

PALO ALTO UNIVERSITY, INC.

JULY 31, 2020 AND 2019

INDEPENDENT AUDITORS' REPORT

AND

FINANCIAL STATEMENTS

Palo Alto University, Inc.

Independent Auditors' Report and Financial Statements

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Independent Auditors' Report

THE BOARD OF TRUSTEES
PALO ALTO UNIVERSITY, INC.
Palo Alto, California

Report on the Financial Statements

We have audited the accompanying financial statements of **PALO ALTO UNIVERSITY, INC. (the University)** which comprise the statement of financial position as of July 31, 2020 and 2019, and the related statements of activities and change in net assets, functional expenses, and cash flows for the years then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the 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 University'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 University'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 University as of July 31, 2020 and 2019 and the change in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Hood & Strong LLP

San Francisco, California
December 8, 2020

Palo Alto University, Inc.

Statement of Financial Position

<i>July 31,</i>	2020	2019
Assets		
Current Assets:		
Cash and cash equivalents	\$ 10,522,927	\$ 10,939,827
Student receivables, net of allowance of \$881,314 for 2020 and \$793,723 for 2019	9,429,772	8,308,443
Contributions receivable, net	291,243	401,858
Grants receivable	669,147	516,402
Prepaid expenses and other assets	877,435	831,184
Total current assets	21,790,524	20,997,714
Investments	3,417,153	2,959,144
Contributions Receivable, net	20,610	78,720
Property and Equipment, net	8,329,001	8,646,668
Goodwill	573,000	573,000
Total assets	\$ 34,130,288	\$ 33,255,246
Liabilities and Net Assets		
Current Liabilities:		
Accounts payable and accrued expenses	\$ 2,901,450	\$ 3,384,860
Deferred revenue	10,357,617	9,547,125
Contingent consideration	413,000	413,000
Other liabilities	198,559	188,097
Total liabilities	13,870,626	13,533,082
Net Assets:		
Without donor restrictions	18,662,431	18,195,141
With donor restrictions	1,597,231	1,527,023
Total net assets	20,259,662	19,722,164
Total liabilities and net assets	\$ 34,130,288	\$ 33,255,246

See accompanying notes to financial statements.

Palo Alto University, Inc.

Statement of Activities and Change in Net Assets

For the Year Ended July 31,

	2020			2019		
	Without Donor Restrictions	With Donor Restrictions	Total	Without Donor Restrictions	With Donor Restrictions	Total
Revenues:						
Gross tuition	\$ 28,219,357		\$ 28,219,357	\$ 27,823,186		\$ 27,823,186
Gross fees	3,855,439		3,855,439	3,964,550		3,964,550
	32,074,796		32,074,796	31,787,736		31,787,736
Less financial aid	(1,411,600)		(1,411,600)	(965,423)		(965,423)
Net tuition and fees	30,663,196		30,663,196	30,822,313		30,822,313
Contributions	60,779	\$ 60,963	121,742	14,812	\$ 53,639	68,451
Grants	838,249		838,249	484,480		484,480
Investment income	267,439	175,969	443,408	385,745	(104,347)	281,398
Program services income	1,055,903		1,055,903	661,896		661,896
Other	230,202		230,202	188,759		188,759
Net assets released from restrictions	166,724	(166,724)	-	103,131	(103,131)	-
Total revenues	33,282,492	70,208	33,352,700	32,661,136	(153,839)	32,507,297
Expenses:						
Program services:						
Instruction	20,872,506		20,872,506	20,300,498		20,300,498
Student services	4,307,724		4,307,724	4,094,025		4,094,025
Supporting services:						
Institutional support	7,421,195		7,421,195	6,945,817		6,945,817
Development	213,777		213,777			-
Total expenses	32,815,202	-	32,815,202	31,340,340	-	31,340,340
Change in Net Assets	467,290	70,208	537,498	1,320,796	(153,839)	1,166,957
Net Assets, beginning of period	18,195,141	1,527,023	19,722,164	16,874,345	1,680,862	18,555,207
Net Assets, end of period	\$ 18,662,431	\$ 1,597,231	\$ 20,259,662	\$ 18,195,141	\$ 1,527,023	\$ 19,722,164

See accompanying notes to financial statements.

Palo Alto University, Inc.

