,324,599
2004 Bonds / 2008 Bonds (Series C) interest rate swap agreement	786,168	871,776
Total fixed rate payments	5,232,638	5,443,874
Variable rate payments		
1999 Bonds / 2008 Bonds (Series D) interest rate swap agreement	(62,591)	(62,725)
2001 Bonds / 2008 Bonds (Series A) interest rate swap agreement	(52,818)	(53,205)
2002 Bonds / 2008 Bonds (Series B) interest rate swap agreement	(48,857)	(49,241)
2004 Bonds / 2008 Bonds (Series C) interest rate swap agreement	(33,382)	(36,129)
Total variable rate payments	(197,648)	(201,300)
Net payments to interest rate swap provider	$ 5,034,990	$ 5,242,574

NOTE 12: Long-Term Debt

A summary of long-term debt at December 31, 2012 and 2011 follows:

	2012	2011
Lancaster County Hospital Authority (Series of 1996) - variable rate demand/fixed rate bonds, maturing through 2027	$ 14,875,000	$ 15,600,000
Lancaster County Hospital Authority (Series of 2006) - 3.90% to 5.00% bonds, maturing through 2036	35,005,000	35,800,000
Lancaster County Hospital Authority (Series of 2008) - variable rate demand bonds, maturing through 2034	120,750,000	126,065,000
Total long-term debt	170,630,000	177,465,000
Add premium on 2006 bonds payable	915,456	977,870
Less current installments of long-term debt	(7,125,000)	(6,835,000)
	$ 164,420,456	$ 171,607,870

Under the terms of the bond purchase agreements with the Lancaster County Hospital Authority, the Masonic Homes is required to maintain certain deposits with the Trustee. Such deposits are included with assets whose use is limited in the consolidated financial statements. The loan agreements place limits on the incurrence of additional borrowing and require that the Masonic Homes satisfy certain measures of financial performance as long as the debt is outstanding. For the years ended December 31, 2012 and 2011, Masonic Homes met the minimum debt service coverage ratio contained in the loan agreements.

The 2006 Bonds maturing on and after November 1, 2017 are subject to redemption, at the option of the Authority and at the direction of Masonic Homes, any time after November 1, 2016. Any such redemption will be at a redemption price equal to 100% of the principal amount plus interest accrued through the redemption date.

A schedule of principal repayments on long-term debt for the next five years and thereafter follows:

Bond Series	2013	2014	2015	2016	2017	Thereafter	Total
1996	$ 755,000	$ 780,000	$ 810,000	$ 845,000	$ 875,000	$ 10,810,000	$ 14,875,000
2006	825,000	860,000	895,000	930,000	970,000	30,525,000	35,005,000
2008 (A)	1,135,000	1,180,000	1,235,000	1,285,000	1,345,000	26,250,000	32,430,000
2008 (B)	990,000	1,030,000	1,075,000	1,120,000	1,170,000	24,975,000	30,360,000
2008 (C)	2,405,000	2,505,000	2,615,000	2,720,000	2,840,000	6,015,000	19,100,000
2008 (D)	1,015,000	1,060,000	1,115,000	1,175,000	1,230,000	33,265,000	38,860,000
	$ 7,125,000	$ 7,415,000	$ 7,745,000	$ 8,075,000	$ 8,430,000	$ 131,840,000	$ 170,630,000

The fair value of Masonic Homes' total outstanding bonds, based on quoted market prices, at December 31, 2012 and 2011 was approximately $ 172,942,000 and $ 178,141,000, respectively.

NOTE 12: Long-Term Debt – Continued

A summary of interest costs on borrowed funds and investment income on funds held by the Trustee under the bond purchase agreement during the years ended December 31, 2012 and 2011 follows:

2012	Capitalized	Interest Expense	Investment Income	Total
Bond premium amortization	$ -	$ (62,414)	$ -	$ (62,414)
Interest cost	(1,020,236)	1,943,064	-	922,828
Net payments to interest rate swap provider	-	5,034,990	-	5,034,990
Investment income - Funds held by Trustee	-	-	(120,353)	(120,353)
	$ (1,020,236)	$ 6,915,640	$ (120,353)	$ 5,775,051

2011	Capitalized	Interest Expense	Investment Income	Total
Bond premium amortization	$ -	$ (63,484)	$ -	$ (63,484)
Interest cost	-	1,960,223	-	1,960,223
Net payments to interest rate swap provider	-	5,242,574	-	5,242,574
Investment income - Funds held by Trustee	-	-	(124,265)	(124,265)
	$ -	$ 7,139,313	$ (124,265)	$ 7,015,048

On November 1, 2010, Masonic Homes entered a Continuing Covenants Agreement with Wells Fargo Bank, NA (Wells Fargo) for Wells Fargo to directly purchase all outstanding principal of the 2008 Bonds, Series A, B, and C. On December 1, 2010, Masonic Homes entered a Continuing Covenants Agreement with Wells Fargo for Wells Fargo to directly purchase all outstanding principal of the 1996 Bonds. Under the terms of these agreements, Wells Fargo will hold the outstanding principal of the 1996 Bonds and the 2008 Bonds, Series, A, B, and C as an investment asset for a minimum of three years. As of December 31, 2012, Masonic Homes' 2008 Bonds, Series D issued through the Lancaster County Hospital Authority is supported by a letter of credit provided by J.P. Morgan Chase Bank, NA. The 2006 Bonds are the only long-term debt without credit enhancement as of December 31, 2012.

NOTE 13: Endowments

Masonic Homes' endowment consists of several individual funds established for a variety of purposes. Masonic Homes' endowment includes both donor-restricted endowment funds and funds designated by the Committee on Masonic Homes to function as an endowment. Net assets associated with endowment funds, including funds designated by the Committee on Masonic Homes to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The Commonwealth of Pennsylvania has not adopted the Uniform Prudent Management of Institutional Funds Act of 2006. Guidance for the administration of endowment funds in Pennsylvania is provided in Act 141, which was passed by the Pennsylvania legislature in 1998. Under Act 141, Pennsylvania not-for-profit organizations are permitted to elect an annual amount that may be used from their endowment funds based on an annual spending rate between 2% and 7%. Act 141 permits the spending of accumulated principal and income from an endowment fund if the amount withdrawn is less than or equal to the annually elected percentage. Masonic Homes' interpretation of Act 141 classifies interest income, dividends, and capital appreciation earned by donor-restricted endowment fund investments as temporarily restricted activity. All interest income, dividends, and capital appreciation in excess of the annual spending amount are reported as temporarily restricted net assets available to be spent in subsequent years. Masonic Homes intends to preserve 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, Masonic Homes 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 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 Masonic Homes in a manner consistent with the standard of prudence described by Act 141.

Masonic Homes considers several factors when making a determination to appropriate or accumulate donor-restricted endowment funds. These factors include the duration and preservation of the fund, the mission of the Masonic Homes, the purpose of the donor-restricted endowment fund, satisfaction of specific donor instructions, general economic conditions, the possible effect of inflation and deflation, the expected total return from income and the appreciation of investments, other resources of Masonic Homes, and the investment policy of the Consolidated Fund.

Masonic Homes has invested substantially all of its endowment assets in the Consolidated Fund. The Trustees of the Consolidated Fund have adopted an investment policy and strategies to achieve the greatest return possible for the amount of risk assumed by the Consolidated Fund. Under this policy, assets are invested in a manner intended to produce results that exceed the Consumer Price Index by 4.0% for the entire Consolidated Fund. There are also goals established for categories of fixed income and equity investments within the Consolidated Fund to meet or exceed the performance of appropriate generally recognized financial indices. Actual returns in any year may vary from these goals.

To satisfy the long-term rate-of-return objectives of the organizations participating in the Consolidated Fund, the Trustees of the Consolidated Fund rely 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 Consolidated Fund 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.

The Consolidated Fund investment policy includes specific guidance on the maximum amounts that each participating organization may withdraw from its Consolidated Fund investments each year. The maximum amount that may be withdrawn and spent is equal to a percentage of the three-year average fair value of a participating organization's Consolidated Fund investments. This approach is consistent with the provisions of Act 141. For the years ended December 31, 2012 and 2011, the spending percentage elected by the Trustees of the Consolidated Fund was 5.00%. In establishing this policy, the Trustees of the Consolidated Fund considered the long-term expected return on the endowment funds of the organizations participating in the Consolidated Fund.

