

SOUTHWESTERN UNIVERSITY

CONSOLIDATED FINANCIAL STATEMENTS

As of and for the Years Ended June 30, 2020 and 2019

And Reports of Independent Auditor

SOUTHWESTERN UNIVERSITY

TABLE OF CONTENTS

REPORT OF INDEPENDENT AUDITOR 1-2

CONSOLIDATED FINANCIAL STATEMENTS

Consolidated Statements of Financial Position3
Consolidated Statements of Activities..... 4-5
Consolidated Statements of Cash Flows6
Notes to the Consolidated Financial Statements 7-33

Report of Independent Auditor

To the Board of Trustees
Southwestern University
Georgetown, Texas

We have audited the accompanying consolidated financial statements of Southwestern University and Southwestern Foundation (collectively, the “University”), which comprise the consolidated statements of financial position as of June 30, 2020 and 2019, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management’s Responsibility for the Consolidated 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 audits. 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 Southwestern University and Southwestern Foundation as of June 30, 2020 and 2019, and the changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Changes in Financial Statement Presentation

As discussed in Note 2, Southwestern University and Southwestern Foundation adopted Accounting Standards Update ("ASU") 2017-07, *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. The ASU has been applied retrospectively to all periods presented. Our opinion is not modified with respect to this matter.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 5, 2020 on our consideration of the University'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 solely 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 effectiveness of the entity's 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 the University's internal control over financial reporting and compliance.

Cheryl Behant LLP

Charlotte, North Carolina
October 5, 2020

SOUTHWESTERN UNIVERSITY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

JUNE 30, 2020 AND 2019

	<u>2020</u>	<u>2019</u>
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 29,213,874	\$ 37,223,150
Receivables:		
Student accounts receivable, net	34,079	57,136
Unconditional promises receivable, net	4,583,801	3,667,579
Investment income	1,516	41,616
Other receivables	592,495	478,322
Prepays and other current assets	1,208,579	1,265,819
Total Current Assets	35,634,344	42,733,622
Unconditional promises receivable, net	5,546,567	6,779,822
Investments	289,110,284	296,183,512
Funds held in trusts by others ("FHITBO")	4,818,067	4,954,362
Investment in plant, net	124,460,780	120,840,568
Student loans receivable, net	3,313,930	3,725,781
Other assets	15,945	18,603
Total Assets	\$ 462,899,917	\$ 475,236,270
LIABILITIES AND NET ASSETS		
Current Liabilities:		
Accounts payable, accrued and other liabilities	\$ 6,609,065	\$ 9,258,263
Bonds and notes payable	1,097,703	1,008,555
Capital lease payable	730,232	706,765
Accrued post-retirement benefits	491,868	522,250
Deposits and deferred revenue	4,360,181	3,268,677
Total Current Liabilities	13,289,049	14,764,510
Bonds and notes payable, long-term portion	34,280,548	35,448,250
Capital lease payable, long-term portion	136,037	866,270
Accrued post-retirement benefits, long-term portion	7,791,136	6,251,540
Refundable advances	2,386,228	3,008,205
Deferred compensation and other long-term liabilities	11,400	419,301
Total Liabilities	57,894,398	60,758,076
Net Assets:		
Without donor restrictions	129,209,242	132,310,325
With donor restrictions	275,796,277	282,167,869
Total Net Assets	405,005,519	414,478,194
Total Liabilities and Net Assets	\$ 462,899,917	\$ 475,236,270

SOUTHWESTERN UNIVERSITY
CONSOLIDATED STATEMENT OF ACTIVITIES

YEAR ENDED JUNE 30, 2020 (WITH COMPARABLE TOTALS FOR 2019)

	2020			2019
	Without Donor Restrictions	With Donor Restrictions	Total	
Operating Revenues:				
Net tuition and fees	\$ 27,442,046	\$ -	\$ 27,442,046	\$ 24,906,229
Private gifts and grants	1,762,602	3,083,099	4,845,701	4,097,048
Government grants	300,805	1,459,103	1,759,908	751,052
Endowment return used for operations, net	1,175,372	10,881,097	12,056,469	11,687,070
Investment return from nonendowment, net	876,226	7,577	883,803	1,674,108
Distributions from FHITBO	325	191,472	191,797	175,882
Other income	984,105	9,532	993,637	1,273,830
Auxiliary enterprises	9,927,782	-	9,927,782	11,920,968
Net assets released from restrictions	15,222,071	(15,222,071)	-	-
Total Operating Revenues	57,691,334	409,809	58,101,143	56,486,187
Operating Expenses:				
Instructional services	23,423,875	-	23,423,875	23,749,109
Student services	11,765,808	-	11,765,808	11,482,369
Auxiliary services	8,266,121	-	8,266,121	8,597,684
Institutional support	13,574,034	-	13,574,034	13,487,874
Scholarships (Higher Education Relief Funds)	606,725	-	606,725	-
Total Operating Expenses	57,636,563	-	57,636,563	57,317,036
Change in net assets from operating activities	54,771	409,809	464,580	(830,849)
Nonoperating Activities:				
Gifts for endowment and plant improvements	-	3,366,445	3,366,445	8,334,375
Net (loss) gain in excess of defined spending limit	(870,438)	(9,700,173)	(10,570,611)	9,576,961
Loss on disposal of fixed assets	(635,784)	-	(635,784)	(164,235)
Change in value of split-interest agreements	-	(175,878)	(175,878)	53,168
Other components of net periodic pension costs	2,987,762	-	2,987,762	4,199,124
Post-retirement related changes other than net periodic pension cost	(4,945,515)	-	(4,945,515)	(4,013,383)
Net assets released from restrictions for plant improvements	271,795	(271,795)	-	-
Other	36,326	-	36,326	23,088
Total Nonoperating Activities	(3,155,854)	(6,781,401)	(9,937,255)	18,009,098
Change in net assets	(3,101,083)	(6,371,592)	(9,472,675)	17,178,249
Net assets, beginning of year	132,310,325	282,167,869	414,478,194	397,299,945
Net assets, end of year	<u>\$ 129,209,242</u>	<u>\$ 275,796,277</u>	<u>\$ 405,005,519</u>	<u>\$ 414,478,194</u>

