HOLLENBECK PALMS
REPORT OF INDEPENDENT AUDITOR AND FINANCIAL STATEMENTS

YEARS ENDED JUNE 30, 2017 AND 2016

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CliftonLarsonAllen LLP
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INDEPENDENT AUDITORS' REPORT

Board of Trustees
Hollenbeck Palms
Los Angeles, California

We have audited the accompanying financial statements of Hollenbeck Palms (the Palms) which comprise the statements of financial position as of June 30, 2017, and the related statements of activities and cash flows for the year 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.

Auditors' Responsibility

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

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

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

Opinion

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

Other Matter

The June 30, 2016 financial statements were audited by Vicenti, Lloyd & Stutzman LLP, whose practice became part of CliftonLarsonAllen LLP as of June 1, 2017, and whose report dated October 4, 2016, expressed an unmodified opinion on those statements.

Emphasis of Matter

As discussed in Note 2 to the financial statements, the Palms adopted a recently issued accounting standard related to the accounting for debt issuance costs. The new standard requires entities to present debt issuance costs as a direct deduction from the face amount of the related borrowings, amortize debt issuance costs using the effective interest rate method over the life of the debt, and record amortization as a component of interest expense. Our opinion is not modified with respect to this matter.

CliftonLarsonAllen LLP

CliftonLarsonAllen LLP

Glendora, California
October 5, 2017

HOLLENBECK PALMS.
STATEMENTS OF FINANCIAL POSITION
JUNE 30, 2017 AND 2016

	2017	2016
ASSETS:		
Cash and Cash Equivalents (Notes 2 and 3)	$ 9,456,222	$ 11,884,000
Accrues interest receivable	56,322	51,463
Due from residents and third-party payers, less allowance for bad debts of $59,596 and $78,170 for 2017 and 2016, respectively	1,132,598	1,480,322
Pledges and other contributions receivable less discount (Note 4)	426,117	838,277
Prepaid expenses and other assets	381,343	349,507
Investments (Note 5)	43,610,246	43,400,924
Property and equipment, net (Note 6)	30,383,089	28,889,280
TOTAL	$ 85,445,937	$ 86,893,773
LIABILITIES AND NET ASSETS:		
LIABILITIES		
Accounts payable and accrued expenses	2,753,500	3,111,310
Accrued interest payable	481,579	589,937
Deferred revenue from entrance fees (Note 2)	3,783,783	3,934,543
Assigned assets, net (Note 2)	4,443,399	3,612,847
Long term debt (Note 9)	28,698,985	30,860,000
Total liabilities	40,161,246	42,108,637
NET ASSETS (Note 2)		
Unrestricted	40,129,271	40,039,070
Temporarily restricted	4,382,097	3,972,743
Permanently restricted	773,323	773,323
Total net assets	45,284,691	44,785,136
TOTAL	$ 85,445,937	$ 86,893,773

See accompanying Notes to Financial Statements.

HOLLENBECK PALMS
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2017

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total 2017
REVENUES, GAINS, AND OTHER SUPPORT:				
Resident service fees, including amortization of entrance fees (Note 2)	$ 13,715,998	$ -	$ -	$ 13,715,998
Investment income, including realized gains (Note 5)	2,232,739	63,156	-	2,295,895
Donor contributions	58,209	135,315	-	193,524
Resident contributions - assigned assets released (Note 2)	781,824	-	-	781,824
Other	234,885	-	-	234,885
Total revenues, gains, and other support	17,023,655	198,471	-	17,222,126
EXPENSES (Note 13)				
Resident care	6,115,648	-	-	6,115,648
General and administrative	4,333,767	-	-	4,333,767
Engineering and plant	1,130,859	-	-	1,130,859
Dietary	2,320,268	-	-	2,320,268
Housekeeping	821,552	-	-	821,552
Depreciation	1,190,453	-	-	1,190,453
Bond interest	1,342,978	-	-	1,342,978
Member's interest (Note 2)	91,725	-	-	91,725
Total Expenses	17,347,250	-	-	17,347,250
CHANGE IN NET ASSETS FROM OPERATIONS	(323,595)	198,471	-	(125,124)
OTHER INCOME (LOSS):				
Unrealized gain (loss) on investments (Note 5)	(257,398)	210,883	-	(46,515)
Change in pension liability (Note 7)	671,194	-	-	671,194
Total Other Income (Loss)	413,796	210,883	-	624,679
CHANGE IN NET ASSETS	90,201	409,354	-	499,555
NET ASSETS:				
Beginning of year	40,039,070	3,972,743	773,323	44,785,136
End of year	$ 40,129,271	$ 4,382,097	$ 773,323	$ 45,284,691

See accompanying Notes to Financial Statements.

