

UNIVERSITY OF THE NATIONS, KONA, INC.
(A Hawai'i Nonprofit Corporation)

CONSOLIDATED AUDITED FINANCIAL STATEMENTS
WITH INDEPENDENT AUDITOR'S REPORT

FOR THE YEARS ENDED JUNE 30, 2019 AND 2018

UNIVERSITY OF THE NATIONS, KONA, INC.

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INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees and Management of
University of the Nations, Kona, Inc.
Kailua-Kona, Hawaii 96740

We have audited the accompanying consolidated financial statements of University of the Nations, Kona, Inc. (a nonprofit corporation), which comprise the consolidated statements of financial position as of June 30, 2019 and 2018, and the related statements of activities and changes in net assets, functional expenses and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the 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; 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.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated 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 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 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 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 financial position of University of the Nations, Kona, Inc. as of June 30, 2019 and 2018, and the changes 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.

Carbonaro CPAs + Management Group

Hilo, Hawaii
October 24, 2019

UNIVERSITY OF THE NATIONS, KONA, INC.

Consolidated Statements of Financial Position

As of June 30, 2019 and 2018

ASSETS

	<u>2019</u>	<u>2018</u>
CURRENT ASSETS		
Cash and Cash Equivalents (Notes 2 and 10)	\$ 3,137,739	\$ 4,473,236
Cash Advances (Note 2)	571,498	688,313
Accounts Receivable, Net (Note 2)	69,207	92,334
Inventory (Note 2)	17,994	15,359
Prepaid Expenses	21,392	86,251
Current Portion of Notes Receivable (Note 3)	-	100,000
Total Current Assets	<u>3,817,830</u>	<u>5,455,493</u>
FIXED ASSETS (Note 2)		
Land	9,291,209	9,291,209
Buildings	29,314,216	28,652,492
Assets in Progress	4,133,375	4,043,202
Furniture and Equipment	895,488	407,836
Vehicles	462,685	346,013
Less Accumulated Depreciation	<u>(9,106,329)</u>	<u>(8,208,608)</u>
Net Fixed Assets	34,990,644	34,532,144
NON-CURRENT ASSETS		
Investments in Hualalai Condominiums (Notes 5 and 11)	2,565,000	2,330,000
Notes Receivable (Note 3)	<u>197,712</u>	<u>400,000</u>
Total Non-Current Assets	<u>2,762,712</u>	<u>2,730,000</u>
Total Non-Current Assets and Fixed Assets	<u>37,753,356</u>	<u>37,262,144</u>
TOTAL ASSETS	<u><u>\$ 41,571,186</u></u>	<u><u>\$ 42,717,637</u></u>

The accompanying notes are an integral part of these consolidated financial statements.

UNIVERSITY OF THE NATIONS, KONA, INC.

Consolidated Statements of Financial Position

As of June 30, 2019 and 2018

LIABILITIES AND NET ASSETS

	<u>2019</u>	<u>2018</u>
CURRENT LIABILITIES		
Accounts Payable and Accrued Expenses	\$ 1,427,830	\$ 1,269,807
Mortgages and Notes Payable - Current (Note 7)	157,633	217,294
Deferred Tuition and Fees Revenue (Note 2)	<u>1,583,800</u>	<u>1,010,963</u>
Total Current Liabilities	3,169,263	2,498,064
LONG-TERM LIABILITES		
Mortgages and Notes Payable (Note 7)	<u>4,426,774</u>	<u>5,573,786</u>
Total Long-Term Liabilities	4,426,774	5,573,786
Total Liabilities	<u>7,596,037</u>	<u>8,071,850</u>
NET ASSETS (Note 4)		
Net Assets Without Donor Restriction	31,307,812	31,973,994
Net Assets With Donor Restriction	<u>2,667,337</u>	<u>2,671,793</u>
Total Net Assets	<u>33,975,149</u>	<u>34,645,787</u>
TOTAL LIABILITIES AND NET ASSETS	<u><u>\$ 41,571,186</u></u>	<u><u>\$ 42,717,637</u></u>

The accompanying notes are an integral part of these consolidated financial statements.

UNIVERSITY OF THE NATIONS, KONA, INC.

