AMBOW BSC INC.
AND SUBSIDIARY

AUDITED CONSOLIDATED FINANCIAL STATEMENTS

YEAR ENDED
JUNE 30, 2019

OPE ID NUMBER: 00396500

INDEPENDENT AUDITOR'S REPORT

To the Shareholder
Ambow BSC Inc. and Subsidiary
Boston, Massachusetts

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying consolidated financial statements of Ambow BSC Inc. and Subsidiary which comprise the consolidated balance sheet as of June 30, 2019, and the related consolidated statements of operations, changes in shareholder's equity, and cash flows for the year then ended, and the related notes to the consolidated financial statements.

MANAGEMENT'S RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

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

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

OPINION

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Ambow BSC Inc. and Subsidiary as of June 30, 2019, and the results of their operations and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

OTHER REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated December 26, 2019, on our consideration of Ambow BSC Inc. and Subsidiary's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Ambow BSC Inc. and Subsidiary's internal control over financial reporting and compliance.

McClintock & Associates, P.C.

Pittsburgh, Pennsylvania
December 26, 2019

Ambow BSC Inc. and Subsidiary

CONSOLIDATED BALANCE SHEET

ASSETS

		June 30, 2019
CURRENT ASSETS		
Cash and cash equivalents	$	1,707,488
Accounts receivable, net of allowance for doubtful accounts of $64,380		732,264
Prepaid expenses		475,571
Other current assets		42,285
TOTAL CURRENT ASSETS		2,957,608
FURNITURE, EQUIPMENT AND IMPROVEMENTS		
Computers and classroom equipment		2,774,399
Leasehold improvements		2,139,069
Furniture and fixtures		554,045
Library		278,119
Automobiles		29,746
		5,775,378
Less accumulated depreciation and amortization		(4,990,983)
NET FURNITURE, EQUIPMENT AND IMPROVEMENTS		784,395
OTHER ASSETS		
Security deposits		288,313
Receivable from Parent Company		66,351
Restricted cash		606,490
Goodwill		639,746
Deferred tax asset		732,300
TOTAL OTHER ASSETS		2,333,200
TOTAL ASSETS	$	6,075,203

LIABILITIES AND SHAREHOLDER'S EQUITY

CURRENT LIABILITIES		
Accounts payable	$	562,535
Accrued expenses		159,776
Accrued payroll and related expenses		382,374
Deferred lease incentive		16,327
Prepaid tuition		259,519
Deferred tuition		1,412,858
TOTAL CURRENT LIABILITIES		2,793,389
LONG-TERM LIABILITIES		
Deferred rent		19,333
TOTAL LONG-TERM LIABILITIES		19,333
SHAREHOLDER'S EQUITY		
Common stock ($1 par value, 100 shares authorized, issued, and outstanding)		100
Additional paid-in capital		6,965,805
Retained deficit		(3,703,424)
TOTAL SHAREHOLDER'S EQUITY		3,262,481
TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY	$	6,075,203

See accompanying notes to consolidated financial statements.

Ambow BSC Inc. and Subsidiary

CONSOLIDATED STATEMENT OF OPERATIONS

	Year Ended June 30, 2019
REVENUES	
Tuition and fees, net of scholarships of $1,382,843	$ 11,196,203
Dormitory income	828,633
TOTAL REVENUES	12,024,836
OPERATING EXPENSES	
Education	5,065,932
General and administrative	4,082,963
Dormitory	1,192,631
Occupancy	2,131,061
Marketing	1,417,568
Information technology	1,094,672
Depreciation and amortization	623,043
TOTAL OPERATING EXPENSES	15,607,870
LOSS FROM OPERATIONS	(3,583,034)
OTHER INCOME (EXPENSES)	
Other income	23,891
Interest income	1,592
Loss on disposal of furniture, equipment and improvements	(144,013)
TOTAL OTHER INCOME (EXPENSES)	(118,530)
LOSS BEFORE INCOME TAXES	(3,701,564)
Credit for income taxes	160,100
NET LOSS	$ (3,541,464)

See accompanying notes to consolidated financial statements.