HOLLENBECK PALMS
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2016

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total 2016
REVENUES, GAINS, AND OTHER SUPPORT:				
Resident service fees, including amortization of entrance fees (Note 2)	$ 13,738,425	$ -	$ -	$ 13,738,425
Investment income, including realized gains (Note 5)	1,938,024	120,312	-	2,058,336
Donor contributions	26,715	188,895	-	215,610
Resident contributions - assigned assets released (Note 2)	2,250,600	-	-	2,250,600
Other	149,584	-	-	149,584
Total revenues, gains, and other support	18,103,348	309,207	-	18,412,555
EXPENSES (Note 13)				
Resident care	5,996,709	-	-	5,996,709
General and administrative	4,266,890	-	-	4,266,890
Engineering and plant	1,158,018	-	-	1,158,018
Dietary	2,343,827	-	-	2,343,827
Housekeeping	798,916	-	-	798,916
Depreciation	1,133,396	-	-	1,133,396
Bond interest	1,634,684	-	-	1,634,684
Member's interest (Note 2)	103,970	-	-	103,970
Total Expenses	17,436,410	-	-	17,436,410
CHANGE IN NET ASSETS FROM OPERATIONS	666,938	309,207	-	976,145
OTHER INCOME (LOSS):				
Unrealized gain (loss) on investments (Note 5)	927,442	(81,430)	-	846,012
Change in pension liability (Note 7)	(574,119)	-	-	(574,119)
Total Other Income (Loss)	353,323	(81,430)	-	271,893
CHANGE IN NET ASSETS	1,020,261	227,777	-	1,248,038
NET ASSETS:				
Beginning of year	39,018,809	3,744,966	773,323	43,537,098
End of year	$ 40,039,070	$ 3,972,743	$ 773,323	$ 44,785,136

See accompanying Notes to Financial Statements.

HOLLENBECK PALMS
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2017 AND 2016

	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash received from residents	$ 13,859,909	$ 12,488,689
Entrance fees received from residents	1,779,000	2,307,337
Contributions from donors	470,369	26,715
Investment income received	2,291,036	2,075,932
Other cash revenues	234,885	149,584
Cash paid to suppliers and employees	(14,440,546)	(14,450,772)
Interest paid	(1,397,443)	(1,454,831)
Interest paid to members	(91,725)	(96,303)
Net cash provided by operating activities	2,705,485	1,046,351
CASH FLOWS FROM INVESTING ACTIVITIES:		
Investments sold or matured	3,136,338	5,372,297
Investments purchased	(3,386,624)	(5,579,132)
Capital expenditures	(2,684,262)	(2,496,321)
Net cash used by investing activities	(2,934,548)	(2,703,156)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Contributions restricted for capital	135,315	188,895
Entrance fee refunds	(119,122)	(233,245)
Cost of refinancing debt	(304,908)	-
Payment of long term debt	(1,910,000)	(635,000)
Net cash used by financing activities	(2,198,715)	(679,350)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(2,427,778)	(2,336,155)
CASH AND CASH EQUIVALENTS - Beginning of year	11,884,000	14,220,155
CASH AND CASH EQUIVALENTS- End of year	$ 9,456,222	$ 11,884,000

See accompanying Notes to Financial Statements.

HOLLENBECK PALMS
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2017 AND 2016

	2017	2016
RECONCILIATION OF CHANGE IN NET ASSETS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Change in net assets	$ 499,555	$ 1,248,038
Adjustments to reconcile change in net assets to net cash used by operating activities:		
Depreciation	1,190,453	1,133,396
Amortization of debt issuance costs	53,893	-
Earned entrance fees	(1,569,036)	(1,689,635)
Bad debt provision	(18,574)	200,248
Unrealized (gain) loss on investments	46,515	(846,012)
Increase (decrease) in pension liability	(671,194)	574,119
Contributions for financing purposes	(135,315)	(188,895)
Entrance fee refunds	119,122	233,245
Changes in operating assets and liabilities:		
Entrance fee receivable	263,900	170,275
Accrued interest receivable	(4,859)	17,596
Pledges receivable	412,160	150,007
Amounts due from residents and third-party payers	102,398	51,477
Prepaid expenses and other current assets	(31,836)	18,126
Accounts payable and accrued expenses	313,384	199,432
Accrued interest payable	(108,357)	179,853
Deferred revenue from entrance fees	1,418,274	1,517,764
Assigned assets liability	825,002	(1,922,683)
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 2,705,485	$ 1,046,351
SUPPLEMENTAL CASH FLOW INFORMATION:		
Noncash assigned assets	$ 5,550	$ (307,370)
SUPPLEMENTAL DISCLOSURE OF NONCASH FINANCING ACTIVITIES		
Issuance of Series 2016 Revenue Bonds to Refinance Series 2007 Revenue Bonds	$ 20,435,000	$ -

See accompanying Notes to Financial Statements.

NOTE 1 MISSION STATEMENT

The Palms is committed to providing a residence for those in their later years of their lives that encompasses a healthy environment of comfort, safety, and enjoyment; that attends to their physical, mental, and spiritual needs; and that is quick to respond to and assist in those needs whether immediate or long term, and to do so with great compassion, honesty, dignity, and genuine love.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Operations

The Palms, incorporated as a California nonprofit public benefit corporation, owns and operates a retirement community and skilled nursing facility in Los Angeles, California. Residents receive residence, services, and care under three plans, as more fully described below. The facilities include approximately 145 residential units and 99 skilled nursing beds. As of June 30, 2017 and 2016, the total number of residents was 217 and 224, respectively.

The Palms fulfills the need for housing by providing residential facilities that are specifically designed to meet the physical, recreational, social, and similar needs of its residents. The residents' need for health care is provided for in the Palms' skilled nursing care units and through the Palms ongoing relationship with a network of physicians, health care professionals and local hospitals.

The residents' need for financial security is satisfied by the Palms' operational policy of providing its residents lifetime care at the lowest possible cost. The residents' need for financial security is further fulfilled by the Palms' policy of maintaining lifetime care for residents who become unable to pay the regular monthly fee.

