RiverWoods Exeter

A Roadmap for Evaluating a Continuing Care Retirement Community

In the past 14 years of my career, directing the financials for a family of not-for-profit Continuing Care Retirement Communities (CCRC), I have learned a great deal. As an accounting professional, with a background in for-profit manufacturing, I had to learn the ins and outs of a new financial structure.

What I have learned, and have been able to share with hundreds of residents and their financial advisors, is that though accounting principles don't change all that often, it does take some time, and some inside knowledge, to understand how to assess the financial strength of a CCRC.

The purpose of this white paper is to share what I have learned with others so that it is easier for you to analyze different communities' financial strength effectively. Clearly, when you consider a move to a CCRC, there are many criteria you are considering – location, space, the residents who are there, the reputation. My goal with this paper is to help you with due diligence so you ensure the community is financially stable, and able to weather future economic storms, as it will consume a portion of your assets.

There are approximately 1,900 Continuing Care Retirement Communities in the United States, and each community has a slightly different definition of services, many have different contracts and all have different costs. On top of that, there are different state regulations that govern the level and type of service provided. It's worth noting that more than 80% of these communities are non-profit.

For those of you who wish to delve deeper into the financials of a CCRC, we have created a separate white paper geared towards financial advisors that provides more in depth analysis.

What is a CCRC?

A Continuing Care Retirement Community is an over 62 retirement community that welcomes residents who can live independently and provides them the promise of community as well as the guarantee of providing future long-term health care needs within the community. CCRCs are insurance contracts, providing housing and nursing needs for a resident's life; not a real estate contact as is often misunderstood. Typically, CCRCs provide multiple levels of care; independent, assisted living, memory support, long term care and skilled nursing, so that a resident can be cared for during the full continuum of their life, without having to move. It is becoming more common to hear the term Life Plan community instead of CCRC.

What type of contract does the community offer?

There are predominantly three types of contracts in the CCRC industry:

1. **Type A (all-inclusive)** This contract provides the highest level of coverage, and consequently, typically has the highest entrance fees. In these communities, residents who

at some point require a higher level of care (Assisted Living or Nursing) move into those areas without an increase in fees. Type A contract monthly services fees carry the highest insurance component. In practice, independent residents' monthly service fees can be considered a partial "pre-pay" of their possible future health care costs, and are often tax deductible as a pre-paid medical expense.

1. **Type B (limited/ modified)** These contracts typically provide independent residents with the ability to move to Assisted Living or Nursing at no additional cost initially, but only for a limited amount of time. If the resident requires Assisted Living or Nursing services for a longer period, the monthly service fees will increase significantly. Type B contracts have a modified insurance component in the monthly service fees.
2. **Type C (rental)** Independent residents who require access to Assisted Living and/or Nursing do not benefit from any discounts. They will pay higher monthly services fees immediately upon entering the new level of care. Typically, there is no insurance component in a Type C contract.

Does the organization charge an entrance fee, and if so, is there a provision for an entrance fee refund?

The entrance fee is defined as a one-time, up-front payment that is paid to the organization when the contract is put in force. Typically, one will see larger entrance fees with Type A contracts because the monthly service fee with a Type A contract is the same regardless of IL, AL or Nursing care.

Refundability options can range from 100% refundable to declining balance (0%), with numerous variations in between. A declining balance contract starts out at 100% refundable but reduces by a set amount (amortizes) periodically over a defined period, typically, within 48 months. At the end of the defined time, no refund is owed.

When evaluating the refund provision, you should also understand its terms and conditions. What conditions need to be met for the refund to be paid? Is there a time limit? Is the refund amount limited by the re-sale proceeds of the unit to the next resident? What is the average length of time before a refund is processed?

Why is the entrance fee refund amount important?

The entrance fee refund is a key differentiator in many contracts. The terms of the contract are often dictated by the amount of refund, and one community will sometimes offer as many as four different contracts, based on refundability. Many seniors look at this as a component to their overall estate planning, as they see the higher refundability options to preserve their assets.

Understanding the audited financial statements.

CCRC financial statements can be daunting upon first blush. However, there are certain key areas to concentrate on that will help you digest the information. The two major schedules include Statement of Financial Position (also referred to as the Balance Sheet) and Statement of Operations and Changes in Net Assets (the Income Statement). **Cash Margin, Net Operating Margin** and **Cash to Debt** are three metrics to pay close attention to. A positive cash margin reflects the organization’s ability to cover its cash operating expenses with ongoing cash revenues. Net Operating Margin is a ratio that measures the core, sustainable business of on organization and focuses on cash revenues and cash expenses related to resident services. Investment earnings, interest expense and non-cash items are excluded. The Cash to Debt ratio is a common measure of an organization’s capital structure and a higher ratio reflects a better ability to withstand annual fluctuations in cash.

The Cash Flow statement is the third schedule you will find in the audited financials package and it details the “ins” and “outs” of the cash accounts. One area to pay attention to on this schedule is Purchases of Property and Equipment, found in the Investing Activities section. You will want to make sure that the organization is re-investing in its infrastructure, not only for the benefit of its current residents but also for future residents. Occupancy is the “life blood” of a CCRC and having an up to date campus is an important driver to staying full.

After the main financial schedules you will find the footnotes section. There is usually a wealth of knowledge here and it is highly recommended that you spend time reviewing these notes.

Other questions to ask a CCRC

Financial strength is reflected in the numbers of the CCRC but there are other measures to consider as well:

- Ask the CCRC for its historical and current occupancy figures as well as future projections. The industry considers 95% independent living occupancy as full since there are usually some units that are being refurbished for new residents.
- Ask to review a summary of the organization’s Comprehensive Actuarial Study, an analysis that provides important information on the long-term viability of the community.
- Is the CCRC accredited?
- Does the organization have a written financial philosophy and does it make sense to you?
- Does the CCRC have a credit rating from Fitch or S&P?
- Does the CCRC have residents on the board of trustees?
- Does the CCRC have a resident finance committee?
- What is the experience and tenure of senior management?
- How does the organization measure its financial performance? Benchmarks?
- Is the CFO/ Director of Finance willing to meet with you?

These indicators should provide you with information to assess the community’s financial strength. If you are interested in a more detailed analysis, we have an in-depth white paper geared toward financial advisors located at: (link).