Consolidated Statements of Activities and Changes in Net Assets
For the Years Ended June 30, 2019 and 2018

	2019			2018		
	Without Donor Restrictions	With Donor Restrictions	Total 2019	Without Donor Restrictions	With Donor Restrictions	Total 2018
REVENUES AND OTHER SUPPORT						
Student and Staff Fees, Net	\$ 14,437,855	\$ -	\$ 14,437,855	\$ 13,787,410	\$ 6,607	\$ 13,794,017
Contributions and Support	272,387	10,216,568	10,488,955	1,178,547	9,954,832	11,133,379
Sales and Other Revenue	678,579	123,383	801,962	603,006	336,632	939,638
Rental Income on Investments in Hualalai Condominiums, Net (Notes 5 and 9)	5,983	60,250	66,233	2,043	61,573	63,616
Donations In-Kind (Note 12)	-	-	-	610,444	-	610,444
Net Assets Released from Restrictions	10,404,657	(10,404,657)	-	10,446,214	(10,446,214)	-
Total Public Support and Revenue	25,799,461	(4,456)	25,795,005	26,627,664	(86,570)	26,541,094
EXPENSES						
Program Expense	23,897,832	-	23,897,832	21,875,375	-	21,875,375
Management and General Expenses	2,251,758	-	2,251,758	1,884,925	-	1,884,925
Fundraising Expense	316,053	-	316,053	237,781	-	237,781
	26,465,643	-	26,465,643	23,998,081	-	23,998,081
Total Expenses	26,465,643	-	26,465,643	23,998,081	-	23,998,081
CHANGE IN NET ASSETS	(666,182)	(4,456)	(670,638)	2,629,583	(86,570)	2,543,013
NET ASSETS, BEGINNING OF YEAR	31,973,994	2,671,793	34,645,787	29,344,411	2,758,363	32,102,774
NET ASSETS, END OF YEAR	\$ 31,307,812	\$ 2,667,337	\$ 33,975,149	\$ 31,973,994	\$ 2,671,793	\$ 34,645,787

The accompanying notes are an integral part of these consolidated financial statements.

UNIVERSITY OF THE NATIONS, KONA, INC.

Consolidated Statements of Functional Expenses
For the Years Ended June 30, 2019 and 2018

	2019				2018			
	Program Services	Management and General	Fundraising	Total 2019	Program Services	Management and General	Fundraising	Total 2018
Missionary Payments	\$ 9,227,361	\$ -	\$ -	\$ 9,227,361	\$ 9,189,899	\$ -	\$ -	\$ 9,189,899
Outreach Services	5,875,672	-	-	5,875,672	5,295,464	-	-	5,295,464
Occupancy	1,857,320	331,337	22,089	2,210,746	1,354,879	241,703	16,113	1,612,695
Household	1,716,314	429,079	-	2,145,393	1,729,189	432,298	-	2,161,487
Contracted Services	650,669	520,931	130,233	1,301,833	506,909	405,837	101,460	1,014,206
Depreciation Expense	764,299	191,076	-	955,375	700,920	175,231	-	876,151
Schools and Programs	856,840	64,525	-	921,365	709,336	53,418	-	762,754
Supplies	671,304	178,854	44,714	894,872	463,831	123,577	30,894	618,302
Information Technology	405,717	125,114	93,835	624,666	291,533	89,902	67,426	448,861
Travel	492,393	123,099	-	615,492	425,147	106,287	-	531,434
Donations	588,577	-	-	588,577	497,739	-	-	497,739
Merchant Fees	173,900	74,529	-	248,429	120,382	51,593	-	171,975
Interest (Note 7)	187,154	46,789	-	233,943	204,933	51,233	-	256,166
Cost of Sales and Services	204,984	10,834	-	215,818	198,050	10,468	-	208,518
Equipment Rental and Maintenance	109,507	27,833	1,391	138,731	99,761	25,357	1,267	126,385
Legal and Professional	9,080	77,176	4,540	90,796	939	7,974	469	9,382
Telephone	39,307	9,950	498	49,755	36,692	9,288	465	46,445
Printing and Publications	28,185	3,660	4,759	36,604	23,515	3,054	3,971	30,540
Accounting	-	31,625	-	31,625	-	91,479	-	91,479
Postage and Shipping	9,358	5,347	12,031	26,736	10,899	6,226	14,010	31,135
Promotional	17,673	-	1,963	19,636	15,358	-	1,706	17,064
Bad Debt Expense	12,218	-	-	12,218	-	-	-	-
Total Operating Expenses	\$ 23,897,832	\$ 2,251,758	\$ 316,053	\$26,465,643	\$ 21,875,375	\$ 1,884,925	\$ 237,781	\$ 23,998,081

The accompanying notes are an integral part of these consolidated financial statements.

