

University Co-operative Society

Consolidated Financial Statements

For the Fiscal Years Ended
July 2, 2023 and July 3, 2022



TABLE OF CONTENTS

	<u>Page No.</u>
Independent Auditor's Report	1 - 2
Consolidated Statements of Financial Position	3
Consolidated Statements of Activities	4
Consolidated Statements of Cash Flows	5
Notes to Consolidated Financial Statements	6 - 20



INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
University Co-operative Society
Austin, Texas

Opinion

We have audited the accompanying consolidated financial statements of University Co-operative Society (the "Co-op"), which comprise the consolidated statements of financial position as of July 2, 2023 and July 3, 2022, and the related consolidated statements of activities and cash flows and the related notes to the consolidated financial statements.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of University Co-operative Society as of July 2, 2023 and July 3, 2022, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of University Co-operative Society and to meet our other ethical responsibilities in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management 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, and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about University Co-operative Society's ability to continue as a going concern within one year after the date that the consolidated financial statements are available to be issued.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements, including omissions, are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the consolidated financial statements.

In performing an audit in accordance with generally accepted auditing standards, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements.
- Obtain an understanding of internal control relevant to the audit 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 University Co-operative Society's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the consolidated financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about University Co-operative Society's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.



Armanino^{LLP}
Austin, Texas

September 29, 2023

University Co-operative Society
Consolidated Statements of Financial Position
July 2, 2023 and July 3, 2022

	<u>2023</u>	<u>2022</u>
ASSETS		
Current assets		
Cash and cash equivalents	\$ 652,741	\$ 1,722,576
Investments	1,946,632	1,001,740
Trade accounts receivable, net	212,409	119,375
Other accounts receivable	672,454	537,889
Merchandise inventory, net	5,849,750	3,555,846
Prepaid expenses and other	432,190	535,242
Total current assets	<u>9,766,176</u>	<u>7,472,668</u>
Property and equipment, net	9,807,405	10,220,351
Operating lease assets	1,003,986	1,508,914
Other assets	2,589	28,429
Total fixed assets	<u>10,813,980</u>	<u>11,757,694</u>
Total assets	<u>\$ 20,580,156</u>	<u>\$ 19,230,362</u>
LIABILITIES AND NET ASSETS		
Current liabilities		
Accounts payable	\$ 2,448,515	\$ 1,663,716
Accrued expenses	1,111,017	781,598
Deferred revenue	346,896	688,350
Gift in kind liability	1,100,000	-
Operating lease liabilities	519,188	553,481
Long-term debt, current	112,679	108,330
Total current liabilities	<u>5,638,295</u>	<u>3,795,475</u>
Long-term liabilities		
Operating lease liabilities, net of current	564,652	1,083,840
Long-term debt, net of current	2,990,700	3,094,575
Total liabilities	<u>9,193,647</u>	<u>7,973,890</u>
Net assets		
Without donor restrictions	10,966,509	10,836,472
With donor restrictions	420,000	420,000
Total net assets	<u>11,386,509</u>	<u>11,256,472</u>
Total liabilities and net assets	<u>\$ 20,580,156</u>	<u>\$ 19,230,362</u>

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

University Co-operative Society
Consolidated Statements of Activities
For the Fiscal Years Ended July 2, 2023 and July 3, 2022

	<u>2023</u>	<u>2022</u>
Revenue		
Net sales	\$ 24,945,982	\$ 20,570,368
Cost of merchandise sold	<u>(12,957,000)</u>	<u>(10,451,182)</u>
Total gross margin	<u>11,988,982</u>	<u>10,119,186</u>
Operating expenses		
Personnel costs	7,215,964	5,452,486
Building occupancy costs	714,542	702,169
General and administrative	1,734,216	1,324,907
Selling and promotional	<u>458,449</u>	<u>376,069</u>
Total operating expenses	<u>10,123,171</u>	<u>7,855,631</u>
Change in net assets from operations	<u>1,865,811</u>	<u>2,263,555</u>
Other income (expense)		
Other income	943,064	2,251,921
Depreciation and amortization	(562,663)	(636,837)
Interest expense	(120,435)	(140,701)
Unrealized gain (loss) on investments	<u>79,352</u>	<u>(164,285)</u>
Total other income	<u>339,318</u>	<u>1,310,098</u>
Income tax expense	<u>(39,964)</u>	<u>(1,478)</u>
Change in net assets before university gifts	2,165,165	3,572,175
University gifts	<u>(2,035,128)</u>	<u>(178,024)</u>
Change in net assets	<u>130,037</u>	<u>3,394,151</u>
Net assets, beginning of year	<u>11,256,472</u>	<u>7,862,321</u>
Net assets, end of year	<u><u>\$ 11,386,509</u></u>	<u><u>\$ 11,256,472</u></u>

