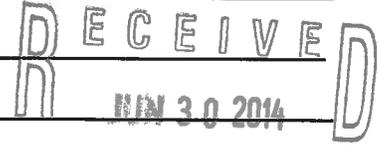


ANNUAL REPORT CHECKLIST

PROVIDER(S): Channing House

CCRC(S): Channing House, 850 Webster Street, Palo Alto CA 94301



CONTACT PERSON: Rhonda Bekkedahl

TELEPHONE NO.: (650) 327-0950

EMAIL: rbekkedahl@channinghouse.org

CONTINUING CARE
CONTRACTS BRANCH

A complete annual report must consist of 3 copies of all of the following:

- Annual Report Checklist.
- Annual Provider Fee in the amount of: \$ 10,613.09
 - If applicable, late fee in the amount of: \$ _____
- Certification by the provider's **Chief Executive Officer** that:
 - The reports are correct to the best of his/her knowledge.
 - Each continuing care contract form in use or offered to new residents has been approved by the Department.
 - The provider is maintaining the required *liquid* reserves and, when applicable, the required refund reserve.
- Evidence of the provider's fidelity bond, as required by H&SC section 1789.8.
- Provider's audited financial statements, with an accompanying certified public accountant's opinion thereon.
- Provider's audited reserve reports (prepared on Department forms), with an accompanying certified public accountant's opinion thereon.
- Provider's "Continuing Care Retirement Community Disclosure Statement" and Form 7-1 "Report on CCRC Monthly Service Fees" for **each** community.
- Provider's Refund Reserve Calculation(s) – Form 9-1 and/or Form 9-2, if applicable.

The Key Indicators Report is required to be submitted within 30 days of the due date of the submission of the annual report, but may be submitted at the same time as the annual report.

FORM 1-1
RESIDENT POPULATION

| <u>Line</u> | <u>Continuing Care Residents</u> | <u>TOTAL</u> |
|----------------------|---|--------------|
| [1] | Number at beginning of fiscal year | 233 |
| [2] | Number at end of fiscal year | 235 |
| [3] | Total Lines 1 and 2 | 468 |
| [4] | Multiply Line 3 by “.50” and enter result on Line 5. | x .50 |
| [5] | Mean number of continuing care residents | 234 |
| All Residents | | |
| [6] | Number at beginning of fiscal year | 233 |
| [7] | Number at end of fiscal year | 235 |
| [8] | Total Lines 6 and 7 | 468 |
| [9] | Multiply Line 8 by “.50” and enter result on Line 10. | x .50 |
| [10] | Mean number of <i>all</i> residents | 234 |
| [11] | Divide the mean number of continuing care residents (Line 5) by the mean number of <i>all</i> residents (Line 10) and enter the result (round to two decimal places). | 1.00 |

FORM 1-2
ANNUAL PROVIDER FEE

| <u>Line</u> | <u>ANNUAL PROVIDER FEE</u> | <u>TOTAL</u> |
|-------------|--|---------------------|
| [1] | Total Operating Expenses (including depreciation and debt service – interest only) | 12,858,809 |
| [a] | Depreciation | 2,245,724 |
| [b] | Debt Service (Interest Only) | |
| [2] | Subtotal (add Line 1a and 1b) | 2,245,724 |
| [3] | Subtract Line 2 from Line 1 and enter result. | 10,613,085 |
| [4] | Percentage allocated to continuing care residents (Form 1-1, Line 11) | 100% |
| [5] | Total Operating Expense for Continuing Care Residents (multiply Line 3 by Line 4) | 10,613,085 |
| [6] | Total Amount Due (multiply Line 5 by .001) | x .001 10,613.09 |

PROVIDER: Channing House
COMMUNITY: Channing House



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CONTINUING CARE
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June 27, 2014

Ms. Alison Nakatomi
Continuing Care Contracts Branch
Department of Social Services
744 P Street, MS 10-90
Sacramento, CA 95814

Re: Channing House Annual Reserve Report and Certification

Dear Ms. Nakatomi:

Attached for your review are our Annual Reserve Report Forms 5-1 through 5-5, Disclosure Statements, Fidelity Bond, Audited Financial Statements for FY 2014 as well as Key Indicators and Form 7-1.

Included in the Key Indicators are budget figures incorporating the current construction of 1) a replacement health care facility and 2) additional apartments. Our construction plans include reducing the current size of our health center from 69 beds to 53 beds, while adding 14 new apartments. Construction began in FY 2011 with completion of the new health center and additional apartments by FY 2016.

I certify that 1) this report and all attachments are correct to the best of my knowledge, 2) all contract forms in current use have been approved by the Department of Social Services, and 3) that Channing House continues to maintain the liquid reserves required by state statute.

This report will be filed in the Channing House library for resident review.

If you have any questions, please contact Rhonda Bekkedahl, our Director of Finance, or me.

Sincerely,

Melvin Matsumoto
Executive Director

Enclosures



ADDITIONAL REMARKS SCHEDULE

| | | | |
|--|-----------------------------|--------------------------|--|
| AGENCY Heffernan Insurance Brokers | | License # 0564249 | NAMED INSURED Channing House |
| POLICY NUMBER SEE PAGE 1 | | | 850 Webster Street |
| CARRIER SEE PAGE 1 | NAIC CODE SEE P 1 | | Palo Alto, CA 94301 |
| | | | EFFECTIVE DATE: SEE PAGE 1 |

ADDITIONAL REMARKS

THIS ADDITIONAL REMARKS FORM IS A SCHEDULE TO ACORD FORM,
 FORM NUMBER: ACORD 25 FORM TITLE: Certificate of Liability Insurance

Remarks:

**D&O and EPL SHARED LIMITS OF LIABILITY
 DIRECTORS & OFFICERS:**
 Limits of Liability
 Policy Per Claim Limit \$5,000,000
 Policy Aggregate Limit of Liability \$5,000,000
 Dedicated Excess Coverage for all Insured Persons \$1,000,000

Retention
 Each and every Claim (not applicable to Insuring Agreement A, D, E, G and H) \$50,000
 Each and every Antitrust Claim under Insuring Agreement D \$100,000
 Each and every Regulatory Claim under Insuring Agreement E \$250,000



EVIDENCE OF PROPERTY INSURANCE

DATE (MM/DD/YYYY)
6/18/2014

THIS EVIDENCE OF PROPERTY INSURANCE IS ISSUED AS A MATTER OF INFORMATION ONLY AND CONFERS NO RIGHTS UPON THE ADDITIONAL INTEREST NAMED BELOW. THIS EVIDENCE DOES NOT AFFIRMATIVELY OR NEGATIVELY AMEND, EXTEND OR ALTER THE COVERAGE AFFORDED BY THE POLICIES BELOW. THIS EVIDENCE OF INSURANCE DOES NOT CONSTITUTE A CONTRACT BETWEEN THE ISSUING INSURER(S), AUTHORIZED REPRESENTATIVE OR PRODUCER, AND THE ADDITIONAL INTEREST.

| | | | |
|--|--|--|---|
| AGENCY Heffernan Insurance Brokers P.O. Box 5608 Walnut Creek, CA 94596 | PHONE (A/C, No, Ext): 1 (925) 934-8500 | COMPANY Affiliated FM Insurance Company 1333 North California Boulevard, Suite 200 Walnut Creek, CA 94596 | CONTINUING CARE CONTRACTS BRANCH |
| FAX (A/C, No): 1 (925) 934-8278 | E-MAIL ADDRESS: | | |
| CODE: | SUB CODE: | | |
| AGENCY CUSTOMER ID #: | License # 0564249 | | |
| INSURED Channing House 850 Webster Street Palo Alto, CA 94301 | LOAN NUMBER | POLICY NUMBER SF444 | |
| | EFFECTIVE DATE 10/6/2013 | EXPIRATION DATE 10/6/2014 | <input type="checkbox"/> CONTINUED UNTIL TERMINATED IF CHECKED |
| THIS REPLACES PRIOR EVIDENCE DATED: | | | |

PROPERTY INFORMATION

LOCATION/DESCRIPTION
 Loc # 1, Bldg # 1, 850 Webster Street, Palo Alto, CA 94301, Independent & Assisted Living, Skilled Nursing
 EXTRA EXPENSE: \$5MM or 15% of Business Interruption values, whichever is greater
 EARTHQUAKE SPRINKLER LEAKAGE: POLICY LIMIT
 BOILER & MACHINERY: INCLUDED
 FUNGUS, MOLD OR MILDEW: \$1,000,000

THE POLICIES OF INSURANCE LISTED BELOW HAVE BEEN ISSUED TO THE INSURED NAMED ABOVE FOR THE POLICY PERIOD INDICATED. NOTWITHSTANDING ANY REQUIREMENT, TERM OR CONDITION OF ANY CONTRACT OR OTHER DOCUMENT WITH RESPECT TO WHICH THIS EVIDENCE OF PROPERTY INSURANCE MAY BE ISSUED OR MAY PERTAIN, THE INSURANCE AFFORDED BY THE POLICIES DESCRIBED HEREIN IS SUBJECT TO ALL THE TERMS, EXCLUSIONS AND CONDITIONS OF SUCH POLICIES. LIMITS SHOWN MAY HAVE BEEN REDUCED BY PAID CLAIMS.

COVERAGE INFORMATION

| COVERAGE / PERILS / FORMS | AMOUNT OF INSURANCE | DEDUCTIBLE |
|---|---------------------|------------|
| Loc # 1, Bldg # 1 ALL RISKS OF DIRECT PHYSICAL LOSS OR DAMAGE AS DEFINED AND LIMITED HEREIN, ON REAL PROPERTY, BUSINESS PERSONAL PROPERTY, BUSINESS INTERRUPTION, SUBJECT TO TERMS, LIMITATIONS, CONDITIONS, EXCLUSIONS, ETC. - POLICY LOSS LIMIT: | 202,434,000 | 10,000 |
| EXTRA EXPENSE: \$5MM or 15% of Business Interruption values, whichever is greater | 5,000,000 | |
| EARTHQUAKE SPRINKLER LEAKAGE: POLICY LIMIT (excludes flood and earthquake) | | 10,000 |
| BOILER & MACHINERY: INCLUDED | | |
| FUNGUS, MOLD OR MILDEW: | 1,000,000 | |

REMARKS (Including Special Conditions)

Special Conditions:
For Evidence of Insurance Only

CANCELLATION

SHOULD ANY OF THE ABOVE DESCRIBED POLICIES BE CANCELLED BEFORE THE EXPIRATION DATE THEREOF, NOTICE WILL BE DELIVERED IN ACCORDANCE WITH THE POLICY PROVISIONS.

ADDITIONAL INTEREST

| | | |
|------------------|-------------------------------|--------------------|
| NAME AND ADDRESS | MORTGAGEE | ADDITIONAL INSURED |
| | LOSS PAYEE | |
| | LOAN # | |
| | AUTHORIZED REPRESENTATIVE | |

EVIDENCE ONLY

SURETY BOND

(Original sent to Regional Office)



Applicant/Licensee Name: Channing House

CONTINUING CARE
CONTRACTS BRANCH

Address: 850 Webster Street, Palo Alto, CA 94301

Bonding Company: Hartford Fire Insurance Company

Address: One Hartford Plaza, Hartford, CT 06155 Telephone #: _____

Local Agent Name: HEFFERNAN INSURANCE BROKERS Telephone #: 925-934-8500

The addresses shown above for licensee and bonding company will be used for service of notices, papers, and other documents.

