EXCEPTIONAL CHILDREN'S FOUNDATION
AND AFFILIATES

CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED JUNE 30, 2014

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CERTIFIED PUBLIC ACCOUNTANTS | BUSINESS ADVISORS

INDEPENDENT AUDITORS' REPORT

Board of Directors
EXCEPTIONAL CHILDREN'S FOUNDATION AND AFFILIATES
Culver City, California

We have audited the accompanying consolidated financial statements of Exceptional Children's Foundation and Affiliates (collectively, "ECF"), which comprise the consolidated statement of financial position as of June 30, 2014, and the related consolidated statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"); this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated 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 consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the U.S. ("U.S. GAAS") and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the U.S. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Exceptional Children's Foundation and Affiliates as of June 30, 2014, and the changes in its net assets and its cash flows for the year then ended in accordance with U.S. GAAP.

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rbz, LLP

INDEPENDENT AUDITORS' REPORT (Continued)

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 25, 2014, on our consideration of ECF's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering ECF's internal control over financial reporting and compliance.

RBZ, LLP

November 25, 2014

EXCEPTIONAL CHILDREN'S FOUNDATION AND AFFILIATES

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

JUNE 30, 2014

ASSETS

Current Assets	
Cash and cash equivalents	$ 542,834
Investments, including current appropriation from endowment	2,396,733
Accounts receivable, net	2,887,135
Inventory	135,077
Prepaid expenses and other current assets	261,288
Land and building held for sale, net	4,552,699
Deferred financing costs, net	82,105
	10,857,871
Other Assets	
Endowment investments, net of current appropriation	9,392,535
Pledges receivable, net of current portion	300,000
Restricted deposits and funded reserves	380,205
Fixed assets, net	13,660,430
	23,733,170
	$ 34,591,041

See accompanying notes to consolidated financial statements.

EXCEPTIONAL CHILDREN'S FOUNDATION AND AFFILIATES

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

JUNE 30, 2014

LIABILITIES AND NET ASSETS

Current Liabilities	
Lines of credit	$ 3,885,449
Current portion of long-term debt	1,538,613
Accounts payable and accrued expenses	1,781,087
	7,205,149
Long-Term Debt, net of current portion	2,740,511
Total Liabilities	9,945,660
Commitments and Contingencies (Notes 6 and 14)	
Net Assets	
Unrestricted	
General	2,685,508
Board-designated	9,060,457
Designated for land and buildings	10,705,595
	22,451,560
Temporarily restricted	1,193,821
Permanently restricted	1,000,000
Total Net Assets	24,645,381
	$ 34,591,041

See accompanying notes to consolidated financial statements.

EXCEPTIONAL CHILDREN'S FOUNDATION AND AFFILIATES

CONSOLIDATED STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2014

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Public Support				
Contributions	$ 1,413,662	$ 321,033	$ -	$ 1,734,695
Fundraising events, net of costs of direct benefits of $14,055	129,725	16,000	-	145,725
Net Assets Released from Restrictions	524,398	(524,398)	-	-
	2,067,785	(187,365)	-	1,880,420
Revenue, Gains, and Losses				
Tuition and fees	18,303,424	-	-	18,303,424
Contract sales	1,762,573	-	-	1,762,573
Rents	700,941	-	-	700,941
Merchandise sales	48,030	-	-	48,030
Interest and dividends, net	193,059	2,105	19,157	214,321
Realized gains on sales of investments	215,929	2,364	21,512	239,805
Unrealized gains on investments	922,809	10,104	91,935	1,024,848
Reclassification of investment earnings	-	132,604	(132,604)	-
Miscellaneous	102,341	-	-	102,341
	22,249,106	147,177	-	22,396,283
	24,316,891	(40,188)	-	24,276,703
Functional Expenses				
Program services	22,400,065	-	-	22,400,065
Management and general	2,346,024	-	-	2,346,024
Fundraising	569,210	-	-	569,210
	25,315,299	-	-	25,315,299
Changes in Net Assets	(998,408)	(40,188)	-	(1,038,596)
Net Assets, beginning of year	23,449,968	1,234,009	1,000,000	25,683,977
Net Assets, end of year	$ 22,451,560	$ 1,193,821	$ 1,000,000	$ 24,645,381

See accompanying notes to consolidated financial statements.