SOUTHWESTERN UNIVERSITY
CONSOLIDATED STATEMENT OF ACTIVITIES

YEAR ENDED JUNE 30, 2019

	2019		
	Without Donor Restrictions	With Donor Restrictions	Total
Operating Revenues:			
Net tuition and fees	\$ 24,906,229	\$ -	\$ 24,906,229
Private gifts and grants	2,082,939	2,014,109	4,097,048
Government grants	307,035	444,017	751,052
Endowment return used for operations, net	1,243,231	10,443,839	11,687,070
Investment return from nonendowment, net	1,662,264	11,844	1,674,108
Distributions from FHITBO	239	175,643	175,882
Other income	1,259,650	14,180	1,273,830
Auxiliary enterprises	11,920,968	-	11,920,968
Net assets released from restrictions	13,401,868	(13,401,868)	-
Total Operating Revenues	<u>56,784,423</u>	<u>(298,236)</u>	<u>56,486,187</u>
Operating Expenses:			
Instructional services	23,749,109	-	23,749,109
Student services	11,482,369	-	11,482,369
Auxiliary services	8,597,684	-	8,597,684
Institutional support	13,487,874	-	13,487,874
Total Operating Expenses	<u>57,317,036</u>	<u>-</u>	<u>57,317,036</u>
Change in net assets from operating activities	<u>(532,613)</u>	<u>(298,236)</u>	<u>(830,849)</u>
Nonoperating Activities:			
Gifts for endowment and plant improvements	2,360,750	5,973,625	8,334,375
Net gain in excess of defined spending limit	1,056,499	8,520,462	9,576,961
Loss on disposal of fixed assets	(164,235)	-	(164,235)
Change in value of split-interest agreements	-	53,168	53,168
Other components of net periodic pension costs	4,199,124	-	4,199,124
Post-retirement related changes other than net periodic pension cost	(4,013,383)	-	(4,013,383)
Net assets released from restrictions for plant improvements	162,895	(162,895)	-
Other	23,088	-	23,088
Total Nonoperating Activities	<u>3,624,738</u>	<u>14,384,360</u>	<u>18,009,098</u>
Change in net assets	3,092,125	14,086,124	17,178,249
Net assets, beginning of year	<u>129,218,200</u>	<u>268,081,745</u>	<u>397,299,945</u>
Net assets, end of year	<u>\$ 132,310,325</u>	<u>\$ 282,167,869</u>	<u>\$ 414,478,194</u>

SOUTHWESTERN UNIVERSITY
CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED JUNE 30, 2020 AND 2019

	<u>2020</u>	<u>2019</u>
Cash flows from operating activities:		
Change in net assets	\$ (9,472,675)	\$ 17,178,249
Adjustments to reconcile change in net assets to net cash flows from operating activities:		
Depreciation and amortization	4,676,149	4,339,129
Loss on disposal of assets	635,784	164,235
Net unrealized and realized gain on investments	(186,979)	(18,415,083)
Change in value of FHITBO	136,295	(93,166)
Gifts and grants restricted for endowment and plant improvements	(3,366,445)	(8,334,375)
Donated stock	-	(2,229,047)
Changes in operating assets and liabilities:		
Student accounts and loans receivable, net	434,908	523,213
Unconditional promises receivable	317,033	(1,731,387)
Investment income receivable	40,101	15,863
Other receivables	(114,174)	7,434
Other assets	59,898	278,032
Accounts payable, accrued and other liabilities	(3,087,780)	(1,907,905)
Accrued post-retirement benefits	1,509,215	(682,958)
Student deposits and advance payments	1,091,505	520,655
Refundable advances	(621,978)	55,437
Deferred compensation and other long-term liabilities	(407,901)	(5,993)
Net cash flows from operating activities	<u>(8,357,044)</u>	<u>(10,317,667)</u>
Cash flows from investing activities:		
Purchases of investments	(172,420,601)	(166,436,255)
Sales of investments	179,680,811	158,503,892
Purchases of fixed assets	(8,543,551)	(14,610,932)
Proceeds from sale of fixed assets	-	19,367
Net cash flows from investing activities	<u>(1,283,341)</u>	<u>(22,523,928)</u>
Cash flows from financing activities:		
Payment on bonds and notes payable	(1,028,571)	(986,129)
Payments on capital leases	(706,765)	(638,278)
Gifts and grants restricted for endowment and plant improvements	3,366,445	8,334,375
Net cash flows from financing activities	<u>1,631,109</u>	<u>6,709,968</u>
Net change in cash and cash equivalents	(8,009,276)	(26,131,627)
Cash and cash equivalents, beginning of year	37,223,150	63,354,777
Cash and cash equivalents, end of year	<u>\$ 29,213,874</u>	<u>\$ 37,223,150</u>
Supplemental disclosure of cash payments for:		
Interest paid	<u>\$ 1,353,709</u>	<u>\$ 1,414,100</u>
Supplemental disclosure of noncash transactions for:		
Fixed assets acquired under capital lease	<u>\$ -</u>	<u>\$ 41,635</u>
Additions to fixed assets in accounts payable	<u>\$ 438,575</u>	<u>\$ 3,488,910</u>

SOUTHWESTERN UNIVERSITY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 1—Nature of operations

Southwestern University (the “University”), located in Georgetown, Texas, is the oldest chartered institution of higher learning in the state. It traces its roots to the 1840 founding of Rutersville College in the Republic of Texas near La Grange. A nationally recognized, independent undergraduate liberal arts college affiliated with the United Methodist Church, the University provided services to 1,562 students and has a current student-to-faculty ratio of 12:1. Students choose from 36 major programs in the University’s two academic areas, The Brown College of Arts and Sciences and the Sarofim School of Fine Arts.

The revenues generated by the University consist primarily of tuition and fees paid by students. Many students rely on funds received from federal financial aid programs under Title IV of the Federal Higher Education Act of 1965 (“HEA”), as amended, to pay for a substantial portion of their tuition. As an educational institution, the University is subject to licensure from various accrediting and state authorities and other regulatory requirements of the United States Department of Education (the “USDE”).

Southwestern Foundation (the “Foundation”), a Texas nonprofit corporation, was founded in 1993. The Foundation’s board is composed of members selected and approved by the Board of Trustees. The Foundation is organized and operated to maintain real or personal property and to use and apply the income therefrom and the principal thereof exclusively for charitable, scientific, literary, and educational purposes. The Foundation is administered solely for the benefit and support of the University. For reporting purposes, the Foundation is consolidated in the University’s consolidated financial statements. Inter-entity transactions have been eliminated in the consolidated financial statements. Hereinafter, the “University” will refer to the consolidated entity including both Southwestern University and Southwestern Foundation.

Tax-Exempt Status – The University claims exemption from federal income tax under Section 501(c)(3) of the Internal Revenue Code. The University files unrelated business income tax and other information returns as required by government authorities. The University has concluded that it does not have any unrecognized tax benefits resulting from current or prior period tax positions. Accordingly, no additional disclosures have been made on the consolidated financial statements regarding uncertain tax provisions.

Student Financial Assistance Programs – The University participates in various student financial aid programs. These programs are subject to periodic review by the USDE pursuant to the HEA, as amended. In order to continue to participate in Title IV Programs, the University must comply with the standards set forth in the HEA and the regulations promulgated thereunder (the “Regulations”). Among other things, these Regulations require the University to exercise due diligence in approving and disbursing funds and servicing loans, and to exercise financial responsibility related to maintaining certain financial ratios and requirements, all of which the University believes they have been met at June 30, 2020 and 2019.

Note 2—Summary of significant accounting policies

Basis of Financial Statement Presentation – The consolidated financial statements of the University have been prepared in accordance with generally accepted accounting principles in the United States of America (“U.S. GAAP”), which require it to report information regarding its financial position and activities according to the following net asset classifications:

Without Donor Restrictions – Net assets without donor restrictions are free of donor-imposed restrictions. All revenues, gains, and losses that are not restricted by donors are included in this classification. All expenditures are reported in the without donor restrictions net asset class, including expenditures funded by restricted contributions. Expenditures funded by restricted contributions are reported in the without donor restrictions net asset class because the funds have been used in accordance with the restricted stipulations; thus, they are released from such restrictions. Additionally, net assets may be set aside by the Board of Trustees to be used for specific activities and guidelines established by the Board of Trustees. As of June 30, 2020 and 2019 the Board of Trustee’s designated \$29,447,351 and \$30,503,307, respectively, to be set aside for the endowment (see Note 7).