BE IT KNOWN THAT:

Licensee, as Principal, and Bonding Company, as Surety, are held and firmly bound to the State of California, as beneficiary, in the amount of \$ 5,000 (Five Thousand) for the payment of which the principal and surety bind themselves, their respective heirs, successors and assigns, jointly and severally.

WHEREAS Health and Safety Code sections 1560, 1568.021, and 1569.60 each require certain applicants for licenses to file with the State Department of Social Services a surety bond; and

WHEREAS the licensee has applied to operate an (check all that apply):

- Adult Residential, Adult Day Programs or Social Rehabilitation Facility, and the licensee handles client/resident funds in any amount; or
- Foster Family Home, Foster Family Agency, Group Home, Small Family Home, Residential Care Facility for Persons with Chronic, Life-Threatening Illness, or Residential Care Facility for the Elderly, and the licensee handles funds of \$50 or more per client/resident or \$500 or more for all clients/ residents in any month;

NOW, THEREFORE, the surety is liable on this bond in the event that the principal fails to handle faithfully and honestly the money of facility clients/residents.

The facility covered by this bond is:

Facility Name: Channing House

Facility Address: 850 Webster St Palo Alto, CA 94301

Facility License Number (if facility is currently licensed): 430700136

(if other facilities are covered by this bond, specify on a separate, attached page the name, address, facility license number, and bond amount for each facility.)

Every person injured as a result of any unfaithful or dishonest handling of client money may bring an action in a proper court on the bond for the amount of damage suffered thereby to the extent covered by the bond.

The aggregate liability of the Surety for all claims against this bond shall not exceed the amount of the bond, shown above.

This bond may be canceled by the Surety in accordance with Code of Civil Procedure section 996.030, and notice of cancellation must be sent in accordance with Code of Civil Procedure section 996.320. This bond is effective May 1, 2014 and remains in effect as long as the license is valid.

I certify under penalty of perjury under the laws of the State of California that the information provided on this page and on any attachments is true and correct.

BONDING COMPANY SIGNATURE:

David G. Harris, Attorney-in-fact

BOND NUMBER:

57BSBG3127

DATE:

05/20/2014

POWER OF ATTORNEY

Direct Inquiries/Claims to:

THE HARTFORD

Bond T-4

One Hartford Plaza

Hartford, Connecticut 06155

call: 888-266-3488 or fax: 860-757-5835

KNOW ALL PERSONS BY THESE PRESENTS THAT:

Agency Code: 57 100101

- Hartford Fire Insurance Company, a corporation duly organized under the laws of the State of Connecticut
- Hartford Casualty Insurance Company, a corporation duly organized under the laws of the State of Indiana
- Hartford Accident and Indemnity Company, a corporation duly organized under the laws of the State of Connecticut
- Hartford Underwriters Insurance Company, a corporation duly organized under the laws of the State of Connecticut
- Twin City Fire Insurance Company, a corporation duly organized under the laws of the State of Indiana
- Hartford Insurance Company of Illinois, a corporation duly organized under the laws of the State of Illinois
- Hartford Insurance Company of the Midwest, a corporation duly organized under the laws of the State of Indiana
- Hartford Insurance Company of the Southeast, a corporation duly organized under the laws of the State of Florida

having their home office in Hartford, Connecticut (hereinafter collectively referred to as the "Companies") do hereby make, constitute and appoint, up to the amount of UNLIMITED :

F. MICHAEL HEFFERNAN, STEPHANIE WORDEN, KIMBERLEY ROMAN, DAVID G. HARRIS, HEATHER PATE, JULIA PITTA OF WALNUT CREEK, CALIFORNIA

their true and lawful Attorney(s)-in-Fact, each in their separate capacity if more than one is named above, to sign its name as surety(ies) only as delineated above by , and to execute, seal and acknowledge any and all bonds, undertakings, contracts and other written instruments in the nature thereof, on behalf of the Companies in their business of guaranteeing the fidelity of persons, guaranteeing the performance of contracts and executing or guaranteeing bonds and undertakings required or permitted in any actions or proceedings allowed by law.

In Witness Whereof, and as authorized by a Resolution of the Board of Directors of the Companies on August 1, 2009, the Companies have caused these presents to be signed by its Vice President and its corporate seals to be hereto affixed, duly attested by its Assistant Secretary. Further, pursuant to Resolution of the Board of Directors of the Companies, the Companies hereby unambiguously affirm that they are and will be bound by any mechanically applied signatures applied to this Power of Attorney.



Wesley W. Cowling

Wesley W. Cowling, Assistant Secretary

M. Ross Fisher

M. Ross Fisher, Vice President

STATE OF CONNECTICUT

COUNTY OF HARTFORD

} ss. Hartford

On this 12th day of July, 2012, before me personally came M. Ross Fisher, to me known, who being by me duly sworn, did depose and say: that he resides in the County of Hartford, State of Connecticut; that he is the Vice President of the Companies, the corporations described in and which executed the above instrument; that he knows the seals of the said corporations; that the seals affixed to the said instrument are such corporate seals; that they were so affixed by authority of the Boards of Directors of said corporations and that he signed his name thereto by like authority.



CERTIFICATE

Kathleen T. Maynard

Kathleen T. Maynard
Notary Public

My Commission Expires July 31, 2016

I, the undersigned, Vice President of the Companies, DO HEREBY CERTIFY that the above and foregoing is a true and correct copy of the Power of Attorney executed by said Companies, which is still in full force effective as of May 20, 2014
Signed and sealed at the City of Hartford.



Gary W. Stumper

Gary W. Stumper, Vice President

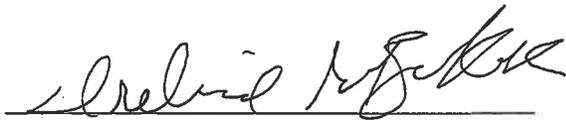
CALIFORNIA ALL-PURPOSE ACKNOWLEDGMENT

State of California)
) ss.
County of Contra Costa)

On May 20, 2014 before me, Irelind Marie Baker, a Notary Public, personally appeared David G. Harris who proved to me on the basis of satisfactory evidence to be the person(s) whose name(s) is/are subscribed to the within instrument and acknowledged to me that he/~~she~~/~~they~~ executed the same in his/~~her~~/~~their~~ authorized capacity(ies), and that by his/~~her~~/~~their~~ signature(s) on the instrument the person(s), or the entity upon behalf of which the person(s) acted, executed the instrument.

I certify under PENALTY OF PERJURY under the laws of the State of California that the foregoing is true and correct.

WITNESS my hand and official seal.


(Signature) Irelind Marie Baker, Notary Public

[SEAL]



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JUN 30 2014

CONTINUING CARE
CONTRACTS BRANCH

Report of Independent Auditors and
Financial Statements



February 28, 2014 and 2013

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JUN 30 2014
CONTINUING CARE
CONTRACTS BRANCH

REPORT OF INDEPENDENT AUDITORS

Board of Trustees
Channing House (a Nonprofit Corporation)
Palo Alto, California

Report on Financial Statements

We have audited the accompanying financial statements of Channing House, which comprise the statements of financial position as of February 28, 2014 and 2013, and the related statements of activities and changes in net assets, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. 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 financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Channing House as of February 28, 2014 and 2013, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.



San Francisco, California
June 5, 2014

FINANCIAL STATEMENTS

CHANNING HOUSE
STATEMENTS OF FINANCIAL POSITION
February 28, 2014 and 2013

| | <u>2014</u> | <u>2013</u> |
|---|-----------------------|-----------------------|
| ASSETS | | |
| Cash and cash equivalents | \$ 1,507,650 | \$ 1,008,358 |
| Accounts receivable | 8,972 | 34,839 |
| Notes receivable | - | 365,485 |
| Inventory | 2,625 | 3,390 |
| Prepaid expenses | 187,258 | 184,805 |
| Investments, at fair value | 20,112,469 | 18,365,064 |
| Assets limited as to use, at fair value | 18,896,891 | 24,394,745 |
| Property and equipment, net | 75,917,302 | 67,967,094 |
| Debt issuance costs, net | 3,613,689 | 3,750,917 |
| | <u>\$ 120,246,856</u> | <u>\$ 116,074,697</u> |
| Total assets | | |
| LIABILITIES AND NET ASSETS | | |
| Liabilities | | |
| Accounts payable and accrued expenses | \$ 3,597,451 | \$ 3,525,946 |
| Liabilities from split interest gifts | 54,215 | 62,977 |
| Deferred revenue from entrance fees | 26,652,023 | 24,124,685 |
| Refundable deposits | 759,220 | 740,038 |
| Debt | 61,778,125 | 62,383,769 |
| | <u>92,841,034</u> | <u>90,837,415</u> |
| Total liabilities | | |
| Net assets | | |
| Unrestricted | | |
| Undesignated | 25,540,550 | 23,529,222 |
| Board designated | 1,061,075 | 974,059 |
| Temporarily restricted | 804,197 | 734,001 |
| | <u>27,405,822</u> | <u>25,237,282</u> |
| Total net assets | | |
| Total liabilities and net assets | <u>\$ 120,246,856</u> | <u>\$ 116,074,697</u> |

See accompanying notes.

CHANNING HOUSE
STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS
Years Ended February 28, 2014 and 2013

| | 2014 | 2013 |
|---|---------------|---------------|
| REVENUES, GAINS, AND OTHER SUPPORT | | |
| Monthly care fees | \$ 9,955,719 | \$ 9,460,601 |
| Resident entrance fees earned | 3,968,662 | 3,714,333 |
| Interest on escrow funds | 157,402 | 643,530 |
| Interest and dividend income | 414,110 | 620,443 |
| Other services | 377,032 | 465,784 |
| Donations and other | 41,618 | 261,412 |
| Net realized loss on abandonment of property and equipment | (173,885) | (17,828) |
| Operating revenues | 14,740,658 | 15,148,275 |
| Net assets released from restriction for operations | 48,624 | 40,268 |
| Total revenues | 14,789,282 | 15,188,543 |
| EXPENSES | | |
| Medical | 2,755,196 | 2,775,775 |
| Food services | 2,521,352 | 2,441,194 |
| Operating and maintenance | 1,884,443 | 1,663,190 |
| Administrative | 2,413,728 | 1,963,616 |
| Housekeeping | 881,782 | 840,720 |
| Depreciation and amortization | 2,402,308 | 2,304,383 |
| Total expenses | 12,858,809 | 11,988,878 |
| INCOME BEFORE INVESTMENT INCOME (LOSS) AND UNREALIZED GAINS ON INVESTMENTS | 1,930,473 | 3,199,665 |
| INVESTMENT INCOME (LOSS) | | |
| Net realized income (loss) on investments | 27,325 | (521,000) |
| Total investment loss | 27,325 | (521,000) |
| NET INCOME | 1,957,798 | 2,678,665 |
| Net unrealized gain on investments | 91,452 | 663,240 |
| Change in value of split interest gifts | (1,970) | (1,672) |
| Increase (decrease) in unrecognized pension obligation | 51,064 | (23,538) |
| Net increase in unrestricted net assets | 2,098,344 | 3,316,695 |
| Temporarily restricted | | |
| Donation | 30,750 | 37,510 |
| Other | 88,070 | - |
| Total temporarily restricted revenues | 118,820 | 37,510 |
| Net assets released from restriction for operations | (48,624) | (40,268) |
| Net increase/(decrease) in temporarily restricted net assets | 70,196 | (2,758) |
| Change in net assets | 2,168,540 | 3,313,937 |
| NET ASSETS | | |
| Beginning of year | 25,237,282 | 21,923,345 |
| End of year | \$ 27,405,822 | \$ 25,237,282 |

See accompanying notes.