NOTE 13: Endowments – Continued

Endowment net assets consisted of the following as of December 31, 2012 and 2011:

	2012	2011
Board designated endowment funds	$ 1,006,240	$ 908,379
Donor restricted endowment funds, temporarily restricted portion	43,411,368	27,626,273
Donor restricted endowment funds, permanently restricted portion	166,157,048	163,949,458
	$ 210,574,656	$ 192,484,110

The changes in endowment net assets for the years ended December 31, 2012 and 2011 were as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets at January 1, 2011	$ 917,638	$ 34,539,073	$ 161,093,378	$ 196,550,089
Investment return:				
Investment income	18,707	3,931,657	-	3,950,364
Realized gains	44,907	9,961,219	-	10,006,126
Unrealized depreciation	(54,425)	(11,952,343)	-	(12,006,768)
Total investment return	9,189	1,940,533	-	1,949,722
Contributions and bequests	-	-	2,675,164	2,675,164
Income from perpetual trust held by third party	-	-	15,819	15,819
Transfers from unrestricted and temporarily restricted funds	-	-	165,097	165,097
Appropriation of endowment assets for expenditure	(18,448)	(8,853,333)	-	(8,871,781)
Endowment net assets at December 31, 2011	908,379	27,626,273	163,949,458	192,484,110
Investment return:				
Investment income	18,286	3,814,505	-	3,832,791
Realized gains	35,975	8,101,678	-	8,137,653
Unrealized appreciation	62,374	12,365,077	-	12,427,451
Total investment return	116,635	24,281,260	-	24,397,895
Contributions and bequests	-	-	2,185,173	2,185,173
Income from perpetual trust held by third party	-	-	17,417	17,417
Transfers from unrestricted and temporarily restricted funds	-	-	5,000	5,000
Appropriation of endowment assets for expenditure	(18,774)	(8,496,165)	-	(8,514,939)
Endowment net assets at December 31, 2012	$ 1,006,240	$ 43,411,368	$ 166,157,048	$ 210,574,656

NOTE 13: Endowments – Continued

The amounts reported as appropriation of temporarily restricted endowment assets for expenditure consist of two components. Income from donor restricted endowments recognized as unrestricted investment income in the statement of operations totaled $ 3,778,291 and $ 3,880,209, respectively, for the years ended December 31, 2012 and 2011. Amounts withdrawn from the endowments and reported as satisfaction of program restrictions in the statements of operations and changes in net assets for the years ended December 31, 2012 and 2011 totaled $ 4,717,874 and $ 4,973,124, respectively.

NOTE 14: Temporarily Restricted Net Assets

Temporarily restricted net assets are available for the following purposes at December 31, 2012 and 2011:

	2012	2011
Support of Masonic Homes and its activities	$ 1,603,503	$ 1,282,384
Support of Children's Home and its activities	1,713,580	973,403
Support of Residential program for developmentally disabled individuals	62,438	22,265
Scholarship awards	1,382,173	1,088,127
General operations of the organization	38,649,674	24,260,094
Total endowment funds	43,411,368	27,626,273
Support of Masonic Homes and its activities	966,675	871,897
Support of Children's Home and its activities	111,898	195,056
Building renovations and construction projects	254,394	254,394
Care and support of eligible Retirement Living residents	1,826,962	1,596,033
Scholarship awards	477,644	40,700
General operations of the organization	1,140,780	1,378,935
	4,778,353	4,337,015
Total temporarily restricted funds	$ 48,189,721	$ 31,963,288

NOTE 15: Permanently Restricted Net Assets

Permanently restricted net assets are restricted to the following purposes at December 31, 2012 and 2011:

	2012	2011
Investment in perpetuity, the investment income from which is expendable to support:		
Support of Masonic Homes and its activities	$ 2,701,214	$ 2,694,937
Support of Children's Home and its activities	8,776,302	7,981,287
Support of Residential program for developmentally disabled individuals	403,354	347,755
Scholarship awards	1,318,029	1,318,029
General operations of the organization	152,958,149	151,607,450
Total endowment funds	166,157,048	163,949,458
General operations of the organization	42,754,968	39,418,442
Total perpetual trusts held by third parties	42,754,968	39,418,442
	$ 208,912,016	$ 203,367,900

NOTE 16: Net Assets Released from Restrictions

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of events specified by the donors. The amounts released during the years ended December 31, 2012 and 2011 are as follows:

	2012	2011
Purpose restrictions accomplished:		
Support of Masonic Homes and its activities	$ 5,889	$ 6,054
Support of Children's Home and its activities	43,999	316,144
Support of Residential Care and its activities	2,715	-
Transfer of Capital Campaign pledge payments to permanently restricted endowment funds	-	250
Payments to beneficiaries of pooled income funds	-	33,301
General operations of the organization	4,803,694	5,040,450
Care and support of eligible Retirement Living residents	46,256	188,523
Scholarship awards	11,750	16,750
Satisfaction of restrictions - Operations	4,914,303	5,601,472
Satisfaction of restrictions - Purchase of property and equipment	680,292	4,147,362
	$ 5,594,595	$ 9,748,834

Masonic Homes is the recipient of promises to give with donor restrictions requiring the contributions to be added to various permanently restricted endowment funds. During 2012 and 2011, Masonic Homes received payments on these promises to give totaling $ 0 and $ 250, respectively. These payments were recorded as satisfaction of the donors' restrictions and transferred to permanently restricted net assets for the years ended December 31, 2012 and 2011.

During the years ended December 31, 2012 and 2011, assets totaling $ 5,000 and $ 164,847, respectively, were transferred from the unrestricted Charitable Gift Annuity Reserve Fund into the permanently restricted endowment fund in accordance with donor restrictions. These assets were transferred upon the deaths of the donors and the corresponding termination of charitable gift annuity arrangements.

NOTE 17: Retirement Plans

The Masonic Homes and Grand Lodge have a noncontributory defined benefit pension plan covering substantially all employees. The benefits are based on achieving a minimum of five years of service and the employee's average annual compensation for the five highest consecutive years of service. The employer contributions to the Plan are determined annually by the Grand Lodge Committee on Finance within limits established by the Employee Retirement Income Security Act (ERISA) of 1974. Masonic Homes made contributions of $ 5,200,000 and $ 6,357,184 to the Plan during the years ended December 31, 2012 and 2011, respectively. Contributions provide for benefits earned to date as well as benefits expected to be earned in the future.

NOTE 17: Retirement Plans - Continued

In September 2010, the Administrators of the Pension Plan and the Grand Lodge Committee on Finance adopted an amendment to the noncontributory defined benefit pension plan. The amendment resulted in ceasing all benefit accruals as of December 31, 2010. Grand Lodge and Masonic Homes will continue to make cash contributions to the defined benefit pension plan until the plan's assets equal or exceed the projected benefit obligation. When this occurs, the defined benefit pension plan will be terminated and annuity contracts will be purchased from insurance companies to provide the guaranteed retirement income for eligible employees. The plan may also be amended and lump sum payments issued to certain participants. The goal of the Administrators of the Pension Plan is to fully fund and terminate the defined benefit plan within the next four years. The Administrators of the Pension Plan also adopted a resolution to implement a defined contribution retirement plan effective January 1, 2011. The new defined contribution retirement plan, which is funded by contributions from both the employer and employees, replaced the defined benefit pension plan.

Generally accepted accounting principles require an employer to recognize the over-funded or under-funded status of a defined benefit post-retirement plan as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through changes in unrestricted net assets. An employer must measure the funded status of a plan as of the date of its year-end statement of financial position. The measurement date requirement has been met, since the fiscal year of the noncontributory defined benefit pension plan is already consistent with the Masonic Homes fiscal year. The recognition of the change in the accrued pension liability is reported separately from net periodic pension expense. The net change in the accrued pension liability reported in the statement of activities for the years ended December 31, 2012 and 2011 consists of the following:

Amortization of net gain	$ 842,452	$ -
Net actuarial loss	(8,999,595)	(12,919,584)
	$ (8,157,143)	$ (12,919,584)

The estimated amount that will be amortized from unrestricted net assets into net periodic pension expense in 2013 is $ 1,353,000.