UNIVERSITY OF THE NATIONS, KONA, INC.

Consolidated Statements of Cash Flows
For the Years Ended June 30, 2019 and 2018

	<u>2019</u>	<u>2018</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in Net Assets	\$ (670,638)	\$ 2,543,013
Expense Items Not Requiring Current Cash:		
Depreciation	955,375	876,151
Bad Debts Expense	12,218	-
Loss on Sale of Assets	-	1,313
Decrease in Prepaid Expenses	64,859	-
Increase in Accounts Payable and Accrued Expenses	158,023	57,552
Cash Received Not Related to Income or Expense:		
Decrease in Accounts Receivable	10,909	-
Decrease in Cash Advances	116,815	-
Decrease in Notes Receivable	302,288	2,532,221
Increase in Deferred Revenue	572,837	236,974
Income Items Not Creating Current Cash:		
Gain on Sale of Assets	(3,462)	-
Donations in-Kind (Non-cash Investing Activity)	-	(610,444)
Increase in Accounts Receivable	-	(73,624)
Cash Paid Not Related to Current Income or Expense:		
Increase in Inventory	(2,635)	(10,683)
Increase in Prepaid Expenses	-	(15,299)
Increase in Cash Advances	-	(229,930)
Net Cash Provided by Operations	<u>\$ 1,516,589</u>	<u>\$ 5,307,244</u>

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UNIVERSITY OF THE NATIONS, KONA, INC.

Consolidated Statements of Cash Flows
For the Years Ended June 30, 2019 and 2018

CASH FLOWS FROM INVESTING ACTIVITIES	2019	2018
Gross Proceeds from Sale of Assets	\$ 11,900	\$ 4,500
Purchases of Property and Equipment, Net of \$-0- and \$610,444 in Donated Construction Labor for the years Ended June 30, 2019 and 2018, Respectively	(1,422,313)	(3,505,387)
Investment in Condos	<u>(235,000)</u>	<u>(235,000)</u>
Net Cash Used by Investing Activities	<u>(1,645,413)</u>	<u>(3,735,887)</u>
 CASH FLOWS FROM FINANCING ACTIVITIES		
Net Reduction in Long-Term Debt	<u>(1,206,673)</u>	<u>(263,567)</u>
Net Cash Used by Financing Activities	<u>(1,206,673)</u>	<u>(263,567)</u>
 NET (DECREASE) INCREASE IN CASH FOR THE YEAR	 (1,335,497)	 1,307,790
 BEGINNING CASH BALANCE	 <u>4,473,236</u>	 <u>3,165,446</u>
 ENDING CASH BALANCE	 <u><u>\$ 3,137,739</u></u>	 <u><u>\$ 4,473,236</u></u>

The accompanying notes are an integral part of these consolidated financial statements.

UNIVERSITY OF THE NATIONS, KONA, INC.

Notes to the Consolidated Financial Statements

June 30, 2019 and 2018

Note 1. UNIVERSITY

The University of the Nations, Kona, Inc. (the University) is a private Christian educational institution located in Kailua-Kona, Hawaii. The University was founded in 1978 and, prior to October 25, 2013, the University's formal name was University of the Nations, Inc.

The University trains individuals to become Christian missionaries who fulfill the University's motto: "To Know God and to Make Him Known". The University grants post-secondary degrees through its seven colleges at its main campus in Kona. The University utilizes a modular class approach where 12 week lecture phases are typically followed by a 12 week practicum, often in a foreign country. The University offers its classes on a calendar quarterly basis. The University also operates a school for the children of students and staff.

The University contracts with outside employment agencies for certain key functions, but is otherwise staffed by volunteers (missionaries). Volunteer staff are responsible for raising their own support and are considered independent contractors and not employees. The University acts as a qualified missions agency and collects and disburses donations to the missionaries. The volunteer staff are individually responsible for any required filings with government agencies.

Two components make up the bulk of the University's revenue: (a) Contributions and Support, which are donations from the general public; and (b) Program-related Tuition and Fees charged to students and staff. Contributions and Support are comprised of donations made to the University's general fund and programs, as well as donations to support the independent missionaries (volunteers) working throughout the world. The University has discretion over the donations received to support its volunteers, thus these transactions are not agency transactions.