CHANNING HOUSE
STATEMENTS OF CASH FLOWS
Years Ended February 28, 2014 and 2013

| | <u>2014</u> | <u>2013</u> |
|---|---------------------|---------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Monthly care fees | \$ 9,981,586 | \$ 9,429,429 |
| Entrance fee proceeds | 6,842,303 | 5,981,196 |
| Other receipts from operations | 377,032 | 465,784 |
| Investment income received | 571,512 | 1,263,973 |
| Donations and miscellaneous revenues | 72,368 | 298,922 |
| Cash paid to employees and suppliers | (10,206,514) | (8,759,488) |
| Interest paid, net of amount capitalized | 5,471 | - |
| Net cash from operating activities | <u>7,643,758</u> | <u>8,679,816</u> |
| CASH FLOWS (USED IN) FROM INVESTING ACTIVITIES | | |
| Realized gain (loss) on investments | (27,325) | 521,437 |
| Proceeds from sales of investments | 14,941,325 | 13,822,106 |
| Cost of purchases of investments | (11,072,099) | (9,328,383) |
| Purchases of property and equipment | (10,369,817) | (13,437,050) |
| Net cash (used in) investing activities | <u>(6,527,916)</u> | <u>(8,421,890)</u> |
| CASH FLOWS USED IN FINANCING ACTIVITIES | | |
| Payments on long-term debt | (625,000) | (605,000) |
| Entrance fee refunds | 19,182 | - |
| Split interest gifts | | |
| Payments to beneficiaries | (10,732) | (29,131) |
| Income reinvested | - | (1,672) |
| Net cash (used in) financing activities | <u>(616,550)</u> | <u>(635,803)</u> |
| NET CHANGE IN CASH AND CASH EQUIVALENTS | 499,292 | (377,877) |
| CASH AND CASH EQUIVALENTS, beginning of year | <u>1,008,358</u> | <u>1,386,235</u> |
| CASH AND CASH EQUIVALENTS, end of year | <u>\$ 1,507,650</u> | <u>\$ 1,008,358</u> |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Change in net assets | \$ 2,168,540 | \$ 3,313,937 |
| Adjustments to reconcile net assets to net cash from operating activities | | |
| Depreciation | 2,245,724 | 2,147,798 |
| Amortization of debt issuance costs | 137,228 | 137,229 |
| Amortization of bond discount | 19,356 | 19,356 |
| Amortization of deferred revenue from entrance fees | (3,968,662) | (3,714,333) |
| Change in fair value of split interest gifts | 1,970 | 1,672 |
| Unrealized (gain) on investments | (91,452) | (663,240) |
| Loss on abandonment of property and equipment | 173,885 | 17,828 |
| Proceeds from entrance fees | 6,476,818 | 5,981,196 |
| Changes in operating assets and liabilities | | |
| Accounts receivable | 25,867 | (31,172) |
| Notes receivable | 365,485 | - |
| Inventory | 765 | - |
| Prepaid expenses | (2,453) | (15,541) |
| Accounts payable and accrued liabilities | 71,505 | 757,048 |
| Refundable deposits | 19,182 | 728,038 |
| Net cash from operating activities | <u>\$ 7,643,758</u> | <u>\$ 8,679,816</u> |

See accompanying notes.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

History and organization – Channing House is a nonprofit public benefit corporation licensed by the State of California Department of Public Health and California Department of Social Services to provide housing, related facilities and health services for elderly persons. Channing House was incorporated in 1960 under the laws of the State of California. The facility it operates has 184 apartments, 48 assisted living beds, and 21 skilled nursing beds.

Upon entering Channing House, residents pay an entrance fee, which varies by resident depending upon the size and location of the apartment. Monthly care fees vary based on apartment size. Residents are provided housing, meals, and nursing care for their stays at Channing House. A decreasing portion of the entrance fee is refundable by cancellation or termination of the care agreement during the first six years of occupancy, subject to a 10% minimum retention by Channing House. Entrance fees subject to refund at February 28, 2014 and 2013, were \$14,941,475 and \$14,646,641, respectively.

Channing House is subject to statutory reserve requirements. At February 28, 2014 and 2013, Channing House's reserves, as calculated in accordance with the continuing care contract statutes of the California Health and Safety Code, were in excess of such requirements.

Channing House is exempt from property taxes; however, it makes an "in-lieu-of" payment to the City of Palo Alto based upon the assessed valuation of land, improvements, and unsecured property.

Net asset classifications – The accompanying financial statements have been prepared in accordance with the standards set forth in Financial Accounting Standards Board (the "FASB") Accounting Standards Codification (the "ASC") Topic 715, *Compensation – Retirement Benefits* and FASB ASC Topic 958, *Not-for-Profit Entities* and the guidelines set forth in the industry audit and accounting guide "*Health Care Organizations*" issued by the American Institute of Certified Public Accountants. Under these guidelines, contributions of cash and other assets are classified as one of the following three categories:

Unrestricted – Unconditional promises to give by donors without any use or time restrictions. Included within unrestricted are board designated funds of \$1,061,075 and \$974,059 at February 28, 2014 and 2013, respectively, subject to board approval. Of these totals, \$852,904 and \$782,511 at February 28, 2014 and 2013, respectively, provide funding for goods and services which enhance the well-being of residents. The balance, to provide on-going support for the charitable needs of Channing House and its residents, at February 28, 2014 and 2013, was \$208,171 and \$191,548, respectively. The Board of Trustees of Channing House is authorized to spend the income and appreciation of these funds as it shall deem reasonable, in order to further the mission and purpose of Channing House.

Temporarily restricted – Unconditional promises to give by donors that specify a specific use or the occurrence of a certain future event. Donor restrictions released in the year received are recorded as unrestricted contributions.

Permanently restricted – Represent net assets, subject to donor imposed stipulations that they be maintained by the organization in perpetuity. Channing House had no permanently restricted net assets as of February 28, 2014 and 2013. Contribution revenue is recognized in the appropriate net asset classification when the gift is unconditionally promised.

Cash and cash equivalents – Channing House considers all highly liquid investments purchased with an original maturity of 90 days or less to be cash equivalents. Cash equivalents will include restricted cash and cash designated for specific projects.

Concentration of credit risk – Financial instruments potentially subjecting Channing House to concentrations of credit risk consist primarily of bank demand deposits in excess of the Federal Deposit Insurance Corporation insurance thresholds and cash held in money market accounts in excess of the amounts insured by the U.S. Treasury insurance for money market funds. Demand deposits are placed with local financial institutions, and management has not experienced any loss related to these demand deposits in the past. Investment securities are exposed to various risks, such as interest rate, market, and credit risks. It is at least reasonably possible, given the level of risk associated with investment securities, that changes in the near term could materially affect the amount reported in the financial statements. The risk associated with the investments is mitigated through diversification.

Inventory – Inventory is stated at cost, which is determined on the first-in, first-out method of accounting. Inventory consisted of gift shop supplies as of February 28, 2014 and 2013.

CHANNING HOUSE

NOTES TO FINANCIAL STATEMENTS

Investments – Investments are carried at fair value based on quoted market prices. The cost of investments sold is determined on an average cost basis. Realized and unrealized gains and losses are included in unrestricted net assets as the investments are considered trading securities.

Assets limited as to use – Assets limited as to use consist of cash and investments that are restricted in its use by regulatory or other agreements. These accounts are primarily escrow funds in U.S. government securities, which were established pursuant to the trust agreement executed in connection with the issuance of the 2010 Revenue Bonds (see Note 4). Assets limited as to use are carried at fair value based on quoted market prices.

Accounts receivable – Channing House extends credit to its residents for the payment of the monthly care fee, since each resident is directly responsible to pay Channing House. Management asserts that collection of monthly care fees are not considered an issue; therefore no allowance for doubtful accounts has been recorded.

Property and equipment – Property and equipment are stated at cost. The cost basis includes any interest, finance charges, and other related costs capitalized during construction. Depreciation is based upon the straight-line method over the estimated useful lives of the various classes of property, which range from 3 to 50 years. Channing House records assets acquired by donation at the estimated fair-market value at the date of donation.

Asset impairment – Channing House periodically evaluates the carrying value of their long-lived assets for impairment. The evaluations address the estimated recoverability of the assets' carrying value, which is principally determined based on projected undiscounted cash flows generated by the underlying tangible assets. When the carrying value of an asset exceeds estimated recoverability, an asset impairment is recognized.

Liabilities from split interest gifts – In conjunction with certain giving arrangements, Channing House is required to pay a certain sum of money to the donor or a designated beneficiary, and consequently, a liability is reflected in obligations under annuity agreements in the accompanying statements of financial position.

Debt issuance costs – The cost of issuing Series 2010 Revenue Bonds (see Note 4) totaled \$4,116,861, and is being amortized using the straight line method over the term of the bond. Accumulated amortization was \$503,172 and \$365,944 for 2014 and 2013, respectively.

Resident entrance fees – Resident entrance fees are recorded as deferred revenue and are amortized on a straight-line basis over the actuarially determined life expectancy of the resident. There is only one type of contract in use in which the entrance fee is refundable by cancellation or termination of the care agreement during the first six years of occupancy, subject to a 10% minimum retention by Channing House. There are no re-occupancy requirements on the current contract. Channing House also offers a "Returnable Contract," whereby 80% of the entrance fee is refunded at move-out or termination of the contract, upon re-occupancy of the apartment. There were no such contracts entered into as of February 28, 2014.

Malpractice insurance coverage – Channing House is covered for malpractice insurance under an occurrence basis policy with coverage of \$1,000,000 each occurrence and \$3,000,000 in the aggregate. Accounting principles generally accepted in the United States of America require that a healthcare organization disclose the estimated costs of claims in the period of the incident, if it is reasonably possible that liabilities may be incurred and losses can be reasonably estimated. Management is unable to reasonably estimate the range of future costs, if any, of unasserted claims arising from incidents in current and prior periods. Management believes that any unreported liability will not have a material adverse effect on Channing House's financial position or results of operations.

Income taxes – Channing House has been granted tax-exempt status under Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the California Revenue and Taxation Code. Accordingly, no provision for income taxes is included in the financial statements. Channing House adopted the provisions of FASB ASC Topic 740-10, *Income Taxes*, relating to accounting for uncertain tax positions on March 1, 2008. They had no unrecognized tax benefits which would require an adjustment to the March 1, 2013, beginning balance of net assets and had no unrecognized tax benefits at February 28, 2014. Channing House files federal and California exempt organization returns. They are no longer subject to income tax examinations by taxing authorities for years before 2006 for its federal and 2005 for its state tax filings.

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

Fair value of financial instruments – Unless otherwise indicated, the fair value of all reported assets and liabilities that represent financial instruments approximate their carrying values. Channing House’s policy is to recognize transfers in and transfer out of Level 1 and Level 2 as of the end of the reporting period. Please see Note 8 for fair value hierarchy disclosures of investments and long-term debt.