NOTE 17: Retirement Plans - Continued

The following table sets forth the Masonic Homes' share of plan obligations and plan assets and amounts recognized in the consolidated financial statements at and for the years ended December 31, 2012 and 2011:

	2012	2011
Change in projected benefit obligation for service rendered to date:		
Projected benefit obligation at January 1	$ 102,220,000	$ 88,107,000
Service cost	287,794	287,473
Interest cost	4,891,732	4,844,954
Actuarial loss	13,281,946	11,747,250
Expenses paid	(302,570)	(325,075)
Benefits paid	(2,603,902)	(2,441,602)
Projected benefit obligation at December 31	117,775,000	102,220,000
Change in plan assets, primarily stocks and bonds:		
Plan assets at fair value at January 1	74,332,870	67,395,459
Actual return on plan assets	9,175,368	3,346,904
Employer contributions	5,200,000	6,357,184
Expenses paid	(302,570)	(325,075)
Benefits paid	(2,603,902)	(2,441,602)
Plan assets at fair value at December 31	85,801,766	74,332,870
Projected benefit obligation in excess of plan assets at December 31	(31,973,234)	(27,887,130)
Accrued pension cost at December 31	$ (31,973,234)	$ (27,887,130)
Accumulated benefit obligation at December 31	$ 117,775,000	$ 102,220,000
Net pension cost for 2012 and 2011 includes the following components:		
Service cost - Benefits earned during the year	$ 287,794	$ 287,473
Interest cost on projected benefit obligation	4,891,732	4,844,954
Expected return on plan assets	(4,893,017)	(4,519,238)
Net amortization and deferrals	842,452	-
Net periodic pension cost	$ 1,128,961	$ 613,189
Benefits paid	$ 2,603,902	$ 2,441,602

NOTE 17: Retirement Plans – Continued

The following assumptions were used in determining the actuarial present value of the projected benefit obligation and the long-term rate of return on assets:

Weighted discount rate	4.80%	5.50%
Rate of compensation increase	0.00%	0.00%
Long-term rate of return on assets	6.50%	6.50%

The overall expected long-term rate of return on assets assumption (6.50%) is based upon the defined benefit pension plan's past investment performance and the general economic conditions at the time the annual pension calculations are prepared. The defined benefit pension plan's investment objective is to achieve the greatest return possible for the amount of risk assumed. To achieve this objective, the defined benefit pension plan's investment policy establishes target asset allocation percentages and permissible ranges of asset allocations between equity securities and fixed income securities. The goal to fully fund and terminate the defined benefit pension plan within the next four years resulted in significant changes to the investment strategy. In 2011 the defined benefit pension plan adopted a liability driven investment strategy focused on accumulating the assets necessary to terminate the plan. The target percentages for the years ended December 31, 2012 and 2011 were 30% in equity securities and 70% in fixed income and cash equivalents, with a permissible additional range of 30% for equity securities and 30% for fixed income securities. There are additional target allocations established for subcategories of potential investments within the equity and fixed income categories. These targets and ranges are periodically reviewed by the administrators of the defined benefit pension plan and adjusted when necessary to meet changes in financial market conditions and future benefit payment requirements.

The investments in the defined benefit pension plan as of December 31, 2012 consisted of approximately 58% in equity securities, 40% in fixed income securities, and approximately 2% in cash equivalents. As of December 31, 2011, the investments in the defined benefit pension plan consisted of approximately 36% in equity securities, 63% in fixed income securities, and approximately 1% in cash equivalents.

The defined benefit pension plan measures the fair value of its investments in accordance with generally accepted accounting principles. Generally accepted accounting principles for fair value measurements are described in Note 23.

NOTE 17: Retirement Plans – Continued

The fair values of the defined benefit pension plan's investments measured on a recurring basis are as follows:

At December 31, 2012	Fair Value	Quote Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Domestic and international common stocks:				
Consumer staples and discretionary	$ 4,672,099	$ 4,672,099	$ -	$ -
Energy	1,411,986	1,411,986	-	-
Financial	2,870,456	2,681,049	189,407	-
Health care	738,264	738,264	-	-
Industrials	5,306,566	5,252,961	53,605	-
Information technology	386,479	386,479	-	-
Materials	916,967	916,967	-	-
Telecommunications services	782,003	782,003	-	-
Transportation	369,577	369,577	-	-
Utilities	340,176	340,176	-	-
Total domestic and international common stocks	17,794,573	17,551,561	243,012	-
U.S. Government securities	3,289,537	-	3,289,537	-
Asset backed securities	7,481,184	-	7,481,184	-
Mortgage backed securities	8,393,002	-	8,393,002	-
Corporate debt:				
Aa credit rating	124,910	-	124,910	-
A credit rating	1,399,082	-	1,399,082	-
Baa credit rating	982,950	-	982,950	-
Ba credit rating	129,523	-	129,523	-
Unrated	3,153,382	-	3,153,382	-
Total corporate debt	5,789,847	-	5,789,847	-
Registered investment companies:				
Domestic equity growth funds	2,654,774	2,654,774	-	-
Fixed income fund	4,205,627	-	4,205,627	-
Total registered investment companies	6,860,401	2,654,774	4,205,627	-
Exchange traded funds	33,893,440	33,893,440	-	-
Municipal bonds:				
Aaa credit rating	-	-	-	-
Unrated	3,045,193	-	3,045,193	-
Total municipal bonds	3,045,193	-	3,045,193	-
Money market funds	3,576,303	-	3,576,303	-
	$ 90,123,480	$ 54,099,775	$ 36,023,705	$ -

NOTE 17: Retirement Plans – Continued

At December 31, 2011	Fair Value	Quote Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Domestic and international common stocks:				
Consumer staples and discretionary	$ 1,214,233	$ 1,214,233	$ -	$ -
Energy	350,213	350,213	-	-
Financial	671,483	671,483	-	-
Health care	547,795	547,795	-	-
Industrials	721,913	721,913	-	-
Information technology	1,168,311	1,168,311	-	-
Materials	117,916	117,916	-	-
Telecommunications services	137,347	137,347	-	-
Utilities	233,496	233,496	-	-
Total domestic and international common stocks	5,162,707	5,162,707	-	-
U.S. Government securities	10,757,516	-	10,757,516	-
Mortgage backed securities	9,683,058	-	9,683,058	-
Corporate debt:				
Aaa credit rating	1,896,155	-	1,896,155	-
Aa credit rating	2,133,209	-	2,133,209	-
A credit rating	4,421,640	-	4,421,640	-
Baa credit rating	3,466,245	-	3,466,245	-
Ba credit rating	870,812	-	870,812	-
B credit rating	1,272,224	-	1,272,224	-
Unrated	4,200,880	-	4,200,880	-
Total corporate debt	18,261,165	-	18,261,165	-
Registered investment companies:				
Domestic equity growth funds	15,877,638	12,911,998	-	2,965,640
Fixed income fund	4,863,944	-	-	4,863,944
International equity growth funds	5,178,587	5,178,587	-	-
Total registered investment companies	25,920,169	18,090,585	-	7,829,584
Exchange traded funds	2,528,819	2,528,819	-	-
Municipal bonds:				
Aaa credit rating	362,778	-	362,778	-
Aa credit rating	3,031,991	-	3,031,991	-
A credit rating	834,170	-	834,170	-
Unrated	169,982	-	169,982	-
Total municipal bonds	4,398,921	-	4,398,921	-
	$ 76,712,355	$ 25,782,111	$ 43,100,660	$ 7,829,584

NOTE 17: Retirement Plans – Continued

The changes in the defined benefit pension plan's assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3 inputs) are as follows for the years ended December 31, 2012 and 2011:

	2012	2011
Fair value as of January 1	$ 7,829,584	$ 8,129,391
Realized gains	806,741	352,427
Unrealized losses on assets held at reporting date	(451,183)	(127,898)
Transfer to Level 2	(4,863,944)	-
Purchases	-	1,871,417
Sales	(3,321,198)	(2,395,753)
Fair value as of December 31	$ -	$ 7,829,584

The following benefit payments are expected to be made from the Masonic Homes portion of the defined benefit pension plan during the years ending December 31:

2013	$ 3,096,000
2014	3,382,000
2015	3,644,000
2016	3,919,000
2017	4,232,000
2018 through 2022	26,359,000
	$ 44,632,000

Masonic Homes will make an estimated contribution of approximately $ 5,200,000 to the defined benefit pension plan during the year ending December 31, 2013.