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

University Co-operative Society
Consolidated Statements of Cash Flows
For the Fiscal Years Ended July 2, 2023 and July 3, 2022

	<u>2023</u>	<u>2022</u>
Cash flows from operating activities		
Cash received from customers	\$ 24,945,982	\$ 20,570,368
Cash received from rental and other activities	1,623,716	2,258,754
Cash paid to suppliers and employees	(26,484,338)	(19,141,658)
Interest paid	<u>(138,695)</u>	<u>(167,462)</u>
Net cash provided by (used in) operating activities	<u>(53,335)</u>	<u>3,520,002</u>
Cash flows from investing activities		
Purchase of property and equipment	(148,645)	(354,901)
Purchase of investments	(919,137)	(1,198,954)
Sale of investments	<u>159,281</u>	<u>32,929</u>
Net cash used in investing activities	<u>(908,501)</u>	<u>(1,520,926)</u>
Cash flows from financing activities		
Payments on line of credit	-	(950,000)
Payments on notes payable	<u>(107,999)</u>	<u>(140,840)</u>
Net cash used in financing activities	<u>(107,999)</u>	<u>(1,090,840)</u>
Net increase (decrease) in cash and cash equivalents	(1,069,835)	908,236
Cash and cash equivalents, beginning of year	<u>1,722,576</u>	<u>814,340</u>
Cash and cash equivalents, end of year	<u><u>\$ 652,741</u></u>	<u><u>\$ 1,722,576</u></u>

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

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

1. NATURE OF OPERATIONS

The University Co-operative Society (the "Co-op" or "Company") is a 501(c)(3) nonprofit organization that was organized on June 20, 1925, under the laws of the State of Texas. The Co-op sells goods and services on-line and through its retail store to the faculty, staff, Board of Regents, and students of The University of Texas at Austin ("UT"), other members of the Co-op, and the general public. The management of the Co-op's affairs is vested in the Board of Directors who are trustees of the Co-op. In the event of dissolution of the Co-op, its net assets would pass in trust to the Board of Regents of UT to be invested in an endowment so that the interest and proceeds shall be award to scholarships for students at UT.

In July 2009, the Co-op formed its wholly-owned subsidiary University Stores, Inc. ("USI"), a Texas for-profit corporation.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Definition of fiscal year

The Co-op reports its results of operations on a 52- or 53-week fiscal year ending on the last Sunday closest to June 30. Fiscal years 2023 and 2022 were 52-week and 53-week years, respectively.

Basis of accounting, consolidation, and financial statement presentation

- *Net assets without donor restrictions* - Net assets whose use is not restricted by donor-imposed stipulations, even though their use may be limited by Board designation.
- *Net assets with donor restrictions* - Net assets subject to donor-imposed restrictions. Some donor imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposes restrictions are perpetual in nature, when the donor stipulates that resources be maintained in perpetuity. Donor-imposed restrictions are released when a restriction expires, that is, when the stipulated time has elapsed, when the stipulated purpose for which the resource was restricted has been fulfilled, or both.

The consolidated financial statements include the accounts of the Co-op and its wholly-owned subsidiary. The accompanying consolidated financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") as defined by the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC). All significant intercompany transactions have been eliminated in consolidation.

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Use of estimates

The preparation of the consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes and supplemental schedules. Actual results could differ from those estimates.

Cash and cash equivalents

The Co-op considers all highly liquid investments acquired with an original maturity of three months or less at the date of purchase to be cash equivalents. Cash equivalents are stated at cost, which approximates market value, because of the short maturity of these instruments.