Ambow BSC Inc. and Subsidiary

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDER'S EQUITY

	Common Stock	Additional Paid-in Capital	Retained Deficit	Total
BALANCE AT JULY 1, 2018	$ 100	$ 3,959,805	$ (161,960)	$ 3,797,945
Capital contributions	0	3,006,000	0	3,006,000
Net loss	0	0	(3,541,464)	(3,541,464)
BALANCE AT JUNE 30, 2019	$ 100	$ 6,965,805	$ (3,703,424)	$ 3,262,481

See accompanying notes to consolidated financial statements.

Ambow BSC Inc. and Subsidiary

CONSOLIDATED STATEMENT OF CASH FLOWS

		Year Ended June 30, 2019
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	$	(3,541,464)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization		623,043
Loss on disposal of furniture, equipment and improvements		144,013
Increase in deferred income taxes		(160,100)
Amortization of deferred lease incentive		(98,095)
Provision for bad debt		370,082
Decrease in deferred rent		(129,326)
Decrease (increase) in:		
Accounts receivable		(417,335)
Prepaid expenses		36,591
Receivable from Parent Company		141,317
Other current assets		6,761
Security deposits		152,315
Increase (decrease) in:		
Accounts payable		(41,236)
Accrued expenses		(242,971)
Accrued payroll and related expenses		(22,873)
Prepaid tuition		289
Deferred tuition		89,590
Total net operating adjustments		452,065
NET CASH USED IN OPERATING ACTIVITIES		(3,089,399)
CASH FLOWS FROM INVESTING ACTIVITIES		
Increase in restricted cash		(606,490)
Acquisition of furniture, equipment and improvements		(183,740)
NET CASH USED IN INVESTING ACTIVITIES		(790,230)
CASH FLOWS FROM FINANCING ACTIVITIES		
Capital contributions		3,006,000
NET CASH PROVIDED BY FINANCING ACTIVITIES		3,006,000
NET DECREASE IN CASH AND CASH EQUIVALENTS		(873,629)
Cash and cash equivalents at beginning of year		2,581,117
CASH AND CASH EQUIVALENTS AT END OF YEAR	$	1,707,488

See accompanying notes to consolidated financial statements.

NOTE A - NATURE OF OPERATIONS

Ambow BSC Inc. (Company) is incorporated under the laws of the State of Delaware and is a wholly-owned subsidiary of Ambow Education Holdings, Ltd (Parent Company). On November 14, 2017 Ambow BSC Inc. acquired 100% of the outstanding common stock of Bay State College, Inc. (College).

The College operates a post-secondary institution with an online division, a campus in Boston and locations in Taunton and Newburyport, Massachusetts, offering training in a variety of programs including bachelor's degrees in Criminal Justice, Information Technology, Management and Nursing; Medical Assisting certification, and associates degrees in Business Administration, Criminal Justice, Entertainment Management, Fashion Design, Fashion Merchandising, Health Studies, Nursing, and Physical Therapist Assistant.

The College participates in Student Financial Aid (SFA) under the Title IV Programs administered by the U.S. Department of Education (ED) pursuant to the Higher Education Act of 1965, as amended (HEA).

The Company is in the process of changing its fiscal year end to December 31.

Management has evaluated subsequent events through December 26, 2019, the date the consolidated financial statements were available to be issued and has no material subsequent events to report.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The consolidated financial statements are prepared on the accrual basis of accounting in accordance with the *Presentation of Financial Statements* topic of the Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC).

Consolidation

The consolidated financial statements include the accounts and results of operation of the Company and its wholly-owned subsidiary Bay State College, Inc. All significant inter-company transactions and account balances have been eliminated in consolidation.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash in the bank and all short-term investments with an original maturity of 90 days or less.

