

CHILDREN'S DAY SCHOOL

JUNE 30, 2019

INDEPENDENT AUDITORS' REPORT

AND

FINANCIAL STATEMENTS

Children's Day School

Independent Auditors' Report and Financial Statements

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A Century Strong

Independent Auditors' Report

THE BOARD OF TRUSTEES
CHILDREN'S DAY SCHOOL
San Francisco, California

Report on the Financial Statements

We have audited the accompanying financial statements of **CHILDREN'S DAY SCHOOL (the School)** which comprise the statement of financial position as of June 30, 2019, the related statements of activities and changes in net assets 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material 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 School as of June 30, 2019, and the changes in net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited the School's 2018 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated October 22, 2018. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2018, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Hood & Strong LLP

San Francisco, California
September 25, 2019

Children's Day School

Statement of Financial Position

<i>June 30, 2019 (with comparative totals for 2018)</i>	2019	2018
Assets:		
Cash and cash equivalents	\$ 10,542,741	\$ 8,103,599
Investments	1,011,201	4,560,851
Prepaid expenses and other assets	138,166	421,998
Pledges receivable, net	249,450	747,981
School facilities, net	33,905,715	32,012,754
Total assets	\$ 45,847,273	\$ 45,847,183
Liabilities and Net Assets		
Liabilities:		
Accounts payable and accrued expenses	\$ 1,526,717	\$ 2,168,685
Deferred tuition	6,508,099	6,398,387
Notes payable	2,463,543	2,703,216
Bonds payable, net	14,429,893	14,856,832
Total liabilities	24,928,252	26,127,120
Net Assets:		
Without restrictions	20,285,998	17,267,061
With restrictions	633,023	2,453,002
Total net assets	20,919,021	19,720,063
Total liabilities and net assets	\$ 45,847,273	\$ 45,847,183

See accompanying notes to financial statements.

Children's Day School

Statement of Activities and Changes in Net Assets

Year Ended June 30, 2019 (with comparative totals for 2018)

	2019			2018 Total
	Without Restrictions	With Restrictions	Total	
Revenue and Support:				
Tuition	\$ 15,872,260		\$ 15,872,260	\$ 14,868,660
Less: Financial assistance	(3,102,885)		(3,102,885)	(2,903,966)
Tuition, net	12,769,375		12,769,375	11,964,694
Contributions	901,654	\$ 262,334	1,163,988	1,138,603
Extended program fees	1,036,007		1,036,007	1,049,699
Interest income	141,288		141,288	90,722
Other income	93,241		93,241	140,230
Total revenue and support	14,941,565	262,334	15,203,899	14,383,948
Expenses:				
Educational program expenses	10,408,294		10,408,294	10,289,818
Extended program expenses	1,229,715		1,229,715	1,126,773
General and administrative expenses	1,379,151		1,379,151	1,392,390
Development expenses	821,949		821,949	797,319
Total expenses	13,839,109	-	13,839,109	13,606,300
Change in Net Assets from Operations	1,102,456	262,334	1,364,790	777,648
Other Changes in Net Assets:				
Contributions to capital campaign		71,247	71,247	1,937,551
Change in value of interest rate swap	(237,079)		(237,079)	72,241
Net assets released from restrictions	2,153,560	(2,153,560)	-	-
Total Change in Net Assets	3,018,937	(1,819,979)	1,198,958	2,787,440
Net Assets - beginning of year	17,267,061	2,453,002	19,720,063	16,932,623
Net Assets - end of year	\$ 20,285,998	\$ 633,023	\$ 20,919,021	\$ 19,720,063

See accompanying notes to financial statements.

Children's Day School

Statement of Cash Flows

<i>Years Ended June 30, 2019 (with comparative totals for 2018)</i>	2019	2018
Cash Flows from Operating Activities:		
Change in net assets	\$ 1,198,958	\$ 2,787,440
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	1,213,681	1,115,296
Loss on disposal of fixed assets	13,006	
Contributions with donor restrictions	(333,580)	(1,879,039)
Unrealized loss (gain) on interest rate swap	237,079	(72,241)
Changes in:		
Prepaid expenses and other assets	46,752	(1,931)
Accounts payable and accrued expenses	(641,967)	827,798
Deferred tuition	109,712	134,680
Net cash provided by operating activities	1,843,641	2,912,003
Cash Flows from Investing Activities:		
Purchase of property and equipment	(3,107,187)	(2,419,040)
Purchase of investments	(31,934)	(2,550,899)
Proceeds from sale of fixed assets	600	
Proceeds from sale of investments	3,581,585	
Net cash provided (used) by investing activities	443,064	(4,969,939)
Cash Flows from Financing Activities:		
Principal payments on note payable	(239,673)	(230,633)
Principal payments on bonds payable	(440,000)	(430,000)
Collection of capital campaign gifts	832,110	1,368,778
Net cash provided by financing activities	152,437	708,145
Net Change in Cash and Cash Equivalents	2,439,142	(1,349,790)
Cash and Cash Equivalents - beginning of year	8,103,599	9,453,389
Cash and Cash Equivalents - end of year	\$ 10,542,741	\$ 8,103,599
Supplemental Disclosure for Cash Flow Information:		
Cash paid for interest	\$ 518,170	\$ 537,682
Accrued capital expenditures included in accounts payable	\$ 181,660	\$ 656,764