Accounts receivable

Trade accounts receivable are recorded at net realizable value and represent amounts due from customers. Other accounts receivable predominantly represent credit amounts due from vendors for returned items. The Co-op continually assesses the collectability of outstanding trade accounts receivable and vendor credits and if deemed necessary, maintains an allowance for estimated losses resulting from the non-collection of trade accounts receivable and vendor credits. The amount of the allowance for doubtful accounts is based upon management's assessment of historical and expected net collections, business and economic conditions, and other collection indicators. Actual customer collections could differ from the Co-op's estimates. The allowance for doubtful accounts was not significant at July 2, 2023 or July 3, 2022.

Concentration of credit risk

Financial instruments that potentially subject the Co-op to concentrations of credit risk consist of cash and cash equivalents and accounts receivable. The Co-op maintains its cash and cash equivalent balances in highly rated financial institutions, which at times may exceed federally insured limits. The Co-op has not experienced any loss relating to cash and cash equivalents in these accounts. The Co-op does not maintain collateral for its receivables and does not believe significant risk exists with respect to receivables. No customer represented more than 10% of total revenues for fiscal year 2023 or 2022.

Customers concentrations in trade accounts receivable were as follows at July 2, 2023 and July 3, 2022:

	<u>July 2, 2023</u>	<u>July 3, 2022</u>
Customer A	49.00 %	33.00 %
Customer B	-	16.00
Customer C	24.00	-
Customer D	18.00 %	- %

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Merchandise inventory

Merchandise inventories, which consists of goods for resale, are stated at the lower of cost or net realizable value. Cost includes the acquisition cost of purchased goods determined by the weighted-average cost method. Net realizable value is the estimated selling price less reasonably predictable costs to sell. Management estimates a reserve for obsolete inventory based on a review of specific inventory items at risk for obsolescence. No obsolescence reserve was considered necessary as of July 2, 2023 or July 3, 2022. The Co-op estimates a shrink reserve based on quarterly trailing sales. The shrink reserve was \$27,001 and \$25,390 at July 2, 2023 and July 3, 2022, respectively.

Investments

Investments in equity securities are carried at fair value based on quoted market prices and unrealized gains and losses are included in other income in the accompanying statements of financial position.

Property and equipment, net

Property and equipment are carried at cost or, if donated, at the estimated fair market value at the date of the donation less accumulated depreciation. Major additions and betterments are capitalized. Repairs, maintenance, and minor replacements that do not materially improve or extend the lives of the respective assets are charged to operating expense as incurred. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets. Leasehold improvements are amortized over the shorter of the remaining terms of the respective leases or the remaining useful lives of the improvements.

Intangible assets, net

Intangible assets include lease premiums, copyrights, and a domain name. Amounts are subject to amortization on a straight-line basis over the estimated period of benefit and are subject to annual impairment consideration. Costs incurred to renew or extend the term of a recognized intangible asset are capitalized as part of the intangible asset and amortized over its revised estimated useful life.

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Leases

The Co-op leases property under non-cancelable leases with terms typically between four and five years and accounts for these leases in accordance with ASC 842, *Leases* ("ASC 842"). This guidance requires lessees to recognize a lease liability and a right-of-use asset for all leases with terms greater than 12 months on its balance sheet. Whether an arrangement contains a lease is evaluated at the inception of the arrangement. The Co-op estimates its lease liability at the present value of future rent payments required under a lease using a risk-free rate for a term approximating the lease term, exclusive of optional term extensions or terminations, in accordance with a policy election available to privately held companies under the guidance. The Co-op's lease asset initially is equal to its lease liability, adjusted for any lease incentives received or lease payments made. Rent expense is recorded on a straight-line basis over the term of a lease. Leases of 12 months or less are not included in the Co-op's lease assets and lease liabilities. Lease expense for such leases is recorded on a straight-line basis over the term of the lease.