New accounting pronouncements – In July 2012, the FASB issued ASU No. 2012-01, *Continuing Care Retirement Communities – Refundable Advance Fees* (“ASU 2012-01”) to clarify that an entity should classify an advance fee as deferred revenue when a continuing care retirement community has a resident contract that provides for payment of the refundable advance fee upon reoccupancy by a subsequent resident, which is limited to the proceeds of reoccupancy. Refundable advance fees that are contingent upon reoccupancy by a subsequent resident but are not limited to the proceeds of reoccupancy should be accounted for and reported as a liability. Channing House implemented this guidance in 2014. The adoption did not have a material impact on Channing House’s financial statements.

In October 2012, the FASB issued ASU No. 2012-05, *Classification of the Sale Proceeds of Donated Financial Assets in the Statement of Cash Flows* (“ASU 2012-05”) to classify cash receipts from the sale of donated financial assets consistently with cash donations received in the statement of cash flows if those cash receipts were from the sale of donated financial assets that upon receipt were directed without any NFP-imposed limitations for sale and were converted nearly immediately into cash. Accordingly, the cash receipts from the sale of those financial assets should be classified as cash inflows from operating activities, unless the donor restricted the use of the contributed resources to long-term purposes, in which case those cash receipts should be classified as cash flows from financing activities. Otherwise, cash receipts from the sale of donated financial assets should be classified as cash flows from investing activities by the NFP. The adoption of ASU 2012-05 is effective for Channing House beginning March 1, 2014. The adoption of ASU 2012-05 is not expected to have a material impact on Channing House’s financial statements.

Reclassifications – Certain 2013 amounts have been reclassified to conform to the 2014 presentation.

NOTE 2 – INVESTMENTS

Investments and assets limited as to use, at fair value, consisted of the following at February 28, 2014 and 2013, respectively:

| | 2014 | 2013 |
|----------------------------|---------------|---------------|
| U.S. government securities | \$ 18,896,891 | \$ 24,394,745 |
| Fixed income mutual funds | 15,963,332 | 15,932,392 |
| International stock funds | 381,273 | 336,691 |
| Large blend mutual funds | 2,580,590 | 2,034,676 |
| Equity mutual funds | 1,136,701 | - |
| Other | 50,573 | 61,305 |
| | \$ 39,009,360 | \$ 42,759,809 |

Investment securities include funds established pursuant to reserve requirements relating to split interest gifts of \$50,573 and \$65,305 at February 28, 2014 and 2013, respectively, as set forth by the State Insurance Commission.

Escrow funds are included in U.S. government securities. Such funds were established pursuant to the trust agreement executed in connection with the issuance of the 2010 Revenue Bonds (see Note 4). The escrow funds consisted of the following at February 28, 2014 and 2013, respectively:

| | 2014 | 2013 |
|----------------------------|---------------|---------------|
| Reserve account | \$ 4,206,409 | \$ 4,228,313 |
| Principal/interest account | 1,760,845 | 1,707,570 |
| Health center project fund | 12,929,637 | 18,458,862 |
| | \$ 18,896,891 | \$ 24,394,745 |

Channing House is required to maintain \$4,200,000 in the reserve account.

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NOTES TO FINANCIAL STATEMENTS

The following table shows the gross unrealized losses and fair value of investments with unrealized losses that are not deemed to be other than temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position:

| | Fair Value Below Cost as of February 28, 2014 | | | | Total | |
|----------------------------|---|-------------------|---------------------|-------------------|------------|-------------------|
| | Less than 12 Months | | 12 Months or Longer | | Fair Value | Unrealized Losses |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | | |
| U.S. Government securities | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - |

| | Fair Value Below Cost as of February 28, 2013 | | | | Total | |
|----------------------------|---|-------------------|---------------------|-------------------|---------------|-------------------|
| | Less than 12 Months | | 12 Months or Longer | | Fair Value | Unrealized Losses |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | | |
| U.S. Government securities | \$ 24,394,745 | \$ 68,378 | \$ - | \$ - | \$ 24,394,745 | \$ 68,378 |

The securities disclosed above have not met the criteria for recognition of other than temporary impairment under management's policy. For the years ended February 28, 2014 and 2013, no securities were determined to be other than temporarily impaired.

Additional disclosures about fair value measurement are included in Note 8.

NOTE 3 – PROPERTY AND EQUIPMENT

Property and equipment at February 28, 2014 and 2013, respectively:

| | 2014 | 2013 |
|-------------------------------|---------------|---------------|
| Land and improvements | \$ 1,506,496 | \$ 1,523,796 |
| Building and improvements | 53,388,734 | 52,771,720 |
| Equipment and furnishings | 5,975,122 | 5,496,093 |
| Construction in progress | 40,391,983 | 31,517,904 |
| Total | 101,262,335 | 91,309,513 |
| Less accumulated depreciation | (25,345,033) | (23,342,419) |
| Property and equipment, net | \$ 75,917,302 | \$ 67,967,094 |

Depreciation expense was \$2,245,724 and \$2,147,798 for 2014 and 2013, respectively.

NOTE 4 – LONG-TERM DEBT

In July 2010, Channing House issued \$64,020,000 of Insured Revenue Bonds ("Series 2010"), net of bond discount of \$577,847, which are due in varying annual principal installments through May 2040. Interest payments are made semi-annually. The stated interest ranges from 3.00% to 6.125% with an average coupon of 5.95%. Principal payments commenced in fiscal year ending February 29, 2012. Payment of the obligations is secured by gross revenues from the facility and is insured with the Office of Statewide Health Planning and Development of the State of California. Proceeds from the Series 2010 bond were used to refund Series 1999 Certificates of Participation, fund the construction of a new two-story health center, and remodel an existing floor with 14 new apartment units. Construction on the new health center building is estimated for completion in July 2014 and the 14 new apartments estimated for completion in March 2015. Interest payments are made semi-annually. Principal payments are made annually.

Channing House is subject to certain financial covenants related to its Series 2010 debt. Management represents that Channing House was in compliance with these covenants as of February 28, 2014 and 2013, respectively.

Capitalized interest expense was \$3,544,948 and \$3,563,572 for 2014 and 2013, respectively.

Maturities of the Series 2010 bond during each of the next five years and thereafter are as follows:

| <u>Year Ending February</u> | |
|-----------------------------|-----------------------------|
| 2015 | \$ 645,000 |
| 2016 | 680,000 |
| 2017 | 8,710,000 |
| 2018 | 1,070,000 |
| 2019 | 1,120,000 |
| Thereafter | <u>49,553,125</u> |
| Total | <u><u>\$ 61,778,125</u></u> |

NOTE 5 – PENSION PLAN

Channing House has a noncontributory defined benefit pension plan (the “Plan”) which covers all employees who had completed one year of service and who had attained the age of 21 as of December 31, 2001. Benefits are computed by a formula based upon years of service and the employee’s average compensation over the final five years of employment, subject to a minimum benefit. Channing House’s funding policy for the Plan is to contribute an amount for each plan year that is no less than the minimum amount required by law under ERISA and the Internal Revenue Code using the Unit Credit actuarial cost method. At Channing House’s discretion, additional amounts may be contributed in excess of the minimum required contribution. Total benefits and expenses paid amounted to \$373,494 and \$204,254, respectively, for the years ended February 28, 2014 and 2013.

The broad-based investment goals of the Plan are to: (1) at a minimum, preserve the inflation-adjustment value of the Pension assets after administrative costs and benefit payments; (2) prudently invest assets in high-quality, diversified manner; (3) achieve the optimal return possible within the specified risk parameters; (4) achieve the actuarial earnings assumptions; and (5) adhere to the established guidelines.

The following table sets forth the changes in benefit obligations, changes in plan assets and components of net periodic benefit costs for the pension plan for the years ended February 28, 2014 and 2013:

| | <u>2014</u> | <u>2013</u> |
|---|----------------------------|----------------------------|
| Change in benefit obligation: | | |
| Benefit obligation at beginning of year | \$ 1,900,940 | \$ 1,902,411 |
| Service cost | 23,448 | 23,467 |
| Interest cost | 115,217 | 119,683 |
| Liability (gain) / loss | (25,217) | 59,633 |
| Expenses and benefits paid | <u>(373,494)</u> | <u>(204,254)</u> |
| Benefit obligation at end of year | <u><u>\$ 1,640,894</u></u> | <u><u>\$ 1,900,940</u></u> |
| Change in plan assets: | | |
| Plan assets beginning of year | \$ 1,744,999 | \$ 1,727,975 |
| Employer contributions | 137,004 | 114,392 |
| Actual return | 100,529 | 106,886 |
| Expenses and benefits paid | <u>(373,494)</u> | <u>(204,254)</u> |
| Plan assets end of year | <u>1,609,038</u> | <u>1,744,999</u> |
| Funded status | (31,856) | (155,941) |
| Effect of adoption of FASB ASC Topic 715 | <u>578,155</u> | <u>629,219</u> |
| Prepaid pension cost | <u><u>\$ 546,299</u></u> | <u><u>\$ 473,278</u></u> |

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The net periodic pension expense included the following components for the years ended February 28, 2014 and 2013:

| | <u>2014</u> | <u>2013</u> |
|---|------------------|------------------|
| Service cost | \$ 23,448 | \$ 23,467 |
| Interest cost | 115,217 | 119,683 |
| Actual return on asset - gain | (100,529) | (106,886) |
| Amortization of net loss from earlier periods | 36,741 | 38,624 |
| Amortization of net gain (loss) during the period | <u>(10,894)</u> | <u>(2,529)</u> |
| Total | <u>\$ 63,983</u> | <u>\$ 72,359</u> |

The following weighted-average assumptions were used to determine the plan's benefit obligation at February 28, 2014 and 2013:

| | <u>2014</u> | <u>2013</u> |
|--------------------------------|-------------|-------------|
| Discount rates | 6.5% | 6.5% |
| Expected return on plan assets | 6.5% | 6.5% |

The composition of plan assets was as follows at February 28, 2014 and 2013:

| | <u>2014</u> | <u>2013</u> |
|-----------------------------------|-------------|-------------|
| Insurance company general account | 72% | 72% |
| Equity funds | 0% | 15% |
| Money market funds | <u>28%</u> | <u>13%</u> |
| Total | <u>100%</u> | <u>100%</u> |

The fair values of Channing House's pension plan assets by asset category were as follows at February 28, 2014 and 2013, pursuant to FASB ASC Topic 820 as more fully described in Note 8:

| | <u>Total 2014</u> | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
|--|---------------------|----------------|-------------------|---------------------|
| Investment contract with insurance company | \$ 1,159,550 | \$ - | \$ - | \$ 1,159,550 |
| Equity funds | 449,488 | - | 449,488 | - |
| Money market funds | - | - | - | - |
| Total investments | <u>\$ 1,609,038</u> | <u>\$ -</u> | <u>\$ 449,488</u> | <u>\$ 1,159,550</u> |
| | <u>Total 2013</u> | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
| Investment contract with insurance company | \$ 1,247,330 | \$ - | \$ - | \$ 1,247,330 |
| Equity funds | 265,253 | - | 265,253 | - |
| Money market funds | <u>232,416</u> | <u>-</u> | <u>232,416</u> | <u>-</u> |
| Total investments | <u>\$ 1,744,999</u> | <u>\$ -</u> | <u>\$ 497,669</u> | <u>\$ 1,247,330</u> |

The investment contract with insurance company is valued at contract value as estimated by the trustees. Contract value approximates fair value.