In addition to the noncontributory defined benefit plan, Masonic Homes sponsors a retirement plan established under Section 403 (b) of the Internal Revenue Code. This retirement plan is available to substantially all Masonic Homes' employees and is funded by contributions made by employees and Masonic Homes to a third party administrator. Annual contributions by the employees are subject to maximum limits established by federal legislation. Masonic Homes made contributions to the defined contribution retirement plan totaling $ 2,283,616 and $ 2,012,347 during the years ended December 31, 2012 and 2011, respectively. Masonic Homes also incurred administrative costs related to the defined contribution retirement plan totaling $ 12,186 and $ 3,165 during the years ended December 31, 2012 and 2011, respectively.

In April 2012, Masonic Homes established a new noncontributory retirement plan under Section 457 (b) of the Internal Revenue Code. This retirement plan is available to certain senior management employees of Masonic Homes and is funded solely by contributions made by employees to a third party administrator. Annual contributions by the employees are subject to maximum limits established by federal legislation. Accumulated assets of this noncontributory retirement plan are included in Masonic Homes' investments with a corresponding liability reported in accrued expenses on the balance sheet. Masonic Homes incurred administrative costs related to this noncontributory retirement plan totaling $ 1,950 during the year ended December 31, 2012.

NOTE 18: Resident Service Revenue

Masonic Homes has agreements with third-party payors that provide for reimbursement to the Masonic Homes at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the billings at established rates for services and amounts reimbursed by third-party payors. Masonic Homes' major third-party payors are Medicare and Medicaid.

For the years ended December 31, 2012 and 2011, services rendered to Medicare program beneficiaries were reimbursed on a prospective payment system or fee schedule, depending on the medical services provided. Under the prospective payment system, Masonic Homes is reimbursed according to the beneficiaries' acuity level and services provided. Under the fee schedule, Masonic Homes is reimbursed the lesser of its charge or the allowable amount per the fee schedule.

Services rendered to Medicaid program beneficiaries are reimbursed based on a prospective case-mix payment system. Under this system, nursing facilities are categorized into peer groups based on geographic location and number of certified beds. The Commonwealth of Pennsylvania's Department of Public Welfare (Department) establishes per diem rates to reimburse nursing facilities using peer group data adjusted for each individual facility's resident acuity.

In January 2005, the Department implemented a nursing facility assessment program for nursing facilities operating in Pennsylvania. Under this program, the Department collects an assessment from nursing facilities operating in Pennsylvania based on each facility's assessment days. The payments received by the Department from this quarterly assessment are used to obtain federal matching funds to maintain reimbursement for those nursing facilities participating in the Medicaid program. Masonic Homes recognized nursing assessment costs of $ 1,620,119 and $ 1,286,825 for the years ended December 31, 2012 and 2011, respectively. Nursing assessment costs are reported as a component of other operating expenses by Masonic Homes in the consolidated statements of operations. Masonic Homes recognized increased Medicaid reimbursement of $ 2,994,875 and $ 2,961,614 from the nursing assessment program for the years ended December 31, 2012 and 2011, respectively. Increased Medicaid reimbursement from the nursing assessment program is reported as a component of contractual adjustments under third party programs. The amount of additional reimbursement recognized as an estimated third party settlement receivable at December 31, 2012 and 2011 was $ 2,303,001 and $ 2,160,705, respectively.

Masonic Homes recognizes resident service revenue associated with services provided to residents who have third party coverage on the basis of contractual rates for the services rendered. For uninsured private pay residents that qualify for charity care, Masonic Homes recognizes revenue on the basis of its standard rates for services provided, reduced by the estimated portion of the standard rate the resident is unable to pay. The estimated portion of the standard rate the resident is unable to be pay is recognized as a charity care allowance. For uninsured private pay residents that do not qualify for charity care, Masonic Homes recognizes revenue on the basis of its standard rates for services provided. On the basis of historical experience, a portion of Masonic Homes' uninsured private pay residents that do not qualify for charity care will be unable or unwilling to pay for the services provided. Masonic Homes records a provision for bad debts related to these uninsured private pay residents in the period the services are provided.

NOTE 18: Resident Service Revenue – Continued

Masonic Homes' major payor sources consist of the Medicaid and Medicare programs, other third party payors (primarily commercial insurance and managed care organizations), and private pay individuals. Resident service revenue, net of contractual and charity care allowances provided (but before the provision for bad debts), recognized in the consolidated statements of operations for the years ended December 31, 2012 and 2011 from these major payor sources is as follows:

	2012			
	Medicare and Medicaid	Other Third Party Payors	Private Pay	Total
Gross resident service revenue	$ 41,745,151	$ 17,853,472	$ 85,398,372	$ 144,996,995
Less provisions for:				
Contractual adjustments under third party reimbursement programs	10,386,866	8,569,773	-	18,956,639
Employee health care/wellness	-	-	85	85
Charity care allowances	-	-	9,658,322	9,658,322
Net resident service revenue, before provision for bad debts	$ 31,358,285	$ 9,283,699	$ 75,739,965	$ 116,381,949

	2011			
	Medicare and Medicaid	Other Third Party Payors	Private Pay	Total
Gross resident service revenue	$ 40,617,809	$ 16,333,315	$ 81,399,393	$ 138,350,517
Less provisions for:				
Contractual adjustments under third party reimbursement programs	4,607,863	7,431,921	-	12,039,784
Employee health care/wellness	-	-	338	338
Charity care allowances	-	-	9,270,949	9,270,949
Net resident service revenue, before provision for bad debts	$ 36,009,946	$ 8,901,394	$ 72,128,106	$ 117,039,446

NOTE 19: Charity Care and Community Service

Masonic Homes' mission has been to provide services to residents, regardless of their ability to pay, who have medical, social, or financial need.

NOTE 19: Charity Care and Community Service - Continued

Masonic Homes provides services to adult individuals who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Criteria considered in Masonic Homes' charity care policy include the income and net worth of the adult individuals applying for charity care. Adult individuals applying for charity care must also be determined to be ineligible for reimbursement from applicable government programs for the services to be provided. Charity care may be provided to qualifying adult individuals for Personal Care, Retirement Living, Residential Care, and certain medical and nonmedical ancillary services. All services provided in the Children's Home are provided as charity care.

Masonic Homes maintains records to identify and monitor the level of charity care and community service it provides. These records include the amount of charges forgone based on established rates for the services and supplies furnished under its charity care policy. Charges forgone for charity care are excluded from net resident service revenue recorded by Masonic Homes. The cost to provide charity care is estimated on an annual basis for each service area providing charity care. Estimated charity care costs for an individual service area are determined by multiplying the individual service area's forgone charges by the ratio of the individual service area's direct and allocated indirect expenses to its gross charges. Masonic Homes' aggregate estimated cost of providing charity care is the sum of the charity care costs calculated for the individual service areas.

Charges forgone for charity care and the estimated costs of providing charity care for the years ended December 31, 2012 and 2011 were as follows:

	2012	2011
Charges forgone	$ 9,658,407	$ 9,271,006
Estimated cost to provide charity care	$ 8,349,442	$ 8,258,999

Masonic Homes has received contributions restricted for the care and support of Retirement Living residents eligible for charity care. These contributions are recorded as temporarily restricted net assets and periodically released from restriction to subsidize charges forgone to provide charity care to Retirement Living residents. Net assets released from donor restriction to subsidize charity care provided to Retirement Living residents totaled $ 46,256 and $ 188,523 for the years ended December 31, 2012 and 2011, respectively.

Masonic Homes also participates in the Medicare and Medical Assistance programs which make payment for services provided to financially eligible residents at rates which are less than the cost of such services. Management estimates the unpaid costs of these programs are approximately $ 7,077,000 and $ 4,020,000 in 2012 and 2011, respectively.