Statement of Functional Expenses

For the Year Ended July 31, 2020

	Student Services				Institutional Support			Total Institutional Support	Development	Total
	Instruction	Library	Student Services	Total Student Services	General & Administrative	Sponsored Programs	Total Institutional Support			
Salaries and wages	\$ 12,382,517	\$ 440,513	\$ 1,980,395	\$ 2,420,908	\$ 2,776,250	\$ 656,162	\$ 3,432,412	\$ 152,556	\$ 18,388,393	
Benefits	2,009,397	83,854	338,666	422,520	505,103	79,691	584,794	24,246	3,040,957	
Consortium payments	3,437,528			-			-		3,437,528	
Consultants	674,596	5,158	60,088	65,246	636,854	88,762	725,616	7,510	1,472,968	
Rent	642,879			-	532,411	24,641	557,052		1,199,931	
Professional dues and license	78,065	289	19,749	20,038	41,215	490	41,705	1,565	141,373	
Building maintenance	84,274			-		14,783	14,783		99,057	
Computer equipment			1,310	1,310	18,453	10,645	29,098		30,408	
Digital material use fees	23,702	250,023		250,023		11,509	11,509		285,234	
Audit services				-	138,927		138,927		138,927	
Graduation			26,247	26,247			-		26,247	
Recruiting and job fairs	19,214		88,783	88,783	98,187		98,187		206,184	
Licensing fees	3,640			-	33,250		33,250		36,890	
Travel and lodging	150,107	2,754	48,569	51,323	43,036	3,163	46,199	2,629	250,258	
Meals and entertainment	44,732	614	46,777	47,391	73,996	2,913	76,909	316	169,348	
Temporary agencies	45,909	536	16,532	17,068	198,257		198,257		261,234	
Advertising and public relations	119,277		44,051	44,051	89,278		89,278		252,606	
Bank and credit card charges	21,114			-	384,837		384,837	19,190	425,141	
Bad debt				-	194,928		194,928		194,928	
Community relations	16,846	106	11,057	11,163	61,688	47,944	109,632		137,641	
Supplies	22,595	3,466	17,430	20,896	26,551	3,838	30,389	756	74,636	
Utilities and telephone	107,114	3,653	15,825	19,478	27,841		27,841	85	154,518	
Business insurance				-	267,620		267,620		267,620	
Legal				-	44,707		44,707		44,707	
Software site licenses	187,021	251,007	172,530	423,537	20,869	45,522	66,391		676,949	
Depreciation and amortization	423,886	219,692	47,848	267,540	10,269	12,033	22,302	664	714,392	
Other expenses	378,093	28,002	82,200	110,202	161,714	32,858	194,572	4,260	687,127	
Total Expenses	\$ 20,872,506	\$ 1,289,667	\$ 3,018,057	\$ 4,307,724	\$ 6,386,241	\$ 1,034,954	\$ 7,421,195	\$ 213,777	\$ 32,815,202	

See accompanying notes to financial statements.

Palo Alto University, Inc.

Statement of Functional Expenses

For the Year Ended July 31, 2019

	Student Services				Institutional Support			Total
	Instruction	Library	Student Services	Total Student Services	General & Administrative	Sponsored Programs	Total Institutional Support	
Salaries and wages	\$ 12,121,834	\$ 384,291	\$ 1,678,934	\$ 2,063,225	\$ 2,561,949	\$ 515,270	\$ 3,077,219	\$ 17,262,278
Benefits	1,700,334	66,541	267,659	334,200	436,477	54,126	490,603	2,525,137
Consortium payments	3,314,238			-			-	3,314,238
Consultants	865,301		232,380	232,380	634,484	47,976	682,460	1,780,141
Rent	670,108		26,590	26,590	572,851	19,254	592,105	1,288,803
Professional dues and license	73,173	261	22,003	22,264	73,537	597	74,134	169,571
Building maintenance	144,719			-			-	144,719
Computer equipment	4,689			-	58,878	1,658	60,536	65,225
Digital material use fees	29,195	155,467		155,467	926	3,425	4,351	189,013
Audit services			100	100	136,300		136,300	136,400
Graduation			120,748	120,748	4,415		4,415	125,163
Recruiting and job fairs	4,991		94,334	94,334	92,864		92,864	192,189
Licensing fees	2,498		48,637	48,637	45,505		45,505	96,640
Travel and lodging	222,808	6,883	64,093	70,976	68,112	13,258	81,370	375,154
Meals and entertainment	101,521	562	130,730	131,292	133,538	4,063	137,601	370,414
Temporary agencies	78,364		15,643	15,643	150,879		150,879	244,886
Advertising and public relations	11,669		52,083	52,083	60,636	500	61,136	124,888
Bank and credit card charges	13,235			-	363,725		363,725	376,960
Bad debt				-	352,270		352,270	352,270
Community relations	13,571	220	13,236	13,456	22,515	1,064	23,579	50,606
Supplies	25,581	3,641	26,191	29,832	19,324		19,324	74,737
Utilities and telephone	95,531	2,356	15,469	17,825	28,700		28,700	142,056
Business insurance				-	156,572		156,572	156,572
Legal				-	72,126		72,126	72,126
Software site licenses	186,023	60,533	176,479	237,012	20,359	40,683	61,042	484,077
Depreciation and amortization	370,262	293,249	5,772	299,021	9,620	9,619	19,239	688,522
Other expenses	250,853	36,947	91,993	128,940	121,304	36,458	157,762	537,555
Total Expenses	\$ 20,300,498	\$ 1,010,951	\$ 3,083,074	\$ 4,094,025	\$ 6,197,866	\$ 747,951	\$ 6,945,817	\$ 31,340,340