Restricted Cash

Restricted cash represents a savings account which secures a letter of credit for one of the College's leases (see Note D).

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable consist primarily of amounts due to the College from its students for tuition and fees. Accounts receivable are recorded at the amounts originally billed, less payments received, and are non-interest bearing. Management has estimated an allowance for doubtful accounts based upon historical losses and the collection risks associated with each student's uncollected balance at year end. Management utilizes the age of accounts receivable and judgment to determine which accounts are written off to bad debts.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Furniture, Equipment and Improvements

Furniture, equipment and improvements are recorded at cost. Expenditures for renewals and betterments which extend the life of the assets are capitalized. Repairs and maintenance items are charged to expense as incurred. Gain or loss on the retirement or disposal of assets is included in operations in the year of disposal. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the assets or applicable lease term, if shorter, as follows:

Computers and classroom equipment	3 to 5 years
Library	7 years
Furniture and fixtures	7 years
Leasehold improvements	5 to 20 years
Automobiles	5 years

Depreciation and amortization charged to operations for the year ended June 30, 2019 was $623,043.

Goodwill

Goodwill represents the excess of the cost of identified assets acquired through business combinations over the estimated fair value of the net assets as of the purchase date.

FASB ASC Topic 350, *Goodwill and Other Intangible Assets*, requires that goodwill be subject to annual impairment testing. In accordance with Accounting Standards Update (ASU) 2011-08, *Testing of Goodwill for Impairment*, management may first assess qualitative factors (macroeconomic conditions, industry and market considerations, cost factors, overall financial performance, other relevant entity-specific events, events affecting the reporting unit, etc.) to determine whether it is more likely than not (a likelihood of more than 50%) that the fair value of the reporting unit is less that its carrying amount, including goodwill. If, after assessing the qualitative factors, management believes that it is more likely than not that the fair value of the reporting unit is less than its carrying amount, management performs a two-step goodwill impairment test to identify potential goodwill impairment and measure that amount of goodwill impairment loss to be recognized (if any). Management's assessment of various qualitative factors did not indicate the amount of goodwill to be impaired as of June 30, 2019. As a result, the two-step goodwill impairment test was not performed, and no impairment loss occurred during the year ended June 30, 2019.

Prepaid Tuition, Deferred Tuition and Revenue Recognition

Amounts remitted by students, in excess of tuition and fees, are recorded as prepaid tuition. Prepayments may be refunded or utilized by the student to pay future tuition and fees. Revenues from student tuition and fees are deferred at the time of enrollment and recognized ratably as the students progress through their academic programs. Tuition adjustments for students who withdraw are calculated in accordance with federal, state, and accrediting agency standards.

Dormitory income is recognized ratably over the period of time the student occupies the dormitory. Security deposits received from students may be refunded or utilized by the student to offset any charges as a result of dormitory damages. Sublease deposits represent amounts remitted by students who attend neighboring colleges and may be refunded or utilized to pay for dormitory charges.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Deferred Rent

The College has entered into operating leases for its educational facilities which contain provisions for escalating rent. The College recognizes rent expense on the straight-line method over the lives of the leases. The College has recorded monthly rent expense equal to the total of the payments due over the lease term, amortized over the number of months of the lease. The difference between rent expense recorded and rent paid is charged to deferred rent. This deferred rent will be used to offset future rent expense for financial statement purposes.

Deferred Lease Incentives

The College was reimbursed by the lessor for improvements made to leased properties. These reimbursements were capitalized as leasehold improvements and a long-term liability was established. The leasehold improvements and the deferred lease incentives are being amortized on a straight-line basis over the corresponding lease terms, which range from four to ten years. Amortization of the deferred lease incentives for the year ended June 30, 2019 was $98,095, and is reflected as a reduction of rent expense. The deferred lease incentive will be fully amortized during the year ended June 30, 2020 and therefore has been reflected as a current liability.