Masonic Homes conducts two programs that benefit people not residing at the Elizabethtown campus. The Home Assistance program (Home Assistance) provides financial resources and other services to Pennsylvania Masons and their families in need. Home Assistance is provided in two forms: charity care and temporary assistance. The cost of providing Home Assistance totaled $ 40,472 and $ 44,995 for the years ended December 31, 2012 and 2011, respectively. Masonic Homes has also established an Outreach program (Outreach) to assist individuals in their communities. People contacting Outreach receive information about various aspects of long-term care, including government programs available, selecting a long-term care facility, insurance, transportation, and counseling. The cost of Outreach totaled $ 1,687 and $ 1,029 for the years ended December 31, 2012 and 2011, respectively.

NOTE 19: Charity Care and Community Service – Continued

During 2012 and 2011, Masonic Homes permitted its meeting and conference facilities to be used by several not-for-profit organizations, including the Pennsylvania Masonic Youth Foundation and the Elizabethtown Area School District. Masonic Homes received no rental fees for the use of the meeting and conference facilities. The cost of providing this service to these organizations totaled approximately $ 211,000 and $ 196,000 for the years ended December 31, 2012 and 2011, respectively.

Masonic Homes made contributions of cash, promises to give, and in-kind services to not-for-profit organizations in the communities it serves. For the years ended December 31, 2012 and 2011, these contributions totaled $ 106,979 and $ 76,154, respectively. Masonic Homes also awarded scholarships to several individuals. Individuals receiving scholarships included graduating high school students based on academic achievement, financial need, and community service. Scholarships for child day care services were awarded for pre-school age children whose families met certain financial need criteria as specified in the Pennsylvania Educational Improvement Tax Credit program. Scholarship payments totaled $ 55,828 and $ 34,500 for the years ended December 31, 2012 and 2011.

NOTE 20: Functional Allocation of Expenses

The costs of providing the various programs and other activities have been summarized on a natural basis in the consolidated statements of operations. The following table summarizes operating expenses on a functional basis for the years ended December 31, 2012 and 2011.

	2012	2011
Program Services:		
Nursing Care	$ 48,907,761	$ 48,456,518
Medical Ancillary Clinics	9,715,588	9,088,082
Personal Care	8,000,493	7,943,719
Retirement Living	36,119,418	34,792,720
Children's Home	1,935,732	1,906,607
Adult Daily Living Center	288,744	305,618
Residential Care Program	258,141	251,041
Hospice	1,411,040	1,211,546
Wellness Center	930,073	924,794
Home Care Services	698,840	563,443
Community Services	148,407	113,524
Child Day Care Center	419,204	444,142
Conference Facilities	2,464,489	2,468,492
Contributions to Affiliates	2,377,651	2,140,236
Employee Housing and Rental Property	1,190,115	926,259
Farm	1,225,520	1,137,672
Communications Services	619,055	582,291
Admissions and Resident Services	1,852,232	1,753,471
Support Services	4,310,054	4,132,981
Maintenance	7,971,812	8,183,098
Food Services	6,346,524	6,512,545
Total program services expense	137,190,893	133,838,799
Management and general - Administration	15,188,407	15,743,101
Fundraising - Gift Planning	1,449,922	1,231,358
	$ 153,829,222	$ 150,813,258

NOTE 21: Transactions with Affiliated Organizations

Contributions from Affiliated Organizations

Masonic Homes receives contributions from certain Grand Lodge permanently restricted net assets. The contributions are made from trusts established by the donors to benefit needy Masons, widows, and children. Contributions were received by Masonic Homes from the following trusts for the years ended December 31, 2012 and 2011:

	2012	2011
Thomas Ranken Patton Contingency Fund	$ 156,195	$ 153,191
Thomas Ranken Patton Masonic Institution for Boys	69,716	68,502
Thomas Ranken Patton Memorial Charity Fund	438,000	876,000
Henry C. and Anna C. Ellis Trust	6,674	6,094
Joseph W. Murray Memorial Fund	14,550	14,306
Gertrude M. Flack Scholarship Fund	82,325	13,539
Nelson Herst Scholarship Fund	82,325	13,538
Charles W. Jackson McClary Memorial Fund #1	3,915	3,846
	$ 853,700	$ 1,149,016

These contributions are included in non-operating gains for the years ended December 31, 2012 and 2011.

The Masonic Charities Fund made contributions to Masonic Homes' permanently restricted endowment fund totaling $ 4,071 and $ 2,219 during the years ended December 31, 2012 and 2011. These contributions to the permanently restricted endowment fund represent undesignated contributions received by the Masonic Charities Fund from a multi-year fundraising effort called the Capital Campaign. The purpose of the Capital Campaign is to increase the permanently restricted endowment funds of the Pennsylvania Masonic charitable entities.

Contributions to Affiliated Organizations

Masonic Homes made contributions to the following related 501(c)(3) charitable organizations:

	2012	2011
Pennsylvania Masonic Youth Foundation	$ 488,956	$ 482,043
The Masonic Library and Museum of Pennsylvania	1,888,298	1,657,779
	$ 2,377,254	$ 2,139,822

These contributions consisted of cash, the use of Masonic Homes' facilities, and donated services provided by Masonic Homes' employees. These annual contributions to the Pennsylvania Masonic Youth Foundation and the operation of the Children's Home support Masonic Homes' mission to improve the welfare of children.

Masonic Homes made contributions totaling $ 1,888,298 to The Masonic Library and Museum of Pennsylvania (Masonic Library and Museum) for the year ended December 31, 2012. These contributions consisted of cash payments of $ 1,874,383 and donated services provided by Masonic Homes' employees with a cost of $ 13,915.

NOTE 21: Transactions with Affiliated Organizations – Continued

Contributions to Affiliated Organizations - Continued

Masonic Homes made contributions totaling $ 1,657,779 to the Masonic Library and Museum for the year ended December 31, 2011. These contributions consisted of cash payments of $ 1,648,594 and donated services provided by Masonic Homes’ employees with a cost of $ 9,185.

Contributions from Masonic Homes Temporarily Restricted Net Assets are made to the Masonic Charities Fund. These contributions are reported as satisfaction of donor restrictions in the consolidated statements of changes in net assets. The contributions are made from the Reidler Helping Hand Fund, which was established to benefit Masonic Homes and the Masonic Charities Fund. Contributions from this trust to the Masonic Charities Fund totaled $ 397 and $ 414 for the years ended December 31, 2012 and 2011, respectively.

Administrative and Program Service Expenses

For the years ended December 31, 2012 and 2011, Masonic Homes' employees provided human resources, accounting, and information technology services to Grand Lodge under an expense reimbursement arrangement with Masonic Homes. Masonic Homes' costs for these services allocated to Grand Lodge for the years ended December 31, 2012 and 2011 were $ 6,397 and $ 13,097, respectively. Reimbursement received for these costs is included in other operating revenue on the consolidated statements of operations.

During the years ended December 31, 2012 and 2011, Masonic Homes' employees provided human resources, accounting, fundraising, and information technology services to the Masonic Library and Museum under a contribution arrangement with Masonic Homes. Masonic Homes' costs for these services contributed to the Masonic Library and Museum totaled $ 13,915 and $ 9,185 for 2012 and 2011, respectively, and are included in operating expenses on the consolidated statement of operations.

Masonic Homes' employees also provided accounting, fundraising, and information technology services to the Pennsylvania Masonic Youth Foundation under a contribution arrangement with Masonic Homes. Masonic Homes' costs for these services contributed to the Pennsylvania Masonic Youth Foundation for the years ended December 31, 2012 and 2011 were $ 20,264 and $ 18,472, respectively. These costs are included in operating expenses on the consolidated statements of operations.

NOTE 21: Transactions with Affiliated Organizations – Continued

Administrative and Program Service Expenses - Continued

During 2012 and 2011, Masonic Homes' employees provided fundraising services to the Masonic Charities Fund under an expense reimbursement arrangement with Masonic Homes. Masonic Homes' cost for these services allocated to the Masonic Charities Fund for the years ended December 31, 2012 and 2011 were $ 69,639 and $ 60,849, respectively, and are included in other operating revenue on the consolidated statements of operations.

For the years ended December 31, 2012 and 2011, Masonic Homes' employees provided administrative and program services to the Pennsylvania Masonic Youth Foundation. Masonic Homes' costs for these services contributed to the Pennsylvania Masonic Youth Foundation for the years ended December 31, 2012 and 2011 were $ 331,748 and $ 325,095, respectively. These costs are included in operating expenses on the consolidated statements of operations.