There are many *Youth with a Mission* non-profit corporations around the world with which the University is associated. Each corporation is autonomous in control and structure. These financial statements include only the operation controlled by University of the Nations, Kona, Inc., Kailua Kona, Hawai'i, USA campus.

Note 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Method of Accounting: The University uses the accrual method of accounting for financial statement reporting according to generally accepted accounting principles. Under this method of accounting, revenue is recognized when earned rather than when received and expenses are recognized when incurred rather than when paid.

Basis of Consolidation: These financial statements include the accounts for all academic and administrative departments of the University. Additionally, the financial statements include the net assets and activities of the University of the Nations Kona Foundation (UNKF), a separate nonprofit corporation that exists to solicit gifts for the University, and which is controlled by the University. All significant inter-company accounts have been eliminated in consolidation.

Revenue Recognition: Contributions received are recorded as with or without restrictions, depending on the existence and/or nature of any donor restrictions. Unconditional promises to give within the next year are reflected as current promises to give and are recorded at their net realizable value. Grants and other contributions of cash are reported as net assets with restrictions if they are received with donor stipulations that limit the use of the donated assets.

UNIVERSITY OF THE NATIONS, KONA, INC.

Notes to the Consolidated Financial Statements

June 30, 2019 and 2018

Note 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Net assets released from restriction: When a donor restriction expires, the related net assets with restrictions they are reclassified to net assets without restrictions and reported in the statement of activities as net assets released from restrictions.

Cash and Cash Equivalents: For the purpose of the statement of cash flows, cash is defined as demand deposits and savings accounts with maturities of three months or less.

Cash Advances: The University uses this account to track cash provided in advance to missionaries and students for travel and outreach purposes. The cash advance is maintained in full on the balance sheet until receipts are provided to support the use of the funds along with the return of any unused cash.

Accounts Receivable: Accounts receivable primarily represents student and staff fees owed to the University. The accounts receivable gross balance from students and staff was \$305,612 and \$282,929 as of June 30, 2019 and 2018, respectively. Management has recorded an allowance for doubtful accounts equal to 80.72% and 82.5% of those receivables as of June 30, 2019 and 2018, respectively. Management considers these percentages to be reasonable based on the University's recent historic rates of collection of accounts receivable. Accounts receivable as of June 30, 2018, also included a double payment made to a vendor in the amount of \$43,863. This payment was refunded to the University in July 2018.

Income Taxes: The University is exempt from Federal income taxes pursuant to Internal Revenue Code section 501 (c) (3), and exempt from State income taxes under Section 237-23 (b) of the Hawaii Revised Statutes. Therefore, no provision for federal or state income taxes is required for the financial statements.

Use of Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Inventory: Inventory consists of food supplies and merchandise and is valued at the lower of cost or market on a first-in, first-out basis.

Fixed Assets: Land, buildings, equipment, and vehicles are stated at cost or at fair value at date of donation. Major renewals and improvements are capitalized, while maintenance and repairs that do not extend the lives of the assets are charged to operations. Management capitalizes items over \$5,000 with a useful life greater than 1 year. Depreciation is provided over the estimated useful lives of the assets using the straight-line method.

Deferred Tuition and Fees Revenue: Deferred tuition and fees revenue represent amounts collected from students and staff for tuition, housing fees, and outreach fees in advance of the time of invoice.

Contributions and Donations: Under FASB ASC 958-605-25-16, contributions of donated goods and services that create or enhance non-financial assets; or that require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation; are recorded at their fair values in the period received.

UNIVERSITY OF THE NATIONS, KONA, INC.

Notes to the Consolidated Financial Statements

June 30, 2019 and 2018

Note 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Functional Allocation of Expenses: The costs of providing the various programs and activities have been summarized on a functional basis in the statement of functional expenses. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

Liquidity: The University structures its financial assets to be available as its general expenditure, liabilities, and other obligations come due. In addition, the University has a \$1 million line of credit (Note 8) to help ensure it has sufficient liquidity during the Summer when there are fewer students and in case of an emergency requiring significant financial assets. The Net Rental Income from the University's board-designated Hawaii Island Scholarship Endowment fund is unavailable to management for general expenditure. Additionally, financial assets with donor restrictions are withheld from financial assets available for expenditure. (Note 6) The University invests cash in excess of daily requirements in interest bearing accounts.