Income Taxes

The Company is a C Corporation and files a consolidated federal and state tax return with the College. The Company provides for deferred income taxes under the asset and liability method of accounting. This method requires the recognition of deferred income taxes based upon the tax consequences of "temporary differences" by applying enacted statutory tax rates applicable to future years to differences between the financial statement carrying amounts and the tax basis of existing assets and liabilities. The deferred taxes represent the future tax return consequences of the difference between the basis of certain assets and liabilities for financial and tax reporting. The type of differences that give rise to significant deferred income tax assets and liabilities are depreciation methods and lives, deferred rent, deferred lease incentives, allowance for doubtful accounts, net operating loss carryforwards, and accrued vacation.

Advertising Costs

The College incurred approximately $1,338,000 in advertising costs for the year ended June 30, 2019. Advertising costs are expensed as incurred.

Financial Instruments

The fair values and carrying amounts of the College's financial instruments, primarily current assets and current liabilities, are approximately equivalent.

Use of Estimates in the Preparation of Consolidated Financial Statements

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America 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 consolidated financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Recent Accounting Pronouncements

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers*. This ASU supersedes the revenue recognition requirements in ACS Topic 605, *Revenue Recognition* and most industry-specific guidance throughout the Codification. The standard requires that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In August 2015, the FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, deferring the effective date of this amendment by one year. This ASU will be effective for the Company's year ended June 30, 2020. The Company has assessed the impact that adopting this new accounting guidance will have on its consolidated financial statements and disclosures. Based on its evaluation of ASU No. 2014-09, the Company expects no material impact on its results of operations or cash flows in the periods after adoption.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*. This ASU supersedes existing guidance on accounting for leases in ASC Topic 840, *Leases*. The standard requires lessees to recognize the assets and liabilities that arise from leases on the balance sheet. A lessee should recognize in the balance sheet 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. This ASU will be effective for the Company's year ended June 30, 2022. The amendments should be applied at the beginning of the earliest period presented using a modified retrospective approach. The Company is currently in the process of assessing the impact of the adoption of this standard on its financial statements.

NOTE C - CONCENTRATION OF CREDIT RISK

The College, at times, has cash deposits which exceed $250,000 in an individual bank. The Federal Deposit Insurance Corporation (FDIC) insures only the first $250,000 of funds at member banks.

The accounts receivable represents amounts due from students for tuition and fees. Many of the College's students are eligible for federal government loan and grant programs and state grant programs which are administered by the College. These receivables are unsecured. As discussed in Note H, 62.13% of tuition and fees is covered by SFA. In addition, the College's students receive funding from Veterans Administration programs and alternative loans. Students typically apply the funds received from SFA and other funding to pay their tuition and fees. The receipt of SFA and other funding reduces the amount due from the student and has no impact on revenue recognition.

NOTE D - LEASE COMMITMENTS

The College leases administrative and instructional facilities under an operating lease expiring in September 2029. In addition, the College is responsible for supplemental lease payments to reimburse the landlord for their proportionate share of the building's operating costs. The College has provided the landlord a $606,000 irrevocable letter of credit in lieu of cash as a security deposit. The letter of credit expires in March 2020 and is expected to be renewed annually. The letter of credit is secured by a savings account at the issuing bank and the savings account is reporting as restricted cash on the balance sheet.

The College leases instructional facilities under an operating lease expiring in July 2035. The College is also responsible for all real estate taxes and common expenses for all fiscal years within the term of the lease. The College has a $45,000 security deposit, which is included as security deposits on the balance sheet.

The College leases student dormitories at three locations from Boston University under an operating lease commencing August 2018 and expiring in May 2021. The College has the right for an extension option through May 2022 and a second extension option through May 2023. The College must provide written notice the January before the extension is put into place.

The amount charged to operations under all operating leases for the year ended June 30, 2019 was approximately $2,523,000.