See accompanying notes to financial statements.

Palo Alto University, Inc.

Statement of Cash Flows

<i>For the Year Ended July 31,</i>	2020	2019
Cash Flows from Operating Activities:		
Change in net assets	\$ 537,498	\$ 1,166,957
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	714,392	688,522
Change in discount and allowance on contributions receivable	(7,191)	(32,663)
Net gain on investments	(433,904)	(26,746)
Changes in operating assets and liabilities:		
Student receivables	(1,121,329)	(2,250)
Contributions receivable	175,916	309,491
Grants receivable	(152,745)	79,672
Prepaid expenses and other assets	(46,251)	116,353
Accounts payable and accrued expenses	(483,410)	1,143,987
Deferred revenue	810,492	(131,761)
Contingent consideration		413,000
Other liabilities	10,462	39,993
Net cash provided by operating activities	3,930	3,764,555
Cash Flows from Investing Activities:		
Purchase of investments	(2,597,106)	(1,200,111)
Proceeds from the sale of investments	2,573,001	1,108,066
Purchase of property and equipment	(396,725)	(1,215,785)
Goodwill from acquisition		(573,000)
Net cash used by investing activities	(420,830)	(1,880,830)
Net Change in Cash and Cash Equivalents	(416,900)	1,883,725
Cash and Cash Equivalents, beginning of the period	10,939,827	9,056,102
Cash and Cash Equivalents, end of the period	\$ 10,522,927	\$ 10,939,827

See accompanying notes to financial statements.

Palo Alto University, Inc.

Notes to the Financial Statements

Note 1 - The University and Summary of Significant Accounting Policies:

a. The University

Palo Alto University (the University), founded in 1975 as Pacific Graduate School of Psychology, is a private, not-for-profit educational institution dedicated to improving the human condition through excellence in teaching, research and scholarship in the fields of psychology and counseling. With an unwavering commitment to diversity and to the communities it serves, the University offers doctorate, master's and bachelor's programs, as well as hands-on clinical training. The University is accredited by the Western Association of Schools and Colleges (WASC).

The University has many collaborative partnerships with community organizations and institutions, including Stanford School of Medicine, the Department of Veterans Affairs, Palo Alto Medical Center, and other mental health care organizations. The University's Gronowski Center teaching clinic delivers low-cost mental health services while also providing valuable, supervised training to University graduate students. In addition, the University sponsors several academic centers devoted to child mental health, evidence-based care for Lesbian, Gay, Bisexual, Transgender, and Questioning clients, excellence in diversity and community care, and internet-based global healthcare.

The University provides premium online professional training for mental health professionals via Consolidated Continuing Education and Professional Training, LLC d/b/a CONCEPT, that has a reputation for excellence in forensic psychology (see Note 14).

b. Basis of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) and, accordingly, reflect all significant receivables, payables, and other liabilities.

c. Basis of Presentation

The University's resources are classified according to the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the University and changes therein are classified and reported as follows:

Net Assets Without Donor Restrictions are not subject to donor-imposed restrictions and include board-designated funds functioning as endowments which have been set aside for special programs, capital projects, and to act as endowment funds.

Palo Alto University, Inc.

Notes to the Financial Statements

Net Assets With Donor Restrictions are subject to donor-imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or by satisfying restrictions specified by the donor. Other donor restrictions are perpetual in nature, whereby the donor has stipulated the funds be maintained in perpetuity.