Earnings of the Palms' are used to improve the care provided and subsidize any residents unable to continue making monthly service fee payments. No part of the Palms' net earnings inures, directly or indirectly, to the benefit of any private shareholder or individual.

Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with generally accepted accounting principles of the United States. Net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Palms and changes therein are classified and reported as follows:

Unrestricted Net Assets: Net assets not subject to donor imposed stipulations. The Board has designated unrestricted net assets, as explained in Note 3.

Temporarily Restricted Net Assets: Net assets subject to donor-imposed stipulations that may or will be met, either by actions of the Palms and/or the passage of time. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of activities as net assets released from restrictions.

Permanently Restricted Net Assets: Net assets subject to donor-imposed stipulations that they be maintained permanently by the Palms. Generally, the donors of these assets permit the Palms to use all or part of the income earned on any related investments for general or specific purposes.

Additional information on temporarily and permanently restricted net assets is provided in Note 11.

Member Care Plans and Assigned Assets

The Palms charges for resident care under three plans. Under Plan A, new residents assign their assets to the Palms upon admission. Noncash assets such as investments and real estate, assigned by new residents, are recorded at their fair market value at the date received. A predetermined amount of the assigned assets is designated as entrance fees. The entrance fee is amortized to income using the straight-line method of 2% per month or amortized over the member's life expectancy, whichever is shorter, commencing with the fourth month of residence.

As care is provided to the residents, the remaining assets are amortized to income at prevailing rates for the residential section or for the nursing unit, as applicable. Upon the expiration of a Plan A resident, an amount equal to assets assigned, less accumulated care costs, is transferred from deferred income to other gain as a resident contribution. Such resident contributions were $781,824 for 2017 and $2,250,600 for 2016. Assigned assets were $4,443,399 and $3,612,847 as of June 30, 2017 and 2016, respectively.

Under Plan B, a resident pays an entrance fee, which is amortized to income using the straight-line method of 2% per month or amortized over the member's life expectancy, whichever is shorter, and a monthly fee based on the prevailing rate for care costs. The Palms also offers a Plan C, under which a resident pays an initial processing fee and a significantly larger monthly fee as opposed to paying an entrance fee.

Rates under all plans are adjusted by the Board of Trustees as the cost of providing care fluctuates. Under both Plans A and B, when members fully deplete their assigned assets, the Palms will absorb their cost of care by reducing rates to the amount of state and federal public aid available. For 2017 and 2016, charity care, which is based on estimated cost per day in excess of service fees received, amounted to $1,081,562 and $1,123,765, respectively.

Entrance Fees

Fees paid by a resident upon entering into a continuing care retirement community contract, net of estimated future refunds, are recorded as deferred revenue, and are amortized to income using the methods described above. Under resident contracts, the full amount of entrance fees is refundable if a resident leaves the Palms within the first 90 days after entering; otherwise, the remaining unamortized entrance fees and unexpended assigned assets are refunded if a resident leaves. Unamortized entrance fees totaled $3,783,783 and $3,934,543 as of June 30, 2017 and 2016, respectively.

Management believes the estimated amount of entrance fees that are expected to be refunded to current residents under the terms of these contracts based on previous attrition experience is not material and, as such, no provision for the liability has been reported. Entrance fee refunds were $119,123 and $233,245 for the years ended June 30, 2017 and 2016, respectively.

Entrance fee receivables are recorded when residents entering into a continuing care retirement community do not have sufficient liquid assets to cover the entrance fee. Entrance fees receivable was $0 and $263,900 June 30, 2017 and 2016, respectively.

Resident Services Fees

Resident services fees are recorded net of a provision for contractual allowances. The contractual allowance represents the difference between established rates and per-diem reimbursement. In addition, resident services fees are presented net of bad debt expense on the Statement of Activities. Receivables associated with resident service fees are written off based on management’s evaluation of uncollectible balances.

Members’ Interest

Residents have the option of opening a member's savings account with the Palms. Residents are able to make deposits and withdrawals from their savings accounts as needed. At the resident's request, payments for various bills and charges at the Palms may be paid by the Palms from the member's savings accounts. The Palms invests the funds deposited and pays members an established interest rate of 3% of the net amount (assigned assets and savings balance less accumulated charges). The calculated interest is recorded as members' interest expense and is included in assigned assets, net, in the statement of financial position and in members’ interest in the statement of activities.

Obligation to Provide Future Services

The Palms calculates the present value of the net cost of future services and use of facilities to be provided to current residents ("estimated obligation") and compares that amount with the balance of deferred revenue from entrance fees. If the estimated obligation exceeds the deferred revenue from entrance fees, a liability is recorded with the corresponding charge to income. As of June 30, 2017 and 2016, the estimated obligation is less than the balance of deferred revenue from entrance fees. The obligation is calculated assuming a 4% inflation rate and a 4% discount rate for June 30, 2017 and 2016, respectively.

Tax Status

The Palms is a not-for-profit corporation and is exempt from federal income taxes under Section 501(a) of the Internal Revenue Code and is exempt from California franchise taxes Section 23701d of the California Revenue and Taxation Code. The Palms is described in Section 501(c)(3) of the Internal Revenue Code and is listed in Internal Revenue Service Publication 78 as a charitable organization qualified to receive donations. The Palms maintains its tax-exempt status through devoting its resources to meet the primary needs of aged persons. These needs are for housing, health care, and financial security.