Note 3. NOTES RECEIVABLE

Notes receivable consist of various non-interest bearing demand notes. The notes are:

- *Restitution Receivable* - \$197,712. In the fiscal year ended June 30, 2017, the University discovered fraud on the part of the former CFO. In addition to losses, the University recorded a fraud settlement receivable of \$300,000 to approximate assets seized by the court which have been ordered liquidated and presented to the University. During the fiscal year ended June 30, 2019, the University received \$102,288 in fraud compensation from various sources leaving a recorded receivable balance of \$197,712. However, the remaining \$3,025,906 of the court-ordered restitution remains collectable by the University.

- *Kama'aina Hale Apartments* - \$200,000 as of June 30, 2018. Full repayment was received in 2019. See Note 5 for further information.

Note 4. NET ASSETS

On August 18, 2016, the Financial Accounting Standards Board (FASB) issued ASU 2016-14, Not-for-Profit Entities (Topic 958) – Presentation of Financial Statements of Not-for-Profit Entities. University of the Nations, Kona, Inc. has adjusted the presentation of its financial statements accordingly, applying the changes retrospectively to the comparative period presented. The new standards change the following aspects of the University's financial statements:

The financial statements include a new disclosure about liquidity and availability of resources (Note 6).

The temporarily restricted and permanently restricted net asset classes have been combined and renamed Net Assets With Donor Restrictions. The unrestricted net asset class has been renamed Net Assets Without Donor Restrictions.

Net assets, revenue, and support are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified as follows:

UNIVERSITY OF THE NATIONS, KONA, INC.

Notes to the Consolidated Financial Statements

June 30, 2019 and 2018

Note 4. NET ASSETS (continued)

Net Assets Without Donor Restrictions include all resources that are not subject to donor-imposed stipulations or contributions with donor-imposed restrictions that are met during the same year as the contribution is made. They are available for support of all organizational operations and services. Net Assets Without Donor Restrictions may be designated by the board of directors for specific purpose at any time.

Net Assets Without Donor Restrictions consist of the following:

	<u>2019</u>	<u>2018</u>
Board-Designated Endowment for Hawaii Island Scholarships	\$ 226,497	\$ 150,000
Undesignated Net Assets	<u>31,081,315</u>	<u>31,823,994</u>
Total Net Assets Without Donor Imposed Restrictions	<u>\$ 31,307,812</u>	<u>\$ 31,973,994</u>

Net Assets With Donor Restrictions include amounts that the donor subjects to restrictions in perpetuity and amounts subject to legal or donor-imposed stipulations that may or will be met either by actions of the University and/or passage of time. Contributions with restriction are reported as increases in Net Assets With Donor Restrictions. When the restriction is met the amount is reclassified to unrestricted net assets and reported in the consolidated statement of activities as net assets released from restrictions.

Net Assets With Donor Restriction through Perpetuity are subject to donor-imposed stipulations that must be maintained permanently by the University. These net assets constitute the University's endowment funds. Income realized by the endowment, as well as unrealized capital appreciation on the endowment, is recorded as an increase in Net Assets With Donor restrictions until the income is appropriated for student scholarships.

Net Assets With Donor Restrictions represent funds received from donors to be used for specific purposes. Net assets are released from donor restrictions primarily by incurring expenses that satisfy the restricted purpose, except for Net Assets With Restriction through perpetuity. Net Assets With Donor Restrictions consist of the following as of June 30:

	<u>2019</u>	<u>2018</u>
Ministry Funds	\$ 473,723	\$ 421,427
Building Funds	138,539	232,381
International Funds	98,123	55,701
Financial Aid and Other Scholarships	95,635	97,565
Endowment Balance (Note 9)	<u>91,317</u>	<u>94,719</u>
Total Net Assets With Time or Donor Imposed Restrictions	897,337	901,793

Net Assets With Donor Restriction through Perpetuity

Endowment Funds:

Scholarships

Total Net Assets With Donor Restriction through Perpetuity

<u>1,770,000</u>	<u>1,770,000</u>
<u>1,770,000</u>	<u>1,770,000</u>

Total Net Assets With Donor Restrictions

<u>\$ 2,667,337</u>	<u>\$ 2,671,793</u>
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UNIVERSITY OF THE NATIONS, KONA, INC.

