

PENNSYLVANIA ACADEMY OF THE FINE ARTS

FINANCIAL STATEMENTS AND REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

JUNE 30, 2021

PENNSYLVANIA ACADEMY OF THE FINE ARTS

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Trustees
Pennsylvania Academy of the Fine Arts
Philadelphia, Pennsylvania

We have audited the accompanying financial statements of Pennsylvania Academy of the Fine Arts (a nonprofit organization), which comprise the statement of financial position as of June 30, 2021, and the related statements of activities and changes in net assets, functional expenses and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Pennsylvania Academy of the Fine Arts as of June 30, 2021, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

**Board of Trustees
Pennsylvania Academy of the Fine Arts
Philadelphia, Pennsylvania**

Report on Summarized Comparative Information

We have previously audited Pennsylvania Academy of the Fine Arts' 2020 financial statements, and our report dated December 10, 2020, expressed an unmodified opinion on those audited financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2020, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Tait, Weller & Baker LLP

**Philadelphia, Pennsylvania
December 17, 2021**

PENNSYLVANIA ACADEMY OF THE FINE ARTS

STATEMENTS OF FINANCIAL POSITION

June 30, 2021 And 2020

| | <u>2021</u> | <u>2020</u> |
|--|------------------------------|------------------------------|
| ASSETS | | |
| ASSETS | | |
| Cash and cash equivalents | \$ 863,458 | \$ 250,315 |
| Accounts receivable, net | 206,869 | 229,691 |
| Prepaid expenses | 449,124 | 280,340 |
| Merchandise held for resale | 117,287 | 189,050 |
| Pledges receivable <i>(Notes 3 and 12)</i> | 2,203,104 | 3,693,504 |
| Other assets <i>(Notes 4, 9 and 12)</i> | 652,419 | 66,425 |
| Operating lease right of use asset | 965,298 | - |
| Long term investments <i>(Notes 4 and 8)</i> | 63,915,173 | 53,601,752 |
| Property, buildings and equipment <i>(Note 5)</i> | 50,741,142 | 52,461,320 |
| Beneficial interest in perpetual trusts <i>(Notes 4 and 6)</i> | <u>13,496,713</u> | <u>10,557,249</u> |
| Total Assets | <u>\$ 133,610,587</u> | <u>\$ 121,329,646</u> |
| LIABILITIES AND NET ASSETS | | |
| LIABILITIES | | |
| Line of credit <i>(Note 8)</i> | \$ - | \$ 1,700,000 |
| Refundable advance <i>(Note 7)</i> | 1,596,447 | 1,799,100 |
| Accounts payable | 922,240 | 673,609 |
| Accrued expenses | 643,212 | 772,622 |
| Deferred revenue | 867,455 | 1,048,782 |
| Operating lease liability | 965,298 | - |
| Bond payable <i>(Note 9)</i> | 24,713,020 | 24,692,460 |
| Other liabilities <i>(Notes 4 and 9)</i> | <u>-</u> | <u>771,462</u> |
| Total Liabilities | <u>29,707,672</u> | <u>31,458,035</u> |
| NET ASSETS | | |
| Without donor restriction | | |
| Undesignated | 56,032,618 | 50,538,480 |
| Board-designated <i>(Note 11)</i> | <u>923,977</u> | <u>774,418</u> |
| Total without donor restriction | 56,956,595 | 51,312,898 |
| With donor restriction <i>(Note 11)</i> | <u>46,946,320</u> | <u>38,558,713</u> |
| Total Net Assets | <u>103,902,915</u> | <u>89,871,611</u> |
| Total Liabilities and Net Assets | <u>\$ 133,610,587</u> | <u>\$ 121,329,646</u> |

The accompanying notes are an integral part of these statements.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS

Year Ended June 30, 2021 With Summarized Information For 2020

| | Without Donor Restrictions | With Donor Restrictions | TOTALS | |
|---|-------------------------------|----------------------------|----------------------|----------------------|
| | | | 2021 | 2020 |
| Program Revenues, Support Revenue and Investment Income | | | | |
| Tuition and fees, net of scholarships | \$ 2,807,248 | \$ - | \$ 2,807,248 | \$ 5,318,236 |
| Continuing and public education | 579,126 | - | 579,126 | 562,930 |
| Museum operations | 34,022 | - | 34,022 | 233,340 |
| Auxiliary operations, net of costs of sales | 287,752 | - | 287,752 | 899,458 |
| Gifts and Grants | 3,974,477 | 2,142,926 | 6,117,403 | 7,616,818 |
| Investment income | | | | |
| Endowment income designated for operations (Note 4) | 718,690 | 947,644 | 1,666,334 | 1,256,209 |
| Income from outside trusts | 471,075 | - | 471,075 | 458,536 |
| PPP loan forgiveness | 1,799,100 | - | 1,799,100 | - |
| Other | 743 | - | 743 | 9,729 |
| Net assets released from restrictions (Note 11) | <u>3,213,461</u> | <u>(3,213,461)</u> | <u>-</u> | <u>-</u> |
| Total operating program revenues, support revenue and investment income | <u>13,885,694</u> | <u>(122,891)</u> | <u>13,762,803</u> | <u>16,355,256</u> |
| Program and Support Expenses | | | | |
| Program Expenses | | | | |
| College | 3,882,411 | - | 3,882,411 | 4,964,568 |
| Campus operations | 3,047,816 | - | 3,047,816 | 3,257,585 |
| Continuing and public education | 925,860 | - | 925,860 | 847,119 |
| Museum operations | 1,435,944 | - | 1,435,944 | 1,810,771 |
| Auxiliary operations | <u>229,026</u> | <u>-</u> | <u>229,026</u> | <u>587,342</u> |
| Total program expenses | <u>9,521,057</u> | <u>-</u> | <u>9,521,057</u> | <u>11,467,385</u> |
| Support Expenses | | | | |
| Management and general | 2,901,729 | - | 2,901,729 | 2,639,376 |
| Fundraising | <u>1,177,222</u> | <u>-</u> | <u>1,177,222</u> | <u>1,428,289</u> |
| Total support expenses | <u>4,078,951</u> | <u>-</u> | <u>4,078,951</u> | <u>4,067,665</u> |
| Total program and support expenses | <u>13,600,008</u> | <u>-</u> | <u>13,600,008</u> | <u>15,535,050</u> |
| Change in net assets before depreciation and amortization, non-operating revenues, expenses and gains (losses) | <u>285,686</u> | <u>(122,891)</u> | <u>162,795</u> | <u>820,206</u> |
| Non-Operating Revenues, Expenses and Gains/(Losses) | | | | |
| Depreciation and amortization | (2,108,725) | - | (2,108,725) | (2,172,594) |
| Investment return in excess (deficit) of amount designated for current operations (Notes 4 and 11) | 149,559 | 5,571,034 | 5,720,593 | (1,117,705) |
| Other investment income (Note 4) | 6,890,934 | - | 6,890,934 | 654,600 |
| Change in beneficial interest in perpetual trusts (Notes 4 and 11) | - | 2,939,464 | 2,939,464 | 43,161 |
| Change in market value of interest rate swap (Note 9) | 1,423,881 | - | 1,423,881 | (539,735) |
| Loss on termination of interest rate swap agreement (Note 9) | - | - | - | (405,046) |
| Loss on early extinguishment of deferred financing expenses (Note 9) | - | - | - | (180,144) |
| Other gain (loss) (Notes 12 and 13) | 78,344 | - | 78,344 | (20,000) |
| Proceeds from art sale | - | - | - | 2,170 |
| Collection items purchased not capitalized | <u>(1,075,982)</u> | <u>-</u> | <u>(1,075,982)</u> | <u>(1,520,803)</u> |
| Total depreciation and amortization, non-operating revenue, expenses and gains/(losses) | <u>5,358,011</u> | <u>8,510,498</u> | <u>13,868,509</u> | <u>(5,256,096)</u> |
| Change in net assets | <u>5,643,697</u> | <u>8,387,607</u> | <u>14,031,304</u> | <u>(4,435,890)</u> |
| Net Assets | | | | |
| Beginning of year | <u>51,312,898</u> | <u>38,558,713</u> | <u>89,871,611</u> | <u>94,307,501</u> |
| End of year | <u>\$56,956,595</u> | <u>\$46,946,320</u> | <u>\$103,902,915</u> | <u>\$ 89,871,611</u> |