See accompanying notes to financial statements.

Children's Day School

Notes to Financial Statements

Note 1 - Organization and Summary of Significant Accounting Policies:

Children's Day School (the School) is an independent school located in San Francisco, California. The School provides quality education to children in pre-school through eighth grade as well as a year-round extended care program.

Significant accounting policies include the following:

a. Basis of Accounting and Presentation

The financial statements have been prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles applicable (U.S. GAAP) to not-for-profit entities. The School reports information regarding its financial position and activities according to two classes of net assets: those without restrictions and those with restrictions.

Net assets without restrictions

The portion of net assets that are not restricted by donor-imposed stipulations. These net assets are intended for use by management and the board of directors for educational programs, school scholarships, maintenance and general operations.

Net assets with restrictions

The portion of net assets for which use by the School is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the School.

b. Revenue Recognition

- Tuition is recognized, net of sliding scale tuition, during the applicable school year. Tuition amounts received for the 2019-2020 school year as of June 30, 2019 are recorded as deferred tuition.
- Contributions and pledges are recognized at their estimated fair value as revenue when they are received or unconditionally pledged. Contributions that are restricted by the donor are reported as an increase in net assets without restriction if the restriction expires in the reporting period in which the support is recognized. All other donor-restricted contributions are reported as increases in net assets with restrictions depending upon the nature of the restrictions. When a restriction expires, restricted net assets are reclassified to net assets without restrictions.

Children's Day School

Notes to Financial Statements

The School uses the allowance method to account for uncollectible tuition and contributions based on historical experience and an evaluation of the outstanding receivables at the end of the year.

c. Cash and Cash Equivalents

For purpose of the statement of cash flows, the School considers all highly liquid investments with an initial maturity of three months or less to be cash equivalents.

d. Restricted Cash

Restricted cash represents cash that is pledged collateral towards the School's line of credit in an equal amount \$1,500,000 and is included in cash and cash equivalents.

e. Investments

Investments consist of certificate of deposits that exceed 90 days. Interest income, realized and unrealized gains and losses are recorded as interest and investment income.

f. School Facilities

School facilities are stated at cost, or if donated, at estimated fair market value at the date of donation. Depreciation has been provided on the straight-line method over the estimated useful life of the assets of 3 to 40 years.

g. Bond Issuance Costs

Bond issuance costs are being amortized over the life of the bonds using the straight-line method, which approximates the effective yield method of amortization and are included as a reduction of bonds payable in the accompanying Statement of Financial Position.

h. Interest Rate Swap

The School entered into an interest rate swap agreement with a large, national financial institution to hedge against interest rate exposure associated with its variable rate debt. The swap is reported as either an asset or liability measured at its fair value. The change in fair value of the agreement is reported in the Statement of Activities.

i. Advertising Costs

The School expenses costs incurred for advertising when incurred.

Children's Day School

Notes to Financial Statements

j. Income Taxes

The School is a tax-exempt organization under Internal Revenue Service Code section 501(c)(3) and the California tax code.

The School's current accounting policy is to evaluate uncertain tax positions. Accordingly, a loss contingency is recognized when it is probable that a liability has been incurred as of the date of the financial statements and the amount of the loss can be reasonably estimated. Management evaluated the School's tax positions and concluded that the School had maintained its tax exempt status and had taken no uncertain tax positions that required adjustment to the financial statements.

k. Functional Allocation of Expenses

The costs of providing various programs and activities have been summarized on a functional basis in the Statement of Activities. Accordingly, certain costs have been allocated among the programs and supporting services that are benefited, based upon, time, costs estimates and usage.

l. Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

m. Fair Value Measurements

Fair Value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The School classifies its financial assets and liabilities measured at fair value on a recurring basis based on a fair value hierarchy with three levels of inputs. Level 1 values are based on unadjusted quoted prices in active markets for identical securities. Level 2 values are based on significant observable market inputs, such as quoted prices for similar securities and quoted prices in inactive markets. Level 3 values are based on significant unobservable inputs that reflect the School's determination of assumptions that market participants might reasonably use in valuing the securities. The valuation levels are not necessarily an indication of the risk or liquidity associated with the assets and liabilities measured at fair value.

n. Financial Statements and Reclassifications

The financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with U.S. GAAP. Accordingly, such information should be read in conjunction with the School's financial statements for the year ended June 30, 2018, from which the summarized information was derived.