Notes to the Consolidated Financial Statements
June 30, 2019 and 2018

Note 4. NET ASSETS (continued)

The changes have the following effect on net assets at June 30, 2018:

<u>Net Asset Class</u>	<u>As Originally Presented</u>	<u>After Adoption of ASU 2016-14</u>
Unrestricted Net Assets	\$ 31,823,994	\$ -
Unrestricted Board Designated Endowment	150,000	
Temporarily Restricted Net Assets	901,793	
Permanently Restricted Net Assets	1,770,000	
Net Assets Without Donor Restriction		31,973,994
Net Assets With Donor Restriction		2,671,793
Total Net Assets	\$ 34,645,787	\$ 34,645,787

Note 5. RELATED PARTY TRANSACTIONS

Economic Interest in Ka Ohana Waiaha:

Ka Ohana Waiaha (KOW) is a community land trust corporation that was created to fund the purchases of housing for long-term members of the University staff. KOW was formed in 2008 and is a tax-exempt for federal and state income tax purposes under Internal Revenue Code 501(c)(3). KOW is a separate entity and is not controlled by the University.

Beginning July 1, 2013, the University leased a parcel of land owned by KOW for \$1 per year. This land comprised 57 undeveloped acres adjacent to the University property. On July 1, 2017, the University also held a note receivable from KOW in the amount of \$2,476,285.

On June 14, 2018, KOW sold the 57 acres to the University along with an additional 5 acres of adjoining land in settlement of the note. The University also paid all fees associated with the transaction, bringing the total cost of acquisition to \$2,493,145.

KOW also owns Hualalai Village, a condominium development located adjacent to University Property. The University owns nine individual condominium units in Hualalai Village, of which seven were purchased as investments of its permanent endowment funds. The ninth unit was purchased during the fiscal year ended June 30, 2019, for \$235,000. All of the units are debt-free.

The University rents the units to staff and students and pays related expenses and association fees to KOW. Net income earned is used for scholarships, in accordance with purpose restrictions established by the endowment donors.

The investments in the condominiums are stated at current realizable value which is the contractual price for which each unit can be sold per deed restrictions. As of both June 30, 2019 and June 30, 2018 this current realizable value was below fair market value.

Indemnity Agreement with KHA:

In August of 2013, a separate nonprofit corporation, Kama'aina Hale Apartments (KHA), was formed to acquire a 128 unit low cost housing development adjacent to the University's campus. The University has signed an indemnity agreement on behalf of KHA, guaranteeing annual sub-lease payments of \$400,000 to the land owner, Kamehameha Schools Bishop Estate (KSBE). The University does not expect to be required to make payments to KSBE on behalf of KHA.

NIVERSITY OF THE NATIONS, KONA, INC.

Notes to the Consolidated Financial Statements
June 30, 2019 and 2018

Note 6. LIQUIDITY AND AVAILABILITY OF FINANCIAL ASSETS

Financial assets available for general expenditures within one year, at June 30, 2019 are as follows:

Cash and Cash Equivalents	\$ 3,137,739
Cash Advances	571,498
Accounts Receivable, Net	<u>69,207</u>
Total Financial Assets at year-end	3,778,444
Less amounts unavailable for general expenditures:	
Donor Restricted Financial Assets	(897,337)
Board of Director Designated Financial Assets	<u>(2,413)</u>
Financial assets available to meet cash needs for general expenditures within one year	<u><u>\$ 2,878,694</u></u>

Note 7. LONG TERM DEBT

As of June 30, 2019 and 2018, long term debt consisted of the following:

	2019	2018
Central Pacific Bank Loan payable-1 carries interest rate of 4.0% fixed until September 2019, at which time the rate will be raised to 4.51%. Monthly payments of principal and interest were \$31,909 until September 1, 2019, at which time they were reduced to \$28,817. The loan matures in 2024 and is secured by a first mortgage on the compaus property.	\$ 4,584,407	\$ 4,933,323
Central Pacific Bank Loan payable-2 was fully paid in December of 2018.	-	857,757
Total Long-Term Debt	<u>4,584,407</u>	<u>5,791,080</u>
Less Current Installments of Long-Term Debt	<u>(157,633)</u>	<u>(217,294)</u>
Net Long-Term Debt	<u>\$ 4,426,774</u>	<u>\$ 5,573,786</u>

Total interest paid on long-term debt was \$233,943 and \$256,166 for the years ended June 30, 2019 and 2018, respectively.