The accompanying notes are an integral part of these statements.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

STATEMENT OF FUNCTIONAL EXPENSES

Years Ended June 30, 2021 With Summarized Information For 2020

| | 2021 | | | | | | | Total | 2020 |
|---|--------------------|--------------------|---------------------------------|--------------------|------------------|------------------------|--------------------|---------------------|---------------------|
| | College | Campus Operations | Continuing And Public Education | Museum Operations | Auxiliary | Management And General | Fundraising | | |
| Personnel costs | | | | | | | | | |
| Salaries | \$2,876,655 | \$ 331,001 | \$ 654,811 | \$ 920,194 | \$146,906 | \$1,253,615 | \$ 656,166 | \$ 6,839,348 | \$ 7,860,199 |
| Benefits and taxes | <u>608,735</u> | <u>72,820</u> | <u>133,307</u> | <u>201,477</u> | <u>31,347</u> | <u>297,261</u> | <u>139,113</u> | <u>1,484,060</u> | <u>1,502,878</u> |
| Total Personnel costs | <u>3,485,390</u> | <u>403,821</u> | <u>788,118</u> | <u>1,121,671</u> | <u>178,253</u> | <u>1,550,876</u> | <u>795,279</u> | <u>8,323,408</u> | <u>9,363,077</u> |
| Operating Expenses | | | | | | | | | |
| Professional fees | 198,506 | 818,993 | 10,177 | 15,715 | 11,193 | 983,331 | 25,031 | 2,062,946 | 1,757,234 |
| Travel and entertainment | 22,066 | 585 | 9,878 | 11,026 | 767 | 31,022 | 95,208 | 170,552 | 514,561 |
| Printing and advertising | 9,040 | - | 2,931 | 58,356 | 23,416 | 187,079 | 45,596 | 326,418 | 473,966 |
| Supplies | 130,249 | 1,530 | 74,756 | 157,981 | 15,397 | 118,376 | 36,108 | 534,397 | 939,308 |
| Occupancy and repairs | 5,615 | 853,748 | - | 1,195 | - | - | - | 860,558 | 1,084,155 |
| Insurance | 1,545 | 307,279 | - | 70,000 | - | - | - | 378,824 | 330,821 |
| Interest expense | - | 661,860 | - | - | - | 31,045 | - | 692,905 | 791,254 |
| Bad debt expense | <u>30,000</u> | <u>-</u> | <u>40,000</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>180,000</u> | <u>250,000</u> | <u>280,674</u> |
| Total operating expenses | <u>397,021</u> | <u>2,643,995</u> | <u>137,742</u> | <u>314,273</u> | <u>50,773</u> | <u>1,350,853</u> | <u>381,943</u> | <u>5,276,600</u> | <u>6,171,973</u> |
| Total personnel costs and operating expenses | <u>\$3,882,411</u> | <u>\$3,047,816</u> | <u>\$925,860</u> | <u>\$1,435,944</u> | <u>\$229,026</u> | <u>\$2,901,729</u> | <u>\$1,177,222</u> | <u>\$13,600,008</u> | <u>\$15,535,050</u> |

PENNSYLVANIA ACADEMY OF THE FINE ARTS

STATEMENTS OF CASH FLOWS

Years Ended June 30, 2021 And 2020

| | <u>2021</u> | <u>2020</u> |
|--|---------------------|---------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Change in net assets | \$ 14,031,304 | \$ (4,435,890) |
| Adjustments to reconcile change in net assets to net cash provided by operating activities | | |
| Depreciation | 2,088,165 | 2,164,245 |
| Net unrealized depreciation (appreciation) on long-term investments | (10,705,080) | 415,399 |
| Net realized gains on long-term investments | (2,834,318) | (417,939) |
| Net unrealized appreciation on outside perpetual trusts | (2,939,464) | (43,161) |
| Contributions restricted for endowment | (378,400) | (297,151) |
| Loss on interest rate swap termination | - | 405,046 |
| Loss on early extinguishment of deferred financing expenses | - | 180,144 |
| Amortization of right of use asset | 363,573 | - |
| Forgiveness of note receivable | 22,142 | 19,512 |
| Bad debt expense, net of recapture | 250,000 | 151,737 |
| Change in market value of swap | (1,423,881) | 539,735 |
| Amortization of deferred bond cost | 20,560 | 8,349 |
| (Increase) decrease in assets | | |
| Accounts receivable | (47,178) | (194,398) |
| Inventories | 71,763 | (23,807) |
| Pledges receivable | 1,310,400 | 2,046,151 |
| Prepaid expenses and other assets | (168,784) | 127,137 |
| Increase (decrease) in liabilities | | |
| Accounts payable | 248,631 | (91,716) |
| Accrued expenses | (129,410) | 200,197 |
| Deferred revenue | (181,327) | (83,825) |
| Net cash provided by (used for) operating activities | <u>(401,304)</u> | <u>669,765</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchase of property and equipment | (367,987) | (659,045) |
| Repayment of note receivable | 44,283 | - |
| Purchases of long-term investments | (7,751,506) | (9,398,623) |
| Proceeds from sale of long-term investments | <u>10,977,483</u> | <u>10,804,487</u> |
| Net cash provided by investing activities | <u>2,902,273</u> | <u>746,819</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Contributions restricted for endowment | 378,400 | 297,151 |
| Net proceeds from (repayments of) line of credit | (1,700,000) | (7,500,000) |
| Interest on lease liability | 20,240 | - |
| Finance lease liability payments | (383,813) | - |
| Payment of interest rate swap termination fee | - | (405,046) |
| Proceeds from refundable advance | 1,596,447 | 1,799,100 |
| Forgiveness of PPP loan | (1,799,100) | - |
| Payment of bond issuance costs | - | (308,396) |
| Issuance of long-term debt | - | 25,000,000 |
| Repayments of long-term debt | <u>-</u> | <u>(20,459,000)</u> |
| Net cash used for financing activities | <u>(1,887,826)</u> | <u>(1,576,191)</u> |
| Net increase (decrease) in cash and cash equivalents | 613,143 | (159,607) |
| CASH AND CASH EQUIVALENTS | | |
| Beginning of year | <u>250,315</u> | <u>409,922</u> |
| End of year | <u>\$ 863,458</u> | <u>\$ 250,315</u> |
| SUPPLEMENTAL INFORMATION | | |
| Cash paid for interest | <u>\$ 692,905</u> | <u>\$ 866,460</u> |
| Right-of-use – asset in exchange for new financing lease liability | <u>\$ 1,328,871</u> | <u>\$ -</u> |