Income Taxes

The Palms has evaluated its tax positions and the certainty as to whether those positions will be sustained in the event of an audit by taxing authorities at the federal and state levels. The primary tax positions evaluated are related to the Palm's continued qualification as a tax-exempt organization and whether there are unrelated business income activities conducted that would be taxable. Management has determined that all income tax positions are more likely than not of being sustained upon potential audit or examination; therefore, no disclosures of uncertain income tax positions are required.

The Palms files informational returns in the U.S. federal jurisdiction and the state of California. The statute of limitations for federal and California state purposes is generally three and four years, respectively.

Cash and Cash Equivalents

The Palms considers all highly liquid debt investments with a remaining maturity of three months or less at the time of purchase to be cash equivalents. Accounts with greater than three month's maturity are included with investments. The Palms holds deposits in excess of Federal Deposit Insurance Corporation ("FDIC") limits. At June 30, 2017 and 2016, respectively, uninsured, uncollateralized deposits were $3,057,459 and $2,083,564. The Palms also holds deposits with a brokerage firm in excess of Securities Investor Protection Corporation ("SIPC") limits. At June 30, 2017 and 2016 respectively, unsecured brokerage deposits were $5,828,083 and $8,870,189. These deposits are held by creditworthy, high-quality financial institutions.

Donor-Restricted Contributions

The Palms reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the statements of activities as released from restrictions. No temporarily restricted net assets were released from restrictions during the fiscal years ended June 30, 2017 and 2016. Donor-restricted contributions whose restrictions are met within the same year as received are reflected as unrestricted contributions. Temporarily restricted net assets are composed of unexpended restricted contributions received. Gifts permanently restricted by the donor, such as endowments whereby the donor has prohibited the use of the corpus, are recorded as permanently restricted net assets.

Investments

The Palms' investment policy is to adhere to high standards of quality in the selection of all types of investments, with reasonable diversification to be maintained at all times. Specifically, the Palms' policy prohibits investments in derivative financial instruments. Marketable securities are primarily managed by an independent investment manager and held by independent custodial banks.

Investments principally consist of stocks, mutual funds, corporate and municipal bonds, U.S. Treasury Securities, annuity and life insurance policies, mortgage-backed securities, cash and money market and bank deposits. Investments are reported at fair value as described in Note 5. Interest, dividends, and realized gains and losses are included in investment income. The cost of securities sold is based on the specific-identification method.

Investment securities, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and such changes could materially affect the amounts reported in the accompanying statements of financial position.

Property and Equipment

Purchased assets with a cost greater than $500 and an estimated useful life in excess of three years are capitalized as fixed assets. Donations of property and equipment with a value of $1,000 or more are capitalized at their estimated fair value. Routine maintenance and repairs are charged to expense as incurred. Depreciation is computed on the straight-line method, based on the following estimated useful lives:

Buildings and improvements	10-40 years
Equipment	3-7 years
Vehicles	5 years

Professional Liability Insurance Coverage

The Palms purchases professional liability insurance under an occurrence-basis policy with a nominal deductible.

Self-Insurance

The Palms is self-insured for claims under the California Unemployment Insurance Code. Such claims are paid when approved by the Palms. The amounts of such claims were $12,016 and $5,132 in 2017 and 2016, respectively.

Allocation of Expenses

The costs of providing various programs and other activities have been summarized on a departmental basis in the statements of activities. Certain costs have been allocated among the programs and supporting services benefited in Note 13.

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. Actual results could differ from those estimates.

Change in Accounting Principle

The Palms has adopted the accounting guidance in FASB Accounting Standards Update (ASU) No. 2015-03, *Interest – Imputation of Interest (Subtopic 853-30): Simplifying the Presentation of Debt Issuance Costs.* ASU 2015-03 requires organizations to present debt issuance costs as a direct deduction from the face amount of the related borrowings, amortize debt issuance costs using the effective interest method over the life of the debt, and record the amortization as a component of interest expense. The effect of adopting the new standard decreased the debt issuance costs asset to zero and decreased the debt liability by $320,000 as of July 1, 2016. The adoption of the standard had no effect on previously reported net assets. The ASU is effective for fiscal years beginning after December 15, 2015, with early adoption permitted. The ASU is retrospectively applied.

During the year ended June 30, 2017, the Palms has adopted a provision of the Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2016-01, *Financial Instruments – Overall: Recognition and Measurement of Financial Assets and Financial Liabilities*. This provision eliminates the requirement for entities, other than public business entities, to disclose the fair values of financial instruments carried at amortized cost, as previously required by Accounting Standards Codification (ASC) 825-10-50. As such, the Palms has omitted this disclosure for the years ended June 30, 2017 and 2016.

Deferred Financing Costs

Costs incurred in connection with the issuance of debt described in Note 9 have been deferred and are being amortized using the straight-line method (which approximates the effective interest method) over the life of the debt. As discussed above, unamortized deferred financing costs totaled $571,015 and $320,000 at June 30, 2017 and 2016, respectively. Accumulated amortization was $56,893 and $0 at June 30, 2017 and 2016, respectively. Amortization expense totaled $56,893 for the year ended June 30, 2017. Deferred financing costs are included with long-term debt on the statement of financial position and amortization expense is included with interest expense on the statement of activities.

Reclassification

Certain items in the prior year financial statements, including the statements of cash flows, have been reclassified to conform to the current year presentation. Cash reserved for debt service has been reclassified to cash and cash equivalents. Real estate previously classified as investments has been reclassified to property and equipment. Issuance costs previously classified in construction in progress have been reclassified as a reduction in debt.