SOUTHWESTERN UNIVERSITY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 2—Summary of significant accounting policies (continued)

With Donor Restrictions – Net assets with donor restrictions are assets for which use by the University is limited by donor-imposed stipulations that either expire with the passage of time or that can be fulfilled or removed by actions of the University pursuant to those stipulations. Net assets with donor restrictions are designated by donors for specific purposes and include unconditional promises receivable, split-interest agreements, interests in trusts held by others, and accumulated appreciation on donor-restricted endowments which have not been appropriated by the Board of Trustees for expenditure. Some net assets with donor restrictions are required to be held in perpetuity and only the income or a portion of the income earned is to be used for specific purposes.

Measure of Operations – The consolidated statements of activities report all changes in net assets, including changes in net assets from operating and nonoperating activities. Operating activities consist of those items attributable to the University's ongoing education activities and supporting services. Nonoperating activities are limited to resources that generate return from investments, activities related to endowment and plant, other components of net periodic pension costs, and other activities considered to be of a more unusual or nonrecurring in nature.

Cash and Cash Equivalents – The University considers all highly liquid assets with a maturity of three months or less when purchased as cash and cash equivalents. Cash and cash equivalents held in transition for investment are included in investments. The University places its cash and cash equivalents with high quality financial institutions, which at times may exceed federally insured limits. The University has not experienced any losses on such accounts.

Loans Receivable – The Federal Perkins Loan Program consists primarily of funds advanced to students by the U.S. government. Under the terms of the program, these loans are subject to forgiveness or assignment back to the federal government under certain circumstances. The amount to be forgiven or assigned is based on the occurrence of certain future events that cannot be anticipated.

Investments – Investments with readily determinable fair values are stated at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Investments in securities traded on a national securities exchange are valued at the last reported sales price on the last business day of the fiscal year. Investments in government obligations are valued at the bid price or the average of the bid and asked price on the last business day of the year from published sources where available and, if not available, from other sources considered reliable. Purchases and sales of securities are recorded as of the trade date. Realized gains and losses on sales of securities are determined on the basis of average cost. Interest income is recognized on the accrual basis. Dividend income is recognized on the ex-dividend date. Investments in real estate and mineral rights are reported at either cost or the fair value at the date the gift was received.

Alternative investments consist of the University's investments in hedge funds, private equity, venture capital, real estate, and other alternative investments that are not publicly traded. Participation in these funds is achieved via ownership of shares in limited partnerships and limited liability companies. Some of these alternative investments may entail liquidity risks to the extent that they are difficult to sell or cannot be converted readily to cash at favorable prices. The University's alternative investments are not traded in an active market; however, the net asset value ("NAV") of the shares is reported by the fund manager on a monthly or quarterly basis.

Debt Issuance Costs – Debt issuance costs are amortized by the straight-line method over the remaining terms of the related debt and are included in bonds and notes payable on the consolidated statements of financial position. The University believes the use of the straight-line method does not differ significantly from the use of the effective interest method. Amortization expense related to these costs was \$13,934 for both of the years ended June 30, 2020 and 2019, and is included in interest expense on the accompanying note of functional expenses (see Note 15).

SOUTHWESTERN UNIVERSITY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 2—Summary of significant accounting policies (continued)

Contributions – All contributions are considered to be available for undesignated use unless specifically restricted by the donor. Amounts received that are designated for future periods or restricted by the donor for specific purposes are reported as net assets with donor restrictions. Unconditional promises receivable are recorded at the present value of their estimated future cash flows, net of allowances. An allowance for uncollectible promises receivable is determined by a specific review based upon management’s judgment, including such factors as prior collection history and currently available information relating to the donor’s intent and ability to satisfy the promises receivable. The discounts on those amounts are computed using risk-free interest rates applicable to the years in which the promises are expected to be received. Amortization of the discounts is included in contribution revenue. Conditional promises to give, that is, those with a measurable performance or other barrier, and a right of return or right of release, are not recognized until the conditions on which they depend have been substantially met.

Bequests in Probate and Conditional Promises Receivable – The University considers unconditional bequests, as declared valid by probate court, to be unconditional promises receivable. Unconditional bequests that are not in probate are considered to be intentions to give and are not recognized in the consolidated financial statements.

Revenue Recognition –

Net Tuition and Fees – The University recognizes revenue from student tuition and fees within the fiscal year in which academic services are rendered. Discounts in the form of scholarships and financial aid grants provided by the University, including those funded by the endowment and gifts, are reported as a reduction of student revenue. A discount represents the difference between the stated charge for the academic period and the amount that is due on the student account. Scholarships and grants awarded to students were \$36,647,897 and \$34,389,292 at June 30, 2020 and 2019, respectively.

Campus-based programs are delivered in fall (mid-August to mid-December) and spring (mid-January to mid-May) academic terms, as well as two summer terms described below. Payment for fall term is due in July, and payment for spring term is due in December. The University offers a payment plan for the fall term that can start as early as April. Any payments received for the future fall term that are received prior to July 1 are recorded as deferred revenue and later recognized as the fall term performance obligations are met.

Payments for tuition for all summer terms are recognized as performance obligations are met. During summer 2020, the University’s Summer 1 term began in May and ended prior to the fiscal year-end June 30. The University no longer has a summer 2 term. Summer 3 term starts in mid-May and ends in mid-August, spanning two reporting periods. The University determined that the tuition amounts for summer 3 that related to July are not significant.

Student Deposits – For the academic year 2019-2020, first-year students secure their enrollment and housing at the University by paying a nonrefundable deposit by May 1 for the following fall academic term. The normal student deposit of \$500 includes a \$250 enrollment deposit and a \$250 housing deposit. The enrollment deposit is applied against the charges for the academic term, while the housing deposit is held until on-campus housing is vacated. For the academic year 2020-2021, the student nonrefundable deposit was increased from \$500 to \$700, to include an additional \$200 student orientation fee. Because of the Coronavirus (“COVID-19”) pandemic, the three student orientation sessions held in June ended up being virtual as opposed to in person, so the \$200 fee was allocated as \$100 to the student orientation fee and an additional \$100 to the enrollment deposit to be applied to the fall 2020 term. Only the \$100 fee related to the June 2020 student orientation sessions was recognized as income in the year ended June 30, 2020. Since the remaining deposit amounts were received in advance of services rendered, they are recorded as deferred revenue and recognized when services are provided.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 2—Summary of significant accounting policies (continued)

Auxiliary Enterprises – Auxiliary services exist to furnish good or services to students, faculty, staff, or incidentally to the general public. Fees charged for auxiliary services are priced to offset the cost of the goods and services provided. The distinguishing characteristic of auxiliary services is that they are managed as an essentially self-supporting activity.

Auxiliary services revenue includes activities for student housing and dining facilities. Payments for housing and dining services are due the same time as tuition and fees or upon receipt if added after the initial due date. Student housing and dining facilities services are provided for fall (mid-August to mid-December) and spring (mid-January to mid-May) academic terms. Normally for summer terms, dining plans are not offered and housing is billed on a daily basis. Performance obligations for housing and dining services are delivered over the academic terms and recognized as the performance obligation is met. In March 2020 due to the COVID-19 pandemic, the University moved to distance learning and closed on-campus housing for students. As a result, the University refunded approximately \$2.3 million in prorated room and board charges to students. In addition, the University student housing remained closed for the entire summer 2020.

Deferred revenue amounts for advance tuition payments and student deposits are shown in Note 17.