Long-lived assets

Long-lived assets, which consist primarily of property and equipment, intangible assets, and operating lease assets, are reviewed for impairment whenever events or circumstances indicate their carrying value may not be recoverable. When such events or circumstances arise, an estimate of future undiscounted cash flows produced by the asset, or the appropriate grouping of assets, is compared to the asset's carrying value to determine if impairment exists. Conditions that would necessitate an impairment assessment include a significant decline in the observable market value of an asset, a significant change in the extent or manner in which an asset is used, or any other significant adverse change that would indicate that the carrying amount of an asset or group of assets may not be recoverable. If the asset is determined to be impaired, the impairment loss is measured based on the excess of its carrying value over its fair value. The Co-op determines fair value based on discounted cash flows using a discount rate commensurate with the risk inherent in the Co-op's current business model for the specific asset being valued. No indicators of impairment were identified during the fiscal years ended July 2, 2023 or July 3, 2022.

Unredeemed gift certificates

Upon issuance of a gift certificate, a liability is established for its cash value. The liability is relieved and revenue is recorded upon redemption by the customer. The total liability related to unredeemed gift certificates was approximately \$133,000 and \$102,000 as of July 2, 2023 and July 3, 2022, respectively, and is included in accrued expenses in the accompanying consolidated statements of financial position.

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Deferred revenue

The Co-op has recognized deferred revenue associated with the cash received for the UT for Me program ("UT for Me"), funded by the Michael and Susan Dell Foundation ("MSDF"). The UT for Me program supports student course material purchases from the Co-op. The UT for Me program is funded annually by MSDF based on student cohort enrollment, and unused funds are rolled over to subsequent program years and cohorts. Excess funds must be returned at the request of MSDF.

As of July 2, 2023 and July 3, 2022, the Co-op has received conditional contributions of \$2,410,200 and \$1,879,425, respectively, for the UT for Me program. Revenue recognized was \$2,238,185 and \$1,107,427 for fiscal years ended July 2, 2023 and July 3, 2022, respectively. Revenue is recognized when the conditions imposed by MSDF are met through sale of course materials to students participating in the UT for Me program.

Gift in kind liability

As of July 2, 2023, the Co-op has unconditionally promised to give \$1,100,000 of course materials to students through the Course Material Scholarship ("CMS") program. The CMS program is funded by the Co-op with an unconditional in-kind donation. Excess funds will roll over to subsequent program years. The Co-op recognized university gifts expense of \$1,100,000 for fiscal year 2023 in the accompanying consolidated statements of activities.

Debt issuance costs

The Co-op records underwriting, legal, and other direct costs incurred related to the issuance of debt as a deduction from the debt liability and amortizes these costs to interest expense over the term of the related debt on a straight-line basis, which approximates the effective interest rate method. Upon the extinguishment of the related debt, any unamortized capitalized deferred financing costs are recorded to interest expense.

Cost of merchandise sold

Cost of merchandise sold includes cost of inventory sold during each fiscal year (net of discounts) and freight-in costs.

Advertising

The Co-op expenses advertising costs as incurred. Advertising expenses were approximately \$458,000 and \$376,000 for the fiscal years ended July 2, 2023 and July 3, 2022, respectively, and are included in other selling and promotional costs in the accompanying consolidated statements of activities.

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Sales taxes

The Co-op records sales and other taxes collected from customers and subsequently remitted to government authorities as sales tax payable. The Co-op relieves the sales tax payable balances from the balance sheet as cash is remitted to the tax authority. Revenue is recorded net of sales tax.

University gifts

University gifts from the Co-op to UT are declared periodically at the discretion of the Board. All university gifts are recorded as expenses at the time of declaration.

Income taxes

The Co-op is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code, except to the extent of unrelated business income, if any. The Co-op did not incur significant tax liabilities due to unrelated business income in fiscal year 2023 or 2022. The Co-op files Form 990 tax returns in the U.S. federal jurisdiction and is subject to routine examinations of its returns; however, there are no examinations currently in progress.

USI is subject to federal income taxation as a C corporation and files income tax returns in the U.S. federal jurisdiction and the state of Texas. USI uses the asset and liability method of accounting for income taxes as set forth in the applicable guidance. Under this method, deferred tax assets and liabilities are recognized for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred tax assets and liabilities will be recognized in the period that includes the enactment date. A valuation allowance is established against the deferred tax assets to reduce their carrying value to an amount that is more likely than not to be realized.