The following table reconciles the beginning and ending balances of recurring fair value measurements recognized in the accompanying financial statements using significant unobservable (Level 3) inputs:

| | Investment Contract with Insurance Company |
|---|---|
| Beginning balance at February 28, 2013 | \$ 1,247,330 |
| Actual return on plan assets: | |
| Relating to assets still held at the reporting date | 47,701 |
| Relating to assets sold during the period | - |
| Purchases, sales, and settlements | (135,481) |
| Transfers in and/or out of Level 3 | - |
| Ending balance at February 28, 2014 | \$ 1,159,550 |
| | |
| | Investment Contract with Insurance Company |
| Beginning balance at February 29, 2012 | \$ 1,279,688 |
| Actual return on plan assets: | |
| Relating to assets still held at the reporting date | 53,332 |
| Relating to assets sold during the period | - |
| Purchases, sales, and settlements | (85,690) |
| Transfers in and/or out of Level 3 | - |
| Ending balance at February 28, 2013 | \$ 1,247,330 |

The effect of the adoption of FASB ASC Topic 715, *Compensation - Retirement Benefits*, was to decrease the liability of the pension plan by \$124,085 in 2014 and decrease the liability by \$18,495 in 2013, which is included in Accrued Liabilities. There was also a corresponding increase to unrestricted net assets of \$51,064 in 2014 and decrease to unrestricted net assets of \$23,538 in 2013.

Estimated future benefit payments – Expected benefits to be paid in the next ten years as calculated by consulting the actuary are:

| Fiscal Year | Expected Payment |
|--------------------|-----------------------------|
| 2015 | \$ 176,000 |
| 2016 | \$ 184,900 |
| 2017 | \$ 195,100 |
| 2018 | \$ 207,700 |
| 2019 | \$ 216,600 |
| 2020-2023 | \$ 1,102,400 |

Plan amendment – At December 31, 2001, the Board of Trustees approved changes to the defined benefit pension plan that effectively froze the plan. No new participants are permitted into the plan and no future benefits will accrue for participants in the plan on or before December 31, 2001. The effect of the change was a curtailment gain of \$177,087, which reduced the projected benefit obligation in accordance with FASB ASC Topic 715, *Compensation - Retirement Benefits*. Also in accordance with FASB ASC Topic 715, the previously unrecognized prior service cost of \$17,581 was accelerated in prior years.

Defined contribution plan – Effective January 1, 2002, Channing House established a 403(b) plan for substantially all employees. Participants may contribute a percentage of compensation up to the maximum permitted by the Internal Revenue Code. Employer contributions and costs are based on a percentage of covered employees' salaries. Employer contributions were \$144,051 and \$136,993 for the years ended February 28, 2014 and 2013, respectively.

CHANNING HOUSE
NOTES TO FINANCIAL STATEMENTS

Deferred compensation plan – Effective November 1, 2008, Channing House established a 457(b) plan for key management staff. This plan is intended to constitute an unfunded, eligible deferred compensation plan as described in IRC Section 457(b). The Plan calls for discretionary contributions as approved each year by the Board of Trustees. Participants may contribute a percentage of compensation up to the maximum permitted by the Internal Revenue Code. Employer contributions were \$43,217 and \$38,922 for the year ended February 28, 2014 and 2013, respectively.

NOTE 6 – FUTURE SERVICE OBLIGATION

Channing House is obligated to provide its residents continuous care throughout the residents' stay at the facility. Management's estimate of the liability for "future service obligation" represents the excess of the discounted net care expenses over the deferred revenue from entrance fees. The obligation is discounted at 5% for both February 28, 2014 and 2013. The obligations were \$0 for both February 28, 2014 and 2013.

NOTE 7 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consisted of the following at February 28, 2014 and 2013:

| | <u>2014</u> | <u>2013</u> |
|-----------------------|-------------------|-------------------|
| Healthcare center | \$ 539,688 | \$ 479,051 |
| Residents' assistance | 264,509 | 254,950 |
| | <u>\$ 804,197</u> | <u>\$ 734,001</u> |

Temporarily restricted net assets were released for the following as of February 28, 2014 and 2013:

| | <u>2014</u> | <u>2013</u> |
|-----------------------|------------------|------------------|
| Residents' assistance | \$ 48,624 | \$ 40,268 |
| | <u>\$ 48,624</u> | <u>\$ 40,268</u> |

NOTE 8 – FAIR VALUE OF FINANCIAL INSTRUMENTS

FASB ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. FASB ASC Topic 820 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

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

Level 2 – Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in active markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; or net asset value per share (or its equivalent) with the ability to redeem the investments in the near term.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Following is a description of the valuation methodology used for instruments measured at fair value on a recurring basis and recognized in the accompanying financial statements, as well as the general classification of such instruments pursuant to the valuation hierarchy:

Investments: Fair values, which are the amounts reported in the statement of financial position, are based on quoted market prices, if available, or estimated using quoted market prices for similar securities.

The following table presents the fair value measurements of investments recognized in the accompanying financial statements measured at fair value on a recurring basis and the level within the FASB ASC Topic 820 fair value hierarchy in which the fair value measurements fall at February 28, 2014 and, 2013:

| | <u>Total 2014</u> | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
|----------------------------|----------------------|----------------------|----------------|----------------|
| U.S. Government securities | \$ 18,896,891 | \$ 18,896,891 | \$ - | \$ - |
| Fixed income mutual fund | 15,963,332 | 15,963,332 | - | - |
| International stock funds | 381,273 | 381,273 | - | - |
| Large blend mutual funds | 2,580,590 | 2,580,590 | - | - |
| Equity mutual funds | 1,136,701 | 1,136,701 | - | - |
| Charitable gift annuities | 50,573 | 50,573 | - | - |
| Total investments | \$ 39,009,360 | \$ 39,009,360 | \$ - | \$ - |

| | <u>Total 2013</u> | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
|----------------------------|----------------------|----------------------|----------------|----------------|
| U.S. Government securities | \$ 24,394,745 | \$ 24,394,745 | \$ - | \$ - |
| Fixed income mutual fund | 15,932,392 | 15,932,392 | - | - |
| International stock funds | 336,691 | 336,691 | - | - |
| Large blend mutual funds | 2,034,676 | 2,034,676 | - | - |
| Charitable gift annuities | 61,305 | 61,305 | - | - |
| Total investments | \$ 42,759,809 | \$ 42,759,809 | \$ - | \$ - |

As required by FASB ASC Topic 820, the investments are classified within the level of the lowest significant input considered in determining fair value. In evaluating the level at which Channing House's investments have been classified, Channing House has assessed factors including, but not limited to, the ability to redeem at net asset value ("NAV") at the measurement date and the existence or absence of certain restrictions at the measurement date. In accordance with this guidance, if Channing House has the ability to redeem from the investment at the measurement date or in the near-term at NAV, the investment would be classified as a Level 2 fair value measurement. Alternatively, if Channing House will never have the ability to redeem from the investment or is restricted from redeeming for an uncertain or extended period of time from the measurement date, the investment would be classified as a Level 3 fair value measurement.

Debt - The fair value of long-term debt is based on quoted market prices in an active market (Level 1).

The carrying amounts and fair values of Channing House's financial instruments at February 28, 2014 and 2013, were as follows:

| | <u>2014</u> | | <u>2013</u> | |
|---------------------------------------|------------------------|-------------------|------------------------|-------------------|
| | <u>Carrying Amount</u> | <u>Fair Value</u> | <u>Carrying Amount</u> | <u>Fair Value</u> |
| Cash and equivalents | \$ 1,507,650 | \$ 1,507,650 | \$ 1,008,358 | \$ 1,008,358 |
| Investments | \$ 20,112,469 | \$ 20,112,469 | \$ 18,365,064 | \$ 18,365,064 |
| Assets limited as to use | \$ 18,896,891 | \$ 18,896,891 | \$ 24,394,745 | \$ 24,394,745 |
| Accounts payable and accrued expenses | \$ 3,597,451 | \$ 3,597,451 | \$ 3,525,946 | \$ 3,525,946 |
| Liabilities from split interest gifts | \$ 54,215 | \$ 54,215 | \$ 62,977 | \$ 62,977 |
| Debt | \$ 61,778,125 | \$ 65,693,180 | \$ 62,383,769 | \$ 67,605,260 |

Considerable judgment is required to develop estimates of fair value, and the estimates presented are not necessarily indicative of the amounts that Channing House would realize in a current market exchange. The use of different market assumptions and/or estimation methods could have a material effect on the estimated fair values. The estimates presented are based on pertinent information available to management as of February 2014 and 2013. Current estimates of fair value may differ significantly from the amounts presented.

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NOTES TO FINANCIAL STATEMENTS

NOTE 9 – HEALTH AND SAFETY CODE SECTION 1790(A)(3) DISCLOSURE

The Board of Trustees of Channing House in 2010 established a Capital Reserve Fund to be used to pay for future board-approved capital improvements. These improvements are necessary and consistent with Channing House's tax exempt purpose to maintain and provide facilities essential to meet the housing, health care, and other needs of its elderly residents. The amount of this fund was \$5,931,000 and \$3,112,000 at February 28, 2014 and 2013, respectively.

Improvements made during the year included: a) Safety and security system upgrades of \$257,317; b) Apartment renovations of \$533,168; and c) Other Building Equipment & Furnishings of \$389,413.

In order to provide up-to-date health care facilities for Channing House's continuum of care, the Board of Trustees in 2010 issued \$64,020,000 of Insured Revenue Bonds. Consistent with Channing House's nonprofit status, the Bonds were necessary to improve facilities essential to their provision of housing, nursing care, and financial security to their aged residents. These bonds were used in the following manner: a) Withdrawals for construction costs of \$5,597,388 and \$7,748,237 for fiscal years ending February 28, 2014 and 2013, respectively; and b) the Bond Reserve Account was maintained and ended the years with a balance of \$4,206,409 and \$4,228,312 as of February 28, 2014 and 2013, respectively.

NOTE 10 – CONTINGENCIES

Litigation – Channing House is party to claims and legal actions in the normal course of business. In the opinion of management, and based on current facts and circumstances, the resolution of such matters is not expected to have a material adverse effect on the financial position of Channing House.