Use of Facilities

The Pennsylvania Masonic Youth Foundation conducts most of its activities at conference facilities owned by Masonic Homes. The use of these conference facilities was provided to the Pennsylvania Masonic Youth Foundation under a contribution arrangement with Masonic Homes. Masonic Homes' costs for the use of the conference facilities contributed to the Pennsylvania Masonic Youth Foundation for the years ended December 31, 2012 and 2011 were $ 132,675 and $ 134,472, respectively. These costs are included in operating expenses on the consolidated statements of operations.

Reimbursement for Costs

The Pennsylvania Masonic Youth Foundation has developed and maintained an internet page for Grand Lodge and its affiliated entities. Costs incurred by the Pennsylvania Masonic Youth Foundation were reimbursed by Grand Lodge and its affiliated entities based on each entity's pro rata share of space on the internet page. Masonic Homes' cost for internet page space totaled $ 0 and $ 3,375 for the years ended December 31, 2012 and 2011, respectively. These costs are included in operating expenses on the consolidated statements of operations.

NOTE 22: Split-Interest Agreements

Masonic Homes has entered into several split-interest agreements with donors. These split-interest agreements include charitable gift annuities, charitable remainder unitrusts, charitable lead trusts, pooled income funds, and perpetual trusts held by third parties. Under split-interest agreements, a donor makes an initial gift to a trust or directly to Masonic Homes in which Masonic Homes has a beneficial interest. Donated assets are maintained by a trust or Masonic Homes and distributions are made to a beneficiary or beneficiaries during the term of the agreement. At the end of the agreement's term, any remaining assets covered by the agreement are distributed to Masonic Homes.

Assets received under split-interest agreements are recorded at the fair value of the assets on the date received. Liabilities to beneficiaries are recorded at the net present value of expected payments based upon the amount of the contribution, any contractual rate of return, and the life expectancy of the beneficiary. Contribution revenue is classified as either unrestricted or temporarily restricted based on the existence of any donor imposed conditions in the split-interest agreement.

As of December 31, 2012 and 2011, the fair value of assets recognized under split-interest agreements by Masonic Homes, consisting principally of cash and investments, was as follows:

	2012	2011
Perpetual trusts held by third parties	$ 42,754,968	$ 39,418,442
Charitable gift annuities	12,621,008	11,434,598
Charitable remainder unitrusts	618,560	616,315
	$ 55,994,536	$ 51,469,355

Contribution revenues recognized by Masonic Homes under split-interest agreements for the years ended December 31, 2012 and 2011 were as follows:

	2012	2011
Unrestricted -		
Charitable gift annuities	$ 546,200	$ 365,002
Permanently restricted -		
Perpetual trusts held by third parties	-	62,685
Total unrestricted and restricted	$ 546,200	$ 427,687

Masonic Homes is an income beneficiary of several perpetual trusts held by third parties. Distributions of income are made at the discretion of the trustees. Income distributed to the Masonic Homes by perpetual trusts held by third parties amounted to $ 1,736,421 and $ 1,796,662 for the years ended December 31, 2012 and 2011, respectively.

NOTE 23: Fair Value Measurements

Generally accepted accounting principles define fair value, describe a framework for measuring fair value, and require disclosure about fair value measurements. The established framework includes a three-level hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. 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 assets or liabilities fall within different levels of the hierarchy, the classification is based on the lowest level input that is significant to the fair value measurement of the asset or liability. Classification of assets and liabilities within the hierarchy considers the markets in which the assets and liabilities are traded and the reliability and transparency of the assumptions used to determine fair value. The hierarchy requires the use of observable market data when available. The levels of the hierarchy and those investments included in each are as follows:

Level 1 – Represented by quoted prices available in an active market. Level 1 securities include highly liquid government bonds, treasury securities, mortgage products, and exchange traded equities

Level 2 – Represented by assets and liabilities similar to Level 1 where quoted prices are not available, but are observable, either directly or indirectly through corroboration with observable market data, such as quoted prices for similar securities and quoted prices in inactive markets and estimated using pricing models or discounted cash flows. Level 2 securities would include U.S. agency securities, mortgage-backed agency securities, obligations of states, and political subdivisions and certain corporate, asset backed securities, swap agreements, and internally developed values with little uncertainty.

Level 3 – Represented by financial instruments where there is limited activity or unobservable market prices and pricing models significant to determining the fair value measurement including the reporting entity’s own assumptions about the market risk. Level 3 securities would include hedge funds, private equity securities, and internally developed values with significant uncertainty.

NOTE 23: Fair Value Measurements – Continued

As described in Note 7, Masonic Homes' most significant investment is its share of the Consolidated Fund. The fair values of the Consolidated Fund's assets measured on a recurring basis as of December 31, 2012 and 2011 are as follows:

At December 31, 2012	Fair Value	Quote Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Domestic and international common stocks:				
Consumer staples and discretionary	$ 35,808,993	$ 35,808,993	$ -	$ -
Energy	8,637,302	8,637,302	-	-
Financial	20,104,291	19,754,572	349,719	-
Health care	4,260,826	4,260,826	-	-
Industrials	46,173,215	46,173,215	-	-
Information technology	4,165,727	4,153,559	12,168	-
Materials	9,790,476	9,790,476	-	-
Transportation	5,342,807	5,342,807	-	-
Telecommunications services	6,650,389	6,650,389	-	-
Utilities	3,489,654	3,489,654	-	-
Total domestic and international common stocks	144,423,680	144,061,793	361,887	-
U.S. Government securities	13,044,938	-	13,044,938	-
Domestic corporate bonds:				
Aa credit rating	4,034,901	-	4,034,901	-
A credit rating	26,216,218	-	26,216,218	-
Baa credit rating	3,814,435	-	3,814,435	-
B credit rating	875,307	-	875,307	-
Bb credit rating	2,200,786	-	2,200,786	-
Bbb credit rating	14,104,553	-	14,104,553	-
Unrated	54,399,949	-	54,399,949	-
Total domestic corporate bonds	105,646,149	-	105,646,149	-
Municipal bonds:				
Unrated	8,721,044	-	8,721,044	-
Total municipal bonds	8,721,044	-	8,721,044	-
Mutual funds - Equity securities	160,190,815	136,251,013	23,939,802	-
Collective investment fund - Hedge funds	348,532	-	-	348,532
Exchange traded funds	47,851,370	47,851,370	-	-
Limited partnership - International	24,559,334	-	-	24,559,334
Mortgage backed securities	29,192,561	-	29,192,561	-
Asset backed securities	29,182,437	-	29,182,437	-
Demand notes	875,079	-	875,079	-
Real estate investment trusts	772,978	772,978	-	-
Money Market funds	37,664,547	-	37,664,547	-
	$ 602,473,464	$ 328,937,154	$ 248,628,444	$ 24,907,866

NOTE 23: Fair Value Measurements – Continued

At December 31, 2011	Fair Value	Quote Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Domestic and international common stocks:				
Consumer staples and discretionary	$ 28,918,336	$ 28,918,336	$ -	$ -
Energy	10,736,489	10,736,489	-	-
Financial	18,395,408	18,395,408	-	-
Health care	19,665,000	19,665,000	-	-
Industrials	53,360,351	53,360,351	-	-
Information technology	5,312,864	5,273,383	39,481	-
Materials	12,091,016	12,091,016	-	-
Transportation	5,346,215	5,346,215	-	-
Telecommunications services	7,263,988	7,263,988	-	-
Utilities	3,163,047	3,163,047	-	-
Total domestic and international common stocks	164,252,714	164,213,233	39,481	-
U.S. Government securities	13,061,030	-	13,061,030	-
Domestic corporate bonds:				
Aa credit rating	10,214,440	-	10,214,440	-
A credit rating	36,213,330	-	36,213,330	-
Baa credit rating	15,433,757	-	15,433,757	-
Ba credit rating	3,818,709	-	3,818,709	-
B credit rating	1,642,190	-	1,642,190	-
Bbb credit rating	887,100	-	887,100	-
Unrated	36,107,444	-	36,107,444	-
Total domestic corporate bonds	104,316,970	-	104,316,970	-
Municipal bonds:				
Unrated	10,794,189	-	10,794,189	-
Total municipal bonds	10,794,189	-	10,794,189	-
Mutual funds - Equity securities	112,580,661	100,320,656	12,260,005	-
Collective investment fund - Hedge funds	348,532	-	-	348,532
Exchange traded funds	31,926,790	31,926,790	-	-
Limited partnership - International	33,508,735	-	-	33,508,735
Mortgage backed securities	41,825,007	-	41,825,007	-
Asset backed securities	22,081,339	-	22,081,339	-
Real estate investment trusts	1,049,895	1,049,895	-	-
Money Market funds	34,984,696	-	34,984,696	-
	$ 570,730,558	$ 297,510,574	$ 239,362,717	$ 33,857,267