The accompanying notes are an integral part of these statements.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS

June 30, 2021 And 2020

(1) NATURE OF ORGANIZATION

NATURE OF ORGANIZATION

Founded in 1805, the Pennsylvania Academy of the Fine Arts (“PAFA”) is the first and oldest art college and art museum in the United States. PAFA’s mission statement declares:

As the first art museum and college in the United States, PAFA celebrates the transformative power of art and art making.

PAFA inspires the public by expanding the stories of American art through its collections, exhibitions, and programs; and educates artists from around the world to be innovative makers and critical thinkers with a deep understanding of traditions and the ability to challenge conventions.

Through its world-class museum and college, PAFA nurtures and recognizes artists at every turn in their career.

The museum collects, preserves, exhibits and interprets works of American art, both historic and contemporary, for the benefit of public education. The museum is committed to expanding knowledge of, and appreciation for, American artists and their work.

The College of Fine Arts at PAFA offers four nationally and regionally accredited degree and certificate programs – a Bachelor of Fine Arts degree program, offering concentrations in painting, drawing, sculpting, illustration, and printmaking; a post-baccalaureate certificate program; a Master of Fine Arts degree program; and a second Master of Fine Arts degree program that combines three summers of intensive residency with two academic years of virtual classroom study. Students may also earn a Bachelor of Fine Arts Degree via a collaborative program with the University of Pennsylvania, dating back to 1929.

The Brodsky Center is an innovative art making venture that publishes prints, artist books, and handmade paper objects in collaboration with artists in residence and teaches entrepreneurial skills to PAFA’s students.

In addition, PAFA offers a wide array of public education programs, serving audiences ranging from young children to adults.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies followed by PAFA are described below.

BASIS OF PRESENTATION

CASH EQUIVALENTS

PAFA considers highly liquid financial instruments purchased with an original maturity of three months or less to be cash equivalents.

CONCENTRATION OF CREDIT RISK

PAFA occasionally maintains deposits in excess of federally insured limits. Accounting Standards Codification (“ASC”) 825, “*Financial Instruments*”, identifies these items as a concentration of credit risk requiring disclosure, regardless of the degree of risk. The risk is managed by monitoring the financial institutions in which deposits are made.

PAFA’s principal financial instruments subject to credit risk are its investments. The investments are managed by professional advisors subject to PAFA’s investment goals for total investment return, yield, and tolerance of investment risk and investment turnover. The degree and concentration of credit risk vary by the type of investment.

USE OF ESTIMATES

The preparation of the financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure 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.

INVESTMENTS

PAFA records investments at fair market value. Fair value of investments is determined using quoted market prices of a national securities exchange. Unrealized and realized gains and losses on investments are recognized as increases or decreases in net assets without donor restriction unless their use is restricted by explicit donor stipulations or by law.

PROPERTY, BUILDINGS AND EQUIPMENT

Property, buildings and equipment are stated at cost or appraised value at the date of donation.

Maintenance, repairs and minor renewals are charged to expense. Major renewals, improvements or renovations which prolong the life of the assets are capitalized. The cost of current additions to exhibits, books and art literature is charged to expense. A portion of such cost may be reimbursed by designated contributed funds and income of certain endowment funds.

Depreciation is provided over the estimated useful lives of the assets using the straight-line method. Estimated useful lives are as follows:

| | |
|-----------------------------------|---------------|
| Buildings | 10 – 40 years |
| Building improvement | 10 – 20 years |
| Equipment, furniture and fixtures | 3 – 5 years |

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

FUNDS HELD IN TRUST BY OTHERS

PAFA is the recipient/beneficiary of several irrevocable perpetual trust arrangements which are held by others. PAFA accounts for perpetual trusts held by third parties at the fair value of the assets.

WORKS OF ART

PAFA maintains a collection of rare American art that is held for public exhibition. The collection is kept under curatorial care and is subject to PAFA's policy that requires the proceeds from the sales of accessioned collection items to be used only to acquire other items for collection. PAFA does not recognize the contributions of donated collection items, as its collections are not capitalized. During the year ended June 30, 2021 and 2020, PAFA had donated accessions with approximate appraised values totaling \$283,700 and \$455,180, respectively. Collection items purchased but not capitalized totaled \$1,075,982 and \$1,520,803 during the years ended June 30, 2021 and 2020, respectively. In addition, PAFA received \$2,170 for the sale of art works during the year ended June 30, 2020. There was no sale of art works during the year ended June 30, 2021.

INCOME TAXES

PAFA has been granted tax-exempt status as a nonprofit organization under Section 501(c)(3) of the Internal Revenue Code, which is not a private foundation under Section 509(a) of the Code, and files a Form 990 (Return of Organization Exempt from Income Tax) annually for information purposes. Accordingly, no provision for income taxes is provided in the accompanying financial statements.

PAFA has reviewed its tax positions and has concluded that no liability for unrecognized tax benefits should be recorded related to uncertain tax positions taken on federal and state tax returns for the open tax years (2017 – 2019) or is expected to be taken in the current 2020 tax year.

NET ASSETS

PAFA's financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America. The principles require that net assets, revenues, gains, expenses and losses be classified without donor restriction or with donor restriction based on the existence or absence of donor-imposed restrictions as follows:

Net Assets Without Donor Restrictions: Net assets that are not subject to donor-imposed stipulations. Net assets without restriction of PAFA include the following:

Undesignated: Include the revenues and expenses associated with the principal educational mission of PAFA.

Funds Functioning as Endowment: Includes the contribution without donor restriction bequests which the Board of Trustee have designated as funds functioning as endowment for the purpose of administering the operations of the Brodsky Center (the "Center" – see **Note 11**). Investment income in excess of the spending rate utilized by PAFA for its endowment funds will be reinvested and used for future Center operations.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

Net Assets With Donor Restrictions: Net assets whose use by PAFA is subject to donor-imposed or legal stipulations that can be fulfilled by actions of PAFA pursuant to those stipulations or that expire by the passage of time. Expiration of the restriction is reported by reclassification from net assets with donor restriction by time/purpose to net assets without donor restrictions. Net assets with donor restrictions also includes gifts, trusts and pledges which require, by donor restriction, that the corpus be invested in perpetuity and only the income be made available for program operations in accordance with donor restrictions and beneficial interest in perpetual trusts, which are held by third parties for the benefit of PAFA.