Minimum future lease payments for the five years subsequent to June 30, 2019 and in the aggregate are as follows:

Years Ending June 30,	
2020	$ 3,304,000
2021	3,599,000
2022	2,387,000
2023	2,893,000
2024	1,971,000
Thereafter	14,317,000
	$ 28,471,000

NOTE E - RETIREMENT SAVINGS PLAN

The College sponsors a 401(k) retirement plan for all eligible employees as defined by the Plan. The participants may contribute up to the Internal Revenue Code limits. The College may make a discretionary matching or a discretionary profit sharing contribution. For the year ended June 30, 2019, the College did not make any discretionary contributions.

NOTE F - INCOME TAXES

The College is a C Corporation and files a consolidated federal and state tax return with the Company. As of June 30, 2019, the Company has a federal tax net operating loss (NOL) carryforward of approximately $4,978,000 which does not expire. In addition, the Company has a Massachusetts tax NOL carryforward of approximately $5,021,000 which begins to expire in 2038. On an annual basis, the Company evaluates both positive and negative evidence to determine the net realizable value of their deferred tax assets. As of June 30, 2019, the Company had a valuation allowance for Federal and State NOL carryforwards of $545,900 and $209,800, respectively. The establishment of the NOL valuation allowance are the result of the Company anticipating to not utilize the NOL carryforwards in the near future.

The Company's deferred tax assets and liabilities as of June 30, 2019 are as follows:

	2019
Deferred tax asset	$ 1,524,000
Deferred tax liability	(36,000)
NOL valuation allowance	(755,700)
Net deferred tax asset	$ 732,300

The net deferred tax asset (liability) by jurisdiction as of June 30, 2019 is as follows:

	2019
Federal	$ 1,051,900
State	436,100
NOL valuation allowance	(755,700)
	$ 732,300

The provision (credit) for income taxes for the year ended June 30, 2019 is comprised of the following:

	2019
Current:	
Federal	$ 0
State	0
	0
Deferred:	
Federal	(673,000)
NOL valuation allowance	545,900
State	(242,800)
NOL valuation allowance	209,800
	(160,100)
	$ (160,100)

NOTE G - RELATED PARTY TRANSACTIONS

The College participates in SFA under the Title IV Programs administered by ED pursuant to the HEA. The College must comply with the regulations promulgated under the HEA. Those regulations require that all related party transactions be disclosed, regardless of their materiality to the financial statements.

The Company has a receivable due from the Parent Company of $66,351. The amount is unsecured, non-interest bearing and there are no specific terms of repayment.

This information is required by ED and is presented for purposes of additional analysis and is not a required part of the basic financial statements.

NOTE H - 90/10 CALCULATION

The College derives a substantial portion of its revenues from SFA received by its students under the Title IV Programs administered by ED pursuant to the HEA. To continue to participate in the SFA programs, the College must comply with the regulations promulgated under the HEA. The regulations restrict the proportion of cash receipts for tuition, fees, and other institutional charges from eligible programs to not be more than 90% from the Title IV Programs. The failure of the College to meet the 90% limitation for two consecutive years will result in the loss of the College's ability to participate in Title IV Programs. If a school receives more than 90% of its revenue from Title IV Programs during its fiscal year, the school becomes provisionally certified for the next two fiscal years. This information is required by ED and is presented for purposes of additional analysis and is not a required part of the basic financial statements. For the fiscal year ended June 30, 2019, the College's cash basis calculation is:

	OPE ID#	00396500
Adjusted Student Title IV Revenue		
Subsidized Loan	$	2,503,426
Unsubsidized Loan		3,431,096
Plus Loan		892,884
Federal Pell Grant		1,723,829
FSEOG (subject to matching reduction)		87,400
Federal Perkins Loan		0
Federal Work Study Applied to Tuition and Fees (subject to matching reduction)		0
Student Title IV Revenue		8,638,635
Revenue Adjustment		(1,010,565)
Title IV funds returned for a student under 34 C.F.R. § 668.22 (withdrawal)		(205,097)
Adjusted Student Title IV Revenue	$	7,422,973
Adjusted Student Non-Title IV Revenue		
Grant funds for the student from non-Federal public agencies or private sources independent of the institution	$	99,416
Funds provided for the student under a contractual arrangement with a Federal, State, or local government agency for the purpose of providing job training to low-income individuals		4,783
Institutional scholarships disbursed to the student		0
Funds used by a student from savings plans for educational expenses established by or on behalf of the student that qualify for special tax treatment under the Internal Revenue Code		0
Student payments on current charges		5,198,943
Student Non-Title IV Revenue		5,303,142
Revenue Adjustment		(777,902)
Adjusted Student Non-Title IV Revenue	$	4,525,240
Revenue From Other Sources		
Activities conducted by the institution that are necessary for education and training	$	0
Funds paid to the institution by, or on behalf of, students for education and training in qualified non-Title IV eligible programs		0
Allowable student payments + allowable amounts from account receivable or institutional loan sales – any required payments under a recourse agreement		0
Revenue from Other Sources	$	0
Adjusted Student Title IV Revenue	$	7,422,973
Adjusted Student Title IV Revenue + Adjusted Student Non-Title IV Revenue + Revenue from Other Sources	$	11,948,213
		62.13%

NOTE I - REGULATORY

The College participates in SFA under the Title IV Programs administered by ED pursuant to the HEA. Political and budgetary concerns can significantly affect the Title IV Programs and Congress must reauthorize the HEA approximately every six years. An institution must also demonstrate to ED its compliance with the HEA and the regulations promulgated thereunder on an ongoing basis.

To participate in the Title IV Programs, an institution is subject to extensive regulation and periodic reviews by the federal and state governmental agencies, and accrediting bodies involved. An institution must be authorized to offer its programs of instruction by the relevant agencies of the state in which it is located, accredited by an accrediting agency recognized by ED, and certified as eligible by ED. On a periodic basis, an institution must be re-approved by these agencies and bodies to continue to receive Title IV funds. As of June 30, 2019, the College was properly authorized by the regulatory agencies involved, and no regulatory reviews were being conducted by the respective agencies.

Regulations have been established which impose limitations on institutions whose former students default on the repayment of their federally guaranteed or funded student loans above a specific cohort default rate (CDR). An institution whose CDR equals or exceeds 30% for three consecutive years will no longer be eligible to participate in the William D. Ford Federal Direct Loan (Direct Loan) and Federal Pell Grant programs for the remainder of the fiscal year in which the school is notified of its sanction and for the following two fiscal years. An institution whose CDR exceeds 40% will lose Direct Loan program eligibility for the remainder of the fiscal year in which the school is notified of its sanction and for the following two fiscal years. The College's most recent official three-year CDR (FY2016) published by ED, is 6.5%.

Under the federal regulations mentioned above, ED calculates the institution's composite score based on a three-factor financial responsibility ratio. An institution which does not meet ED's minimum composite score of 1.5 can demonstrate financial responsibility by meeting the "zone alternative" or posting a letter of credit in favor of ED. The "zone alternative" includes a delayed method of cash funding for Title IV aid, and the providing of additional information to ED, upon request. As of June 30, 2019, the Company had a composite score equal to 1.5 out of a possible score of 3.0.