Investment in Plant – Additions are generally recorded at cost at the date of acquisition or at fair value at the date of donation. Normal replacements of movable plant assets are charged to expense as maintenance. The University's asset capitalization threshold is \$2,500 for individual asset acquisitions.

Depreciation of physical plant and equipment was \$4,726,132 and \$4,389,112 for 2020 and 2019, respectively. Depreciation is computed using the straight-line method for all depreciable assets over their estimated useful lives as follows:

Computers and software	5 years
Automobiles	5 years
Furniture and equipment	7 years
Grounds improvements	15 years
Library books	25 years
Buildings (prior to July 2012)	40 years

Starting in July 2012, depreciation for new physical plant building renovations and construction is computed using the straight-line method for all depreciable assets over the following useful lives:

Building shell	70 years
Elevator system	20 years
Fire protection system	20 years
Fixed equipment assets	20 years
Plumbing system	20 years
Electrical and lighting system	20 years
Floor coverings	15-30 years
HVAC	15 years
Interior finish	15 years
Furniture and lab startup items	7 years
Miscellaneous	15 years
Roof covering	10-30 years

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 2—Summary of significant accounting policies (continued)

Collections – The University has 19 collections within the Special Collections of the A. Frank Smith, Jr. Library Center that contain a variety of books, records, papers, maps, and manuscripts that are protected and preserved for public exhibition, education, research, and the furtherance of public service. They are neither disposed of for financial gain nor encumbered in any manner. Accordingly, such collections are not reported for financial statement purposes.

Split-Interest Agreements – The University is the income or remainder beneficiary for various perpetual and charitable remainder trusts held by third party trustees where the trustee has no discretion regarding the beneficiaries’ participation in the trust. The University’s beneficial interest in these agreements and related contribution revenue is recognized at the fair value at the date of donation. Changes from year to year in the fair value of the University’s beneficial interest are reported as a change in value of split-interest agreements in the appropriate net asset class according to the trust restrictions.

Scholarships and Grants – The consolidated statements of activities present financial assistance provided to students in the form of institutional scholarships and grants as a reduction to tuition and fees revenues. Scholarships and grants include programs supported by donor-restricted endowments, donor-restricted gifts, and grants and programs supported by general operations of the University. The following table presents the amount of scholarships and grants revenue reduction, and the related percentage of tuition and fee revenues supported by donor-restricted and general operation support:

	2020		2019	
	Amount	Discount Rate to Tuition	Amount	Discount Rate to Tuition
Scholarships and grants supported by endowments and gifts	\$ 3,472,484	5.4%	\$ 3,368,805	5.7%
Scholarships and grants supported by general operations	<u>33,175,413</u>	51.8%	<u>31,020,487</u>	52.4%
Total scholarships and grants	<u>\$ 36,647,897</u>	57.2%	<u>\$ 34,389,292</u>	58.1%

Use of Estimates – The preparation of 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 related notes. Actual results could differ from those estimates.

Accounting Pronouncement Adopted – As of July 1, 2019, the University adopted the provisions of Financial Accounting Standards Board (“FASB”) Accounting Standards Update (“ASU”) 2017-07 *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. ASU 2017-07 applies to all employers that offer to their employees defined benefit pension plans, other postretirement benefit plans, or other types of benefits accounted for under Topic 715. The University implemented ASU 2017-07 and have accordingly adjusted the presentation of service cost and other components of net benefit cost in the consolidated financial statements. Following the adoption of the ASU, the University recognizes the service cost component in operating expenses under institutional support and other components of net benefit cost as a nonoperating activity. There was no material impact to the consolidated financial statements as a result of this adoption. The ASU has been applied retrospectively to all periods presented, with no effect on net assets, as shown below.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 2—Summary of significant accounting policies (continued)

Effect of ASU 2017-07 on consolidated statements of activities:

	2020			2019
	Without Donor Restrictions	With Donor Restrictions	Total	
Operating Activities:				
Previous change in net assets	\$ 3,042,533	\$ 409,809	\$ 3,452,342	\$ 3,368,275
Cumulative effect of implementation of ASU 2017-07	(2,987,762)	-	(2,987,762)	(4,199,124)
Reclassified change in net assets	<u>\$ 54,771</u>	<u>\$ 409,809</u>	<u>\$ 464,580</u>	<u>\$ (830,849)</u>
	2020			2019
	Without Donor Restrictions	With Donor Restrictions	Total	
Nonoperating Activities:				
Previous total nonoperating activities	\$ (6,143,616)	\$ (6,781,401)	\$ (12,925,017)	\$ 13,809,974
Cumulative effect of implementation of ASU 2017-07	2,987,762	-	2,987,762	4,199,124
Reclassified total nonoperating activities	<u>\$ (3,155,854)</u>	<u>\$ (6,781,401)</u>	<u>\$ (9,937,255)</u>	<u>\$ 18,009,098</u>
	2020			2019
	Without Donor Restrictions	With Donor Restrictions	Total	
Total net assets:				
Previous total net assets	\$ 129,209,242	\$ 275,796,277	\$ 405,005,519	\$ 414,478,194
Cumulative effect of implementation of ASU 2017-07	-	-	-	-
Reclassified net assets	<u>\$ 129,209,242</u>	<u>\$ 275,796,277</u>	<u>\$ 405,005,519</u>	<u>\$ 414,478,194</u>

Future Accounting Pronouncements – In February 2016, FASB issued ASU 2016-02, *Leases (Topic 842)*. The guidance in this ASU supersedes the leasing guidance in Topic 840, *Leases*. Under the new guidance, lessees are required to recognize lease assets and lease liabilities on the statement of financial position for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classifications affecting the pattern of expense recognition in the consolidated statement of activities. The new standard is effective for fiscal years beginning after December 15, 2021. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the consolidated financial statements, with certain practical expedients available.

Management is currently evaluating the impact that this standard will have on University's consolidated financial statements.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 3—Student accounts and loans receivable

Student Accounts – Student accounts receivable are reported net of allowances for doubtful accounts of \$561,179 and \$606,461 for the years ended June 30, 2020 and 2019, respectively. Allowance for doubtful accounts are established based on prior collection experience and current economic factors which, in management’s judgment, could influence collectability of the balance outstanding. For student accounts the allowance percentage is 100% for accounts over 181 days past due but still undergoing collection procedures. For institutional loans, the allowance percentage ranges from 25% for accounts past 31 days due to 100% for accounts greater than five years past due. Balances are written off only when they are deemed permanently uncollectible. Amounts due under the Perkins loan program are guaranteed by the government and, therefore, no reserves are placed on any past due balances under the program.

Loans Receivable – The University makes uncollateralized loans to students based on financial need. Student loans are funded through federal government loan programs or institutional resources. At June 30, 2020 and 2019, student loans represent .72% and .78% of total assets, respectively.

At June 30, student loans consists of the following:

	<u>2020</u>	<u>2019</u>
Federal government programs	\$ 2,359,929	\$ 2,748,939
Institutional programs	2,057,770	1,991,896
	<u>4,417,699</u>	<u>4,740,835</u>
Less allowance for doubtful accounts:		
Beginning of year	(1,015,054)	(855,855)
Increases	<u>(88,715)</u>	<u>(159,199)</u>
End of year	<u>(1,103,769)</u>	<u>(1,015,054)</u>
Student loans receivable, net	<u>\$ 3,313,930</u>	<u>\$ 3,725,781</u>

The University participated in the Perkins federal revolving loan program, but the program expired on September 30, 2017, so no additional disbursements were permitted after June 30, 2018. As such, no new Perkins loans were issued for fiscal years ended June 30, 2020 and 2019. Funds advanced by the federal government and net accumulations in the revolving loan fund were \$2,369,584 and \$2,998,260 at June 30, 2020 and 2019, respectively, and are ultimately refundable to the government and are classified as refundable advances in the consolidated statements of financial position. Outstanding loans cancelled under the program result in a decrease in the liability to the government.