EXCEPTIONAL CHILDREN'S FOUNDATION AND AFFILIATES

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES

FOR THE YEAR ENDED JUNE 30, 2014

	Program Services	Management and General	Fundraising	Total
Personnel Expenses				
Rehab and administration				
Salaries	$ 12,564,013	$ 1,401,084	$ 405,142	$ 14,370,239
Payroll taxes	1,027,439	105,752	32,025	1,165,216
Employee benefits	1,601,568	117,074	23,896	1,742,538
Client payroll				
Payroll	791,419	-	-	791,419
Payroll taxes	60,544	-	-	60,544
Employee benefits	282,929	-	-	282,929
	16,327,912	1,623,910	461,063	18,412,885
Other Expenses				
Agency support	13,914	741	112	14,767
Bad debt	-	24,517	-	24,517
Depreciation and amortization	800,939	21,883	7,754	830,576
Equipment rental and maintenance	146,755	6,819	2,474	156,048
Events and publications	5,870	358	7,125	13,353
Facility maintenance	457,742	8,352	1,613	467,707
Facility rent	368,665	2,286	-	370,951
Insurance	130,222	87,572	1,398	219,192
Interest	281,821	49,718	2,349	333,888
Licenses and fees	86,352	14,382	425	101,159
Miscellaneous	126,257	51,856	5,321	183,434
Office supplies	104,231	20,693	9,816	134,740
Other production costs	197,207	-	-	197,207
Production related	287,633	-	-	287,633
Professional services	874,456	285,270	26,916	1,186,642
Program supplies	445,717	-	-	445,717
Staff mileage	102,074	2,553	607	105,234
Staff support services	139,604	120,295	1,309	261,208
Staff training and development	43,838	3,310	2,050	49,198
Telephone	199,398	14,352	37,111	250,861
Transportation and auto	913,213	-	-	913,213
Utilities	346,245	7,157	1,767	355,169
	$ 22,400,065	$ 2,346,024	$ 569,210	$ 25,315,299

See accompanying notes to consolidated financial statements.

EXCEPTIONAL CHILDREN'S FOUNDATION AND AFFILIATES

CONSOLIDATED STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED JUNE 30, 2014

Cash Flows from Operating Activities	
Changes in net assets	$ (1,038,596)
Adjustments to reconcile changes in net assets to net cash used in operating activities	
Depreciation and amortization	830,576
Increase in allowance for doubtful accounts	60,000
Realized gains on sales of investments	(239,805)
Unrealized gains on investments	(1,024,848)
(Increase) decrease in operating assets	
Accounts receivable	(186,767)
Pledges receivable	392,500
Inventory	24,697
Prepaid expenses and other current assets	(130,996)
Security deposits	36,529
Increase (decrease) in operating liabilities	
Accounts payable and accrued expenses	401,315
Net Cash Used in Operating Activities	(875,395)
Cash Flows from Investing Activities	
Proceeds from sales of investments	3,958,655
Purchases of investments	(3,522,219)
Withdrawals from restricted deposits and funded reserves	250,809
Payments to and interest earned on restricted deposits and funded reserves	(285,507)
Purchases of fixed assets	(681,553)
Net Cash Used in Investing Activities	(279,815)
Cash Flows from Financing Activities	
Net borrowings (payments) on lines of credit	1,632,638
Principal payments on long-term debt	(686,056)
Net Cash Provided by Financing Activities	946,582
Net Decrease in Cash and Cash Equivalents	(208,628)
Cash and Cash Equivalents, beginning of year	751,462
Cash and Cash Equivalents, end of year	$ 542,834

See accompanying notes to consolidated financial statements.

EXCEPTIONAL CHILDREN'S FOUNDATION AND AFFILIATES

CONSOLIDATED STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED JUNE 30, 2014

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION

Cash Paid during the Year for Interest	$ 327,554

SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES

Transfer of fixed assets to land and building held for sale	$ 4,552,699
Conversion of line of credit balance to note payable	$ 772,444

See accompanying notes to consolidated financial statements.