Children's Day School

Notes to Financial Statements

Certain reclassifications have been made to the 2018 financial statements in order to conform to the 2019 presentation. These reclassifications had no impact on net assets or the change in net assets.

o. Recent Accounting Pronouncements

Pronouncements adopted:

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*, which changes presentation and disclosure requirements for nonprofit entities to provide more relevant information about their resources (and the changes in those resources) to donors, granters, creditors, and other users. These include qualitative and quantitative requirements in the following areas: net asset classes, investment return, functional expenses, and liquidity. Accordingly, the accounting change has been retrospectively applied to all periods presented with the exception of the omission of the liquidity, functional expenses and availability of resource information as permitted by the ASU.

The adoption of this standard resulted in additional footnote disclosures related to liquidity, functional expense, and changes to the classification of net assets and disclosures to net assets.

p. Subsequent Events

The School evaluated subsequent events from June 30, 2019 through September 25, 2019, the date these financial statements were available to be issued. There were no material subsequent events that required recognition or additional disclosure in these financial statements.

Note 2 - Investments:

At June 30, 2019, investments consist of certificates of deposit which management has assessed fair value at level 1.

Children's Day School

Notes to Financial Statements

Note 3 - Pledges Receivable:

The School is currently concluding a capital campaign for the renovation of a new campus facility and concluding a capital campaign for the update of an older facility.

Pledges receivable as of June 30, 2019 are due as follows:

Less than one year	\$ 277,150
Less allowance for doubtful pledges	(27,700)
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	\$ 249,450

Note 4 - School Facilities:

School facilities at June 30, 2019 consist of:

Land	\$ 5,850,000
Buildings and Improvements	34,425,298
Furniture and Equipment	1,525,852
Vehicles	3,500
Construction in progress	46,748
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	41,851,398
Less: accumulated depreciation	(7,945,683)
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	\$ 33,905,715

Depreciation expense was \$1,200,620 for the year ended June 30, 2019.

Children's Day School

Notes to Financial Statements

Note 5 - Debt:

Bond Financing:

In June 2010, the School authorized the issuance of California Municipal Finance Authority Revenue Bonds Series 2010 (2010 Bonds) in the aggregate principal amount of \$9,500,000. The 2010 Bonds are secured by deeds of trust on the real properties in which the School and administrative offices are located and by School income.

The 2010 Bonds bear interest at a rate of 3.087% per annum for a period ending June 30, 2015. The bonds were renewed July 1, 2015 at a rate of 2.9 percent per annum for a period ending June 30, 2022. Thereafter, the bonds shall accrue interest at an agreed upon rate as set forth in the agreement. Interest on the bonds is due monthly. The bond maturity date is July 1, 2039.

In July 2012, the School authorized the issuance of California Municipal Finance Authority Revenue Bonds Series 2012, Subseries A and B (2012A and 2012B Bonds), in the aggregate principal amount of \$7,500,000 to repay the bridge loan used to purchase and renovate 601 Dolores Street.

The 2012A Bonds in the amount of \$5,430,000 were funded on July 23, 2012, while the 2012B Bonds, in the amount of \$2,070,000 were funded during the construction of 601 Dolores Street in 2015. The bank incorporated the entire \$7,500,000 bond issuance at the rate of 2.807 percent with a refinance date of July 31, 2019. An interest rate swap agreement has been entered into that will be effective August 1, 2019. Interest on the bonds is due monthly. The final bond maturity date is August 1, 2042.

The 2010 and 2012 Bond Agreements include certain financial covenants. At June 30, 2019, the School is in compliance with all such covenants.

For the year ended June 30, 2019, interest paid on the 2010 and 2012 Bonds was \$234,046 and \$192,706, respectively.

Children's Day School

Notes to Financial Statements

Bonds payable at June 30, 2019:

June 30,	
2020	\$ 450,000
2021	475,000
2022	490,000
2023	505,000
2024	520,000
Thereafter	12,275,000
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	14,715,000
Less: debt issuance costs, net	(285,107)
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	\$ 14,429,893

In order to minimize the risk of interest rate movement on the bonds, the School entered into a swap agreement in connection with the bonds during the year ended, June 30, 2018, whereby it exchanged a variable rate of interest for a fixed rate of 1.61%.