Donor-imposed restrictions are released when a restriction expires, that is, when the stipulated time has elapsed, when the stipulated purpose for which the resource was restricted has been fulfilled, or both. Net assets with donor restrictions consist primarily of restricted grants, pledges, and contributions, together with income specifically restricted by donors.

d. 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 amounts of assets and liabilities and disclosures 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.

e. Cash and Cash Equivalents

Cash and cash equivalents consist of cash and money market funds excluding those held for investment purposes.

f. Investments

Investments are recorded at fair value. Investments received through gifts are recorded at estimated fair value at the date of donation. All debt and equity securities with readily determinable market values are carried at estimated fair value based on closing market prices. Investments in privately held companies are held at values as determined by the management of those companies. Gains and losses that result from market fluctuations are recognized in the statement of activities and change in net assets in the period such fluctuations occur. Dividend and interest income are accrued when earned.

g. Student and Grants Receivable

Student receivables include tuition and fees due from students and grants receivable include reimbursements due from sponsors of externally funded research and amounts due from federal agencies for student financial aid programs. These receivables are carried at cost, which represents fair value.

Palo Alto University, Inc.

Notes to the Financial Statements

The University grants credit primarily to individuals for the purpose of paying for their tuition and fees. Student receivables are payable by a certain date each quarter and are stated at amounts due, net of an allowance for doubtful accounts, if any. The allowance is established as losses are estimated to have occurred, through a charge to expense. Receivables are charged against the allowance when management believes that collectability is unlikely. Should a student not pay their tuition amounts by the due date for the quarter, his/her classes are dropped and he/she is charged a reinstatement fee before being allowed to attend classes.

Grants are expected to be fully collectible in the upcoming year.

h. Property and Equipment

Property and equipment are stated at cost at the date of acquisition or fair value at the date of donation in the case of gifts in kind. The University capitalizes all expenses for property and equipment, with the exception of library books, in excess of \$1,000; library books of any amount are capitalized. Depreciation is computed using the straight-line method based upon the estimated useful lives of the assets, generally 3 to 40 years.

i. Goodwill

Goodwill represents the excess of the cost of net assets acquired over the fair value of identifiable net assets at the date of acquisition. Goodwill acquired and determined to have an indefinite useful life is not amortized but tested for impairment at least annually or more frequently if events and circumstances exist that indicate that a goodwill impairment test should be performed. Goodwill impairment tests consist of a comparison of the reporting unit's fair value with its carrying value. Impairment exists when the carrying amount of goodwill exceeds the implied fair value for the reporting unit. The evaluation of impairment requires the University to make assumptions about future cash flows over the life of the asset being evaluated. These assumptions require significant judgment and are subject to change as future events and circumstances change. Actual results may differ from assumed and estimated amounts. Management determined that no impairment write-downs were required as of July 31, 2020.

j. Revenue Recognition

Student receivables are recorded when students are billed. Tuition and fee revenues are recorded as earned on a pro rata basis over the applicable teaching period in which educational services are provided (performance obligation). Collection or development of payment plans for tuition and fees is required prior to registration for the following term. Financial aid, in the form of fellowships and waivers, reduces the published price of tuition for students receiving such aid. As such, financial aid represents the difference between the stated charge for tuition (transaction price) and fees and the amount that is billed to the student and/or third parties making payments on behalf of the student.

Palo Alto University, Inc.

Notes to the Financial Statements

Tuition amounts received for the 2020-2021 school year as of July 31, 2020 in the amount of \$10,260,327 are recorded as deferred revenue, a contract liability. Deferred revenue as of July 31, 2019 of \$9,456,419 was recognized as revenue during the year ended July 31, 2020.

Contributions and grants are recognized as revenues when they are received by, or unconditionally pledged to, the University. The University classifies 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 such donor restrictions expire, that is, when stipulated time restrictions end or purpose restrictions are accomplished, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statement of activities and change in net assets as net assets released from restrictions. When the restriction is met in the same period as the contribution is received, contributions are reported as increases in net assets without donor restrictions.

Contributions that are promised in one year but are expected to be received after the end of that year (or over a number of years) are discounted at an appropriate discount rate. An allowance for uncollectible pledges has been established based on prior experience. The financial statements reflect these pledges net of the discount and allowance reserve. Conditional promises, that is, those with a measurable performance or other barrier, and a right of return, are not recognized until the conditions on which they depend are substantially met. The University had no conditional contributions as of July 31, 2020 and 2019.

Grant revenues are recognized as grant expenditures are incurred. Grant proceeds received in advance of grant expenditures as of July 31, 2020 in the amount of \$97,290 are recorded as deferred revenue, a contract liability. Deferred revenue related to grants as of July 31, 2019 of \$90,706 was recognized as revenue during the year ended July 31, 2020.