Revenues and net gains are reported as increases in net assets without donor restrictions unless the revenue is restricted by donor-implied restrictions. Expenses are reported as decreases in net assets without donor restrictions. Periodically donor restrictions related to net assets may be clarified or changed; such changes are reflected as fund transfers in the period in which they are identified.

REVENUE RECOGNITION

PAFA recognizes revenue from student tuition and fees during the year in which the related services are provided to students. The performance obligation of delivering educational services is simultaneously received and consumed by the students; therefore, the revenue is recognized ratably over the course of the academic year. Payment for tuition can be made in full or in installments. All amounts received prior to the commencement of the academic year, including enrollment deposits, are deferred to the applicable period. Scholarships provided to students are recorded as a reduction from the posted tuition rates at the time revenue is recognized. PAFA recognizes revenue from its summer programs during the summer of the fiscal year in which the majority of the program occurs.

PAFA recognizes contributions when cash, securities or other assets are received, upon receipt of an unconditional promise to give, or upon notification of a beneficial interest. Conditional contributions include donor-imposed conditions with one or more barriers that must be overcome before PAFA is entitled to the assets transferred or promised and there is a right of return to the contributor for assets transferred or a right of release of the promisor from its obligation to transfer assets. PAFA recognizes the contribution when the conditions are substantially met or explicitly waived. Unconditional contributions are classified as without donor restrictions unless there are donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose of the restriction is accomplished, net assets with donor restrictions are then classified to net assets without donor restrictions and reported in the statement of activities as “**net assets released from restrictions.**”

ALLOCATION OF FUNCTIONAL EXPENSES

The costs of providing PAFA’s programs have been summarized on a functional basis in the statement of functional expenses. Costs are directly charged to a specific activity when the costs pertain solely to such activity. Certain program costs have been allocated based on revenues and other costs have been allocated between programs and supporting services based on direct expenses attributable to programs and supporting services.

PRIOR YEAR INFORMATION

The financial statements include certain prior year summarized comparative information in total, but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with PAFA’s financial statements for the year ended June 30, 2020, from which the summarized information was derived.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

NEW ACCOUNTING PRONOUNCEMENTS ADOPTED

In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-02, *Leases (Topic 842)*. Topic 842 requires an organization to recognize in the statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. The Academy implemented the provisions of ASU 2016-02 during the year ended June 30, 2021 by applying the modified retrospective transition approach for leases existing as of the beginning of the period of adoption. As such, the Academy has not adjusted the statement of financial position for comparative periods: and, this ASU did not result in a cumulative effect adjustment to the opening balance of net assets. The Academy has elected to apply the package of practical expedients within ASU 2016-02 such that the Academy did not reassess: (1) if expired or existing contracts are, or contain, leases; (2) lease classification for any expired or existing leases; and (3) initial direct costs for any existing leases. The Academy has elected, as a practical expedient, not to separate non-lease components from lease components, and instead account for each separate component as a single lease component for all lease arrangements, as lessee. In addition, the Academy has elected, as a practical expedient, not to apply lease recognition requirements to short-term lease arrangements, generally those with a lease term of less than 12-months, for all classes of underlying assets. Refer to Note 13 for additional details.

RECLASSIFICATION

Certain account balances in the 2020 financial statements have been reclassified to conform to the 2021 financial statement presentation.

(3) CONTRIBUTIONS RECEIVABLE

Contributions receivable consist of the following at June 30:

| | <u>2021</u> | <u>2020</u> |
|-------------------------------------|--------------------|--------------------|
| Amounts due in: | | |
| Less than one year | \$1,698,512 | \$2,412,604 |
| One to five years | 775,833 | 1,551,375 |
| More than five years | <u>-</u> | <u>-</u> |
| Total pledges receivable | 2,474,345 | 3,963,979 |
| Less: discount to net present value | (16,448) | (45,421) |
| Allowance for doubtful accounts | <u>(254,793)</u> | <u>(225,054)</u> |
| Pledges receivable – long-term | <u>\$2,203,104</u> | <u>\$3,693,504</u> |

Amounts due in the future have been discounted to their present values using discount rates ranging from 0.07% to 1.82%.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

(4) INVESTMENTS

Investments consist of the following at June 30:

| | 2021 | | | |
|---|---------------------|-------------------------|--------------------------|---------------------|
| | <u>Cost</u> | <u>Unrealized Gains</u> | <u>Unrealized Losses</u> | <u>Market Value</u> |
| Money Market Funds | \$ 1,627,115 | \$ - | \$ - | \$ 1,627,115 |
| Common Stocks | 11,950,027 | 8,594,833 | - | 20,544,860 |
| Mutual Funds/Exchange Traded Funds | 19,483,871 | 3,687,379 | - | 23,171,250 |
| Pooled Investment Fund - Private Equity/Hedge Fund | <u>11,053,300</u> | <u>7,518,648</u> | <u>-</u> | <u>18,571,948</u> |
| | <u>\$44,114,313</u> | <u>\$19,800,860</u> | <u>\$ -</u> | <u>\$63,915,173</u> |

| | 2020 | | | |
|---|---------------------|-------------------------|--------------------------|---------------------|
| | <u>Cost</u> | <u>Unrealized Gains</u> | <u>Unrealized Losses</u> | <u>Market Value</u> |
| Money Market Funds | \$ 1,056,826 | \$ - | \$ - | \$ 1,056,826 |
| Common Stocks | 12,172,160 | 4,782,597 | - | 16,954,757 |
| Mutual Funds/Exchange Traded Funds | 22,041,638 | 526,855 | - | 22,568,493 |
| Pooled Investment Fund - Private Equity/Hedge Fund | <u>9,235,348</u> | <u>3,786,328</u> | <u>-</u> | <u>13,021,676</u> |
| | <u>\$44,505,972</u> | <u>\$9,095,780</u> | <u>\$ -</u> | <u>\$53,601,752</u> |

PAFA has various pooled investment funds, within BBH Wealth Strategies, LLC REMS Group Series, for \$18,571,948 and \$13,021,676 as of June 30, 2021 and 2020, respectively. The fair value of the investments is based on the net asset value of the funds and is furnished by each fund's management. The investment objective of the BBH Wealth Strategies Series of investment funds is to achieve long-term capital growth and current income by investing in a portfolio of debt and domestic and international equity securities including private debt and publicly traded equity securities. As of June 30, 2021 and 2020, PAFA has no outstanding commitment for further investment into this Series of funds. Investors of these funds are eligible for redemptions ranging from month-end to annual redemptions with proper prior notification.

Investments as of June 30, 2021 and 2020, include without donor restricted investments of \$31,580,175 and \$27,841,967 respectively, which are invested separately from those investments for the endowment funds. Other investment income of \$6,890,934 and \$654,600 for the years ended June 30, 2021 and 2020, respectively, represents the net investment income on these without donor restricted investments.