The Co-op and USI account for uncertain tax positions based on a "more-likely-than-not" threshold for the recognition and de-recognition of tax positions, which includes the accounting for interest and penalties relating to tax positions. At July 2, 2023 and July 3, 2022, the Co-op and USI did not have any unrecognized tax benefits resulting from their tax positions.

The Co-op and USI recognize interest and penalties related to unrecognized tax benefits as a component of income tax expense. No such interest or penalties were recognized during the periods presented. The Co-op and USI had no accruals for interest and penalties at July 2, 2023 or July 3, 2022.

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Subsequent events

Subsequent events have been evaluated through September 29, 2023, which represents the date the financial statements were available to be issued and no events have occurred through that date that would impact the financial statements.

3. FUNCTIONAL EXPENSES

The Co-op has allocated expenses, comprised of cost of merchandise sold, operating expenses, depreciation and amortization, and interest expense, as follows on a functional basis for the fiscal years ended July 2, 2023 and July 3, 2022:

	<u>July 2, 2023</u>	<u>July 3, 2022</u>
Program		
Cost of merchandise sold	\$ 12,957,000	\$ 10,451,182
Personnel costs	3,754,462	2,783,179
Building occupancy costs	588,732	575,327
Depreciation and amortization	400,889	418,552
General and administrative, other selling and promotional costs, and interest expense	<u>1,455,356</u>	<u>1,052,087</u>
	<u>19,156,439</u>	<u>15,280,327</u>
Management and general		
Personnel costs	3,461,502	2,669,307
Building occupancy costs	125,810	126,842
Depreciation and amortization	161,775	218,285
General and administrative, other selling and promotional costs, and interest expense	<u>857,743</u>	<u>812,157</u>
	<u>4,606,830</u>	<u>3,826,591</u>
	<u>\$ 23,763,269</u>	<u>\$ 19,106,918</u>

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

4. LIQUIDITY AND AVAILABILITY OF RESOURCES

The following table represents the Co-op's financial assets available to meet cash needs for general expenditures within one year of July 2, 2023 and July 3, 2022:

	<u>July 2, 2023</u>	<u>July 3, 2022</u>
Cash and cash equivalents	\$ 652,741	\$ 1,722,576
Investments	1,946,632	1,001,740
Trade accounts receivable, net	212,409	119,375
Other accounts receivable	<u>672,454</u>	<u>537,889</u>
	<u>\$ 3,484,236</u>	<u>\$ 3,381,580</u>

The Co-op maintains a policy of structuring its financial assets to be available as its general expenditures, liabilities, and other obligations come due. In addition, the Co-op plans to convert inventory to cash to contribute to its cash needs.

5. INVESTMENTS

The cost basis of available for sale investments as of July 2, 2023 was \$1,867,280 and their aggregate estimated fair value was \$1,946,632, resulting in an unrealized gain of \$79,352 recognized in net income. The value of these mutual fund securities at July 2, 2023 has been determined using Level 1 inputs consisting of quoted prices for identical assets in active markets.

6. PROPERTY AND EQUIPMENT, NET

Property and equipment, net consisted of the following at July 2, 2023 and July 3, 2022:

	<u>July 2, 2023</u>	<u>July 3, 2022</u>
Land	\$ 1,155,694	\$ 1,155,694
Buildings	14,983,296	14,915,956
Furniture & office equipment	3,298,917	3,250,946
Leasehold improvements	2,180,358	2,180,358
Construction in progress	<u>81,493</u>	<u>79,404</u>
	21,699,758	21,582,358
Accumulated depreciation	<u>(11,892,353)</u>	<u>(11,362,007)</u>
	<u>\$ 9,807,405</u>	<u>\$ 10,220,351</u>

Estimated useful lives are from 5 to 50 years for buildings and improvements and 5 to 7 years for furniture and office equipment.

For the fiscal years ended July 2, 2023 and July 3, 2022, respectively, depreciation and amortization expense for the above assets was \$536,824 and \$581,675, and is included in depreciation and amortization expense in the accompanying consolidated statements of activities.