NOTE 1 - NATURE OF OPERATIONS

Exceptional Children's Foundation and its affiliates, Valverde, Inc. and ERAS Home II (collectively, "ECF") are California tax-exempt nonprofit corporations whose mission is to provide the highest quality services for children and adults who are challenged with developmental, learning, and emotional disabilities empowering them to reach their greatest potential. ECF provides a wide range of programs and services to infants, youths, adults, and their families each year. People served include individuals with learning disabilities, intellectual disabilities, cerebral palsy, epilepsy, autism, and related conditions. ECF has 15 program sites located throughout Los Angeles County.

ECF programs are as follows:

Kayne ERAS Center

The Kayne Eras Center ("KEC") is a large multi-service center serving children and their families each year through its mental health, and special education programs and services. Based in Culver City, California, KEC provides the highest quality educational programs and therapeutic services to meet the needs of students with special learning, emotional and developmental challenges. KEC's state-certified and Western Association of Schools and Colleges-accredited K-12 nonpublic school provides special education services to students from school districts throughout greater Los Angeles. KEC also includes on-site and home-based mental health as well as diagnostic and therapeutic services.

Programs and services provided by KEC include:

- Therapeutic creative enrichment programs
- Specialized speech, behavioral and educational therapy services
- Physical education and recreational services
- Specialized full day classroom programs
- Mental health programs

Early Start

The Early Start program provides early intervention services to developmentally delayed children and their families in central Los Angeles and the San Fernando Valley communities of Southern California. Early Start offers center-based and home visit services for infants and toddlers from birth to age three who are developmentally delayed and/or disabled. The program includes a variety of therapies and structured activities designed to help young children develop language, gross and fine motor, cognitive and social skills.

NOTE 1 - NATURE OF OPERATIONS (Continued)

Developmental Activity Centers

Developmental Activity Centers in Culver City and Los Angeles offer adults with moderate to profound developmental disabilities an opportunity to build self-care and social skills, volunteer in the community and enjoy craft activities and recreational outings in a creative learning environment.

Art Centers

With studios in Culver City, San Pedro, Downtown and South Los Angeles, the Art Center program encourages, assists and supports the maximum personal artistic development for adults with developmental disabilities. The Art Center program is nationally recognized for its leadership in demonstrating that individuals with developmental disabilities can often produce fine art. In addition to providing art instruction, the program markets and sells the artists' work.

Work Activity

At two Packaging Assembly and Rework ("PAR") Work Activity sites in Culver City and Santa Fe Springs, California, adults learn good work habits and appropriate social skills while meeting governmental and private contract requirements for packaging, assembly, and rework. The program provides facility based vocational training and paid work to improve earning potential and independent functioning of persons with developmental disabilities and to promote transition to community employment settings.

Supported Employment

Adults with developmental disabilities and acquired brain injuries receive community integrated job placement, on the job training, and support services through supported employment. For program participants, this is a much awaited gateway to greater independence. Under the supervision of an ECF job coach, participants are hired by local businesses to perform a variety of tasks including (but not limited to) clerical, janitorial, and food service assignments.

NOTE 1 - NATURE OF OPERATIONS (Continued)

Residential Services

Residential Services provide adults with developmental disabilities the opportunity to live in the community with the level of support each person needs to optimize his or her quality of life. ECF operates six different residential facilities, including group homes and independent living centers for individuals located in Los Angeles, Whittier, and Culver City, California. Four of ECF's residential facilities (the "HUD Projects") are funded by the U.S. Department of Housing and Urban Development ("HUD") to benefit people living with developmental disabilities. Permanent financing for the HUD Projects is provided by HUD under Sections 202 and 811 of the Housing Act of 1959, which regulates the HUD Projects with respect to their rents and operating methods. The HUD Projects also receive HUD Sections 8 and 811 housing assistance and project rental assistance payments. The four HUD Projects are as follows:

Valverde
HUD Project No. 122-EH310-WHH-L8
A 12-bed group home in Los Angeles, California.

Westington
HUD Project No. 122-EH151-WHC-L8
A 13-unit apartment complex in Los Angeles, California.

Whittier Springs
HUD Project No. 122-EH157-WHC-L8
A 13-unit apartment complex in Whittier, California.