The change in unrealized gain/(loss) was \$10,705,080 and \$(415,399) in 2021 and 2020, respectively.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

For the years ended June 30, 2021 and 2020, the Board approved a 10% and 5% spending rate, respectively, to its net assets to ensure preservation and growth of the corpus and to provide for a constant stream of income. The spending rate is based on the average net asset balance for the previous three years. If investment income during the year is in excess of the spending rate, the balance is reinvested. If investment income is not sufficient, the balance is provided from previously reinvested amounts. The following schedule summarizes the investment return of the endowment funds and its classification in the statement of activities:

| | <u>Without Donor Restrictions</u> | <u>With Donor Restrictions</u> | <u>June 30, 2021 Total</u> | <u>June 30, 2020 Total</u> |
|---|---------------------------------------|------------------------------------|------------------------------------|------------------------------------|
| Interest and dividends (net of fees of \$121,644 in 2021 and \$116,674 in 2020, respectively) | \$ 482,953 | \$ - | \$ 482,953 | \$ 507,195 |
| Net realized and unrealized gains/(losses) | <u>385,296</u> | <u>6,518,678</u> | <u>6,903,974</u> | <u>(368,691)</u> |
| Return on long-term investments | 868,249 | 6,518,678 | 7,386,927 | 138,504 |
| Investment return designated for current operations | <u>718,690</u> | <u>947,644</u> | <u>1,666,334</u> | <u>1,256,209</u> |
| Investment return in excess(deficit) of amounts designated for current operations | <u>\$ 149,559</u> | <u>\$ 5,571,034</u> | <u>\$ 5,720,593</u> | <u>\$ (1,117,705)</u> |

PAFA utilized various methods to measure the fair value of its investments on a recurring basis. Generally accepted accounting principles establish a hierarchy that prioritizes inputs to valuation methods. The three levels of inputs are described below:

- Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities that PAFA has the ability to access.
- Level 2 – Observable inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These inputs may include quoted prices for the identical instrument on an inactive market, prices for similar instruments, interest rates, prepayment speeds, credit risk, yield curves, default rates and similar data.
- Level 3 – Unobservable inputs for the asset or liability, to the extent relevant observable inputs are not available, representing PAFA's own assumptions about the assumptions a market participant would use in valuing the asset or liability, and would be based on the best information available.

The inputs methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

The summary of inputs used to value PAFA’s assets and liabilities that are carried at fair value as of June 30, 2021 and 2020 are as follows:

| | 2021 | | | Total |
|---|---------------------|--------------------|---------------------|---------------------|
| | Level 1 | Level 2 | Level 3 | |
| Investments | | | | |
| Money Market Funds | \$ 1,627,115 | \$ - | \$ - | \$ 1,627,115 |
| Common Stocks | 20,544,860 | - | - | 20,544,860 |
| Mutual Funds | <u>23,171,250</u> | <u>-</u> | <u>-</u> | <u>23,171,250</u> |
| | <u>\$45,343,225</u> | <u>\$ -</u> | <u>\$ -</u> | 45,343,225 |
| Alternative Investments reported at Net Asset Value | | | | <u>18,571,948</u> |
| | | | | <u>\$63,915,173</u> |
| Beneficial Interest in Perpetual Trust | <u>\$ -</u> | <u>\$ -</u> | <u>\$13,496,713</u> | <u>\$13,496,713</u> |
| Interest Rate Swap Asset | <u>\$ -</u> | <u>\$ 652,419</u> | <u>\$ -</u> | <u>\$ 652,419</u> |
| | | | | |
| | 2020 | | | |
| | Level 1 | Level 2 | Level 3 | Total |
| Investments | | | | |
| Money Market Funds | \$ 1,056,826 | \$ - | \$ - | \$ 1,056,826 |
| Common Stocks | 16,954,757 | - | - | 16,954,757 |
| Mutual Funds | <u>22,568,493</u> | <u>-</u> | <u>-</u> | <u>22,568,493</u> |
| | <u>\$40,580,076</u> | <u>\$ -</u> | <u>\$ -</u> | 40,580,076 |
| Alternative Investments reported at Net Asset Value | | | | <u>13,021,676</u> |
| | | | | <u>\$53,601,752</u> |
| Beneficial Interest in Perpetual Trust | <u>\$ -</u> | <u>\$ -</u> | <u>\$10,557,249</u> | <u>\$10,557,249</u> |
| Interest Rate Swap Obligation | <u>\$ -</u> | <u>\$(771,462)</u> | <u>\$ -</u> | <u>\$(771,462)</u> |

The Beneficial Interest in Perpetual Trust is measured at the estimated cash flows which involve unobservable inputs. As a result, the present value technique is a Level 3 input.

There were no transfers between Level 1 and Level 2 during the years ended June 30, 2021 or 2020.

The changes in investments measured at fair value for which PAFA used Level 3 inputs to determine fair value are as follows:

| | Beneficial Interest In Perpetual Trust | |
|------------------|--|---------------------|
| | 2021 | 2020 |
| Balance, July 1 | \$10,557,249 | \$10,514,088 |
| Unrealized gains | <u>2,939,464</u> | <u>43,161</u> |
| Balance, June 30 | <u>\$13,496,713</u> | <u>\$10,557,249</u> |

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

(5) PROPERTY, BUILDINGS AND EQUIPMENT

A summary of property, buildings and equipment as of June 30 is as follows:

| | <u>2021</u> | <u>2020</u> |
|-----------------------------------|----------------------|----------------------|
| Land, buildings and improvements | \$ 76,965,560 | \$ 76,145,275 |
| Furniture, fixtures and equipment | <u>5,463,884</u> | <u>5,428,101</u> |
| | 82,429,444 | 81,573,376 |
| Less accumulated depreciation | <u>(31,688,302)</u> | <u>(29,600,138)</u> |
| | 50,741,142 | 51,973,238 |
| Construction in progress | <u>-</u> | <u>488,082</u> |
| | <u>\$ 50,741,142</u> | <u>\$ 52,461,320</u> |

Conditional asset retirement obligations (“**AROs**”) that meet the definition of liabilities should be recognized when incurred if their fair value can be reasonably estimated. As of June 30, 2021, PAFA was unable to determine the extent of any remediation AROs that would be required in the future.

Depreciation expense was \$2,088,165 and \$2,164,245 for years ended June 30, 2021 and 2020, respectively.

(6) BENEFICIAL INTEREST IN PERPETUAL TRUSTS

The beneficial interest in perpetual trusts of \$13,496,713 and \$10,557,249 at June 30, 2021 and 2020, respectively, includes PAFA’s respective share of the fair value of the total funds held in trust by others for which PAFA is the recipient of all or a percentage of the income.