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

7. ACCRUED EXPENSES

Accrued expenses consisted of the following at July 2, 2023 and July 3, 2022:

	<u>July 2, 2023</u>	<u>July 3, 2022</u>
Accrued payroll and benefits	\$ 421,100	\$ 380,734
Accrued property, sales, and Texas margin taxes	214,999	205,029
Other accrued expenses	<u>474,918</u>	<u>195,835</u>
	<u>\$ 1,111,017</u>	<u>\$ 781,598</u>

8. LONG-TERM DEBT

Long-term debt consisted of the following at July 2, 2023 and July 3, 2022:

	<u>July 2, 2023</u>	<u>July 3, 2022</u>
Notes payable	<u>\$ 3,103,379</u>	<u>\$ 3,202,905</u>
	3,103,379	3,202,905
Less: unamortized debt issuance costs	<u>63,708</u>	<u>71,928</u>
	3,167,087	3,274,833
Current portion	<u>(112,679)</u>	<u>(108,330)</u>
	<u>\$ 3,054,408</u>	<u>\$ 3,166,503</u>

The future maturities of the long-term debt are as follows:

<u>Fiscal years ending</u>	
2024	\$ 112,679
2025	117,562
2026	122,657
2027	127,973
2028	133,519
Thereafter	<u>2,552,697</u>
	<u>\$ 3,167,087</u>

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

8. LONG-TERM DEBT (continued)

In March 2021, the Co-op entered into a loan and security agreement (the "LSA") with a financial institution, including a revolving line of credit and a term loan. The LSA offers a revolving line of credit up to a maximum principal amount of \$3.0 million. The revolving line of credit was not utilized in 2023. Under the LSA, the Co-op also entered into a term loan in the amount of \$3,301,157. Amounts due under the term loan bear interest at 4.24% per annum. Interest is payable monthly beginning April 2021 until March 2022. Beginning April 2022, interest and principal is payable in monthly installments until maturity in March 2031, computed on a 20-year amortization basis. The Co-op incurred aggregate debt issuance costs of approximately \$82,000 in connection with the LSA. Substantially all of the Company's assets are pledged as collateral for these loans.

As part of the federal government's response to the economic impacts of COVID-19, in March 2020, the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act") was enacted which, among other measures, provided for the Paycheck Protection Program (PPP) administered by the U.S. Small Business Administration. The Company has elected to account for PPP loans per the guidance of ASC 470, *Debt*. In January 2021, the Co-op applied and was approved for a PPP loan in the amount of \$1,019,600. All or a portion of the PPP loan may qualify for forgiveness under the terms of the PPP. Amounts not qualifying for forgiveness bear interest at a rate of 1% per annum and will be repaid in monthly installments of principal and accrued interest through February 2026, at which time the loan matures and all outstanding principal and accrued interest is due. The Co-op received notification of forgiveness on April 11, 2022. The forgiveness of the first and second PPP loans was recorded as non-operating income in the accompanying consolidated statements of activities.

For the fiscal years ended July 2, 2023 and July 3, 2022, interest expense on the Co-op's long-term debt was \$146,916 and \$159,838, respectively, inclusive of non-cash interest expense related to debt issuance costs of \$8,220 for both fiscal years.

9. COMMITMENTS AND CONTINGENCIES

Leases

The Co-op leases facilities that have terms expiring between 2023 and 2026. The terms of the store leases are considered their initial obligation periods, which do not include option periods. The facility leases generally have renewal clauses of five years exercisable at the option of the Co-op. Most lease agreements contain rent holidays and/or rent escalation clauses.

Lease expense totaled \$590,459 during the fiscal years ended July 2, 2023 and July 3, 2022, of which \$146,485 is included in building occupancy costs and \$443,974 is included in other income in the accompanying consolidated statements of activities.

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

9. COMMITMENTS AND CONTINGENCIES (continued)

Leases (continued)

The scheduled minimum lease payments under the lease terms are as follows:

<u>Fiscal years ending</u>	
2024	\$ 541,728
2025	464,782
2026	<u>110,330</u>
	1,116,840
Less: discount to present value	<u>(33,000)</u>
	<u><u>\$ 1,083,840</u></u>

Operating cash flows related to operating leases were \$590,810 and \$580,355 for the fiscal years ended July 2, 2023 and July 3, 2022, respectively. The weighted-average discount rate was 2.69% and the weighted average remaining lease term in years was 2.13 and 3.02 as of July 2, 2023 and July 3, 2022, respectively.