Program services income includes Gronowski Center teaching clinic and CONCEPT online professional training revenues. Revenue is recognized as the services are provided (performance obligation), typically upon receipt of payment. Deferred revenue, if any, is recorded for services paid for but not provided as of year end. As of July 31, 2020 and 2019, there was no deferred revenue recorded as these amounts were not material.

k. Advertising Expenses

The University's policy is to expense advertising costs as they are incurred. Advertising costs for the year ended July 31, 2020 and 2019 were \$252,606 and \$124,888, respectively.

Palo Alto University, Inc.

Notes to the Financial Statements

l. Functional Expense Allocations

The costs of providing various programs and activities have been summarized on a functional basis in the statement of activities and change in net assets. Certain expenses, such as depreciation and amortization expense, building services, including information technology, and personnel, are allocated among program services and supporting services based primarily on direct payroll charges and other direct expenses.

Allocations for other information technology and operations and maintenance are based on a percentage of the total expenses. The remaining expenses are allocated based on a direct identification methodology.

m. Income Taxes

The University is recognized by the Internal Revenue Service as an organization exempt from income taxes on related activities under Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the California Revenue and Taxation Code.

As of July 31, 2020 and 2019, management evaluated the University's tax positions and concluded that the University had maintained its tax-exempt status and had taken no uncertain tax positions that require adjustment to the financial statements. Therefore, no provision or liability for income taxes has been included in the financial statements.

n. Concentrations of Risk

Financial instruments which potentially subject the University to concentrations of credit risk consist principally of cash and student receivables.

The University grants credit to students in the normal course of operations and the credit risk with respect to these receivables is generally considered minimal due to the wide dispersion of receivables among individual students.

During the year, the University regularly maintains cash balances in excess of federally insured limits.

o. Fair Value Measurements

The University carries certain assets and liabilities at fair value. Fair value is 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 University classifies its financial assets and liabilities that the University has the ability to access at the measurement date based on a valuation method using three levels. Level 1 values are based on quoted prices (unadjusted) in active markets for identical securities. Level 2 values are based on significant observable market inputs, such as quoted prices in inactive markets. Level 3 values are based on significant unobservable inputs that reflect the University's determination of assumptions that market participants might reasonably use in valuing the securities.

Palo Alto University, Inc.

Notes to the Financial Statements

p. Reclassifications

Certain prior year amounts in the accompanying financial statements and notes have been reclassified to conform to the 2020 presentation. These reclassifications had no effect on the University's change in net assets as previously reported.

q. Recent Accounting Pronouncements

Pronouncements Adopted

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*. The University adopted this ASU, as amended, as of August 1, 2019. Analysis of various provisions of this standard resulted in no significant changes in the way the University recognizes revenue, and therefore no changes to the previously issued audited financial statements were required on a modified retrospective basis.

In June 2018, the FASB issued ASU 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made (Topic 958)* which clarifies and improves current guidance about whether a transfer of assets, or the reduction, settlement, or cancellation of liabilities, is a contribution or an exchange transaction. The University adopted this ASU on a modified prospective basis as of August 1, 2019. The impact of adopting this guidance is reflected in the financial statements and did not have a significant impact on the financial statements or disclosures.

Pronouncements effective in the future

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. The amendments in this update will supersede much of the existing authoritative guidance for leases. This guidance requires lessees, among other things, to recognize right-of-use assets and liabilities on their balance sheet for all leases with lease terms longer than twelve months. The standard will be effective for the University for its fiscal year beginning after December 15, 2021 with early application permitted. Entities are required to use the modified retrospective application for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements with the option to elect certain transition reliefs. The University is currently evaluating the impact of this pronouncement on its financial statements.

r. Subsequent Events

The University evaluated subsequent events from July 31, 2020 through December 8, 2020, 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, except as noted in note 15.

Palo Alto University, Inc.

Notes to the Financial Statements

Note 2 - Investments and Fair Value Measurements:

The table below presents the balances of assets measured at fair value at July 31, 2020 on a recurring basis:

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Cash and money market funds	\$ 264,981	\$ 264,981		
Bonds and fixed income funds	1,034,986	1,034,986		
Equity funds	1,748,478	1,748,478		
Alternative strategy funds	299,183	299,183		
Common stock – privately held companies	69,525			\$ 69,525
Total	\$ 3,417,153	\$ 3,347,628	\$ -	\$ 69,525

The table below presents the balances of assets measured at fair value at July 31, 2019 on a recurring basis:

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Cash and money market funds	\$ 240,727	\$ 240,727		
Bonds and fixed income funds	849,986	849,986		
Equity funds	1,484,304	1,484,304		
Alternative strategy funds	314,602	314,602		
Common stock – privately held companies	69,525			\$ 69,525
Total	\$ 2,959,144	\$ 2,889,619	\$ -	\$ 69,525

An investment's categorization within the valuation hierarchy is based on the lowest level of input that is significant to the fair value measurement. There has been no change in the methodology used for July 31, 2020 and 2019.