NOTE 23: Fair Value Measurements – Continued

The Consolidated Fund has investments in certain financial instruments whose fair values are determined using significant unobservable inputs. This feature may limit the ability of the Consolidated Fund to liquidate these financial instruments quickly if necessary. Financial instruments whose fair values are determined using significant unobservable inputs and their redemption features are as follows as of December 31, 2012:

	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Collective investment fund - Hedge fund	$ 348,532	$ -	Quarterly	45 Days
Limited partnership - International	1,256,501	-	Quarterly	45 Days
Limited partnership - International	23,302,833	-	No limits	None
	$ 24,907,866	$ -		

The redemption restrictions for these financial instruments are included in the contracts with the investment management firms responsible for these investments. The Consolidated Fund started the process of completely redeeming its collective investment fund – hedge funds in early 2009. The Consolidated Fund expects this redemption will conclude in 2013 at the fair value reported as of December 31, 2012.

Changes in the Consolidated Fund's investments in financial instruments whose fair values are determined using significant unobservable inputs were as follows for the years ended December 31, 2012 and 2011:

	Total	Collective Investment Fund - Hedge Funds	Limited Partnership - International
Fair value at January 1, 2011	$ 34,628,300	$ 348,532	$ 34,279,768
Realized gains	63,890	-	63,890
Unrealized losses	(141,863)	-	(141,863)
Sales	(776,063)	-	(776,063)
Purchases	83,003	-	83,003
Fair value at December 31, 2011	33,857,267	348,532	33,508,735
Realized gains	2,627,860	-	2,627,860
Unrealized losses	(162,018)	-	(162,018)
Sales	(11,486,836)	-	(11,486,836)
Purchases	71,593	-	71,593
Fair value at December 31, 2012	$ 24,907,866	$ 348,532	$ 24,559,334

NOTE 23: Fair Value Measurements – Continued

The fair values of Masonic Homes' assets are measured using different techniques. Fair values for investments are determined by reference to quoted market prices and other relevant information generated by market transactions. Fair values of perpetual trusts held by third parties are measured by applying known beneficiary percentages to the fair values of the trust's assets which consists of a combination of actively traded securities and other securities which are valued using significant other observable inputs. When unable to obtain a fair value for a perpetual trust, the fair value is estimated by calculating the present value of income received from the trust under a reasonable rate of return percentage. Fair value for the contribution receivable from a beneficial interest in a charitable lead annuity trust is determined by calculating the present value of the annuity using published life expectancy tables and a 4.25% discount rate. Fair values for the contributions receivable from beneficial interests in several charitable remainder unitrusts are determined by calculating the present value of the future distributions expected to be received, using published life expectancy tables and discount rates ranging from 6.50% to 7.00%. Fair values for unconditional promises to give are determined by calculating the present value of the future cash flows expected to be received, using the stated terms of the promises to give and discount rates ranging from 1.84% to 4.69%. The fair values of assets measured on a recurring basis as of December 31, 2012 and 2011 are as follows:

	Fair Value	Quote Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Input (Level 2)	Significant Unobservable Inputs (Level 3)
At December 31, 2012				
Investments (excluding consolidated fund)				
Money Market Funds	$ 10,877,149	$ 10,877,149	$ -	$ -
Other investments	355,440	355,440	-	-
Real Estate	320,000	-	320,000	-
Equity Funds	254,570	254,570	-	-
Common Trust Funds	434,929	-	434,929	-
Perpetual Trusts Held by Third Parties	42,754,968	-	42,754,968	-
Contributions receivable - Charitable lead annuity trusts	416,623	-	416,623	-
Contributions receivable - Charitable remainder unitrusts	32,020	-	32,020	-
Contributions receivable - Promises to give	125,343	-	-	125,343
	$ 55,571,042	$ 11,487,159	$ 43,958,540	$ 125,343
At December 31, 2011				
Investments (excluding consolidated fund)				
Money Market Funds	$ 14,720,529	$ 14,720,529	$ -	$ -
Other investments	198,559	198,559	-	-
Real Estate	320,000	-	320,000	-
Equity Funds	177,354	177,354	-	-
Common Trust Funds	438,961	-	438,961	-
Perpetual Trusts Held by Third Parties	39,418,442	-	39,418,442	-
Contributions receivable - Charitable lead annuity trusts	442,844	-	442,844	-
Contributions receivable - Charitable remainder unitrusts	22,286	-	22,286	-
Contributions receivable - Promises to give	78,105	-	-	78,105
	$ 55,817,080	$ 15,096,442	$ 40,642,533	$ 78,105

NOTE 23: Fair Value Measurements – Continued

The changes in assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3 inputs) are as follows for the years ended December 31, 2012 and 2011:

	2012	2011
Fair value as of January 1	$ 78,105	$ 43,571
Promises to give received	100,000	40,000
Cash payments received	(51,800)	(4,250)
Actuarial adjustment of fair value based on remaining terms of promises to give and risk-free interest rates	(962)	(1,216)
Fair value as of December 31	$ 125,343	$ 78,105

The fair values of Masonic Homes' liabilities are measured using different techniques. Fair values for annuities payable resulting from charitable gift annuity agreements and charitable remainder unitrust agreements with donors are determined by calculating the present value of the annuity using published life expectancy tables and the contractual discount rates. Fair values for interest rate swap agreements are determined based on the terms of each agreement and proprietary valuation techniques of Wells Fargo Bank, NA, which consider the present value of estimated expected future cash flows. The fair values of liabilities measured on a recurring basis as of December 31, 2012 and 2011 are as follows:

	Fair Value	Quote Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Input (Level 2)	Significant Unobservable Inputs (Level 3)
At December 31, 2012				
Annuities payable	$ 7,616,599	$ -	$ 7,616,599	$ -
Interest rate swap agreements	34,912,253	-	34,912,253	-
	$ 42,528,852	$ -	$ 42,528,852	$ -
At December 31, 2011				
Annuities payable	$ 7,598,376	$ -	$ 7,598,376	$ -
Interest rate swap agreements	35,834,510	-	35,834,510	-
	$ 43,432,886	$ -	$ 43,432,886	$ -

NOTE 24: Minimum Liquid Reserve Requirement

Masonic Homes is licensed as a continuing care provider by the Commonwealth of Pennsylvania's Insurance Department (Insurance Department). In accordance with this licensure, Masonic Homes must establish and maintain certain minimum liquid reserves. Masonic Homes' minimum liquid reserve amount equals the greater of the next twelve months long-term debt service (Debt Service Method) or 10% of the operating expenses excluding depreciation (Operating Expense Method). Masonic Homes' governing body, the Committee on Masonic Homes, has designated a portion of the Masonic Homes Reserve Fund to satisfy this minimum liquid reserve requirement. On October 31, 1996, the Insurance Department approved this approach to compliance with the minimum reserve requirement. The minimum required reserve amounts calculated under the two methods were as follows for the years ended December 31, 2012 and 2011:

	2012	2011
Operating Expense Method		
Operating expenses	$ 153,829,222	$ 150,813,258
Less: Depreciation expense	16,255,648	15,435,444
Cash expenses for minimum liquid reserve	137,573,574	135,377,814
Percentage of cash expenses to be held in reserve	10%	10%
Minimum liquid reserve requirement under Operating Expense Method	$ 13,757,357	$ 13,537,781
Debt Service Method		
Interest expense	$ 5,895,404	$ 7,139,313
Principal payments	6,835,000	6,555,000
Minimum liquid reserve requirement under Debt Service Method	$ 12,730,404	$ 13,694,313

The fair value of the Masonic Homes Reserve Fund at December 31, 2012 and 2011 totaled $ 193,028,588 and $ 192,165,764, respectively. Masonic Homes met the minimum liquid reserve required by the Insurance Department for the years ended December 31, 2012 and 2011.