As of June 30, 2019, estimated maturities of long-term debt were as follows:

Fiscal Year	
2020	\$ 157,633
2021	149,214
2022	156,084
2023	163,270
2024	170,789
Thereafter	<u>3,787,417</u>
Total	<u><u>\$ 4,584,407</u></u>

UNIVERSITY OF THE NATIONS, KONA, INC.

Notes to the Consolidated Financial Statements

June 30, 2019 and 2018

Note 8. LINE OF CREDIT

The University also holds a \$1,000,000 line of credit with Central Pacific Bank available for short-term working capital needs. Any loan under this line of credit would be at the bank base rate of interest plus 0.25% and would be secured by all assets of the University. To date, the University has not made any use of this line of credit as of June 30, 2019 and 2018.

Note 9. ENDOWMENTS

The University has invested its net assets with restrictions through perpetuity in debt-free condominiums in the Hualalai Village project (See Note 5). The endowments include both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. As required by generally accepted accounting principals (GAAP), net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

As of June 30, 2019 and 2018, the net assets with restrictions through perpetuity amounted to \$1,770,000.

Changes are shown in the following chart:

	Without Donor Restrictions	With Donor Restrictions	With Donor Restrictions Through Perpetuity	Total
Endowment net assets June 30, 2017	\$ -	\$ 89,795	\$ 1,755,851	\$ 1,845,646
Investment Return:				
Net Rental Income	-	47,424	14,149	61,573
Board Designated Endowment Funds	150,000	-	-	-
Appropriation of endowment assets for expenditure	-	(42,500)	-	107,500
Endowment net assets June 30, 2018	\$ 150,000	\$ 94,719	\$ 1,770,000	\$ 2,014,719
Investment Return:				
Net Rental Income	2,413	60,250	-	62,663
Board Designated Endowment Funds	74,084	-	-	74,084
Appropriation of endowment assets for expenditure	-	(63,652)	-	(63,652)
Endowment net assets June 30, 2019	\$ 226,497	\$ 91,317	\$ 1,770,000	\$ 2,087,814

Endowments without donor restrictions totaling \$226,497 were authorized by the Board of Trustees. These funds have been invested in a condominium to provide earnings to fund scholarships for residents of Hawaii Island. The net rental income from this condominium in fiscal year 2019 was \$2,413.

Notes to the Consolidated Financial Statements
June 30, 2019 and 2018

Note 9. ENDOWMENTS (continued)

Interpretation of the law

The Board of Trustees of the University has interpreted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the University classifies net assets with restrictions through perpetuity as (a) the original value of gifts donated to the permanent endowment, and (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift.

The remaining portion of the donor-restricted endowment fund that is not classified in net assets with restrictions through perpetuity is classified as net assets with restrictions until those amounts are appropriated for expenditure by the University in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, management considers in its determination to appropriate or accumulate donor restricted endowment funds the following factors:

1. The duration and preservation of the fund
2. The purposes of the organization and the donor-restricted endowment fund
3. General economic conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of the University
7. The investment policies of the University

Return Objectives and Risk Parameters

The University has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding while still maintaining purchasing power of the endowed assets. The University's endowment assets are invested in such a way that will generate a long-term, predictable rate of return from rental income (net of expenses) and will preserve the value of the endowment assets.

Strategies Employed for Achieving Objectives

In order to meet the endowment's return objectives, the Board of Trustees has stipulated that the fixed monthly rental amount received by the University for each condominium unit is to be used for the benefit of the endowment fund.

Spending Policy

It is the policy of the University that it may distribute all the net rental income derived from the endowment assets. In accordance with the purpose restrictions established by the endowment donors, all distributions are to be used exclusively to fund student scholarships.

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Notes to the Consolidated Financial Statements

June 30, 2019 and 2018

Note 9. ENDOWMENTS (concluded)

Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the University to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature are reported in Net Assets With Donor Restrictions.

Note 10. CONCENTRATION OF RISK

The University maintains its cash accounts at Central Pacific Bank. These balances exceed the Federal Deposit Insurance Corporation (FDIC) insured limit per corporate depositor. Management acknowledges the possibility of risk in this arrangement; however, the size and the longevity of the depository institution minimize such risk.

Balances over \$500,000 in the operations checking account are transferred nightly in and out of an investment account with Federated Investors of Kansas City, Missouri. This investment account is made up of government obligations and earnings are credited to the University monthly. Central Pacific Bank acts as the University's agent in these transactions, but this investment account is not insured by the FDIC.