Subsequent Events

The Palms has evaluated subsequent events through October 5, 2017 which is the date these financial statements were available to be issued.

NOTE 3 CASH RESTRICTIONS, DESIGNATIONS AND RESERVATIONS

Cash and cash equivalents at June 30, 2017 includes $90,189 temporarily restricted for life care membership purposes and $2,710,049 for future building and asset replacement purposes. The board has designated $4,113,370 in bond funds for building projects and $357,491 for scheduled debt service payments.

Cash and cash equivalents at June 30, 2016 includes $67,025 temporarily restricted for life care membership purposes and $1,920,425 for future building and asset replacement purposes. The board has designated $6,566,895 in bond funds for building projects. In addition, $1,626,714 in bond debt service reserves is required as a condition of the bond issue to be used in the event of a principal or interest payment deficiency and $343,862 was reserved for scheduled debt service payments.

NOTE 4 PLEDGES RECEIVABLE

Pledges receivable expected to be received in one year or less are recorded at net realizable value, which approximates fair value. Pledges receivable have been discounted to present value using a discount rate of 1.89% and 1.01% for 2017 and 2016, respectively. An allowance for uncollectable amounts has not been recorded based on management's assessment of the donors' creditworthiness. At June 30, the Palms had unconditional promises to give expected to be received in the following periods:

	2017	2016
In one year or less	$ 226,734	$ 251,667
Between one and five years	100,334	502,151
More than five years	100,000	100,000
Gross unconditional pledges receivable	427,068	853,818
Less: discount on pledges receivable	(951)	(15,541)
Net pledges receivable	$ 426,117	$ 838,277

NOTE 5 INVESTMENTS

Investments in equity and debt securities are reported at fair value in the statement of financial position. Gains and losses on investments are reported in the statement of activities as increases or decreases in unrestricted net assets unless their use is temporarily or permanently restricted by explicit donor stipulations or by law. Investments in equity and debt securities traded on national securities exchanges are valued at the closing price on the last business day of the fiscal year; equity and debt securities traded on the over-the-counter market are valued at the last reported bid price.

For fair value measurements a disclosure presentation, levels 1 through 3 have been assigned to the fair value measurement of investments. The fair value measurement is determined as follows:

Level 1 – quoted prices in an active market for identical assets.
Level 2 – quoted prices for similar assets and market-corroborated inputs.
Level 3 – the organizations' own assumptions about market participation, including assumptions about risk, developed based on the best information available in the circumstances.

The composition of investments at June 30, 2017 and 2016 is as follows:

	2017	2016
Cash and money market (Level 1)	$ 116,795	$ 456,866
Bank deposits (Level 1)	158,332	133,993
Mutual funds (Level 1)	10,416,934	10,176,328
U.S. Treasury Securities (Level 1)	1,497,344	2,003,438
Stocks (Level 1)	24,374,868	24,173,026
	36,564,273	36,943,651
Corporate bonds (Level 2)	3,021,920	2,747,768
Mortgage-backed securities (Level 2)	652,161	581,672
Municipal bonds (Level 2)	2,235,224	1,988,863
Annuity and life insurance policies (Level 2)	1,134,837	1,137,139
	7,044,142	6,455,442
Oil interest (Level 3)	1,831	1,831
Total investments	$ 43,610,246	$ 43,400,924

There was no change in assets measured at fair value using significant unobservable inputs at Level 3.

Investment return for the years ended June 30, 2017 and 2016 are composed of the following:

	2017	2016
Dividend and interest income	$ 1,098,879	$ 1,099,905
Realized gains on sales of investment, net	1,287,286	1,048,966
Less: fees	(90,270)	(90,535)
Net investment income included in operations	2,295,895	2,058,336
Unrealized gains (losses)	(46,515)	846,012
Net Investment income	$ 2,249,380	$ 2,904,348

NOTE 6 PROPERTY AND EQUIPMENT

Property and equipment at June 30, 2017 and 2016 consist of the following:

	2017	2016
Land	$ 11,086	$ 11,086
Buildings and improvements	40,093,230	40,053,738
Furniture and equipment	5,955,151	5,884,529
Vehicles	255,253	257,567
Cemetery lots	21,326	21,326
	46,336,046	46,228,246
Less accumulated depreciation	(22,553,064)	(21,464,517)
	23,782,982	24,763,729
Construction in progress	6,600,107	4,125,551
	$ 30,383,089	$ 28,889,280

Depreciation expense for the years ended June 30, 2017 and 2016 was $1,190,453 and $1,133,396, respectively.

NOTE 7 RETIREMENT PLANS

Cash Balance Pension Plan

Effective January 1, 2009 the Retirement Plan for the Employees of Hollenbeck Palms (the Plan) was amended. The amendment changed the noncontributory traditional Defined Benefit Plan to a noncontributory Cash Balance Pension Plan (CBPP). The Plan is subject to the provisions of the Employees Retirement Income Security Act of 1974 (ERISA). Participants over 50 years of age with at least 15 years of service as of January 1, 2009 were grandfathered. This sub-group of grandfathered participants will receive a Special Annual Accrual contribution which is determined using the traditional Defined Benefit Plan formula. Active participants who are not a part of the sub-group will receive contribution credits equal to 5% of their annual salary along with interest at the 30 year Treasury Bond Rate, imputed on their beginning balance. In addition, all Plan participants are credited with their present value of accrued benefit under the traditional Defined Benefit Plan.