NOTE 25: Subsequent Events

Masonic Homes has evaluated events and transactions subsequent to December 31, 2012 through April 8, 2013, the date these financial statements were available to be issued. Based on the definitions and requirements of generally accepted accounting principles, except for the event discussed below, Masonic Homes has not identified any events that have occurred subsequent to December 31, 2012 and through April 8, 2013, that require recognition or disclosure in the financial statements.

On January 1, 2013, Masonic Homes transferred all of its operations, assets, and liabilities to a separate not-for-profit corporation, the Masonic Villages of the Grand Lodge of Pennsylvania (Masonic Villages). Grand Lodge is the sole member of this not-for-profit corporation. Masonic Villages will continue to operate Masonic Homes' services under the not-for-profit corporation in 2013 and subsequent years. Masonic Homes incurred costs related to this transfer totaling $ 340,386 during the year ended December 31, 2012. These costs, which consisted primarily of legal expenses ($ 336,421), accounting fees ($ 1,500), and licensing fees ($ 2,465) for the not-for-profit corporation, are included in purchased services in the statement of operations. The transfer also resulted in the termination of financial guaranty insurance policies covering three of Masonic Homes' interest rate swap agreements as of December 31, 2012. These policies had been issued by AMBAC Assurance Corporation for the interest rate swap agreements related to the 1999 Bonds, the 2001 Bonds, and the 2004 Bonds. Masonic Homes forfeited unamortized premium payments totaling $ 72,158 as a result of the termination of these financial guaranty insurance policies. This amount is included in depreciation and amortization in the statement of operations for the year ended December 31, 2012.

NOTE 26: Commitments and Contingencies

Masonic Homes has signed contracts for various construction projects approximating $ 65,679,000. At December 31, 2012, approximately $ 51,225,000 has been paid or accrued on these contracts.

Masonic Homes is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Masonic Homes' financial position.

During the year ended December 31, 2008, Masonic Homes negotiated an agreement with the Elizabethtown Area School District (School District), Elizabethtown Borough (Borough), West Donegal Township (Township), and Lancaster County (County) for annual payments in lieu of taxes for all properties located at Masonic Homes' Elizabethtown campus. This agreement became effective in 2008 and will expire on June 30, 2029. The agreement includes a specific annual payment schedule for lieu of tax payments to the School District, the Borough, the Township, and the County for the 20-year term of the agreement. The agreement also contains provisions for an annual contribution of $ 15,000 from Masonic Homes to the School District's Education Foundation. Masonic Homes will also annually fund up to six $ 2,500 college scholarships for qualified students from the School District. Masonic Homes paid $ 1,221,262 and $ 1,216,916, respectively, in lieu of tax payments under this agreement for the years ended December 31, 2012 and 2011. For the year ending December 31, 2013, Masonic Homes' commitment under the agreement is approximately $ 1,236,000.

During the year ended December 31, 2004, Masonic Homes negotiated an agreement with Aleppo Township (Aleppo), the Quaker Valley School District (Quaker Valley), and the County of Allegheny (Allegheny) for annual payments in lieu of taxes for certain tax-exempt properties at Masonic Homes' Sewickley campus. This agreement became effective in 2004 and will expire December 31, 2024. The agreement includes a specific annual payment schedule for lieu of tax payments to Aleppo, Quaker Valley, and Allegheny for the 21-year term of the agreement. The agreement also includes provisions for an annual contribution from Masonic Homes to the Sewickley Public Library. Masonic Homes is also required to fund annually a minimum amount for college scholarships for Quaker Valley students. Masonic Homes paid $ 784,025 and $ 750,387, respectively, under this agreement for the years ended December 31, 2012 and 2011. For the year ending December 31, 2013 Masonic Homes' commitment under the agreement is approximately $ 779,000.

Masonic Homes' Lafayette Hill campus has two agreements with Whitemarsh Township (Whitemarsh) for annual payments in lieu of taxes for the tax-exempt Masonic Homes property. The first agreement, for gross receipts tax, requires a minimum annual payment to Whitemarsh of $ 10,000, adjusted for an inflation factor based on the Consumer Price Index for the Philadelphia region. The second agreement, for real estate taxes, requires an annual payment to Whitemarsh based on the assessed value of the Lafayette Hill campus and Whitemarsh's current millage rate. Masonic Homes paid Whitemarsh $ 45,230 and $ 44,890 under these two agreements for the years ended December 31, 2012 and 2011, respectively.

During the year ended December 31, 2012, Masonic Homes negotiated an agreement with Dallas Township, Dallas Area School District, and Luzerne County for annual payments in lieu of taxes for certain tax-exempt properties at Masonic Homes' Dallas campus. This agreement became effective retroactive to 2011 and will expire December 31, 2030. The agreement includes a specific payment schedule for lieu of tax payments to Dallas Township, Dallas Area School District, and Luzerne County for the 20-year term of the agreement. The agreement also includes provisions for an annual contribution from Masonic Homes to Dallas Township to support the local fire and ambulance organizations. Masonic Homes paid $ 26,814 under this agreement for the year ended December 31, 2012. For the year ending December 31, 2013, Masonic Homes' commitment under the agreement is approximately $ 34,000.

NOTE 26: Commitments and Contingencies – Continued

Masonic Homes entered into an agreement to invest the debt service reserve fund for the 2006 Bonds in November 2006. This agreement is a Debt Service Reserve Guaranteed Investment Contract with Bank of America, NA. This agreement requires Masonic Homes to invest $ 2,524,015, which is on deposit in the 2006 Bonds' Debt Service Reserve Fund, with Bank of America, NA. The money invested pursuant to this agreement earns interest at a rate of 5.23% through the maturity of the contract on November 1, 2036. The investments that collateralize the debt service reserve fund are held in custody of US Bank for the benefit of Masonic Homes, beginning on January 9, 2012.

On February 28, 1997, Masonic Homes entered an Agreement of Remediation (Agreement) with Waste Management Disposal Services of Pennsylvania, Inc. (Waste Management). The Agreement concerns remediation of an inactive landfill site adjacent to the Masonic Homes campus. A Masonic Homes secondary well was contaminated with manganese believed to have been caused by the inactive landfill site. Under the Agreement, Waste Management will pay Masonic Homes a total of $ 300,000 for costs to be incurred by Masonic Homes during the remediation process. It is anticipated the remediation process may require thirty years to complete. In April 1997, Masonic Homes received a payment totaling $ 150,000 to be used for costs incurred during the first fifteen years of the remediation process. This payment has been recorded as deferred revenue and is amortized, using the straight-line method, as a reduction of the related operating expenses incurred by Masonic Homes. An additional payment of $ 75,000 was received by Masonic Homes in 1998, to be used for costs incurred during the second fifteen years of the remediation process. Waste Management also agreed to reimburse Masonic Homes for the cost of drilling a new well. Two new wells were installed in 2000 to replace the existing water supply and the costs associated with installation were reimbursed by Waste Management.

NOTE 27: Risk

Financial instruments which subject the Masonic Homes to concentrations of credit risk consist primarily of cash and cash equivalents, short-term investments (i.e. certificates of deposit), fixed income securities, common stocks, and resident accounts receivable.

Masonic Homes typically maintains cash and cash equivalents which, at times, exceed $ 250,000, in banks. Cash and cash equivalents and certain short-term investments are insured by the Federal Deposit Insurance Corporation up to a limit of $ 250,000 per bank. Fixed income securities and common stocks are uninsured.

Masonic Homes grants credit to its residents and other third-party payors, primarily Medicare, Medical Assistance, and various commercial insurance companies. Masonic Homes maintains reserves for potential credit losses and such losses have historically been within management's expectations.

Masonic Homes' investments are exposed to various risks, such as interest rate, market, currency, and credit risks. Due to the level of risk associated with certain investments and the level of uncertainty related to changes in the value of investments, it is at least reasonably possible that changes in risks in the near term would materially affect investment assets reported in the financial statements.

NOTE 28: Reclassifications

Certain items in the 2011 financial statements have been reclassified to conform to the 2012 presentation.