ERAS Home II
HUD Project No. 122-HD044-WDD-NP
A 6-bed group home in Culver City, California.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Income Tax Status

ECF is comprised of three nonprofit public benefit corporations organized under the laws of California and, as such, are exempt from federal and state income taxes under Internal Revenue Code ("IRC") Section 501(c)(3) and corresponding state provisions.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Tax Status (Continued)

The federal informational tax returns of Exceptional Children's Foundation, Valverde, Inc., and ERAS Home II for tax years ended June 30, 2011, and subsequent remain subject to examination by the Internal Revenue Service. The returns for California, ECF's only state tax jurisdiction, remain subject to examination by the California Franchise Tax Board for tax years ended June 30, 2010, and subsequent.

Basis of Consolidation

The accompanying consolidated financial statements include the accounts of Exceptional Children's Foundation, Valverde, Inc., and ERAS Home II. All significant inter-agency transactions and balances have been eliminated in consolidation.

Financial Statement Presentation

ECF reports information regarding its financial position and activities according to three classes of net assets: unrestricted, temporarily restricted and permanently restricted.

Unrestricted Net Assets, General - Include contributions, fundraising, fees, sales and other forms of revenue that are not restricted by the donor or grantor as well as expenditures related to the general operations of ECF.

Unrestricted Net Assets, Board-Designated - Include unrestricted net assets ECF's Board of Directors has segregated to be used for capital improvements, purchases, future projects, and operations.

Unrestricted Net Assets, Designated for Land and Buildings - Include unrestricted net assets designated for land and buildings in use, net of accumulated depreciation and debt secured by the land and building.

Temporarily Restricted Net Assets - Include contributions that are temporarily restricted by the donor or grantor. When the restriction expires, the net assets of this classification are reclassified to unrestricted net assets. Restricted contributions where restrictions are met in the same reporting period are classified as unrestricted.

Permanently Restricted Net Assets - Include contributions that have been restricted by the donor in perpetuity.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Use of Estimates

Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could differ from these estimates.

Cash and Cash Equivalents

ECF considers all highly-liquid financial instruments purchased with an original maturity of three months or less to be cash equivalents, except for certain money market account balances included in investments (see Note 3).

Cash Held-in-Trust

ECF maintains bank accounts, segregated from ECF's assets, for cash held-in-trust for clients. At June 30, 2014, the amount of such funds held-in-trust totaled $13,320. Balances in such accounts are insured by the Federal Deposit Insurance Corporation (FDIC) up to the applicable limits.

Investments

Investments are monitored by the Board of Directors' investment committee and are stated at fair value. Unrealized gains and losses are recognized aggregately. Realized gains and losses are recognized immediately upon sale and are computed using the specific identification method.

The Board of Directors has limited the use of investments such that investment principal cannot be used unless approved by a vote of 75% of the Board of Directors in attendance in person or telephonically.

Accounts Receivable

Accounts receivable are unsecured and ECF is at-risk to the extent that such amounts become uncollectible. Management anticipates it will collect substantially all of its accounts receivable balances; however, an allowance for doubtful accounts totaling $110,000 has been established as of June 30, 2014, based on management's concerns regarding the collectability of certain government agency receivables.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Pledges Receivable

The pledges receivable balance consists of unconditional promises to give monetary assets to ECF. Management anticipates it will collect 100% of the pledges receivable balance; thus no allowance for potentially uncollectible pledges has been established as of June 30, 2014.

Inventory

Inventory consists of paper products and is stated at cost (first-in, first-out), which approximates fair value.

Fixed Assets

Purchases of fixed assets are recorded at cost. Donated items are recorded at fair value when received. Depreciation and amortization on both purchased and donated items are recorded using the straight-line method over the shorter of the estimated useful life of the related asset or, for leasehold improvements, the term of the lease, as follows:

Buildings and improvements	10 - 40 years
Land improvements	40 years
Furniture and fixtures	3 - 5 years
Equipment (computer, transportation, and other)	5 - 7 years

Normal repairs and maintenance are expensed as incurred, whereas significant charges that materially increase values or extend useful lives are capitalized and depreciated over the estimated useful lives of the related assets.

Impairment of Long-Lived Assets

Management reviews each asset or asset group for impairment whenever events or circumstances indicate the carrying value of an asset or asset group may not be recoverable, but at least annually. No impairment provision was recorded by ECF during the year ended June 30, 2014.