The change in the value of the interest rate swap agreement is included in the accompanying Statement of Activities. As of June 30, 2019, the valuation of the interest swap resulted in a net unrealized loss in the amount of \$237,079. Domestic and international capital markets have experienced significant volatility. As a result, fluctuations in the fair value of interest rate swap may have occurred subsequent to June 30, 2019.

The fair value of the interest rate swap is included in prepaid expenses and other assets in the accompanying Statement of Financial Position and management has assessed fair value at Level 3.

Notes Payable:

The School signed a Construction Term Loan Agreement on February 23, 2015 totaling \$2,600,000 at 3.91% interest with US Bank National Association for completion of construction associated with the 601 Dolores Street property. Principal and interest payments are made monthly with a maturity date of February 23, 2020. As of June 30, 2019 the principal balance is \$1,763,542.

The School has notes payable to various parties totaling \$700,000 at 2% interest in connection with the completion of construction of the School's new facility located at 601 Dolores Street. All note holders signed Subordination Agreements making the notes subordinate to the outstanding bonds, bank loans, and other debt obligations through its maturity date of August 31, 2025.

The School has a \$1,500,000 revolving credit note with US Bank National Association secured by a deposit of an equal amount. The borrowing rate is 1% plus the one-month LIBOR rate and matures June 1, 2019. As of June 30, 2019 the principal balance is \$0.

Children's Day School

Notes to Financial Statements

Note 6 - Net Assets with restrictions:

Net assets are restricted for the following purposes as of June 30, 2019:

601 Dolores Campaign	\$	2,650
Elevating SJH Campaign		294,590
Founders Hall Lighting Project		10,000
Scholarships		93,411
Fund-A-Need		232,372
		<hr/>
	\$	633,023

Net assets of \$2,153,560 were released from donor restrictions during 2019 by incurring expenses and costs satisfying the restricted purposes.

Note 7 - Retirement Plan:

The School has a defined contribution retirement plan covering substantially all employees. Employee contributions up to 5% of their regular salary are matched by the School. Total contributions recognized as an expense by the School for the Plan were \$231,248 for the year ended June 30, 2019.

Deferred Compensation Plan

The School has a 457(b) deferred compensation plan that provides eligible employees with the opportunity to defer a portion of their compensation. Deferrals are made at the discretion of the participants, subject to certain limitations. Total participant deferrals, gains, interest, and employer contributions reflected in the accompanying Statement of Financial Position are \$150,947 as of June 30, 2019. The assets related to participant deferrals and employer contributions are available to the general creditors of the School and are included in prepaid expenses and other assets and accrued liabilities in the accompanying Statement of Financial Position.

Children's Day School

Notes to Financial Statements

Note 8 - Functional Classification of Expenses:

Educational Program and Extended Program Expenses

Expenses related to providing educational and extended care programs by functional classification are as follows for the year ended June 30, 2019:

Academic salaries and related expenses	\$ 7,470,122
Educational material and others	1,645,642
Auxiliary and other program expenses	958,147
Interest and depreciation expense	1,564,098
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	\$ 11,638,009

General and Administrative Expenses

Expenses pertaining to running the general operations of the School are as follows for the year ended June 30, 2019:

Salaries and benefits	\$ 828,979
Building and grounds	64,990
Development including salaries and related expenses	796,167
Professional services	213,258
Office supplies and expenses	143,014
Interest and depreciation expense	154,692
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	\$ 2,201,100

Children's Day School

Notes to Financial Statements

Note 9 - Availability of Financial Assets and Liquidity:

The following reflects the School's financial assets as of June 30, 2019, reduced by amounts not available for general use within one year of the balance sheet date because of contractual or donor-imposed restrictions or internal designations. Amounts not available include amounts set aside for long-term investing in the operating and capital reserves that could be drawn upon if the governing board approves that action.

Financial assets at year-end:	
Cash and cash equivalents	\$ 10,542,741
Investments	1,011,201
Receivables	249,450
<hr/>	
Total financial assets	11,803,392
Donor restricted net assets	(633,023)
Funds restricted by lender	(1,500,000)
Board designated for endowment	(205,292)
Board designated for operating reserves	(1,060,231)
Board designated for plant reserves	(960,000)
Board designated for refinancing reserves	(1,000,000)
<hr/>	
Financial assets available to meet cash needs for general expenditures within one year	\$ 6,444,846
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Note 10 - Concentration of Risk:

The School has defined its financial instruments, which are potentially subject to risk as cash and pledges receivable. The School maintains cash equivalents with commercial banks in excess of federally insured limits. Pledges receivable are unsecured and concentrated in the San Francisco Bay Area. However, concentrations of credit risk with respect to these receivables are limited due to the number of donors.