(7) COVID-19 AND REFUNDABLE ADVANCE/PAYROLL PROTECTION PROGRAM

In December 2019, a novel strain of the coronavirus (“COVID-19”) was reported in China. The World Health Organization has declared COVID-19 to constitute a “Public Health Emergency of International Concern”. This outbreak has affected virtually every industry and has created volatility in stock markets throughout the world. Many federal and state governments have implemented numerous restrictions, mandated various closures and quarantine requirements in connection with the COVID-19 outbreak. The extent of the impact of COVID-19 on PAFA’s operational and financial performance will depend on future developments, including the duration and spread of the outbreak and the impact on PAFA’s funders, donors, employees and vendors, all of which are uncertain and cannot be predicted.

On April 14, 2020, PAFA received a \$1,799,100 loan under the Small Business Administration’s (“**SBA**”) Payment Protection Program (the “**PPP Loan**”). PAFA considered this to be a conditional contribution as it expected to meet the criteria for loan forgiveness upon incurring eligible expenditures and when its application for forgiveness is accepted by the SBA. PAFA considered the incurrence of eligible expenses and the acceptance of its application for forgiveness to be barriers in the PPP Loan agreement and as such, would recognize contribution income when these conditions were substantially met. As of June 30, 2020, PAFA had recorded \$1,799,100 as a refundable advance. During the year ended June 30, 2021, PAFA had met all conditions of the program and the loan was forgiven on June 26, 2021. As such, the loan has been recognized in the Statement of Activities and Changes in Net Assets as PPP loan forgiveness in fiscal year 2021.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

On March 24, 2021, PAFA received a \$1,596,447 loan under the Small Business Administration's ("**SBA**") Paycheck Protection Program Second Draw Loan ("**PPP Second Draw Loan**") under the Consolidated Appropriations Act 2021, Additional Coronavirus Response and Relief Provisions. PPP Second Draw Loans are eligible for forgiveness if PAFA incurs qualifying expenses over a period of time not to exceed 24 weeks. The period of time in which qualifying expenses may be incurred commences upon receipt of the loan. Any portion of the loan not forgiven is payable over a 5-year period at an interest rate of 1%. PAFA considers the incurrence of eligible expenses and the acceptance of its application for forgiveness to be barriers in the PPP Second Draw Loan agreement and as such, will recognize contribution income when these conditions are substantially met. As of June 30, 2021, PAFA had recorded \$1,596,447 as a refundable advance for the PPP Second Draw Loan.

(8) LINE OF CREDIT

PAFA has two revolving lines of credit for \$10,000,000. The lines of credit, \$5,000,000 for capital projects and \$5,000,000 for working capital, are collateralized by certain marketable securities held by a financial institution and expire July 31, 2023. Interest on the line of credit is payable monthly at a variable percentage based upon the J.P. Morgan Chase Guaranty Prime Rate minus 1.40% (2.75% as of both June 30, 2021 and 2020). There was no balance outstanding on the lines of credit as of June 30, 2021. At June 30, 2020, the outstanding balance on the lines of credit was \$1,700,000. Interest expense on the lines of credit was \$31,046 and \$306,548 for the years ended June 30, 2021 and 2020, respectively.

In addition, PAFA opened a revolving line of credit for \$1,500,000 from the financial institution who purchased the Revenue Bonds, Series 2020A of which PAFA borrowed the Bond proceeds (see Note 9). The line of credit of \$1,500,000 for working capital is collateralized by certain property owned by PAFA and expires on March 31, 2022. Interest on the line of credit is payable monthly at the LIBOR rate plus 2.50%, however, at no time shall the rate be below 4.25%. At June 30, 2021 and 2020, there was no outstanding balance on the line of credit. PAFA is subject to the same financial covenants for the line of credit as those disclosed for the Revenue Bond, Series 2020A debt.

(9) LONG-TERM DEBT

On June 17, 2020, PAFA borrowed \$25,000,000 through the issuance of tax-exempt Revenue Bonds, Series 2020A from the Philadelphia Authority for Industrial Development (the "**Authority**"), the proceeds of which were used to refinance its 2015A Bonds, a portion of the outstanding credit lines with Haverford Trust, and to finance the costs of issuance. The Bryn Mawr Trust Company purchased the Bonds from the Authority.

The tax-exempt Bonds will mature on June 17, 2035 and may be prepaid in whole or in part at any time. The tax-exempt interest rates are variable and are adjustable monthly by The Bryn Mawr Trust Company. The floating rate per annum is the sum of LIBOR plus 2.50% multiplied by seventy-eight percent (effective rate as of June 30, 2021 and 2020 was 2.02% and 2.08% respectively). Interest is paid monthly on the outstanding principal of the 2020 Bonds. Bonds payable of \$24,713,000 and \$24,692,460 as of June 30, 2021 and 2020 reflects bonds payable of \$25,000,000 and \$25,000,000, net of unamortized deferred financing expenses of \$286,980 and \$307,540, respectively. Deferred financing expenses are being amortized on a straight-line basis over the life of the Bonds. In conjunction with the repayment of 2015 Bonds, the remaining deferred bond issuance cost of \$180,144 associated with those Bonds was written off and is included as loss on early extinguishment of deferred financing expenses for the year ended June 30, 2020.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

In connection with the issuance of the 2020 Bonds, PAFA entered into an interest rate swap agreement with the Bryn Mawr Trust Company. The swap agreement requires PAFA to pay a fixed interest rate of 2.75% on a notional balance of \$20,000,000 while receiving a variable interest rate equal to the rate paid for the Bond. Prior to the issuance of the 2020 Bonds on June 17, 2020, the swap agreement in effect required PAFA to pay a fixed interest rate of 2.62% on a notional balance of \$12,600,000 while receiving a variable interest rate equal to the rate paid for the 2015 Bond. The purpose of the interest rate swap agreement currently in effect is to hedge against increases in the variable interest rates on the 2020 Bonds. The market value of the interest rate swaps was \$652,419 and \$(771,462) in favor of PAFA (the bank) as of June 30, 2021 and 2020, respectively, and is included in other assets (liabilities) in the statements of financial position. As a result of the refinancing of the 2015 Bonds, PAFA incurred an interest rate swap termination fee of \$405,046 for the year ended June 30, 2020 which is reflected as a loss on termination of interest rate swap within non-operating revenues, expenses and gains/losses in the statement of activities and changes in net assets.

PAFA must maintain certain financial covenants in accordance with the 2020 Bond agreement:

- a. Maintain unencumbered liquidity at least equal to \$27,000,000 tested semi-annually
- b. Maintain net assets without donor restriction at least equal to \$32,000,000 tested semi-annually

Total interest expense on the tax-exempt bonds, 2020 and 2015 issues, was \$661,859 and \$484,705 for the years ended June 30, 2021 and 2020, respectively.