For benefits accrued prior to January 1, 2009, a participant's interest becomes fully vested after completion of five years of service. For benefits accrued on or after January 1, 2009, a participant’s interest becomes fully vested after completion of three years of service.

As of January 1, 2009 the Plan has been frozen and there will be no new entrants.

The Palms has established a separate qualified trust, under IRC Section 401 for the Plan. The assets of the Plan may only be distributed to plan participants, and therefore, they are not included in these financial statements. Plan assets are invested in cash and debt and equity securities whose values are subject to fluctuations of the securities markets. Changes in these values attributable to the differences between actual and assumed returns on plan assets are defined as unrecognized gains or losses and are included in the determination of the net pension expense over time. The Palms uses a June 30 measurement date for its plan.

A summary of the plan, amounts reflected in the statements of financial position, and the components of net periodic pension cost as of the date of the latest valuation is as follows:

	2017	2016
Change in benefit obligation:		
Benefit obligation-beginning of year	$ 5,484,775	$ 6,153,574
Service Cost	262,921	317,866
Interest Cost	224,768	265,292
Benefits Paid	(475,416)	(1,590,543)
Actuarial loss	(403,628)	338,586
Benefit obligation- end of year	$ 5,093,420	$ 5,484,775
Change in plan assets:		
Fair value of assets- beginning of year	$ 4,524,179	$ 5,803,302
Actual return on plan assets	465,687	111,420
Employer contribution	200,000	200,000
Benefits paid	(475,416)	(1,590,543)
Fair value of assets- end of year	$ 4,714,450	$ 4,524,179
Funded status	$ (378,970)	$ (960,596)
Amounts Recognized in the statement of financial position are included in:		
Accounts payable and accrued liabilities	$ (378,970)	$ (960,596)
Amounts recognized in accumulated unrestricted net assets consist of:		
Actuarial loss	$ 1,116,509	$ 1,787,703
Source of change in the statement of net activities consist of:		
Actuarial (gain) loss arising during period	$ (671,194)	$ 574,119
Components of net periodic benefit cost:		
Service Cost	$ 262,921	$ 317,866
Interest Cost	224,768	265,292
Expected return on plan assets	(309,964)	(398,658)
Amortization of prior service cost	N/A	N/A
Amortization of loss	111,843	51,705
Benefit obligation- end of year	$ 289,568	$ 236,205

Accumulated Benefit Obligation

The accumulated benefit obligation for the Palms was $5,093,420 and $5,484,775 on June 30, 2017 and 2016, respectively. Accounting principles generally accepted in the United States of America require the recognition of an additional liability in the amount of the unfunded accumulated benefit obligation, with an equal amount to be recognized as an intangible asset, provided that the asset recognized shall not exceed the amount of unrecognized prior service cost and unrecognized transition obligation. Any additional amounts are charged to unrestricted net assets.

Weighted-average assumptions used to determine benefit obligations at June 30, 2017 and 2016, are as follows:

	2017	2016
Discount rate (on benefit obligations)	4.50%	4.25%
Expected long-term rate of return on plan assets	7.00%	7.00%
Rate of compensation increase	2.50%	2.50%

Weighted-average assumptions used to determine net periodic pension cost at June 30, 2017 and 2016, are as follows:

	2017	2016
Discount rate (on net periodic costs)	4.25%	4.50%
Expected long-term rate of return on plan assets	7.00%	7.00%
Rate of compensation increase	2.50%	3.00%

The Palms employs a vigorous process to determine the estimates of expected long-term rate of return on assets. The estimates are primarily driven by actual historical asset-class returns and advice from external actuarial firms while incorporating specific assets-class risk factors, such as the variation of the annual rate of return as compared to the average expected rate of return.

The Plan invests primarily in asset categories with sufficient size, liquidity, and cost efficiency to permit investments of reasonable size. The Plan invests in asset categories that provide diversification benefits and are easily measured. Maximum and minimum holding ranges for each of these asset categories are set by the Board of Trustees. The current target allocations for cash management, equity, and fixed income are 5%, 60%, and 35%, respectively. Actual asset allocation within these approved ranges is based on a variety of economic and market conditions and consideration of specific asset category risk. To assess the Plan's investment performance, a long-term asset allocation policy benchmark has been established.

The fair value of the Plan's assets as of June 30, 2017 and 2016 by assets are as follows:

Plan Assets	2017	2016
Cash (Level 1)	$ 19,818	$ 38,040
Mutual funds (Level 1)	4,694,632	4,486,139
Total Plan Assets	$ 4,714,450	$ 4,524,179

Contributions

The Palms expects to contribute to the Plan the ERISA recommended amount of approximately $150,000 in the next year.

Estimated Future Benefit Payments

The estimated future benefit payments are as follows:

Years beginning July 1,	
2018	$ 308,001
2019	166,990
2020	277,112
2021	281,444
2022	184,744
2023-2027	1,683,352

Amount Expected to be Recognized in Net Periodic Benefit Costs

The estimated net actuarial loss that will be amortized from changes in unrestricted net assets into net periodic benefit cost in the year ended June 30, 2018 is $56,692.