Endowments

Net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor imposed restrictions.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Contributions

Contributions consist primarily of donations from foundations, businesses and the general public. Contributions are recorded when committed to ECF by the donor.

Wills and Trusts

In the past, ECF has been named as a beneficiary in a substantial number of wills and trusts. These contributions are recorded when estate proceeds become a liability of the estate and ECF has been so notified. Contributions in the form of irrevocable charitable remainder trusts are recognized when the trusts are established and ECF is named irrevocably as a beneficiary.

Functional Expenses

ECF allocates its expenses on a functional basis among its various programs and support services. Expenses that can be identified with a specific program or support service are allocated directly according to their natural expenditure classification. Other expenses that are common to several functions are allocated accordingly.

Concentration of Risk

Occasionally ECF's cash balances exceed FDIC-insured limits. ECF has not experienced and does not anticipate any losses related to these balances.

ECF had two major funding sources that comprised 21% and 15% of its revenue and 21% and 13%, respectively, of its accounts receivable at June 30, 2014. Management anticipates this funding will continue at present levels.

Subsequent Events

ECF has evaluated events subsequent to June 30, 2014, to assess the need for potential recognition or disclosure in the consolidated financial statements. Such events were evaluated through November 25, 2014, the date the consolidated financial statements were available to be issued. Based upon this evaluation, it was determined no subsequent events occurred that require recognition or additional disclosure in the consolidated financial statements, except as disclosed in Notes 5, 9 and 10.

NOTE 3 - INVESTMENTS

ECF reports its investments at fair value among three categories of price inputs available. These categories of inputs are quoted prices in active markets for identical assets (Level 1); significant other observable inputs (Level 2); and significant unobservable inputs (Level 3). The following table sets forth by level, within the fair value hierarchy, investments as of June 30, 2014:

	Level 1	Level 2	Level 3	Total
Exchange-traded and closed-end funds	$ 5,077,567	$ -	$ -	$ 5,077,567
Equities	2,718,950	-	-	2,718,950
Mutual funds	2,567,146	-	-	2,567,146
U.S. Government obligations	514,126	-	-	514,126
Corporate bonds	-	492,477	-	492,477
Money market accounts	231,941	-	-	231,941
U.S. Government-Agency obligations	-	187,061	-	187,061
	$ 11,109,730	$ 679,538	$ -	$ 11,789,268

Investments are reported on the consolidated statement of financial position as follows:

Investments, unrestricted	$ 1,521,733
Endowment investments, current appropriation	875,000
Endowment investments, net of current appropriation	9,392,535
	$ 11,789,268

Activity in the investments during the year was as follows:

Balance, beginning of year	$ 10,961,051
Purchases of investments	3,522,219
Proceeds from sales of investments	(3,958,655)
Realized gains on sales of investments	239,805
Unrealized gains on investments	1,024,848
	$ 11,789,268

NOTE 4 - PLEDGES RECEIVABLE

A pledge receivable totaling $300,000 is scheduled to be received in one to five years.

ECF has not discounted the pledge receivable as management has determined the impact is immaterial to the consolidated financial statements.

NOTE 5 - LAND AND BUILDING HELD FOR SALE

In April 2014, ECF determined the real estate market was at a record level and, after careful analysis, decided to sell its corporate office in Culver City, California, consisting of land and building totaling $4,552,699, net of accumulated depreciation totaling $2,537,276, and seek a new location.

As of November 25, 2014, a buyer has committed to purchasing the land and building held for sale, with escrow scheduled to close in May 2015. The land and building held for sale, the bond liability, and the corresponding deferred financing costs have all been reclassified to current assets and liabilities on the accompanying consolidated statement of financial position.

The contracted sales price is $22,300,000. A deposit of $4 million, of which $1 million is non-refundable, was received from the buyer by ECF on November 4, 2014. ECF used $815,024 to pay off its CHFFA Insured Revenue Bonds described in Note 10 and $2,584,976 was used to pay down the lines of credit described in Note 9. Upon close of escrow in May 2015, management plans to use the additional proceeds to add a minimum of $5 million to the board-designated endowment fund described in Note 13, purchase and renovate new property, and further reduce debt.