The change in level 3 assets and liabilities measured on a recurring basis for the year ended July 31, 2020 was immaterial. The change for the year ended July 31, 2019 was a \$195,000 realized loss on the write off of private common stock (Avantis Medical).

Palo Alto University, Inc.

Notes to the Financial Statements

Note 3 - Contributions Receivable:

Contributions receivable as of July 31, consisted of the following:

	2020	2019
Unconditional promises to be collected in the short-term:		
Less than one year (net of allowance for uncollectible contributions of \$57,158)	\$ 291,243	\$ 401,858
Unconditional promises to be collected in the long-term:		
Two to five years	15,334	80,634
More than five years	12,960	12,960
	28,294	93,594
Less discount to present value	(7,683)	(14,874)
Net long-term contributions receivable	\$ 20,610	\$ 78,720

Note 4 - Property and Equipment:

Property and equipment as of July 31 consisted of the following:

	2020	2019
Land	\$ 2,950,000	\$ 2,950,000
Building	5,104,174	4,956,599
Furniture and equipment	3,840,863	3,668,212
Library books	1,409,320	1,345,321
Software	1,623,503	1,611,003
	14,927,860	14,531,135
Less accumulated depreciation and amortization	(6,598,859)	(5,884,467)
	\$ 8,329,001	\$ 8,646,668

Note 5 - Leases:

The University leases classroom and clinical space under non-cancelable operating leases with monthly payments ranging from \$868 to \$97,703 expiring at various times through October 2024. One classroom space lease provides the University with an option to extend the lease for three years.

Palo Alto University, Inc.

Notes to the Financial Statements

The future minimum lease payments under the above leases are as follows:

Year ending July 31,	
2021	\$ 1,041,700
2022	1,072,900
2023	1,105,100
2024	1,138,300
2025	293,100
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Total minimum lease payments	\$ 4,651,100

Total rent expense under the above operating leases was approximately \$1,024,300 and \$1,214,100 for the years ended July 31, 2020 and 2019, respectively.

Note 6 - Credit Agreements:

The University has a \$1,500,000 line of credit with Comerica Bank. As of July 31, 2020 and 2019, there was no outstanding balance on the line of credit. The agreement requires, among other things, compliance with covenants including a certain positive change in net assets, and timely submission of internal and external financial statements. The agreement is secured by investments and real and personal property, can expire on demand and is to be reviewed on an annual basis. At July 31, 2020 and 2019, the University was in compliance with all of the covenants.

The University has no outstanding debt at July 31, 2020 and therefore its maximum annual debt service would be zero for the year ending in 2021.

Note 7 - Related Party Transactions:

Contributions receivable, prior to discounts or allowances, from employees of the University and members of its Board of Trustees totaled \$263,485 and \$465,124 at July 31, 2020 and 2019, respectively. The contributions received from employees of the University and members of its Board of Trustees totaled \$61,025 and \$52,989 at July 31, 2020 and 2019, respectively.

Palo Alto University, Inc.

Notes to the Financial Statements

Note 8 - Net Assets Without Donor Restrictions:

Net assets without donor restrictions as of July 31 are comprised of the following:

	2020	2019
Board designated	\$ 11,077,112	\$ 10,464,161
Undesignated	7,585,319	7,730,980
	<hr/>	<hr/>
	\$ 18,662,431	\$ 18,195,141

The University's governing board has designated net assets without donor restrictions for the following purposes as of July 31:

	2020	2019
Quasi-endowment	\$ 2,651,617	\$ 2,240,602
Liquidity reserve	8,425,495	8,223,559
	<hr/>	<hr/>
	\$ 11,077,112	\$ 10,464,161

Note 9 - Net Assets With Donor Restrictions:

Net assets with donor restrictions are available for the following purposes as of July 31:

	2020	2019
Endowments restricted in perpetuity by donors subject to spending policy and appropriation	\$ 601,239	\$ 594,739
	<hr/>	<hr/>
Project and program purpose restriction:		
Student fellowships	87,427	163,802
Faculty chair	6,167	15,625
Other programs	902,398	752,857
	<hr/>	<hr/>
	995,992	932,284
	<hr/>	<hr/>
	\$ 1,597,231	\$ 1,527,023

Palo Alto University, Inc.