Defined contribution plans

The Co-op has defined contribution 401(k) and 403(b) retirement plans (the "Plans") and a custodial account covering individuals who have been employed by the Co-op at least one year, who work a minimum of 1,000 hours per year, and who have attained the age of 21. Participants in the 403(b) Plan are permitted to make elective deferrals of their pre-tax compensation to the 403(b) Plan, not to exceed limits set by Internal Revenue Code Section 402(g). The 403(b) Plan is administered by a custodial trustee under the guidance of the Board.

The Coop has a match program which deposits an amount to each eligible employee's 401(k) and 403(b) accounts, not to exceed 5% of the eligible employee's annual compensation. The Co-op's contributions under the Plans totaled \$133,823 and \$90,635 during the fiscal years ended July 2, 2023 and July 3, 2022, respectively.

The Board has agreed to fund the post-retirement medical benefits for the former President/CEO and spouse not to exceed amounts paid to his successor. Post-retirement medical benefit expenses were not significant for fiscal year 2023 or 2022.

Litigation

In the normal course of business, the Co-op may become involved in various lawsuits and legal proceedings. While the ultimate results of these matters cannot be predicted with certainty, management does not expect them to have a material adverse effect on the consolidated financial position or results of operations of the Co-op.

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

10. NET ASSETS WITH DONOR RESTRICTIONS

On September 1, 2005, University Presbyterian Church (the "Church") contributed to the Co-op a tract of land adjacent to two parking lots owned by the Co-op. The land was valued at \$420,000 on the date of contribution and was recorded at its fair value. The Co-op constructed a parking garage on the three lots, which was completed in August 2006. In exchange for the contributed land, the Co-op granted the Church an easement to certain parking spaces upon completion of the parking garage for a term of 99 years. In accordance with the reversion clause of the deed, the contributed land must be operated as a parking garage for the term of 99 years or ownership or the land will revert back to the Church. Due to the donor-imposed use and time restrictions, the contribution was recorded as non-operating income classified as a net asset with donor restrictions.

11. REVENUE RECOGNITION

Revenues are recognized when control of the promised goods or services is transferred to a customer in an amount that reflects the consideration the Coop is expected to be entitled to in exchange for those goods. Revenues are recognized net of sales credits and allowances. Revenue is recognized net of any taxes collected from customers, which are subsequently remitted to governmental authorities.

Revenue is recognized based on the following five-step model in accordance with ASC 606, *Revenue from Contracts with Customers*:

1. Identification of the contract with a customer
2. Identification of the performance obligations in the contract
3. Determination of the transaction price
4. Allocation of the transaction price to the performance obligations in the contract
5. Recognition of revenue when, or as, the Co-op satisfies a performance obligation

Revenue-generating activities consist of retail sales, textbook rentals, and custom publishing activities for various departments of the University of Texas. The Co-op recognizes revenue from retail sales when goods are provided to the customer, either in-person at a retail location, or when products are shipped from the warehouse. Textbook rental revenue is recognized when the rental occurs, although performance obligations are satisfied throughout the rental term. Rentals are short-term in nature and are only made for a single semester at a time. The Co-op recognizes revenue from custom publishing services when orders are completed. The Co-op's contracts with customers do not typically include multiple performance obligations and goods and services are sold at their standalone selling price.

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

11. REVENUE RECOGNITION (continued)

The following table disaggregates the Co-op's revenue based on contract type and the timing of satisfaction of performance obligations:

	<u>July 2, 2023</u>	<u>July 3, 2022</u>
Major contracts		
Retail sales	\$ 24,707,503	\$ 20,282,420
Other sales	<u>238,479</u>	<u>287,948</u>
	<u>24,945,982</u>	<u>20,570,368</u>
Timing of revenue recognition		
Performance obligations satisfied at a point in time	<u>24,945,982</u>	<u>20,570,368</u>
	<u>\$ 24,945,982</u>	<u>\$ 20,570,368</u>

Principal and Agent Considerations

The Co-op evaluated principal vs. agent considerations to determine whether it is appropriate to record digital textbook purchase costs paid to the originating vendor as an expense or as a reduction of revenue. Digital textbook purchase costs are recorded as a reduction of revenue and not cost of revenue because the Co-op does not control the goods before they are transferred to the customer. While the Co-op transfers the product to the final customer, the Co-op is not responsible for establishing prices, does not hold inventory, and does not have any additional responsibilities to the customer once the digital textbook has been purchased.