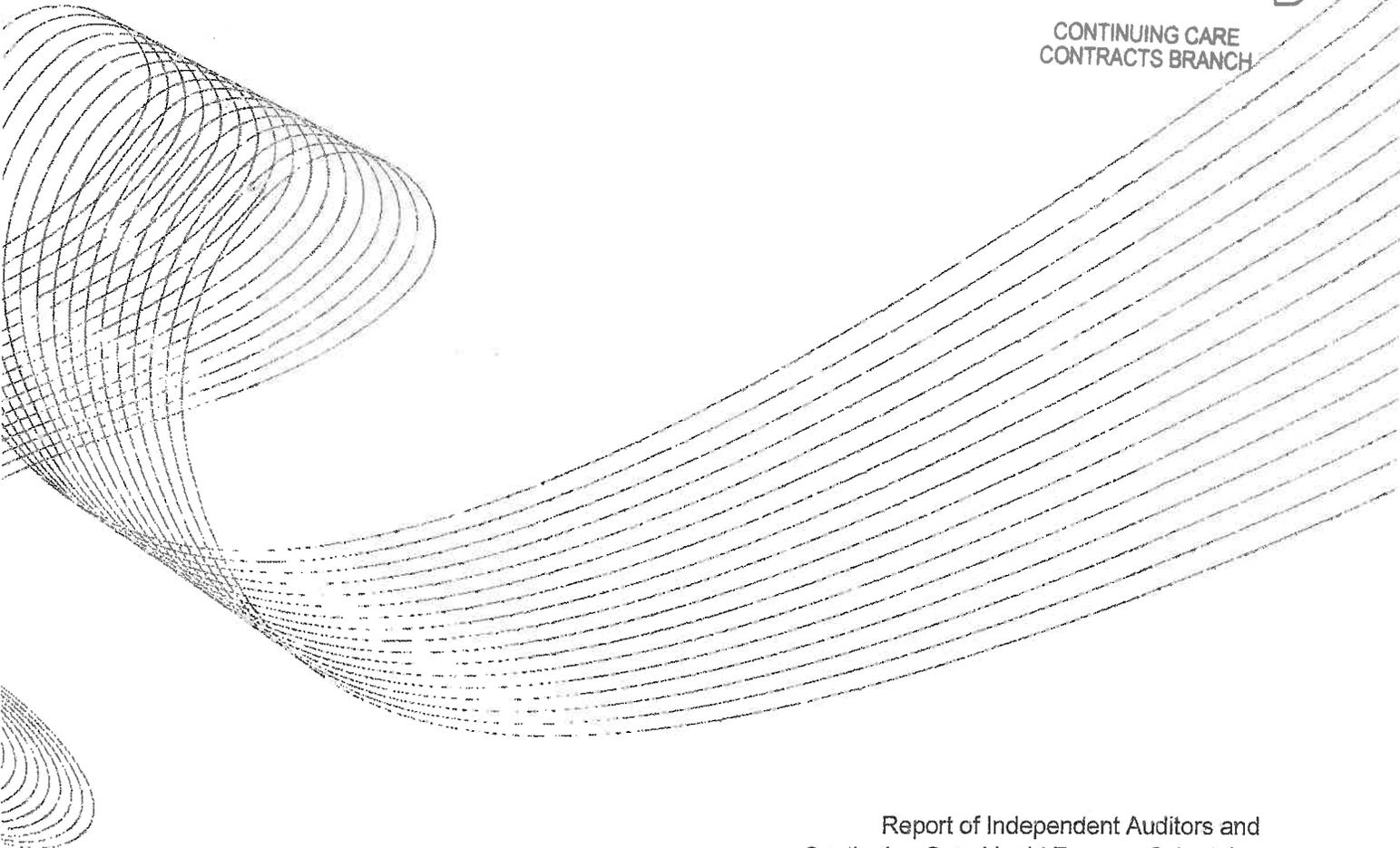
Health care reform – In March 2010, President Obama signed the Health Care Reform Legislation into law. The new law will result in sweeping changes across the health care industry. The primary goal of this comprehensive legislation is to extend coverage to approximately 32 million uninsured legal U.S. residents through a combination of public program expansion and private sector health insurance reforms. To fund the expansion of insurance coverage, the legislation contains measures designed to promote quality and cost efficiency in health care delivery and to generate budgetary savings in the Medicare and Medicaid programs. Channing House is unable to predict the full impact of the Health Care Reform Legislation at this time due to the law's complexity and current lack of implementing regulations or interpretive guidance. However, Channing House expects that provisions of the Health Care Reform Legislation will have some effect on its business.

NOTE 11 – SUBSEQUENT EVENTS

Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are available to be issued. Channing House recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing the financial statements. Channing House's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after the balance sheet date and before financial statements are available to be issued. Channing House will review effects of the Health Care Reform Legislation as discussed in Note 10 and disclose impacts accordingly.

Channing House has evaluated subsequent events through June 5, 2014, which is the date the financial statements were issued.

RECEIVED
JUN 30 2014
CONTINUING CARE
CONTRACTS BRANCH



Report of Independent Auditors and
Continuing Care Liquid Reserve Schedules

Channing House

As of and for the Year Ended February 28, 2014

MOSS ADAMS LLP

Certified Public Accountants | Business Consultants

Acumen. Agility. Answers.

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REPORT OF INDEPENDENT AUDITORS

To the Board of Trustees
 Channing House

Report on the Financial Statements

We have audited the accompanying financial statements of Channing House, which comprise the continuing care liquid reserve schedules, Form 5-1 through Form 5-5 as of and for the year ended February 28, 2014.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the liquid reserve requirements of California Health and Safety Code Section 1792. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the continuing care reserve of Channing House as of and for the year ended February 28, 2014, in conformity with the liquid reserve requirements of California Health and Safety Code Section 1792.

Basis of Accounting

We draw attention to the basis of accounting used to prepare the financial statements. The financial statements are prepared by Channing House on the basis of the liquid reserve requirements of California Health and Safety Code Section 1792, which is a basis of accounting other than accounting principles generally accepted in the United States of America, to meet the requirements of California Health and Safety Code Section 1792. Our opinion is not modified with respect to this matter.

Other Matter

Our audit was conducted for the purpose of forming an opinion on the financial statements, as a whole. The accompanying supplementary schedules of Attachment I to Form 5-5: Reconciliation of Investment Securities and Debt Service Reserve – State of California – Department of Social Services; Annual Report, Continuing Care Division Section 5-5 Additional Information (Board Designated Funds); and Supplementary Information – Statement of Cash Flows - Direct Method, presented as supplementary schedules, are presented for the purpose of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of financial statements, and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements, or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements, taken as a whole.

Restriction on Use

Our report is intended solely for the information and use of the Board of Trustees and management of Channing House and the California Department of Social Services and is not intended to be, and should not be, used by anyone other than these specified parties.

A handwritten signature in black ink that reads "Moss Adams LLP". The signature is written in a cursive, flowing style.

San Francisco, California
June 23, 2014

CHANNING HOUSE
FORM 5-1
LONG-TERM DEBT INCURRED IN A PRIOR FISCAL YEAR
(INCLUDING BALLOON DEBT)
For The Year Ended February 28, 2014

| FORM 5-1 LONG-TERM DEBT INCURRED IN A PRIOR FISCAL YEAR (Including Balloon Debt) | | | | | |
|---|----------------------|---|--|--|--|
| Long-Term Debt Obligation | (a) Date Incurred | (b) Principal Paid During Fiscal Year | (c) Interest Paid During Fiscal Year | (d) Credit Enhancement Premiums Paid in Fiscal Year | (e) Total Paid (columns (b) + (c) + (d)) |
| 1 | 07/01/10 | \$625,000 | \$3,544,948 ** | | \$4,169,948 |
| 2 | | | | | \$0 |
| 3 | | | | | \$0 |
| 4 | | | | | \$0 |
| 5 | | | | | \$0 |
| 6 | | | | | \$0 |
| 7 | | | | | \$0 |
| 8 | | | | | \$0 |
| TOTAL: | | \$625,000 | \$3,544,948 | \$0 | \$4,169,948 |

*(Transfer this amount to
Form 5-3, Line 1)*

NOTE: For column (b), do not include voluntary payments made to pay down principal.

** Capitalized interest, not included in total operating expenses on the financial statements

PROVIDER: Channing House

CHANNING HOUSE
FORM 5-2
LONG-TERM DEBT INCURRED DURING FISCAL YEAR
(INCLUDING BALLOON DEBT)
For The Year Ended February 28, 2014

| FORM 5-2 | | | | | |
|---|----------------------|---|--|---|--|
| LONG-TERM DEBT INCURRED DURING FISCAL YEAR (Including Balloon Debt) | | | | | |
| Long-Term Debt Obligation | (a) Date Incurred | (b) Total Interest Paid During Fiscal Year | (c) Amount of Most Recent Payment on the Debt | (d) Number of Payments over next 12 months | (e) Reserve Requirement (see instruction 5) (columns (c) x (d)) |
| 1 | | | | | \$0 |
| 2 | | | | | \$0 |
| 3 | | | | | \$0 |
| 4 | | | | | \$0 |
| 5 | | | | | \$0 |
| 6 | | | | | \$0 |
| 7 | | | | | \$0 |
| 8 | | | | | \$0 |
| TOTAL: | | \$0 | \$0 | 0 | \$0 |

(Transfer this amount to Form 5-3, Line 2)

NOTE: For column (b), do not include voluntary payments made to pay down principal.

PROVIDER: Channing House

CHANNING HOUSE
FORM 5-3
CALCULATION OF LONG-TERM DEBT RESERVE AMOUNT
For The Year Ended February 28, 2014

FORM 5-3
CALCULATION OF LONG-TERM DEBT RESERVE AMOUNT

| Line | | TOTAL |
|------|--|--------------------|
| 1 | Total from Form 5-1 bottom of Column (e) | \$4,169,948 |
| 2 | Total from Form 5-2 bottom of Column (e) | \$0 |
| 3 | Facility leasehold or rental payment paid by provider during fiscal year (including related payments such as lease insurance) | \$0 |
| 4 | TOTAL AMOUNT REQUIRED FOR LONG-TERM DEBT RESERVE: | \$4,169,948 |

PROVIDER: Channing House

CHANNING HOUSE
FORM 5-4
CALCULATION OF NET OPERATING EXPENSES
For The Year Ended February 28, 2014

FORM 5-4
CALCULATION OF NET OPERATING EXPENSES

| Line | Amounts | TOTAL |
|------|---|--------------|
| 1 | Total operating expenses from financial statements | \$12,858,809 |
| 2 | Deductions: | |
| | a. Interest paid on long-term debt (see instructions) | \$0 |
| | b. Credit enhancement premiums paid for long-term debt (see instructions) | \$0 |
| | c. Depreciation | \$2,245,724 |
| | d. Amortization | \$156,584 |
| | e. Revenues received during the fiscal year for services to persons who did not have a continuing care contract | \$0 |
| | f. Extraordinary expenses approved by the Department | \$0 |
| 3 | Total deductions | \$2,402,308 |
| 4 | Net operating expenses | \$10,456,501 |
| 5 | Divide line 4 by 365 and enter the result. | \$28,648 |
| 6 | Multiply line 5 by 75 and enter the result. This is the provider's operating expense reserve amount. | \$2,148,596 |

PROVIDER: Channing House

CHANNING HOUSE
FORM 5-5
ANNUAL RESERVE CERTIFICATION
For The Year Ended February 28, 2014

FORM 5-5
ANNUAL RESERVE CERTIFICATION

Provider Name: Channing House
 Fiscal Year Ended: 2/28/2014

We have reviewed our debt service reserve and operating expense reserve requirements as of, and for the period ended 2/28/2014 and are in compliance with those requirements.