In October 2014, ED issued gainful employment regulations that measure our students' ability to repay their educational loans and debts, incurred at our institution, subsequent to their enrollment. These regulations are effective for all of our Title IV eligible programs. The regulations require a debt-to-earnings ratio (D/E Rate) be computed which is based upon the median debt loan repayment compared to their earnings as provided by the Social Security Administration (SSA). This D/E Rate is computed separately for each Title IV eligible program. An institution may appeal the loan and debt information compiled by ED and has the right to submit alternative earnings in lieu of the SSA information under specific conditions and requirements. Each individual program subject to gainful employment is deemed to be either passing, failing, or in the zone. An individual program is deemed to be ineligible for Title IV aid if it fails two out of three consecutive years or has a combination of zone and failing rates for four consecutive years. A program deemed to be ineligible will lose Title IV aid beginning on the date ED notifies the institution or the institution voluntarily discontinues a failing program or program in the zone. In October 2016, ED issued draft 2015 year gainful employment D/E Rates and in January 2017, issued final D/E Rates. No 2016 or subsequent year D/E Rates have been issued by ED.

NOTE I - REGULATORY (CONTINUED)

On July 1, 2019, ED issued a new federal rule which rescinds the entirety of the gainful employment regulations effective July 1, 2020. In addition, ED allowed for the new federal rule to be early adopted as of July 1, 2019. The College adopted these new federal rules as of July 1, 2019 and, as such, is no longer subject to the gainful employment regulations.

During 2016, ED issued final regulations to change the borrower defense to repayment (BDTR) regulations. The current ED administration was sued for delaying the 2016 BDTR regulations and a federal judge ruled on October 12, 2018 that the 2016 BDTR regulations were effective immediately. The 2016 BDTR regulations included significant revisions to the financial responsibility standards, closed school loan discharge, and false certification discharge, and new provisions concerning pre-dispute arbitration clauses, class action waivers, and repayment rates. On March 15, 2019, ED issued guidance in regard to the implementation of the BDTR 2016 regulations. The guidance includes financial responsibility reporting requirements for mandatory and discretionary triggering events.

On August 30, 2019, ED issued new final regulations to change the BDTR regulations. Under these final 2019 BDTR regulations, significant revisions were maintained related to the financial responsibility standards, closed school loan discharge and false certification discharge, and provisions concerning pre-dispute arbitration clauses and class action waivers. ED believes the 2019 BDTR regulations maintain a balance between the rights of the institution and the student borrower. Mandatory and discretionary triggers still exist which allow ED to impose a letter of credit on an institution prior to their submission of annual financial statements if certain negative events occur. In addition, ED issued guidance related to the composite score ratio to change the treatment of long-term debt, in certain instances, and to amend the ratio as a result of ASU No. 2016-02, Leases. The 2019 BDTR regulations will be effective as of July 1, 2020. An institution has the option to adopt the provisions related to the composite score ratio immediately. Management has elected to not adopt these provisions. The 2016 BDTR regulations remain in effect until July 1, 2020. Management is in process of determining the impact of the 2019 BDTR regulations on the Company.

REPORT ON INTERNAL CONTROL
OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

INDEPENDENT AUDITOR'S REPORT

To the Shareholder
Ambow BSC Inc. and Subsidiary
Boston, Massachusetts

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained *in Government Auditing Standards*, issued by the Comptroller General of the United States, the consolidated financial statements of Ambow BSC Inc. and Subsidiary, which comprise the consolidated balance sheet as of June 30, 2019, and the related consolidated statements of operations, changes in shareholder's equity, and cash flows for the year then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated December 26, 2019.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements, we considered Ambow BSC Inc. and Subsidiary's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of Ambow BSC Inc. and Subsidiary's internal control. Accordingly, we do not express an opinion on the effectiveness of the Ambow BSC Inc. and Subsidiary's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether Ambow BSC Inc. and Subsidiary's consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. Such tests included compliance tests as set forth in the *Guide For Audits of Proprietary Schools and For Compliance Attestation Engagements of Third-Party Servicers Administering Title IV Programs*, issued by the U.S. Department of Education, Office of Inspector General (the Guide) including those relating to related parties and percentage of revenue derived from Title IV Programs. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or the Guide.

PURPOSE OF THIS REPORT

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

McClintock & Associates, P.C.

Pittsburgh, Pennsylvania
December 26, 2019