Shipping and handling

The Co-op has elected to account for shipping and handling as fulfillment activities, even if those activities occur after control of the goods has been transferred to the customer. As such, the Co-op expenses shipping and handling costs associated with the contract when the associated revenue is recognized. Shipping and handling costs are included in general and administrative expenses in the consolidated statements of activities.

Payment terms

Payment terms and conditions vary by contract type, although terms generally include a requirement of payment within 30 to 60 days and include no general rights of return. Payment for retail sales is due at the time of purchase. In instances where the timing of revenue recognition differs from the timing of invoicing, the Co-op has determined that contracts do not include a significant financing component. The timing of revenue recognition, billings and cash collections can result in billed trade accounts receivable, presented on the accompanying consolidated statements of financial position.

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

12. RENTAL INCOME

The Co-op leases portions of its buildings to unrelated third-parties under lease agreements. As of July 2, 2023 and July 3, 2022, the property held for leasing, which was included in property and equipment on the consolidated statements of financial position, had a cost basis of \$667,746 and \$264,054, respectively, and accumulated depreciation of \$429,424 and \$154,829 respectively. Rental income is included in other income on the accompanying statements of activities.

Future minimum lease payments receivable are as follows:

<u>Fiscal years ending</u>	
2024	\$ 681,498
2025	875,465
2026	260,895
2027	235,521
2028	255,000
Thereafter	<u>998,750</u>
	<u><u>\$ 3,307,129</u></u>

13. OTHER INCOME

Non-operating income consisted of the following for the fiscal years ended July 2, 2023 and July 3, 2022:

	<u>July 2, 2023</u>	<u>July 3, 2022</u>
Rental income	\$ 775,081	\$ 576,913
Gain on parking lot	414,063	419,502
Sales tax discount	11,069	9,472
PPP forgiveness	-	1,019,600
Property tax refund	-	811,000
Other expense	<u>(257,149)</u>	<u>(584,566)</u>
	<u><u>\$ 943,064</u></u>	<u><u>\$ 2,251,921</u></u>

14. INCOME TAX

The provision for current income tax consist of the following:

	<u>July 2, 2023</u>	<u>July 3, 2022</u>
Current		
Federal	<u>\$ 39,964</u>	<u>\$ 1,478</u>
	<u><u>\$ 39,964</u></u>	<u><u>\$ 1,478</u></u>

University Co-operative Society
Notes to Consolidated Financial Statements
July 2, 2023 and July 3, 2022

14. INCOME TAX (continued)

Significant components of the Company's deferred income tax assets and liabilities are as follows:

	<u>July 2, 2023</u>	<u>July 3, 2022</u>
Deferred		
Net operating loss carryforward	2,441,700	2,441,270
Charitable contribution carryforward	<u>3,709</u>	<u>5,572</u>
Total deferred	2,445,409	2,446,842
Valuation allowance	<u>(2,445,409)</u>	<u>(2,446,842)</u>
 Total net deferred tax asset	 <u>\$ -</u>	 <u>\$ -</u>

The Co-op's consolidated provision for income taxes attributable to continuing operations differs from the expected tax expense amount computed by applying the statutory federal income tax rate of 21% to income before income taxes, primarily as a result of the application of the valuation allowance, losses generated that are exempt from income taxation, and permanent differences.

USI has established a valuation allowance equal to the net deferred tax asset due to uncertainties regarding the realization of the deferred tax asset based on USI's lack of earnings history. At July 2, 2023, USI has U.S. net operating loss carryforwards of approximately \$1,549,000, of which \$1,202,000 will begin to expire in 2037 if not utilized, and \$347,000 will carry forward indefinitely.

Utilization of the net operating loss and tax credit carryforwards is likely subject to annual limitations due to the "change in ownership" provisions (Section 382) of the Internal Revenue Code. The annual limitations may result in the expiration of net operating losses before their utilization. The net operating loss carryforwards are subject to Internal Revenue Service adjustments until the statute closes on the year the net operating loss is utilized.