At June 30, 2020 and 2019, the following amounts were due under the student loan programs:

<u>June 30,</u>	<u>Deferrals</u>	<u>Currently Due</u>	<u>31-90 Days Past Due</u>	<u>90+ Days Past Due</u>	<u>Total Due</u>
2020	\$ 911,998	\$ 1,608,333	\$ 184,470	\$ 1,712,898	\$ 4,417,699
2019	\$ 1,266,335	\$ 1,649,214	\$ 217,127	\$ 1,608,159	\$ 4,740,835

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 4—Unconditional promises receivable

As of June 30, 2020 and 2019, the unconditional promises receivable are as follows:

	2020	2019
Less than one year*	\$ 9,583,801	\$ 8,672,675
One to five years	5,706,873	7,033,604
More than five years	100	300
	<u>15,290,774</u>	<u>15,706,579</u>
Present value discount	(160,406)	(259,178)
Allowance for uncollectable promises receivable	<u>(5,000,000)</u>	<u>(5,000,000)</u>
Total unconditional promises receivable	<u>\$ 10,130,368</u>	<u>\$ 10,447,401</u>

* The amount of the allowance for uncollectable promises receivable is related to a gift that is past due; thus, the amount reported for less than one year is unusually high without considering the off-setting allowance of \$5,000,000 when analyzing the unconditional promises due to be received in less than one year.

The University uses discount rates associated with the risks involved to discount anticipated cash flows for unconditional promises receivable. The rates used to discount the anticipated cash flows ranged from .3% to 4.9% for 2020 and 2019.

Note 5—Investments

Investments consist of long-term assets controlled by the University. Investment securities are exposed to various risks such as interest rate, liquidity, market, currency, and credit. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and such changes could materially affect the amounts reported in the consolidated statements of financial position.

A summary of investments at June 30, 2020 and 2019 are as follows:

	2020	2019
At fair value:		
Cash equivalents	\$ 2,895,000	\$ 4,109,566
Equities, equity mutual funds and co-mingled equity funds	117,519,535	122,378,547
Fixed income and co-mingled fixed income funds	47,846,755	46,524,629
Alternative investments	<u>112,327,851</u>	<u>114,649,627</u>
Total at fair value	280,589,141	287,662,369
At cost or market at date of acquisition:		
Real estate	8,356,045	8,356,045
Mineral interests	<u>165,098</u>	<u>165,098</u>
Total at cost or market at date of acquisition	<u>8,521,143</u>	<u>8,521,143</u>
Total investments	<u>\$ 289,110,284</u>	<u>\$ 296,183,512</u>

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 6—Fair value measurement

The University measures the fair value of investments using a hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. Inputs are used in applying the various valuation techniques and broadly refer to the assumptions that market participants use to make valuation decisions, including assumptions about risk. Inputs may include price information, volatility statistics, specific and broad credit data, liquidity statistics, and other factors. A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement.

The fair value hierarchy is categorized into three levels based on the inputs as follows:

Level 1 – Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities that the University has the ability to access. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these securities does not entail a significant degree of judgment.

Level 2 – Valuations based on quoted prices for similar assets or liabilities in active markets and in markets that are not active and for which all significant inputs are observable, either directly or indirectly.

Level 3 – Valuations based on inputs that are unobservable and supported by little or no market activity. The University holds Level 3 investments, which included collateralized debt obligations, some privately held currently non-marketable common stock, and funds held in trust by others. When observable prices are not available for these securities, the University uses one or more valuation techniques for which sufficient and reliable data is available. The degree of judgment exercised in determining fair value is greatest for securities categorized in Level 3, due to the inherent uncertainty of these valuations. Level 3 estimated values may differ significantly from the values that would have been used had a ready market for the investment existed, and the differences could be material.

The inputs used by the University in estimating the value of Level 3 investments include the original transaction price and completed or pending third party transactions in the investment or comparable issuers. Level 3 investments may also be adjusted to reflect illiquidity and/or non-transferability, with the amount of such discount estimated by the University in the absence of market information. The fair value measurement of Level 3 investments does not include transaction costs that may have been capitalized as part of the security's cost basis.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 6—Fair value measurement (continued)

The following table presents the financial instruments carried on the consolidated statements of financial position by caption and by level within the valuation hierarchy:

	Assets at Fair Value as of June 30, 2020				Total
	Level 1	Level 2	Level 3	Investments Measured at NAV ¹	
Cash and cash equivalents	\$ 2,895,000	\$ -	\$ -	\$ -	\$ 2,895,000
Equities:					
Large cap equity, mutual funds, and co-mingled funds	544,476	-	-	-	544,476
International co-mingled funds	-	-	-	116,975,059	116,975,059
Fixed income:					
Bonds co-mingled funds	-	-	-	33,865,678	33,865,678
Credit Securities	-	-	-	12,295,387	12,295,387
U.S. Treasury and agency co-mingled funds	-	-	-	1,685,690	1,685,690
Alternative investments:					
Hedge strategies co-mingled funds	-	-	-	26,536,920	26,536,920
Natural resources stock index co-mingled funds and limited partnerships	-	-	-	21,955,600	21,955,600
Distressed debt limited partnerships	-	-	-	655,381	655,381
Private capital limited partnerships	-	-	-	45,486,292	45,486,292
Private capital loan fund	-	-	7,325,149	-	7,325,149
Private credit	-	-	-	6,768,489	6,768,489
Private equity	-	-	3,600,020	-	3,600,020
Total investments valued at fair value	3,439,476	-	10,925,169	266,224,496	280,589,141
Funds held in trust by others	-	-	4,818,067	-	4,818,067
	<u>\$ 3,439,476</u>	<u>\$ -</u>	<u>\$ 15,743,236</u>	<u>\$ 266,224,496</u>	<u>\$ 285,407,208</u>

¹ Investments that are measured at fair value using NAV per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 6—Fair value measurement (continued)

The following table presents the financial instruments carried on the consolidated statements of financial position by caption and by level within the valuation hierarchy:

	Assets at Fair Value as of June 30, 2019				Total
	Level 1	Level 2	Level 3	Investments Measured at NAV ¹	
Cash and cash equivalents	\$ 4,109,566	\$ -	\$ -	\$ -	\$ 4,109,566
Equities:					
Large cap equity, mutual funds, and co-mingled funds	27,995,369	-	-	142,586	28,137,955
International co-mingled funds	-	-	-	94,240,592	94,240,592
Fixed income:					
Mutual funds	-	-	-	424,699	424,699
Bonds co-mingled funds	-	-	-	42,700,180	42,700,180
U.S. Treasury and agency co-mingled funds	-	-	-	3,399,750	3,399,750
Alternative investments:					
Hedge strategies co-mingled funds	-	-	-	28,693,635	28,693,635
Natural resources stock index co-mingled funds and limited partnerships	-	-	-	25,667,245	25,667,245
Distressed debt limited partnerships	-	-	-	901,247	901,247
Private capital limited partnerships	-	-	-	42,331,497	42,331,497
Private capital loan fund	-	-	7,747,456	-	7,747,456
Private credit	-	-	-	5,708,527	5,708,527
Private equity	-	-	3,600,020	-	3,600,020
Total investments valued at fair value	32,104,935	-	11,347,476	244,209,958	287,662,369
Funds held in trust by others	-	-	4,954,362	-	4,954,362
Total	\$ 32,104,935	\$ -	\$ 16,301,838	\$ 244,209,958	\$ 292,616,731

¹ Investments that are measured at fair value using NAV per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy.