The following represents a summary of cash balances as of June 30, 2019 and 2018:

	<u>2019</u>	<u>2018</u>
Fully Insured Deposits	\$ 250,000	\$ 250,000
Uninsured and Uncollateralized	<u>2,887,739</u>	<u>4,223,236</u>
	<u>\$ 3,137,739</u>	<u>\$ 4,473,236</u>

The University's endowment investments are concentrated in the Hualalai Village condominium development. Also, a large portion of the fundraising for the University is conducted by Loren Cunningham, co-founder of the University and President of the Board of Trustees. The University does not believe that these concentrations represent a material risk of loss with respect to its financial position.

Note 11. INVESTMENTS

The University follows FASB ASC 820-10-50-1 which establishes a hierarchy for inputs to be used in measuring fair market value. This maximizes the use of observable inputs and minimizes the use of unobservable inputs. Observable inputs are those that market participants would use in pricing the asset or liability based on the best information available in each circumstance.

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Notes to the Consolidated Financial Statements
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Note 11. INVESTMENTS (continued)

This fair value hierarchy consists of three broad levels:

- Level 1 inputs consist of unadjusted quoted prices in active markets such as stock exchanges for identical assets.
- Level 2 inputs consist of significant other observable inputs such as quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset and liability, either directly or indirectly, for substantially the full term of a financial instrument.
- Level 3 inputs consist of significant unobservable inputs and include situations where there is little, if any, market activity for the investment. The inputs require significant judgment or estimates, such as those associated with discounted cash flow methodologies and appraisals.

Fair values of the Hualalai Condominiums measured on a recurring basis at June 30, 2019 and 2018 are summarized in the following chart:

	Quoted Prices: Level 1	Significant Other Inputs: Level 2	Significant Non- Observable Inputs: Level 3	Total
June 30, 2018	\$ -	\$ -	\$ 2,330,000	\$ 2,330,000
June 30, 2019	\$ -	\$ -	\$ 2,565,000	\$ 2,565,000

The Hualalai Condominiums measured at level 3 are based on the real estate value capped at the allowable sales price. The increase in value occurring during the year ending June 30, 2019 and 2018 was the result of purchasing an additional condominium unit for \$235,000 during each of the years.

There are no other assets or liabilities measured at fair value on a recurring or non-recurring basis.

Note 12. DONATED SERVICES, MATERIALS, AND FACILITIES

In Fiscal Year Ending June 30, 2018, the University placed the Building J dormitory into service and accordingly capitalized donated labor in addition to purchased costs of its construction. An in-kind donation of \$610,444 was recorded on the books to reflect the estimated value of this donation as required by FASB ASC 958-605- 25-16. (See Note 2, Contributions and Donations.)

UNIVERSITY OF THE NATIONS, KONA, INC.

Notes to the Consolidated Financial Statements
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Note 13. RECENT ACCOUNTING PRONOUNCEMENTS

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers, which requires an entity to recognize revenue from the transfer of promised goods or services in an amount that reflects the consideration the entity expects to receive for those goods or services. An entity also should disclose sufficient information to enable financial statements users to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from its contracts with customers. The new standard is effective for the University's fiscal year ending June 30, 2020. Management does not expect the adoption of these provisions to have a significant impact on the financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases, which requires lessees, among other changes, to recognize most leases on the balance sheet as assets and liabilities as well as provide additional qualitative and quantitative disclosures. ASU 2016-02 is effective for the University's fiscal year ending June 30, 2022, but permits early adoption and mandates a modified retrospective transition method. Management is currently evaluating the impact that the adoption of these provisions will have on the financial statements, but expects ASU 2016-02 to add significant assets and liabilities to the statement of financial position.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash, which requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. As a result, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The new standard is effective for the University's fiscal year ending June 30, 2020 and should be applied using a retrospective transition method to each period presented. Management does not expect the adoption of these provisions to have a significant impact on the financial statements.

Note 14. RECLASSIFICATIONS

Certain account balances in the financial statements for the fiscal year ended June 30, 2018, have been reclassified for comparative purposes to conform to the presentation for fiscal year ended June 30, 2019. These had no effect on the Total Assets or Change in Net Asset figures reported for the fiscal year ended June 30, 2018.

Note 15. SUBSEQUENT EVENTS

In preparing these financial statements, the University has evaluated events and transactions for potential recognition or disclosure through October 24, 2019, and there were none to be reported.