NOTE 6 - RESTRICTED DEPOSITS AND FUNDED RESERVES

Restricted deposits and funded reserves are as follows:

Bond Reserves		
ECF is required to make monthly deposits of $20,643 to bond reserve accounts for payments of principal, interest, mortgage insurance and administration of the bonds (see Note 10).	$	108,857
Replacement Reserves		
The HUD Projects are required to make monthly deposits to replacement reserves totaling $1,393 per month. In accordance with provisions of the regulatory agreements, the replacement reserves are to be used for the replacement of fixed assets with the prior approval of HUD.		144,186
Residual Receipts Reserves		
The HUD Projects are required to make annual deposits to the extent of their "surplus cash," as defined by HUD. In accordance with provisions of the regulatory agreements with HUD, the residual receipts reserve is to be used for major expenditures of the HUD Projects with the prior approval of HUD. The HUD Projects are reporting surplus cash totaling $11,932 as of June 30, 2014. As a result, this amount is required to be deposited into the residual receipts reserve during the year ending June 30, 2015.		82,778
Tenant Security Deposits		
The HUD Projects are required to maintain separate cash accounts for tenants' rental security deposits.		44,384
	$	380,205

NOTE 7 - FIXED ASSETS

Fixed assets consist of the following:

Buildings and improvements	$ 16,153,389
Land and improvements	5,153,266
Furniture and fixtures	3,491,155
Computer equipment	1,736,561
Transportation equipment	1,141,047
Leasehold improvements	566,964
	28,242,382
Accumulated depreciation and amortization	(14,581,952)
	$ 13,660,430

See Note 5 for additional information regarding fixed assets.

NOTE 8 - DEFERRED FINANCING COSTS

Deferred financing costs are recorded at cost and are amortized on a straight-line basis over the respective terms of the debt as follows:

Deferred financing costs	$ 247,879
Accumulated amortization	(165,774)
	$ 82,105

See Note 5 for additional information regarding deferred financing costs.

NOTE 9 - LINES OF CREDIT

ECF has a $4,000,000 revolving line of credit with Merrill Lynch Private Finance, Inc., with monthly payments of interest-only at the 1-month LIBOR (London InterBank Offered Rate) (.19428% at June 30, 2014) plus 1.25%. This line is secured by ECF's securities, cash and other assets held in a Merrill Lynch Trust Company account and is available for as long as ECF maintains sufficient investments in this account. The line of credit agreement contains various covenants including a requirement to maintain ECF's Merrill Lynch Trust Company account at a sufficient value to cover the outstanding balance. At June 30, 2014, $2,252,719 was outstanding on this line and ECF was in compliance with these covenants.

ECF has a $3,406,000 revolving line of credit agreement with Morgan Stanley, with monthly payments of interest-only at the 1-month LIBOR plus 1.25%. This line is secured by ECF's securities, cash and other assets held in a Morgan Stanley account and is available for as long as ECF maintains sufficient investments in this account. The line of credit agreement contains various covenants including a requirement to maintain ECF's Morgan Stanley account at a sufficient value to cover the outstanding balance. At June 30, 2014, $1,632,730 was outstanding on this line and ECF was in compliance with these covenants.

In connection with the $4 million deposit received from the buyer of the land and building held for sale described in Note 5, principal totaling $2,584,976 was paid on these lines of credit in November 2014.

NOTE 10 - LONG-TERM DEBT

Long-term debt is as follows:

Note payable to California United Bank, secured by KEC's land and building, with monthly principal and interest installments of $40,774. Interest is fixed at a rate of 5.125% through June 2016, at which time all outstanding principal and interest are due.	925,566
California Health Facilities Financing Authority ("CHFFA") Insured Revenue Bonds, 1995 Series A, secured by a deed of trust on ECF's headquarters' land and building, payable in monthly installments of $20,094, sufficient to pay semi-annual payments of bond interest (6.1%) and annual bond principal payments. This was paid off November 5, 2014 (see Note 5) and reported as a current liability at June 30, 2014.	936,466

NOTE 10 - LONG-TERM DEBT (Continued)