The following provides additional disclosures required by ASC 820, *Fair Value Measurements and Disclosures*, for alternative investment strategies included in Level 3:

Private Capital Loan Fund – The University holds an investment at a private foundation, which is reported at fair market value. This private foundation invests in a Methodist loan portfolio, which provides loans to members of the constituent community for building programs and other capital investments. This fixed rate investment began in fiscal year 2014, and there are no future commitments. Its redemption relates to a note payable with the private foundation.

Private Equity – The University received donations of common stock shares in a bank holding company in fiscal years 2013 and 2019. A third party report containing per share valuation was provided when each donation was received. This valuation report was reviewed along with public financial reports for the bank to determine the value of the stock and the University has discounted the stock value until the shares become marketable. The University adjusts the stock value if the change in fair market value is greater than 15% between the current year and the year of valuation.

SOUTHWESTERN UNIVERSITY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 6—Fair value measurement (continued)

The following provides additional disclosures required by ASC 820 for alternative investments in funds valued based on NAV value as a practical expedient for fair value:

Equities

Large Cap Equity, Mutual Funds, and Co-Mingled Funds – This category includes domestic mutual funds and only relates to fiscal year 2019.

International Co-Mingled Funds – This category includes funds with investments in global equity securities.

Fixed Income

Mutual Funds – This category includes mutual funds with fixed income securities and only relates to fiscal year 2019.

Bond Funds – This category includes funds with fixed income securities.

Credit Securities – This category consists of a fund comprised of fixed income credit securities that were acquired in fiscal year 2020.

U.S. Treasury and Agency Co-Mingled Funds – This category includes a fund that invests primarily in obligations issued or guaranteed as to principal or interest by U.S. government securities.

Alternative Investments

Hedge Strategies Co-Mingled Funds – This category includes third party investment funds invested in four broad investment categories: event-driven, credit, equity market neutral, and absolute return multi-strategy. Some or all of the marketable alternative strategies may be deployed across U.S. and non-U.S. markets.

Natural Resources Co-Mingled Funds and Limited Partnerships – This category includes funds and limited partnerships invested primarily in oil, gas and other natural resources-related investments.

Distressed Debt Limited Partnerships – This category includes a fund invested in performing restructured debt, stressed debt, distressed debt, “special situation” debt, and mezzanine debt investments.

Private Capital Limited Partnerships – This category includes limited partnerships invested in equity securities, warrants or other options, real estate, and international emerging growth companies.

Private Credit – This category includes funds that invests on a leveraged basis, in whole or in part, in collateralized and unsecured commercial loans and debt securities of corporations, partnerships, companies, or other securities.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 6—Fair value measurement (continued)

The following table includes additional disclosures required by ASC 820, *Fair Value Measurements and Disclosures*, for investments measured at fair value and ASU 2015-07, *Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (or Its Equivalent)*, which amends the disclosure requirements of ASC 820, *Fair Value Measurements and Disclosures*, for the fair value measurements of investments valued at NAV at June 30, 2020.

Category	Level 3 Fair Value	Investments Measured as NAV	Unfunded Commitment	Redemption Frequency	Redemption Notice Period
International equity co-mingled funds	\$ -	\$ 116,975,059	\$ -	Daily	N/A
Bonds co-mingled funds	-	33,865,678	-	1-7 days	2-5 days
Credit Securities	-	12,295,387	-	Monthly	any amount
U.S. Treasury and agency co-mingled funds	-	1,685,690	-	Daily	N/A
Hedge strategies co-mingled funds	-	26,536,920	-	May redeem 25% of their shares on any calendar quarter	65 days
Natural resources stock index co-mingled funds	-	11,717,871	-	Daily	2 days
Natural resources limited partnership	-	10,237,729	6,362,500	No redemption capability until respective partnership liquidation	
Distressed debt limited partnerships	-	655,381	803,200	No redemption capability until respective partnership liquidation	
Private capital LP-Strategic Core Real Estate Fund	-	7,405,930	2,000,000	Quarterly	120 days
Private capital LP's - Realty Opportunity Funds 2011, 2014, 2018	-	5,573,186	12,123,157	No redemption except as approved by GP	
Private capital - Loan Fund	7,325,149	-	-	Redemption relates to notes payable	
Private capital limited partnerships	-	32,507,176	26,069,750	No redemption capability until respective partnership liquidation	
Private credit	-	6,768,489	3,907,889	No redemption capability until fund liquidation	
Private equity - Non-Marketable	3,600,020	-	-	N/A	
	\$ 10,925,169	\$ 266,224,496	\$ 51,266,496		

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 6—Fair value measurement (continued)

The following table includes a roll forward for the year ended June 30, 2020 and 2019 of amounts for all financial instruments classified within Level 3. The classification of a financial instrument within Level 3 is based upon the significance of the unobservable inputs to the overall fair value measurement. The unobservable inputs and valuation techniques are not disclosed due to all information being provided by third parties.

	<u>2020</u>	<u>2019</u>
Beginning balance	\$ 16,301,838	\$ 15,204,156
Stock donation and adjustment	-	2,229,046
Withdrawals	(516,555)	(1,355,470)
Net investment income	94,248	130,941
Change in value of split-interest agreements	<u>(136,295)</u>	<u>93,165</u>
Ending balance	<u>\$ 15,743,236</u>	<u>\$ 16,301,838</u>

Note 7—Endowments

The University’s endowment consists of approximately 500 individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. Net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Adoption and Interpretation of Relevant Law – The University interprets the *Uniform Prudent Management of Institutional Funds Act of 2006* (“UPMIFA”) enacted in the state of Texas as allowing the University, absent explicit donor stipulations to the contrary as stated in the gift instrument, to appropriate as much of a donor-restricted endowment fund as the University determines is prudent for the uses, benefits, purposes, and duration for which the endowment is established. However, during the years ended June 30, 2020 and 2019, the University continued to preserve the fair value of the original gift as of the gift date of the donor-restricted endowment funds. As a result of this interpretation, the University classifies as net assets with donor restrictions (a) the original value of gifts donated to the endowment, (b) the original value of subsequent gifts to the endowment, (c) accumulations to the endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund, and (d) the remaining portion of the donor-restricted endowment fund until those amounts are appropriated for expenditure by the University in a manner consistent with the standard of prudence prescribed by UPMIFA.