Redemption payments required under the Bond Agreements are as follows:

| <u>Year Ending June 30,</u> | <u>Amount</u> |
|--------------------------------------|----------------------|
| 2022 | \$ - |
| 2023 | 45,305 |
| 2024 | 540,309 |
| 2025 | 557,468 |
| 2026 | 573,211 |
| Thereafter | <u>23,283,707</u> |
| Bond Payable at June 30, 2021, gross | 25,000,000 |
| Deferred Financing Expenses | <u>(286,980)</u> |
| Bond Payable at June 30, 2021, Net | <u>\$ 24,713,020</u> |
| Bond Payable at June 30, 2020, gross | 25,000,000 |
| Deferred Financing Expenses | <u>(307,540)</u> |
| Bond Payable at June 30, 2020, Net | <u>\$ 24,692,460</u> |

(10) RETIREMENT PLANS

PAFA has a defined contribution plan covering employees over the age of 21 who work 1,000 hours or more in a calendar year. Under this plan, employees can contribute to the plan immediately, not to exceed the limits imposed by IRC 402(g). Effective after ninety days of employment, PAFA matches up to 4% for each employee contribution. During the years ended June 30, 2021 and 2020, PAFA contributed approximately \$181,000 and \$186,000, respectively, to the plan.

PAFA also has a defined benefit pension plan covering one former employee. Benefits under the plan are based on the employee's years of service and compensation. The related assets and liabilities of this plan are not material to the financial statements.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

(11) NET ASSETS

Net assets with a donor restriction at June 30, 2021 and 2020 are available for the following purposes:

| | <u>2021</u> | <u>2020</u> |
|--|---------------------|----------------------|
| Subject to expenditure for a specified purpose: | | |
| Major gifts-time restriction/purpose | \$ 1,613,066 | 1,386,228 |
| Scholarships | <u>122,411</u> | <u>850,540</u> |
| | <u>1,735,477</u> | <u>2,236,768</u> |
| Perpetual in nature: | | |
| Operations | 4,917,018 | 5,064,406 |
| Art acquisitions and conservation | 3,349,691 | 3,349,691 |
| Museum operations | 1,531,868 | 1,031,868 |
| College scholarships and prizes | 16,394,984 | 16,369,196 |
| College – other | 1,309,979 | 1,309,979 |
| Beneficial interest in perpetual trusts | <u>13,496,713</u> | <u>10,557,249</u> |
| | <u>41,000,253</u> | <u>37,682,389</u> |
| Accumulated endowment income | <u>4,210,590</u> | <u>(1,360,444)</u> |
| Total net assets with donor restrictions | <u>\$46,946,320</u> | <u>\$ 38,558,713</u> |

Net assets were released from donor restrictions by satisfying the restricted purpose during the year ended June 30, 2021, as follows:

Purpose and time restrictions accomplished:

| | <u>2021</u> |
|--------------------------------------|--------------------|
| Acquisition of art | \$ 271,779 |
| Major gifts-time restriction/purpose | 1,320,739 |
| Scholarships | <u>1,620,943</u> |
| | <u>\$3,213,461</u> |

Endowment net asset composition by type of fund as of June 30, 2021 and 2020:

| | <u>2021</u> | | |
|--------------------------------------|----------------------|----------------------|----------------------|
| | <u>Without Donor</u> | <u>With Donor</u> | <u>Total</u> |
| | <u>Restrictions</u> | <u>Restrictions</u> | |
| Donor restricted endowment funds | | | |
| perpetual in duration – | | | |
| Original gift amount | \$ - | \$ 41,000,253 | \$ 41,000,253 |
| Accumulated endowment income | - | 4,210,590 | 4,210,590 |
| Funds functioning as endowment funds | <u>923,977</u> | <u>-</u> | <u>923,977</u> |
| Total Fund | <u>\$ 923,977</u> | <u>\$ 45,210,843</u> | <u>\$ 46,134,820</u> |

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

| | 2020 | | <u>Total</u> |
|--------------------------------------|---------------------------------------|------------------------------------|----------------------|
| | <u>Without Donor Restrictions</u> | <u>With Donor Restrictions</u> | |
| Donor restricted endowment funds | | | |
| perpetual in duration – | | | |
| Original gift amount | \$ - | \$ 37,682,389 | \$ 37,682,389 |
| Accumulated endowment income | - | (1,360,444) | (1,360,444) |
| Funds functioning as endowment funds | <u>774,418</u> | <u>-</u> | <u>774,418</u> |
| Total Fund | <u>\$ 774,418</u> | <u>\$ 36,321,945</u> | <u>\$ 37,096,363</u> |

PAFA classifies the original value of gifts received with donor stipulations that require them to be held in perpetuity as net assets with donor restriction. Commonwealth of Pennsylvania law stipulates that realized and unrealized gains on endowment assets may be expended for the purposes stipulated by the donors only to the extent that the total of such expenditures, including dividends and interest and less fees, do not exceed 7% of the average of the three most recent fiscal years' fair values of the net assets with donor restriction held in perpetuity. Realized and unrealized gains in excess of the annual limitation would be included in the statements of activities as increases in the net assets with donor restriction. Such restricted amounts may be released to net assets without donor restriction in future years based on authorization by PAFA only to the extent of the 7% limitation applicable to the year in which they are to be released. During the year ended June 30, 2021, the Commonwealth of Pennsylvania allowed up to 10% to be spent on endowment assets as a result of the COVID-19 pandemic restrictions.

PAFA maintains a quasi-endowment fund known as the Brodsky Center (the "Center"). The Center was established to promote the art of printmaking through the use of its printing equipment. In connection with receiving the quasi-endowment funds, PAFA has agreed to spend the investment earnings from these quasi-endowment funds in compliance with its Board of Trustees' policy with respect to all of its endowment funds. The board-designated net assets related to the Brodsky Center as presented in the statement of financial position was \$923,977 and \$774,418 as of June 30, 2021 and 2020, respectively.

FUNDS WITH DEFICIENCIES

The fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor requires PAFA to retain as a fund of perpetual duration. In accordance with generally accepted accounting principles, deficiencies of this nature are reported in net assets with donor restrictions. As of June 30, 2020, restricted endowment funds had deficiencies which amounted to \$1,360,444. These deficiencies resulted primarily from unfavorable market fluctuations in the current year. The market value and cost basis associated with endowments with deficiencies was \$25,764,696 and \$27,125,140 as of June 30, 2020. As of June 30, 2021, no restricted endowment funds had deficiencies.