Deferred Compensation Plan

On September 1, 2005, a nonqualified deferred compensation plan covering management or highly compensated employees as defined by ERISA was adopted by the Board of Trustees. This plan is not intended to be a qualified plan under Section 401(a) of the IRC, but is referred to as an 'eligible plan' pursuant to Section 457(b) of the IRC. The expense associated with this 457(b) plan was $46,052 and $42,381 in 2017 and 2016, respectively. The contributions to this plan are set aside in a grantor trust, but remains subject to the claims of creditors until distributed to the participants or beneficiaries.

401(k) Plan

The Palms has a 401(k) defined contribution plan, which covers employees with one year of service and who work at least 1,000 hours per year. The Palms contributes 10% of each employee's contributions. Employer contributions for the years ended June 30, 2017 and 2016, were $24,869 and $25,139, respectively.

NOTE 8 CONTINGENCIES

Workers' Compensation Self-Insurance

Effective December 12, 2002, the Palms entered into a contractual agreement to form Guardian Comp, Inc., which, through its risk-sharing provisions, provides insurance coverage for workers' compensation liability exposure. Guardian Comp, Inc. is a multi-organization insurance company for long-term care organizations incorporated under the laws of the state of California.

Guardian Comp, Inc. provides occurrence-based insurance coverage using a combination of self-insured retentions and excess commercial insurance coverage. Guardian Comp, Inc. has engaged the services of a professional actuarial consultant for the determination of premiums to be assessed to participants under the plan coverage. As a self-insurance administrator, Guardian Comp, Inc. enables risk sharing among participating long-term care organizations. The participants are required to pay assessed premiums. Insurance expense under the Guardian Comp, Inc. amounted to $837,675 and $712,645 in 2017 and 2016, respectively.

Litigation

The Palms is, from time to time, subject to litigation and claims arising in the normal course of business. In the opinion of management, the ultimate resolution of legal proceedings will not have a material adverse effect on the Palms' financial statements.

NOTE 9 LONG TERM DEBT

2014 Revenue Bonds

On July 17, 2014, the Palms issued $10,000,000 of Revenue Bonds sold through a private financing arrangement to finance the renovation of the skilled nursing facility. The bonds are payable beginning February 1, 2015, with annual payments scheduled through February 1, 2044.

The bonds have a 4.58% fixed rate of interest. Revenues are pledged to punctual payment of bond principal and interest.

The following table sets forth the amounts required to be made available at the principal payment date, for the payment of interest with respect to the Bonds and for the principal due, interest and total payments with respect to the Bonds:

Debt Service Due Fiscal Year Ended	Principal Payments Due Within Fiscal Year	Interest Components Due Within Fiscal Year	Total Payments
2018	$ 190,000	$ 449,756	$ 639,756
2019	200,000	441,054	641,054
2020	205,000	431,894	636,894
2021	220,000	422,505	642,505
2022	230,000	412,429	642,429
Thereafter	8,775,000	5,333,868	14,108,868
Total bond payable	9,820,000	$ 7,491,506	$ 17,311,506
Unamortized cost of issuance	(272,000)		
Net	$ 9,548,000		

2016 Revenue Bonds

In December 1, 2016, the Palms issued $20,435,000 in 2016 Tax-Exempt Revenue Bonds to refinance the 2007 Revenue Bonds. The Bonds require annual principal payments and semi-annual interest payments beginning February 1, 2017, with annual payments scheduled through February 1, 2037.

The bonds have a 3.63% fixed rate of interest. Revenues are pledged to punctual payment of bond principal and interest. The bonds are secured by gross revenues and real property in parity with the 2014 Revenue Bonds.

The following table sets forth the amounts required to be made available at the principal payment date, for the payment of interest with respect to the Bonds and for the principal due, interest and total payments with respect to the Bonds:

Debt Service Due Fiscal Year Ended	Principal Payments Due Within Fiscal Year	Interest Components Due Within Fiscal Year	Total Payments
2018	$ 720,000	$ 706,035	$ 1,426,035
2019	740,000	679,899	1,419,899
2020	775,000	653,037	1,428,037
2021	800,000	624,905	1,424,905
2022	830,000	595,865	1,425,865
Thereafter	15,585,000	4,623,894	20,208,894
Total bond payable	19,450,000	$ 7,883,635	$ 27,333,635
Unamortized cost of issuance	(299,015)		
Net	$ 19,150,985		

NOTE 10 REDEVELOPMENT PLAN OBLIGATION (AB1169 DISCLOSURE)

Bond debt is designated for master plan projects to meet the needs of the organization by providing additional housing and facilities for residents, which is consistent with the Palms' tax exempt status.

The bonded debt issuance of $20,435,000 refinanced original bonded debt of $28,000,000. The original debt was primarily designated for the Magnolia Court project, which was completed in 2009. As of June 30, 2017, related to the Magnolia Court project, proceeds were fully expended and included $24,898,534 for construction costs and $3,101,466 in issuance and debt service costs.

The bonded debt issuance of $10,000,000 is primarily designated for the skilled nursing facility renovation project. As of June 30, 2017, related to the skilled nursing facility renovation project, $6,528,733 has been expanded for project costs. In addition, as of June 30, 2017, the Palms had donor restricted and Board designated net assets, including debt financing proceeds, for project costs of $6,823,425. As of June 30, 2017, the Palms was committed under construction agreements for the skilled nursing facility renovation project totaling approximately $5,257,165.

NOTE 11 ENDOWMENT RESTRICTED ASSETS

The Palms' endowment consists of funds established to provide life care membership for seniors whose limited resources prevent their entry into the Palms without such assistance.