Our liquid reserve requirements, computed using the audited financial statements for the fiscal year are as follows:

| | <u>Amount</u> |
|--------------------------------------|--------------------|
| [1] Debt Service Reserve Amount | <u>\$4,169,948</u> |
| [2] Operating Expense Reserve Amount | <u>\$2,148,596</u> |
| [3] Total Liquid Reserve Amount: | <u>\$6,318,544</u> |

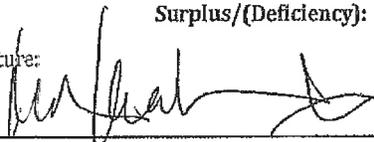
Qualifying assets sufficient to fulfill the above requirements are held as follows:

| <u>Qualifying Asset Description</u> | <u>Amount</u> (market value at end of quarter) | |
|--|---|--------------------------|
| | <u>Debt Service Reserve</u> | <u>Operating Reserve</u> |
| [4] Cash and Cash Equivalents | <u>\$0</u> | <u>\$1,507,650</u> |
| [5] Investment Securities | <u>\$0</u> | <u>\$20,061,896</u> |
| [6] Equity Securities | <u>\$0</u> | <u>\$0</u> |
| [7] Unused/Available Lines of Credit | <u>\$0</u> | <u>\$0</u> |
| [8] Unused/Available Letters of Credit | <u>\$0</u> | <u>\$0</u> |
| [9] Debt Service Reserve | <u>\$5,967,254</u> | (not applicable) |
| [10] Other: | <u>\$0</u> | <u>\$0</u> |

(describe qualifying asset)

| | | |
|--------------------------------|-------------------------|--------------------------|
| Listed for Reserve Obligation: | [11] <u>\$5,967,254</u> | [12] <u>\$21,569,546</u> |
| Reserve Obligation Amount: | [13] <u>\$4,169,948</u> | [14] <u>\$2,148,596</u> |
| Surplus/(Deficiency): | [15] <u>\$1,797,306</u> | [16] <u>\$19,420,950</u> |

Signature:



(Authorized Representative)

Date: 6-23-2014

Executive Director
 (Title)

SUPPLEMENTARY SCHEDULES



CHANNING HOUSE
ATTACHMENT I TO FORM 5-5
RECONCILIATION OF INVESTMENT SECURITIES AND DEBT SERVICE RESERVE
STATE OF CALIFORNIA - DEPARTMENT OF SOCIAL SERVICES
For The Year Ended February 28, 2014

#5 INVESTMENT SECURITIES

| | | |
|-----------------------------|----|-------------------|
| Fixed income mutual funds | \$ | 15,963,332 |
| International stock funds | | 381,273 |
| Equity mutual funds | | 1,136,701 |
| Large blend mutual funds | | 2,580,590 |
| Total investment securities | \$ | <u>20,061,896</u> |

#9 DEBT SERVICE RESERVE

| | | |
|----------------------------|----|------------------|
| Reserve account | \$ | 4,206,409 |
| Principal/interest account | | 1,760,845 |
| Total debt service reserve | \$ | <u>5,967,254</u> |

CHANNING HOUSE
ANNUAL REPORT, CONTINUING CARE DIVISION SECTION 5-5 ADDITIONAL INFORMATION (BOARD
DESIGNATED FUNDS)
For The Year Ended February 28, 2014

Annual Report, Continuing Care Contracts Division
Section 5-5
Channing House

ADDITIONAL INFORMATION

Board Designated Funds, as of February 28, 2014, include the following:

| | |
|---|---------------------|
| a. Heritage Circle Fund to enhance resident well-being | \$ 852,904 |
| b. Residents' Assistance Fund (for charity care of residents) | <u>208,171</u> |
| Total Board Designated Funds | <u>\$ 1,061,075</u> |

CHANNING HOUSE
SUPPLEMENTARY INFORMATION
STATEMENT OF CASH FLOWS - DIRECT METHOD
For The Year Ended February 28, 2014

| | |
|---|---------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | |
| Monthly care fees | \$ 9,981,586 |
| Entrance fees proceeds | 6,842,303 |
| Other receipts from operations | 377,032 |
| Investment income received | 571,512 |
| Donations and miscellaneous revenues | 72,368 |
| Cash paid to employees and suppliers | (10,206,514) |
| Interest paid, net of amount capitalized | 5,471 |
| | <hr/> |
| Net cash provided by operating activities | 7,643,758 |
| CASH FLOWS FROM INVESTING ACTIVITIES | |
| Realized loss on investments | (27,325) |
| Proceeds from sales of investments | 14,941,325 |
| Cost of purchases of investments | (11,072,099) |
| Purchases of property and equipment | (10,369,817) |
| | <hr/> |
| Net cash used in investing activities | (6,527,916) |
| CASH FLOWS FROM FINANCING ACTIVITIES | |
| Payments on long-term debt | (625,000) |
| Entrance fees refunds | 19,182 |
| Split interest gifts | |
| Payments to beneficiaries | (10,732) |
| | <hr/> |
| Net cash used in financing activities | (616,550) |
| NET CHANGE IN CASH AND CASH EQUIVALENTS | 499,292 |
| CASH AND CASH EQUIVALENTS, beginning of year | 1,008,358 |
| | <hr/> |
| CASH AND CASH EQUIVALENTS, end of year | \$ 1,507,650 |
| | <hr/> <hr/> |

CHANNING HOUSE
SUPPLEMENTARY INFORMATION
STATEMENT OF CASH FLOWS - DIRECT METHOD (continued)
For The Year Ended February 28, 2014

CASH FLOWS FROM OPERATING ACTIVITIES

| | |
|---|---------------------|
| Change in net assets | \$ 2,168,540 |
| Adjustments to reconcile net assets to net cash from operating activities | |
| Depreciation | 2,245,724 |
| Amortization of debt issuance costs | 137,228 |
| Amortization of bond discount | 19,356 |
| Amortization of deferred revenue from entrance fees | (3,968,662) |
| Change in fair value of split interest gifts | 1,970 |
| Unrealized gain on investments | (91,452) |
| Loss on abandonment of property and equipment | 173,885 |
| Proceeds from entrance fees | 6,476,818 |
| Changes in operating assets and liabilities | |
| Accounts receivable | 25,867 |
| Notes receivable | 365,485 |
| Inventory | 765 |
| Prepaid expenses | (2,453) |
| Accounts payable and accrued liabilities | 71,505 |
| Refundable deposits | 19,182 |
| Net cash from operating activities | <u>\$ 7,643,758</u> |

**CHANNING HOUSE
NOTE TO RESERVE REPORTS**

NOTE 1 - BASIS OF ACCOUNTING

The accompanying reserve reports have been prepared in accordance with the provisions of Health and Safety Code Section 1792 administered by the State of California Department of Social Services and are not intended to be a complete presentation of Channing House's assets, liabilities, revenues, and expenses.

FORM 7-1
REPORT ON CCRC MONTHLY SERVICE FEES

| | <u>RESIDENTIAL LIVING</u> | <u>ASSISTED LIVING</u> | <u>SKILLED NURSING</u> |
|--|-------------------------------|----------------------------|----------------------------|
| [1] Monthly Service Fees at beginning of reporting period: (indicate range, if applicable) | <u>\$2,626 - \$8,806</u> | <u>\$2,626 - \$8,806</u> | <u>\$2,626 - \$8,806</u> |
| [2] Indicate percentage of increase in fees imposed during reporting period: (indicate range, if applicable) | <u>3.5%</u> | <u>3.5%</u> | <u>3.5%</u> |

Check here if monthly service fees at this community were not increased during the reporting period. (If you checked this box, please skip down to the bottom of this form and specify the names of the provider and community.)

[3] Indicate the date the fee increase was implemented: March 1, 2013
(If more than 1 increase was implemented, indicate the dates for each increase.)

[4] Check each of the appropriate boxes:

- Each fee increase is based on the provider's projected costs, prior year per capita costs, and economic indicators.
- All affected residents were given written notice of this fee increase at least 30 days prior to its implementation.
- At least 30 days prior to the increase in monthly service fees, the designated representative of the provider convened a meeting that all residents were invited to attend.
- At the meeting with residents, the provider discussed and explained the reasons for the increase, the basis for determining the amount of the increase, and the data used for calculating the increase.
- The provider provided residents with at least 14 days advance notice of each meeting held to discuss the fee increases.
- The governing body of the provider, or the designated representative of the provider posted the notice of, and the agenda for, the meeting in a conspicuous place in the community at least 14 days prior to the meeting.

[5] On an attached page, provide a concise explanation for the increase in monthly service fees including the amount of the increase.

PROVIDER: Channing House
COMMUNITY: Channing House

Channing House
Fiscal Year Ended 2/28/2014

Form 7-1: Explanation for Increase in Monthly Service Fees

Channing House monthly care fees are reviewed and adjusted on at least an annual basis to ensure both the continued coverage of our services and our long-term financial health. Our annual adjustment is predicated on the following steps:

1. Review of resident programs and services expected to be offered during the coming fiscal year, including new service initiatives.
2. Revenues are projected on the basis of expected occupancy, as well as anticipated movement within levels of care, and the impact of different care contracts on our revenues. Additional revenue sources not related to resident room revenues are planned when feasible and taken into account.
3. The budget for operating expenses is developed with input from staff, residents, the Board's Finance Committee and the full Board of Trustees. The budget process begins in September of each year. The final budget is approved in January for a March 1 – February 28 fiscal year. This budget is based on a review of program costs during the previous fiscal year, and the identification of any trends that will affect future costs. Staffing requirements are carefully reviewed, for each department. Adjustments are made for any FTE changes, as well as wage and benefit increases across all departments
4. Supplies, food services, utilities, housekeeping, maintenance, insurance and contract prices for vendors are also studied for potential impacts.
5. The combination of all these factors represents the total annual expected costs for the coming year. Total expected operating expenses were budgeted at \$10.6 M.
6. Channing House's current and expected trends are modeled in meeting certain financial ratios. Board policy is to achieve slight operation surplus in accordance with median operating margin ratios as published by the CARF-CCRC Financial Ratios & Trend Analysis.
7. Based on the budget analysis described above, an increase in rates of 3.5% was applied in order to support all budgeted programs and services. This increase was applied to all units effective March 1, 2013 for the fiscal year ending 2/28/14.

**Continuing Care Retirement Community
Disclosure Statement
General Information**

Date Prepared: 6/17/2014



FACILITY NAME: Channing House
 ADDRESS: 850 Webster Street ZIP CODE: 94301 PHONE: 650-327-0950
 PROVIDER NAME: Channing House FACILITY OPERATOR: Channing House
 RELATED FACILITIES: none RELIGIOUS AFFILIATION: none
 YEAR OPENED: 1964 # OF ACRES: 1 SINGLE MULTI-
 STORY STORY OTHER: _____ MILES TO SHOPPING CTR: 0.5
 MILES TO HOSPITAL: 3

NUMBER OF UNITS:

| | |
|---|----------------------------|
| RESIDENTIAL LIVING | HEALTH CARE |
| APARTMENTS — STUDIO: <u>74</u> | ASSISTED LIVING: <u>48</u> |
| APARTMENTS — 1 BDRM: <u>90</u> | SKILLED NURSING: <u>21</u> |
| APARTMENTS — 2 BDRM: <u>20</u> | SPECIAL CARE: <u>0</u> |
| COTTAGES/HOUSES: _____ | DESCRIPTION: > <u>0</u> |
| RLU OCCUPANCY (%) AT YEAR END: <u>95%</u> | > _____ |

TYPE OF OWNERSHIP: NOT-FOR-PROFIT FOR-PROFIT ACCREDITED?: YES NO BY: _____

FORM OF CONTRACT: CONTINUING CARE LIFE CARE ENTRANCE FEE FEE FOR SERVICE
(Check all that apply) ASSIGNMENT OF ASSETS EQUITY MEMBERSHIP RENTAL

REFUND PROVISIONS: *(Check all that apply)* 90% 75% 50% FULLY AMORTIZED OTHER: 80%

RANGE OF ENTRANCE FEES: \$ 145,000 - \$ 1,323,000 **LONG-TERM CARE INSURANCE REQUIRED?** YES NO

HEALTH CARE BENEFITS INCLUDED IN CONTRACT: Nursing Care

ENTRY REQUIREMENTS: MIN. AGE: 65 PRIOR PROFESSION: n/a OTHER: n/a

RESIDENT REPRESENTATIVE(S) TO THE BOARD (briefly describe their involvement): > Two residents are voting members of the Board.
 > In addition, the President and Vice President of the Resident Association attend board meetings.