Note payable to Morgan Stanley, secured by investments held by Morgan Stanley, payable in monthly installments of $7,635, including interest at 3.426% through June 2020, at which time principal totaling approximately $260,000 is due or interest on this note can switch to a variable rate for 3 remaining years or a new fixed rate can be negotiated.	712,130
Note payable to HUD, secured by a first deed of trust on the Valverde 12-bed group home for the developmentally disabled, with living quarters for the site manager, payable in monthly installments of $4,501, including interest at 9.25%, through June 2026.	390,661
Note payable to HUD, secured by a first deed of trust on the Westington 13-unit apartment complex for the developmentally disabled, payable in monthly installments of $5,716, including interest at 9.25%, through March 2024.	444,136
Note payable to HUD, secured by a first deed of trust on the Whittier Springs 13-unit apartment complex for the developmentally disabled, payable in monthly installments of $5,988, including interest at 9.25%, through May 2024.	465,265
Capital advance from HUD, secured by a first deed of trust on the ERAS Home II 6-bed group home for the developmentally disabled, noninterest-bearing, with no payment due as long as ECF continues to provide housing to the developmentally disabled through Sept 2037.	404,900
	4,279,124
Current portion	(1,538,613)
	$ 2,740,511

NOTE 10 - LONG-TERM DEBT (Continued)

Future scheduled maturities of long-term debt are as follows:

Year Ending June 30,	
2015	$ 1,538,613
2016	629,380
2017	166,439
2018	178,047
2019	190,614
Thereafter	1,576,031
	$ 4,279,124

The monthly installment payments for the three notes payable to HUD (described above) are withheld by HUD from the monthly Section 8 vouchers payable by HUD to ECF (see Note 14).

NOTE 11 - EMPLOYEE BENEFIT PLANS

ECF offers IRC Sections 403(b) and 401(k) individual defined contribution plans for all eligible employees. The 401(k) plan is open to all employees except substitutes and temporary employees. Participants may make salary deferrals to their individual accounts up to the maximum allowable deferral amounts for defined contribution plans. ECF may make discretionary matching contributions to the 401(k) plan for eligible employees. ECF made a contribution of $106,593, or 1% of eligible employees' salaries, during the year.

The 403(b) plan is a non-ERISA plan designed for highly-compensated employees. Participants may make annual contributions up to the maximum allowable deferral amount for defined contribution plans.

NOTE 12 - NET ASSETS

Temporarily Restricted Net Assets

Temporarily restricted net assets and releases during the year are as follows:

	Released from Restrictions	Balance, June 30, 2014
Kayne Family Mortgage Pledge (time-restricted)	$ 300,000	$ 300,000
PAR Services	-	231,619
Unappropriated Earnings on Permanent Endowment (see Note 13)	50,000	207,078
Eisner Foundation	-	150,000
Emma Jane Meyers	-	135,490
Kayne Eras School	-	62,500
Dale Fukamaki Memorial Fund	7,500	43,816
Share, Inc.	13,333	18,667
Capital Group	-	15,000
Early Start Program	51,930	14,070
The Siragusa Foundation	1,134	6,366
Developmental - Carrie Estelle Doheny Foundation	2,815	4,185
Supported Employment - Doheney Foundation	-	3,000
CEO's Employee Development Fund	-	850
Women Helping Youth	18,926	597
Milken Foundation	7,927	583
California Community Foundation	42,500	-
Barman House	28,333	-
	$ 524,398	$ 1,193,821

NOTE 13 - ENDOWMENTS

ECF's endowments include both donor-restricted funds and funds designated by the Board of Directors to function as endowments.

Interpretation of Relevant Law

The Board of Directors of ECF has interpreted the California Uniform Prudent Management of Institutional Funds Act ("Cal UPMIFA") as requiring the preservation of the principal of donor-restricted endowment funds, absent further instructions. Earnings from the donor-permanently-restricted endowment fund are classified as temporarily restricted net assets until those amounts are appropriated for expenditure in a manner consistent with the standard of prudence prescribed by Cal UPMIFA.

In accordance with Cal UPMIFA, ECF 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 ECF 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 ECF

(7) The investment policies of ECF

Return Objectives and Risk Parameters

ECF has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowments while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds classified as permanently restricted net assets as well as board-designated funds. Under this policy, as reviewed and monitored by the Investment Committee and approved by the Board of Directors, the endowment assets are invested in a manner that is intended to produce results that do not underperform the price and yield results of a blended benchmark of broad based equity and fixed income indices. Actual returns in any given year may vary from this amount.