Interpretation of Relevant Law

The Board of Trustees of the Palms follows the Uniform Prudent Management of Institutional Funds Act (UPMIFA) in determining the fair value of the donor-restricted endowment fund absent explicit donor stipulations. As a result, the Palms classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Palms in a manner consistent with the standard of prudence prescribed by UPMIFA.

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

(1) The duration and preservation of the fund
(2) The purposes of the organization and the donor-restricted endowment fund
(3) General economic conditions

(4) The possible effect of inflation and deflation
(5) The expected total return from income and the appreciation of investments
(6) Other resources of the organization
(7) The investment policies of the organization.

Endowment Composition and Changes in Endowment Net Assets

Endowment net asset composition by type of fund as of June 30, 2017 and 2016 consisted of donor-restricted endowment funds; temporarily restricted subject to purpose restrictions of $1,667,430 and $1,314,168, respectively, and permanently restricted by explicit donor stipulation of $773,323. Changes in endowment net assets are reported in the statement of activities as temporarily restricted or permanently restricted activities as appropriate.

Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Palms to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature are reported in unrestricted net assets when applicable. There were no such deficiencies as of June 30, 2017 and 2016.

Return Objectives, Risk Parameters and Strategies Employed for Achieving Objectives

The Palms has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to the program supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Palms must hold in perpetuity. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to preserve and protect the assets by earning an appropriate return on the investments.

Spending Policy

The Palms has established a formal spending policy. Appropriations will be made only from accumulated investment earnings maintained as temporarily restricted net assets based on residents' financial needs. Endowment principal (permanently restricted net assets) will not be invaded for any purpose. As such, the Board of Trustees considers all relevant factors annually in determining the amount appropriated for expenditures. This is consistent with the Palms' objective to maintain the purchasing power of the endowment assets held in perpetuity as well as to provide additional real growth through investment return.

	Temporarily Restricted	Permanently Restricted	Totals
Endowment net assets, June 30, 2015	$ 1,305,932	$ 773,323	$ 2,079,255
Investment income	90,657	-	90,657
Net appreciation (realized and unrealized)	(82,421)	-	(82,421)
Endowment net assets, June 30, 2016	1,314,168	773,323	2,087,491
Investment income	63,156	-	63,156
Net appreciation (realized and unrealized)	210,883	-	210,883
Endowment net assets, June 30, 2017	$ 1,588,207	$ 773,323	$ 2,361,530

NOTE 12 PATIENT SERVICE REVENUE

A substantial portion of the Palms' revenue for health care services is provided on behalf of patients under Medi-Cal and Medicare programs. The major sources of revenue are as follows:

	2017	2016
Patient service revenue:		
Medi-Cal program	$ 3,458,194	$ 5,570,371
Medicare program	1,838,098	1,935,041
Managed care	418,579	160,550
Other	3,163,638	3,139,724
Total patient service revenue	8,878,509	10,805,686
Less: contractual provisions	(2,157,788)	(3,625,699)
Less: bad debt expense:		
Medi-Cal program	(24,116)	(58,894)
Medicare program	(26,374)	(50,575)
Managed care	(14,791)	(6,063)
Other	(22,273)	(64,448)
Total bad debt expense	(87,554)	(179,980)
Net patient service revenue	$ 6,633,167	$ 7,000,007

For the year ended June 30, 2017, the Palms derived, net of contractual adjustments, 31% of its patient service revenue from Medi-Cal, 19% from Medicare, 3% from Managed Care and 47% from other sources. For the year ended June 30, 2016 the Palms derived, net of contractual adjustments, 38% of its patient service revenue from Medi-Cal, 18% from Medicare, 1% from Managed Care and 43% from other sources. The aggregate amount due from Medi-Cal, Medicare and Managed Care at June 30, 2017 and 2016, is $827,049 and $990,302, respectively.

Funds received from the Medi-Cal and Medicare programs are subject to governmental audit, which could result in retroactive adjustments. At this time, management is not aware of any ongoing or pending audits.

NOTE 13 CLASSIFICATION OF EXPENSES

2017	Programs: Board and Care	Programs: Skilled Nursing Facility	Total
Resident Care	$ -	$ 5,288,937	$ 5,288,937
Assisted resident living	826,711	-	826,711
General and administrative	3,063,531	1,270,236	4,333,767
Engineering and plant	882,070	248,789	1,130,859
Dietary	1,640,234	680,034	2,320,268
Housekeeping	640,811	180,741	821,552
Depreciation	928,553	261,900	1,190,453
Bond Interest	1,342,978	-	1,342,978
Members' interest	91,725	-	91,725
Total expenses	$ 9,416,613	$ 7,930,637	$ 17,347,250

2016	Programs: Board and Care	Programs: Skilled Nursing Facility	Total
Resident Care	$ -	$ 5,219,543	$ 5,219,543
Assisted resident living	777,166	-	777,166
General and administrative	2,811,661	1,455,229	4,266,890
Engineering and plant	903,254	254,764	1,158,018
Dietary	1,544,562	799,265	2,343,827
Housekeeping	623,154	175,762	798,916
Depreciation	884,049	249,347	1,133,396
Bond Interest	1,634,684	-	1,634,684
Members' interest	103,970	-	103,970
Total expenses	$ 9,282,500	$ 8,153,910	$ 17,436,410