Notes to the Financial Statements

Net assets were released from donor restrictions by incurring expenses satisfying the purpose of the restriction, by the passage of time, or by the occurrence of other specific events by donors for the fiscal year ended July 31 as follows:

	2020	2019
Expiration of time restrictions	\$ 162,265	\$ 90,798
Purpose restriction met:		
Student fellowship	4,459	11,333
Faculty chair		1,000
Private common stock write-off		150,000
	<hr/>	<hr/>
	\$ 166,724	\$253,131

Note 10 - Endowment:

The University's endowments consist of eleven individual funds, all established to generate support for the University's general operations, tuition assistance and programs. Its endowment includes donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments.

Consistent with the with the California enacted version of the State Prudent Management of Institutional Funds Act (SPMIFA) and Board policy, the University classifies as net assets with donor restrictions the original value of gifts of donor-restricted endowment funds and, if applicable, accumulations of donor-restricted endowment funds as required by the donor. Accumulated earnings of donor-restricted endowment funds are classified as net assets with donor restrictions until distributed in accordance with SPMIFA and Board policy.

In accordance with SPMIFA, the University 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 University 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 University, (7) the investment policies of the University.

The University has adopted investment and spending policies for endowment assets that will ultimately provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets.

To achieve a long-term investment rate-of-return, the University relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The University is reinvesting all unspent interest and gain associated with its endowments.

Palo Alto University, Inc.

Notes to the Financial Statements

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the amount to be maintained in perpetuity. In accordance with U.S. GAAP, deficiencies of this nature are reported in net assets with donor restrictions. At July 31, 2020 and 2019, there were no such amounts.

Endowment net asset composition as of July 31, 2020 was:

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Donor restricted		\$ 601,239	\$ 601,239
Board designated	\$ 2,651,617		2,651,617
Total funds	\$ 2,651,617	\$ 601,239	\$ 3,252,856

Changes in endowment net assets for the year ended July 31, 2020 were as follows:

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions Time or Purpose</u>	<u>Perpetuity</u>	<u>Total</u>
Endowment Net Assets, beginning of year	\$ 2,240,602		\$ 594,739	\$ 2,835,341
Investment income	40,707	\$ 39,969		80,676
Net gain (realized and unrealized)	170,308			170,308
Transfers	200,000			200,000
Contributions			6,500	6,500
Appropriated for Expenditure		(39,969)		(39,969)
Change in endowment net assets	411,015	-	6,500	417,515
Endowment Net Assets, end of year	\$ 2,651,617	\$ -	\$ 601,239	\$ 3,252,856

Palo Alto University, Inc.

Notes to the Financial Statements

Endowment net asset composition as of July 31, 2019 was:

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Donor restricted		\$ 594,739	\$ 594,739
Board designated	\$ 2,240,602		2,240,602
Total funds	\$ 2,240,602	\$ 594,739	\$ 2,835,341

Changes in endowment net assets for the year ended July 31, 2019 were as follows:

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions Time or Purpose</u>	<u>Perpetuity</u>	<u>Total</u>
Endowment Net Assets, beginning of year	\$ 2,098,213		\$ 692,236	\$ 2,790,449
Investment income	46,738	\$ 12,295		59,033
Net gain (loss) (realized and unrealized)	20,399		(150,000)	(129,601)
Transfers	75,252			75,252
Contributions			52,503	52,503
Appropriated for Expenditure		(12,295)		(12,295)
Change in endowment net assets	142,389	-	(97,497)	44,892
Endowment Net Assets, end of year	\$ 2,240,602	\$ -	\$ 594,739	\$ 2,835,341

Net assets with perpetual restrictions as of July 31, for which earnings are to be used for the following purposes are as follows:

	2020	2019
Gronowski Clinic	\$ 403,976	\$ 403,976
Library	124,021	124,021
Florence Furst Memorial Student Short-Term Loan Fund	10,000	10,000
Scholarships	5,439	5,439
Christine Blasey Endowed Scholarship	57,803	51,303
Total net assets with perpetuity restrictions	\$ 601,239	\$ 594,739

Net assets with donor restrictions represented by pledges receivable totaled \$38,750 at July 31, 2020 and 2019.

Palo Alto University, Inc.

Notes to the Financial Statements

Note 11 - Retirement Plan:

Retirement benefits are provided through a defined contribution plan under the Internal Revenue Code, Section 403(b) for University employees after completing consecutive three months of eligible service. Under the terms of the plan, the University has the option to make discretionary contributions to the plan. Eligible participants may contribute amounts not to exceed \$19,500 and \$19,000 for calendar years 2020 and 2019, respectively. The University's contributions were \$679,834 and \$697,491 for the periods ended July 31, 2020 and 2019, respectively.