In accordance with UPMIFA, the University considers the following seven factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

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

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 7—Endowments (continued)

The following is the endowment net asset composition by type of fund as of June 30:

As of June 30, 2020	Without Donor Restrictions	With Donor Restrictions		Total
		Purpose/Time Restrictions	Perpetual in Nature	
Donor-restricted endowment funds	\$ -	\$ 145,360,705	\$ 114,472,552	\$ 259,833,257
Board-designated endowment funds	29,579,054	-	-	29,579,054
Total endowment net assets	<u>\$ 29,579,054</u>	<u>\$ 145,360,705</u>	<u>\$ 114,472,552</u>	<u>\$ 289,412,311</u>

As of June 30, 2019	Without Donor Restrictions	With Donor Restrictions		Total
		Purpose/Time Restrictions	Perpetual in Nature	
Donor-restricted endowment funds	\$ -	\$ 155,064,290	\$ 110,713,399	\$ 265,777,689
Board-designated endowment funds	30,635,010	-	-	30,635,010
Total endowment net assets	<u>\$ 30,635,010</u>	<u>\$ 155,064,290</u>	<u>\$ 110,713,399</u>	<u>\$ 296,412,699</u>

The University's endowment net assets and changes in endowment net assets for the years ended June 30, 2020 and 2019 are reported in the following table. The University's funds held by others in trust of \$4,818,067 and \$4,954,362 for June 30, 2020 and 2019, respectively, are included in endowment net asset balances within the table. Changes in the fair value of the University's funds held by others in trust is reported as change in value of split-interest agreements within the table.

	Without Donor Restrictions	With Donor Restrictions		Total
		Purpose/Time Restrictions	Perpetual in Nature	
Endowment net assets at June 30, 2018	\$ 27,550,811	\$ 146,591,352	\$ 107,333,723	\$ 281,475,886
Investment return, net	1,966,680	18,916,777	93,165	20,976,622
Contributions	2,360,750	-	3,418,214	5,778,964
Appropriated for expenditure	(1,243,231)	(10,443,839)	-	(11,687,070)
Change in value of split-interest agreements	-	-	(131,703)	(131,703)
Endowment net assets at June 30, 2019	30,635,010	155,064,290	110,713,399	296,412,699
Investment return, net	119,416	1,177,512	-	1,296,928
Contributions	-	-	3,895,448	3,895,448
Appropriated for expenditure	(1,175,372)	(10,881,097)	-	(12,056,469)
Change in value of split-interest agreements	-	-	(136,295)	(136,295)
Endowment net assets at June 30, 2020	<u>\$ 29,579,054</u>	<u>\$ 145,360,705</u>	<u>\$ 114,472,552</u>	<u>\$ 289,412,311</u>

SOUTHWESTERN UNIVERSITY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 7—Endowments (continued)

Endowment Funds With Deficiencies – From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level required by the donor-restriction to retain as a fund of perpetual duration. These deficiencies typically result from unfavorable market fluctuations that occur shortly after the investment of new contributions restricted in perpetuity. The University had thirteen endowment funds with donor contributions totaling \$1,666,150 and fair market value of \$1,651,247 resulting in deficiencies totaling \$14,903 as of June 30, 2020. There were no deficiencies of this nature as of June 30, 2019. The University also has an endowment fund consisting of real estate related to a private foundation. Expenses incurred on behalf of this fund are paid by the University. The accumulation of these expenses totaled \$95,701 and \$90,590 as of June 30, 2020 and 2019, respectively. These deficiency amounts were reported as a reduction to the board-designated endowment funds.

Return Objectives and Risk Parameters – The University has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets over time. Endowment assets include those assets of donor-restricted funds that the University must hold in perpetuity or for a donor-specified period(s) as well as board-designated funds.

The University seeks an average total annual return that exceeds the spending/payout rate plus inflation, as measured over five- and ten-year periods in order to preserve, over time, the principal value of the assets as measured in real, inflation-adjusted terms. The endowment is a long-term pool of funds with an indefinite time horizon that runs concurrent with the endurance of the institution, in perpetuity. As such, the endowment assets are invested with a time horizon that extends well beyond a normal market cycle, and can assume an above-average level of risk as measured by the standard deviation of weighted annual returns. The University seeks to minimize portfolio risk through use of professional asset management and sufficient portfolio diversification to smooth volatility and help ensure reasonable consistency of return over time.

Strategies Employed for Achieving Objectives – To satisfy its long-term rate-of-return objectives, the University relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The University targets a diversified asset allocation among both equity and fixed income strategies. As a long-term policy guideline, endowment assets are allocated between equity classes, 70% (with ranges of 60%-80%), and fixed income asset class investments, 30% (with ranges of 20%-40%). The University's policy statement restricts investment in non-traditional (alternative) asset classes to no more than 50% of the portfolio, and restricts the total amount of illiquid investments to 30% or less of the portfolio. An illiquid investment is defined by the policy statement to mean "investments that could not be converted to cash in an orderly market over a period of twelve months or in a shorter period of time by accepting a discount of more than 10%."

Spending Policy – The University has adopted a spending formula for determining that part of the total return on endowment funds which can be expended annually. The spending formula determines spendable endowment return as a percentage of the 20-quarter average endowment market value, excluding investments in real estate, as of June 30 of the second preceding fiscal year. For fiscal years prior to 2020, the spending formula was based on the fair market value of the total endowment pool. Beginning in fiscal year 2020, the spending formula is based on the fair market value of individual funds. The spending rate was 5% for fiscal years 2020 and 2019. The University has approved a 6% spending rate for fiscal year 2021. No spending distributions are made from endowments with a market value of less than \$25,000 unless specified by the donor.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 7—Endowments (continued)

The University employs a reduced spending rate for endowments with deficiencies of market value to donor restricted net asset held in perpetuity as of the date of the spending calculation. For endowments with deficiencies less than 10%, the spending rate is reduced to 4%. For endowments with deficiencies greater than 10% but less than 20%, the spending rate is reduced to 3%. Endowments with deficiencies greater than 20% have no spending appropriation for the year.

In establishing this policy, the University considered the long-term expected return on its endowment. Accordingly, over the long term, the University expects the current spending policy and planned changes to that policy to allow its endowments to grow at an average rate that equals or exceeds inflation.

Note 8—Investment in plant, net

At June 30, 2020 and 2019, investment in plant, net consists of the following:

	2020	2019
Land	\$ 111,510	\$ 111,510
Buildings	178,527,491	152,569,097
Furniture and equipment and computers and software	21,386,798	20,631,947
Library books	10,559,852	10,572,140
Automobiles	1,045,825	1,045,825
Ground improvements	19,476,849	17,929,574
Leased equipment under capital leases	<u>3,432,672</u>	<u>3,432,672</u>
Total property	234,540,997	206,292,765
Less accumulated depreciation	<u>(111,065,605)</u>	<u>(109,844,276)</u>
	123,475,392	96,448,489
Construction in progress	<u>985,388</u>	<u>24,392,079</u>
Investment in plant - net	<u><u>\$ 124,460,780</u></u>	<u><u>\$ 120,840,568</u></u>

Note 9—Bonds and notes payable

The University's notes and bonds payable as of June 30, 2020 and 2019 consist of the following:

	2020	2019
City of Riesel Education Facilities Corporation 2006 Note	\$ 2,980,000	\$ 3,180,000
Texas Methodist Foundation Note	7,318,709	7,737,280
Clifton Higher Education Finance Corporation 2017 Revenue Bonds	<u>23,705,000</u>	<u>24,115,000</u>
	34,003,709	35,032,280
Plus bond premium	1,684,641	1,745,901
Less net debt issuance costs	<u>(310,099)</u>	<u>(321,376)</u>
	<u><u>\$ 35,378,251</u></u>	<u><u>\$ 36,456,805</u></u>

SOUTHWESTERN UNIVERSITY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 9—Bonds and notes payable (continued)