FACILITY SERVICES AND AMENITIES

| COMMON AREA AMENITIES | AVAILABLE | FEE FOR SERVICE | SERVICES AVAILABLE | INCLUDED IN FEE | FOR EXTRA CHARGE |
|---------------------------------------|-------------------------------------|-------------------------------------|--------------------------------------|-------------------------------------|-------------------------------------|
| BEAUTY/BARBER SHOP | <input checked="" type="checkbox"/> | <input checked="" type="checkbox"/> | HOUSEKEEPING (<u>4</u> TIMES/MONTH) | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| BILLIARD ROOM | <input type="checkbox"/> | <input type="checkbox"/> | MEALS (<u>3</u> /DAY) | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| BOWLING GREEN | <input type="checkbox"/> | <input type="checkbox"/> | SPECIAL DIETS AVAILABLE | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| CARD ROOMS | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 24-HOUR EMERGENCY RESPONSE | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| CHAPEL | <input type="checkbox"/> | <input type="checkbox"/> | ACTIVITIES PROGRAM | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| COFFEE SHOP | <input type="checkbox"/> | <input type="checkbox"/> | ALL UTILITIES EXCEPT PHONE | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| CRAFT ROOMS | <input checked="" type="checkbox"/> | <input type="checkbox"/> | APARTMENT MAINTENANCE | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| EXERCISE ROOM | <input checked="" type="checkbox"/> | <input type="checkbox"/> | CABLE TV | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| GOLF COURSE ACCESS | <input type="checkbox"/> | <input type="checkbox"/> | LINENS FURNISHED | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| LIBRARY | <input checked="" type="checkbox"/> | <input type="checkbox"/> | LINENS LAUNDERED | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| PUTTING GREEN | <input type="checkbox"/> | <input type="checkbox"/> | MEDICATION MANAGEMENT | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| SHUFFLEBOARD | <input type="checkbox"/> | <input type="checkbox"/> | NURSING/WELLNESS CLINIC | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| SPA | <input type="checkbox"/> | <input type="checkbox"/> | PERSONAL HOME CARE | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| SWIMMING POOL-INDOOR | <input checked="" type="checkbox"/> | <input type="checkbox"/> | TRANSPORTATION-PERSONAL | <input type="checkbox"/> | <input checked="" type="checkbox"/> |
| SWIMMING POOL-OUTDOOR | <input type="checkbox"/> | <input type="checkbox"/> | TRANSPORTATION-PREARRANGED | <input type="checkbox"/> | <input checked="" type="checkbox"/> |
| TENNIS COURT | <input type="checkbox"/> | <input type="checkbox"/> | OTHER <u>Medical Transportation</u> | <input checked="" type="checkbox"/> | <input type="checkbox"/> |
| WORKSHOP | <input checked="" type="checkbox"/> | <input type="checkbox"/> | | | |
| OTHER <u>ping pong & foosball</u> | <input checked="" type="checkbox"/> | <input type="checkbox"/> | | | |

All providers are required by Health and Safety Code section 1789.1 to provide this report to prospective residents before executing a deposit agreement or continuing care contract, or receiving any payment. Many communities are part of multi-facility operations which may influence financial reporting. Consumers are encouraged to ask questions of the continuing care retirement community that they are considering and to seek advice from professional advisors.

PROVIDER NAME: Channing House

OTHER CCRCs

LOCATION (City, State)

PHONE (with area code)

n/a

MULTI-LEVEL RETIREMENT COMMUNITIES

LOCATION (City, State)

PHONE (with area code)

n/a

FREE-STANDING SKILLED NURSING

LOCATION (City, State)

PHONE (with area code)

n/a

SUBSIDIZED SENIOR HOUSING

LOCATION (City, State)

PHONE (with area code)

n/a

NOTE: PLEASE INDICATE IF THE FACILITY IS A LIFE CARE FACILITY.

| | <u>2011</u> | <u>2012</u> | <u>2013</u> | <u>2014</u> |
|--|-------------|-------------|-------------|-------------|
| INCOME FROM ONGOING OPERATIONS | | | | |
| OPERATING INCOME (Excluding amortization of entrance fee income) | \$9,811 | \$10,066 | \$10,725 | \$10,779 |
| LESS OPERATING EXPENSES (Excluding depreciation, amortization, and interest) | \$9,346 | \$9,360 | \$9,684 | \$10,457 |
| NET INCOME FROM OPERATIONS | \$435 | \$706 | \$1,041 | \$321 |
| LESS INTEREST EXPENSE | \$459 | \$3 | \$0 | \$0 |
| PLUS CONTRIBUTIONS | \$213 | \$743 | \$299 | \$42 |
| PLUS NON-OPERATING INCOME (EXPENSES) (excluding extraordinary items) | \$0 | \$0 | \$0 | \$27 |
| NET INCOME (LOSS) BEFORE ENTRANCE FEES, DEPRECIATION AND AMORTIZATION | \$189 | \$1,455 | \$1,340 | \$390 |
| NET CASH FLOW FROM ENTRANCE FEES (Total Deposits Less Refunds) | \$4,728 | \$5,507 | \$5,981 | \$6,842 |

DESCRIPTION OF SECURED DEBT (as of most recent fiscal year end)

| <u>LENDER</u> | <u>OUTSTANDING BALANCE</u> | <u>INTEREST RATE</u> | <u>DATE OF ORIGINATION</u> | <u>DATE OF MATURITY</u> | <u>AMORTIZATION PERIOD</u> |
|-----------------|----------------------------|----------------------|----------------------------|-------------------------|----------------------------|
| ABAG-2010 Bonds | \$61,778,125 | 5.95% | 07/01/10 | 05/15/40 | 30 Years |
| | | | | | |
| | | | | | |

FINANCIAL RATIOS (see next page for ratio formulas)

**2013 CCAC Medians
50th Percentile
(optional)**

| | <u>2012</u> | <u>2013</u> | <u>2014</u> |
|------------------------------------|-------------|-------------|-------------|
| DEBT TO ASSET RATIO | .58 | .54 | .51 |
| OPERATING RATIO | 1.02 | 1.02 | .97 |
| DEBT SERVICE COVERAGE RATIO | 1.74* | 1.89* | 1.70 |
| DAYS CASH ON HAND RATIO | 642 | 728 | 627 |

HISTORICAL MONTHLY SERVICE FEES (Average Fee and Change Percentage)

| | <u>2011</u> | <u>%</u> | <u>2012</u> | <u>%</u> | <u>2013</u> | <u>%</u> | <u>2014</u> |
|-----------------|-------------|----------|-------------|----------|-------------|----------|-------------|
| STUDIO | \$2,466 | 5.3% | \$2,762 | 3.8% | \$2,897 | 3.5% | \$2,998 |
| ONE BEDROOM | \$3,770 | 5.3% | \$4,147 | 3.8% | \$4,305 | 3.5% | \$4,456 |
| TWO BEDROOM | \$7,079 | 5.3% | \$7,787 | 3.8% | \$8,083 | 3.5% | \$8,366 |
| COTTAGE/HOUSE | \$0 | 0.0% | \$0 | 0.0% | \$0 | 0.0% | \$0 |
| ASSISTED LIVING | \$2,466 | 5.3% | \$2,762 | 3.8% | \$2,897 | 3.5% | \$2,998 |
| SKILLED NURSING | \$2,466 | 5.3% | \$2,762 | 3.8% | \$2,897 | 3.5% | \$2,998 |
| SPECIAL CARE | \$0 | 0.0% | \$0 | 0.0% | \$0 | 0.0% | \$0 |

COMMENTS FROM PROVIDER: > *Calculation includes capitalized interest from the 2010 bond financing

>
>

FINANCIAL RATIO FORMULAS

LONG-TERM DEBT TO TOTAL ASSETS RATIO

$$\frac{\text{Long-Term Debt, less Current Portion}}{\text{Total Assets}}$$

OPERATING RATIO

$$\frac{\begin{array}{l} \text{Total Operating Expenses} \\ - \text{ Depreciation Expense} \\ - \text{ Amortization Expense} \end{array}}{\text{Total Operating Revenues} - \text{ Amortization of Deferred Revenue}}$$

DEBT SERVICE COVERAGE RATIO

$$\frac{\begin{array}{l} \text{Total Excess of Revenues over Expenses} \\ + \text{ Interest, Depreciation, and Amortization Expenses} \\ \text{Amortization of Deferred Revenue} + \text{ Net Proceeds from Entrance Fees} \end{array}}{\text{Annual Debt Service}}$$

DAYS CASH ON HAND RATIO

$$\frac{\begin{array}{l} \text{Unrestricted Current Cash \& Investments} \\ + \text{ Unrestricted Non-Current Cash \& Investments} \end{array}}{(\text{Operating Expenses} - \text{Depreciation} - \text{Amortization})/365}$$

NOTE: These formulas are also used by the Continuing Care Accreditation Commission. For each formula, that organization also publishes annual median figures for certain continuing care retirement communities.

**KEY INDICATORS REPORT
CHANNING HOUSE**

| | | | | | | |
|---|--|----------|----------|----------|----------|-------|
| Please Attach an explanatory memo that summarizes significant trends or variances in key operational indicators | | | | | | |
| | | 2009 | 2010 | 2011 | 2012 | |
| OPERATIONAL STATISTICS | | | | | | |
| 1 | Average Annual Occupancy by Site % | 87.7% | 84.4% | 83.5% | 83.8% | 8 |
| Margin (Profitability) Indicators | | | | | | |
| 2 | Net Operating Margin (%) | 33.5% | 34.3% | 34.7% | 27.1% | 2 |
| 3 | Net Operating Margin - Adjusted (%) | 44.6% | 50.2% | 53.6% | 49.1% | 4 |
| Liquidity Indicators | | | | | | |
| 4 | Unrestricted Cash and Investments (\$000) | \$11,645 | \$12,992 | \$13,060 | \$16,460 | \$19, |
| 5 | Days Cash on Hand (Unrestricted) | 427 | 459 | 485 | 642 | |
| Capital Structure Indicators | | | | | | |
| 6 | Deferred Revenue from Entrance Fees (\$000) | \$17,408 | \$17,882 | \$19,712 | \$21,504 | \$24, |
| 7 | Net annual E/F Proceeds (\$000) | \$2,181 | 3,630 | \$4,728 | \$5,548 | \$5, |
| 8 | Unrestricted Net Assets (\$000) | \$11,741 | \$14,808 | \$16,457 | \$18,546 | \$25, |
| 9 | Annual Capital Asset Expenditure (\$000) | \$3,997 | \$3,155 | \$8,358 | \$11,318 | \$13, |
| 10 | Annual Debt Service Coverage Revenue Basis (x) | 0.26 | 0.11 | 0.68 | 0.35 | |
| 11 | Annual Debt Service Coverage (x) | 1.58 | 2.32 | 3.42 | 1.71 | |
| 12 | Annual Debt Service/Revenue (%) | 13.5% | 13.0% | 12.8% | 27.9% | 2 |
| 13 | Average Annual Effective Interest Rate (%) | 5.5% | 5.5% | 3.4% | 5.6% | |
| 14 | Unrestricted Cash & Investments/Long-Term Debt (%) | 61.9% | 71.3% | 20.7% | 26.4% | 3 |
| 15 | Average Age of Facility (Years) | 11 | 10 | 10 | 10 | |