The University also has 457(b) and 457(f) deferred compensation plans which provide eligible employees with the opportunity to defer a portion of their compensation and the University to make contributions for certain employees. For the 457(b) plan, deferrals are made at the discretion of the participants, subject to certain limitations. For the 457(f) plan, the contributions are made by the University on behalf of key employees. Total participant deferrals and employer contributions are \$33,000 as of July 31, 2020 and 2019. The assets related to participant deferrals and employer contributions are available to the general creditors of the University and are included in cash and cash equivalents and accounts payable and accrued expenses in the accompanying statement of financial position.

Note 12 - Other Commitments and Contingencies:

On August 30, 2016, the University renewed its agreement with Leland Stanford Junior University (Stanford) whereby Stanford faculty will provide certain instruction to students enrolled in the University's PsyD Program, which began in the fall of 2002. The agreement commenced on September 1, 2016. By consent of both parties, this is an "evergreen contract" with no specific end date. According to the agreement, fees to Stanford are paid four times per academic year based on the number of students enrolled in the program and the University-Stanford faculty sharing of teaching load.

The University receives funds from and administers various federal government funded programs which are subject to audit by the cognizant governmental agencies. The University's management believes that the outcome of any such audits will not have a significant effect on the financial position or results of activities of the University.

Palo Alto University, Inc.

Notes to the Financial Statements

Note 13 - Availability of Financial Assets and Liquidity:

The University's financial assets available within one year of July 31, 2020 for general expenditures are as follows:

	2020	2019
Financial assets at year-end:		
Cash and cash equivalents	\$ 10,522,927	\$ 10,939,827
Student receivables, net of allowance	9,429,772	8,308,443
Contributions receivable	311,853	480,578
Grants receivable	669,147	516,402
Investments	3,417,153	2,959,144
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Total financial assets	24,350,852	23,204,394
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Less amounts not available to be used within one year:		
Net assets with donor restrictions	(1,797,231)	(1,527,023)
Net assets designated by the board	(10,877,112)	(10,464,161)
Long term contributions receivable	(20,610)	(78,720)
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	(12,694,953)	(12,069,904)
<hr/>		
Financial assets available to meet general expenditures within one year	\$ 11,655,899	\$ 11,134,490
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The University's goal is generally to maintain financial assets to meet three months (90 days) of operating expenses (approximately \$7,800,000). As part of its liquidity plan, excess cash is invested in the short-term reserve fund. The University has a \$1,500,000 line of credit available for use.

Note 14 - Acquisition:

On December 1, 2018, the University acquired all assets in Consolidated Continuing Education and Professional Training, LLC d/b/a CONCEPT, LLC for a total purchase price of \$750,000 in cash, and \$413,000 in contingent consideration. The results of CONCEPT, LLC are included in the University's financial statements since the date of acquisition.

CONCEPT, LLC adds to the University's post-graduate education and training. The goodwill from the acquisition will provide the foundation for continuing and professional studies, a new program at the University.

Palo Alto University, Inc.

Notes to the Financial Statements

Assets acquired at the date of acquisition consisted of:

Property and equipment	\$ 590,000
Goodwill	573,000
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Purchase price	\$ 1,163,000

At the date of acquisition, the University assessed the probability of payout on the contingent portion of the purchase price consideration and determined the fair value estimate of the payouts at \$466,000, before net present value discount of \$53,000. The contingent consideration is based on the University achieving certain revenue goals measured in the trailing fiscal years ending July 31, 2020, 2021, 2022 and 2023, successively.

Note 15 - Impact of the COVID-19 Pandemic on Operations:

On March 11, 2020, the World Health Organization publicly characterized COVID-19 as a pandemic. Many federal, state and local governmental agencies have declared a state of emergency and issued a variety of recommendations impacting travel, group gatherings, etc. As a result, this has significantly impacted the University's operations in many ways including 100% virtual academic programs and operations. As of July 2020, the University has decided to postpone the implementation of Hi-Flex/Hybrid Model of Teaching until 2021. The receipt of approximately \$500,000 of Coronavirus Aid, Relief and Economic Security Act grant funds assisted students and the University in funding telecommuting and technology changes and operations changes required to satisfy the social distancing protocols required by the County of Santa Clara.

In addition, financial market volatility has significantly increased which may negatively impact investment values and net investment income in the future. Other financial impacts could occur though such potential impact is unknown at this time.

For the 2020-2021 school year, the University has enrolled approximately 1,020 students and began the year with students enrolled via distance learning with the intention to bring students on campus as conditions and regulations permit.