Changes in endowment net assets for the years ended June 30, 2021 and 2020:

| | 2021 | | <u>Total</u> |
|--|---------------------------------------|------------------------------------|----------------------|
| | <u>Without Donor Restrictions</u> | <u>With Donor Restrictions</u> | |
| Endowment net assets, beginning of year | \$ 774,418 | \$ 36,321,945 | \$ 37,096,363 |
| Investment income, net | 482,953 | - | 482,953 |
| Realized and unrealized gains | 385,296 | 6,518,678 | 6,903,974 |
| Contributions | - | 378,400 | 378,400 |
| Endowment income designated for current operations | (718,690) | (947,644) | (1,666,334) |
| Change in beneficial interest in perpetual trust | <u>-</u> | <u>2,939,464</u> | <u>2,939,464</u> |
| | <u>\$ 923,977</u> | <u>\$ 45,210,843</u> | <u>\$ 46,134,820</u> |

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

| | 2020 | | |
|--|---------------------------------------|------------------------------------|----------------------|
| | <u>Without Donor Restrictions</u> | <u>With Donor Restrictions</u> | <u>Total</u> |
| Endowment net assets, beginning of year | \$ 808,024 | \$ 37,065,731 | \$ 37,873,755 |
| Investment income, net | 507,195 | - | 507,195 |
| Realized and unrealized gains/(losses) | 184,600 | (553,291) | (368,691) |
| Contributions | - | 297,152 | 297,152 |
| Endowment income designated for current operations | (725,401) | (530,808) | (1,256,209) |
| Change in beneficial interest in perpetual trust | <u>-</u> | <u>43,161</u> | <u>43,161</u> |
| | <u>\$ 774,418</u> | <u>\$ 36,321,945</u> | <u>\$ 37,096,363</u> |

(12) RELATED PARTY TRANSACTIONS

PAFA had the following related party transactions:

- ♦ PAFA uses the services of a Trust Company where three Board members are paid Directors. Assets under management with this investment company totaled approximately \$32,335,000 and \$25,760,000 as of June 30, 2021 and 2020, respectively. PAFA was charged investment fees by the investment company. The fee was approximately for \$122,000 and \$117,000 for the years ended June 30, 2021 and 2020, respectively. In addition, this Trust Company provides two lines of credit for PAFA; interest expense during the years ended June 30, 2021 and 2020 for these lines of credit was approximately \$31,000 and \$306,500, respectively.
- ♦ PAFA had an employment agreement with its former President whereby PAFA paid \$200,000 during fiscal year 2009 to assist in acquiring a residence. As of June 30, 2020, the principal balance of \$200,000 had been forgiven. The forgiveness of the final principal installment of \$20,000 of the note receivable is reflected in other gain (loss) within non-operating revenues in the statement of activities and changes in net assets during the year ended June 30, 2020. However, a balance of \$66,425 for accrued interest from the note receivable is reflected in other assets as of June 30, 2020 and was to be forgiven over a three-year period contingent on the President's continuing employment. The President resigned effective November 20, 2020. In connection with the President's resignation, PAFA agreed to forgive one year of accrued interest in the amount of \$22,142 which is included in other gain (loss) for the year ended June 30, 2021. The remaining accrued interest of \$44,283 was repaid by the President upon his resignation.
- ♦ PAFA receives the income from a beneficial trust held by a third party, of which one of the Trustees of that beneficial trust is a Board member of PAFA.
- ♦ PAFA has approximately \$720,000 and \$836,000 as of June 30, 2021 and 2020, respectively, in pledges for capital campaign and other purposes from several board members and their foundations.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

(13) LEASES

PAFA leases student housing apartments under a lease arrangement with an initial term greater than 12 months. PAFA determines whether an agreement is or contains a lease at lease inception. Right-of-use assets represent PAFA's right to use an underlying asset for the lease term and lease liabilities represent PAFA's obligation to make lease payments arising from the lease, measured at an amount equal to the present value of the minimum lease payments over the remaining expected term of the lease. Amortization expense and interest expense related to PAFA's finance leases are included in tuition and fees, net of scholarships, on the statement of activities and changes in net assets.

In determination of the lease term, PAFA considers the likelihood of lease renewal options and lease termination provisions.

The discount rate for a lease is derived from the rate implicit in the lease whenever readily determinable or PAFA's incremental borrowing rate.

The following is the quantitative data related to PAFA's operating leases for the year ended June 30, 2021:

| | <u>2021</u> |
|--|-------------|
| Operating Lease Amounts: | |
| Right-of-use assets | \$ 965,298 |
| Lease liabilities | 965,298 |
| Other Information: | |
| Operating outgoing cash flows for operating leases | \$ 383,813 |
| Weighted-average remaining lease term | 2.1 years |
| Weighted average discount rate | 2.08% |

Lease cost information for the year ended June 30, 2021 is as follows:

| | |
|----------------------|-------------------|
| Operating lease cost | <u>\$ 383,813</u> |
|----------------------|-------------------|

Future lease payments at June 30, 2021 are as follows:

| <u>Year Ending June 30, 2021</u> | |
|----------------------------------|-------------------|
| 2022 | \$ 469,024 |
| 2023 | 478,401 |
| 2024 | <u>39,932</u> |
| Total undiscounted cash flows | 987,357 |
| Less: present value adjustment | <u>(22,059)</u> |
| Lease liability | <u>\$ 965,298</u> |

In connection with the adoption of ASU 2016-02, the deferred rent balance of \$100,486 as of June 30, 2020, was written off and is included in other income (loss) on the statement of activities in fiscal year 2021.

PENNSYLVANIA ACADEMY OF THE FINE ARTS

NOTES TO FINANCIAL STATEMENTS – (Continued)

June 30, 2021 And 2020

(14) COMMITMENTS AND CONTINGENCIES

GRANTS

Financial assistance from the federal and state governments in the form of grants and student aid/loans are subject to audit by the granting entity. An audit could result in claims for disallowed costs or noncompliance with regulations. In the opinion of management, any such liability, if any, will not have a material adverse effect on PAFA's financial position.

(15) FINANCIAL ASSETS AND LIQUIDITY RESOURCES

The following table reflects PAFA's financial assets and liquidity resources available as of June 30, 2021 and 2020, reduced by amounts that are not available within one year for general expenses and scheduled principal payments and interest payments on debt because of donor and/or contractual restrictions:

| | <u>2021</u> | <u>2020</u> |
|--|----------------------|----------------------|
| Financial assets: | | |
| Cash and cash equivalents | \$ 863,458 | \$ 250,315 |
| Investments | 63,915,173 | 53,601,752 |
| Accounts receivable | 206,869 | 229,691 |
| Pledge receivable current | <u>1,698,512</u> | <u>2,412,604</u> |
| Total financial assets available within one year | 66,684,012 | 56,494,362 |
| Estimated endowment income designated for operations | 4,747,000 | 3,234,000 |
| Assets restricted/designated as to use: | | |
| Endowment funds without donor restriction | (923,977) | (774,418) |
| Donor restricted endowment funds | (31,714,130) | (25,764,696) |
| Other donor restricted funds | <u>(1,735,477)</u> | <u>(2,236,768)</u> |
| Total financial assets and liquidity resources available within one year | <u>\$ 37,057,428</u> | <u>\$ 30,952,480</u> |

PAFA's cash flows have seasonal variations during the year attributable to tuition billing and a concentration of contributions received at calendar and fiscal year-end. To manage liquidity, PAFA maintains two working capital lines of credit with two banks for \$6,500,000 in total which can be drawn upon as needed to manage cash flows.

(16) SUBSEQUENT EVENTS

Subsequent events after the statement of financial position date through the date that the financial statements were available for issuance, December 17, 2021 have been evaluated in the preparation of the financial statements and management has determined that there are no subsequent events that would require disclosure or adjustment in the financial statements except as noted below.

On November 18, 2021, PAFA was notified that its PPP Second Draw Loan in the amount of \$1,596,447 was forgiven by the SBA.