NOTE 13 - ENDOWMENTS (Continued)

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, ECF uses the total return methodology in which investment returns are achieved through either capital appreciation (realized and unrealized) or current yield (interest and dividends). ECF has a diversified asset allocation policy that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and How Investment Objectives Relate to Spending Policy

Through the budget process, ECF each year appropriates a stated amount, not to exceed 5% of the average board-designated endowment balance, for operations and capital needs. Additional distributions can be made only with Board approval. ECF understands the current spending policy may reduce its board-designated endowment to the extent spending exceeds earnings in any period. From its donor-restricted endowment, ECF may spend a discretionary portion of its annual current earnings, not to exceed 7% per year on a cumulative basis. In establishing this policy, ECF considers the long term expected return on its endowment. ECF is required to maintain the initial principal balance ($1,000,000) of the donor-restricted endowment assets.

Endowment Net Asset Composition by Type of Fund

	Unrestricted Board-Designated	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	$ -	$ 207,078	$ 1,000,000	$ 1,207,078
Board-designated endowment funds	9,060,457	-	-	9,060,457
	$ 9,060,457	$ 207,078	$ 1,000,000	$10,267,535

NOTE 13 - ENDOWMENTS (Continued)

Changes in Endowment Net Assets

	Unrestricted Board-Designated	Temporarily Restricted	Permanently Restricted	Total
Balance, July 1, 2013	$ 8,529,427	$ 109,901	$ 1,000,000	$ 9,639,328
Investment return				
Investment income	228,132	2,939	26,747	257,818
Investment fees	(64,735)	(834)	(7,590)	(73,159)
Net realized and unrealized gains	967,633	12,468	113,447	1,093,548
Reclassification of investment earnings	-	132,604	(132,604)	-
Amounts expended during the year for operational and program expenses	(600,000)	(50,000)	-	(650,000)
Balance, June 30, 2014	$ 9,060,457	$ 207,078	$ 1,000,000	$10,267,535

NOTE 14 - COMMITMENTS AND CONTINGENCIES

Lease Commitments

ECF leases facilities and equipment under several long-term operating lease agreements. Future required minimum lease payments are as follows:

Year Ending June 30,	
2015	$ 85,550
2016	86,457
2017	110,000
2018	116,373
2019	136,980
Thereafter	681,671
	$ 1,217,031

Rent expense, comprised of facilities, equipment, buses and uniforms totaled $515,210 for the year.

NOTE 14 - COMMITMENTS AND CONTINGENCIES (Continued)

HUD Section 8 Housing Assistance Payments Contracts, Section 811 Project Rental Assistance Contract

Each of the HUD Projects has entered into either a Section 8 Housing Assistance Payments ("HAP") Contract or a Section 811 Project Rental Assistance Contract ("PRAC"). The amount earned under the three HAP contracts totaled $419,963 for the year. The amount earned under the PRAC contract totaled $15,930 for the year.

These contracts provide for a maximum annual rent supplement payment by HUD to the HUD Projects. This maximum annual rent supplement payment is subject to adjustment if there is any change in contract rent, number of contract units or family income of the tenant.

Congress has determined not to renew HAP contracts on a long-term basis. Future renewals of terminating HAP contracts will generally be for a period of one to five years and will tend to be at or below comparable market rate rents in the HUD Projects' areas. It cannot be determined what ultimate effect this may have on the HUD Projects' future rental revenue and operations.

Contingent Promissory Note

ECF had a conditional noninterest-bearing promissory note payable to the State of California Department of Housing and Community Development ("CA HCD"), secured by the real estate of ERAS Home I. The terms of the note agreement required ECF to provide housing to the developmentally disabled. For as long as ECF complies with the provisions of its regulatory agreement with CA HCD, the remaining principal was amortized at the rate of $20,000 annually until reduced to $0 during 2012, at which time the mortgage lien was to be released with no payments of principal or interest required. Management is currently working with CA HCD to effect the transfer of clear title to ECF.

Litigation

ECF is occasionally involved in litigation in the normal course of operations. At this time management is not aware of any material adverse financial consequences resulting from known litigation.