On August 1, 2006, the University entered into a bond agreement whereby Wells Fargo loaned \$5,000,000 to the University through the City of Riesel Education Facilities Corporation, a nonprofit education facilities corporation, for the purpose of financing a portion of the construction cost of a new residential apartment complex for students consisting of 32 two-bedroom suites in three residential buildings, as well as an apartment for a residential assistant and related recreational facilities, community facilities, and parking, and to pay costs of issuance of \$53,150. The loan is secured by the net assets without donor restriction of the University. The cost of issuance was capitalized and will be amortized over the life of the loan agreement. Principal repayment is due annually beginning February 15, 2008, payable over a 20-year period based on a 25-year amortization schedule, with a balloon payment of \$1,815,000 due on February 15, 2026. The loan had a fixed rate of 4.76% until January 1, 2018, when the fixed rate increased to 5.79% as a result of the Tax Cuts and Jobs Act passed in December 2017. Interest is paid in arrears on February 15 and August 15 each year. In fiscal years 2021, 2022, 2023, 2024, 2025, and thereafter, principal payments of \$210,000, \$220,000, \$235,000, \$245,000, \$255,000, and \$1,815,000, respectively, will become due.

On June 17, 2014, the University entered into a loan agreement whereby Texas Methodist Foundation (“TMF”) loaned \$10,000,000 to the University for the purpose of replenishing the funds provided by the endowment fiscal year 2013 withdrawals from undesignated funds functioning as endowment for expenses associated with re-initiating the football program and beginning the woman’s lacrosse program. The loan is unsecured. Principal repayment is due monthly beginning July 7, 2016, payable over a 20-year period based on a 22-year amortization schedule. Final payment is due on June 7, 2036. The loan has a variable interest rate equal to the rate of interest as stated by TMF as its Methodist Loan Fund rate (“MLF rate”) plus one-half percent, to be adjusted monthly with the MLF rate in effect as of the first business day of the calendar month (.8% at June 30, 2020). In fiscal years 2021, 2022, 2023, 2024, 2025, and thereafter, principal payments of \$457,703, \$463,875, \$469,925, \$475,853, \$482,259, and \$4,969,094, respectively, will become due.

On December 1, 2017, the University issued bonds whereby U.S. Bank National Association loaned \$24,510,000 to the University through the Clifton Higher Education Finance Corporation, a public nonprofit education facilities corporation, for the purpose of financing Phase II construction of the Fondren-Jones Science Hall, the related conversion of the existing Soule Drive into a pedestrian promenade to achieve better integration into the existing main Academic Mall. The bonds are unsecured. The cost of issuance of \$338,290 was capitalized and will be amortized over the life of the loan agreement. The bond was issued at a premium of \$1,837,790 which will also be amortized over the life of the bonds. Principal repayment is due annually beginning August 15, 2018, payable over a 30-year period based on a 30-year amortization schedule. Final payment is due August 15, 2047. The loan has a fixed rate of interest, ranging from 3.00% to 5.00%. In fiscal years 2021, 2022, 2023, 2024, 2025, and thereafter, principal payments of \$430,000, \$450,000, \$475,000, \$495,000, \$520,000, and \$21,335,000, respectively, will become due.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 10—Capital lease obligation

The University leases certain wireless internet, residential video, and athletic camera equipment under capital leases. The leased equipment is amortized on a straight-line basis over five years, except for the athletic camera equipment that is amortized on a straight-line basis over four years to match the lease terms. Amortization of the leased equipment is included in depreciation expense. Total cost of the leased equipment is \$3,432,672 at June 30, 2020 and 2019. Total accumulated amortization related to the leased equipment is \$2,616,276 and \$1,927,660 at June 30, 2020 and 2019, respectively. The following is a schedule showing the future minimum lease payments under capital leases by years and the present value of the minimum lease payments as of June 30, 2020. The leases have interest rates of 3% and 4% and maturity dates of August 31, 2021 and November 30, 2022.

Years Ending June 30,

2021	\$ 747,629
2022	132,617
2023	<u>4,510</u>
Total minimum lease payments	884,756
Less amount representing interest	<u>(18,487)</u>
Present value of minimum lease payments	<u><u>\$ 866,269</u></u>

At June 30, 2020, the present value of minimum lease payments due within one year is \$730,232.

Note 11—Operating leases

Total rental expense from operating leases totaled \$3,760 and \$3,925 in fiscal years 2020 and 2019, respectively. As of June 30, 2020, the University has operating lease commitments for fiscal years 2021, 2022, 2023, 2024, and 2025, of \$4,313, \$4,313, \$4,313, \$4,313, and \$4,313, respectively.

Note 12—Benefit plans

The University has defined contribution retirement plans for eligible faculty members and non-faculty employees. Contributions equal to various percentages of each eligible participant's regular salary are contributed to the plan and allocated among the plan fiduciary selected list of investment options based on the fund allocation directed by the participant. Teachers Insurance and Annuity Association and/or College Retirement Equities Fund maintains custody of all plan assets. Such contributions totaling \$1,597,179 and \$1,603,106 for fiscal years 2020 and 2019, respectively, were expensed.

The University has a contributory health and welfare plan (the "Health Plan") that became self-funded beginning January 1, 1999. The University and employee contributions are used to provide various medical benefits to eligible active employees and their dependents. The Health Plan has excess loss insurance that, in general, limits the amount of total claims paid by the University during the current plan year to approximately \$4,659,904 and claims paid per employee by the University during the 2019 and 2020 plan year to \$150,000 and \$175,000 respectively. The University recognized expenses related to the Health Plan of \$4,524,674 and \$4,099,275 in fiscal years 2020 and 2019, respectively.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 12—Benefit plans (continued)

The University also provides post-retirement health care benefits for eligible retirees and their spouses. The plan is structured as a defined contribution plan. Eligible retirees (age 65 and over) have access to Medicare supplemental plans and receive a subsidy from the University which may be used to pay for supplemental health insurance premiums or eligible medical expenses. The University will subsidize 100% of the cost of the “benchmark” plan premiums through 2018. Beginning on January 1, 2019, the subsidy was capped at the 2018 rate. The “benchmark” plan is defined as Medicare Supplemental (Medigap) Plan L and the average premiums of the Medicare Part D prescription drug programs available in Travis and Williamson counties.

The University will make contributions annually to the retirees’ health reimbursement arrangement account.

All active employees who were hired on or before July 1, 1996, who meet the eligibility criteria to officially retire from the University, will be eligible for the above schedule of benefits at the time of their retirement. An employee who retires before age 65 and is an Early Retiree or a Faculty Phased Retiree continues coverage (and their spouse, if applicable) under the University’s group medical plan or equivalent coverage and the University will subsidize 100% of the premium cost for the retiree and spouse (if age 65). If the spouse is not yet age 65, the retiree continues to pay premiums for the spouse until the spouse attains age 65. If a retiree is not an Early Retiree or a Faculty Phased Retiree, then the retiree pays 100% of the premiums for the University’s group medical plan (and their spouse’s premium, if applicable). All employees hired after July 1, 1996, are not eligible for retiree medical benefits.

Upon attaining age 65, all eligible retirees are required to enroll into the Extend Health program and discontinue participation in the University’s group medical plan. If the retiree’s spouse is not yet age 65, then the retiree pays 100% of the spouse’s premium for the University’s group medical plan. When the spouse attains age 65, the spouse enrolls in Extend Health program as the retiree’s spouse and discontinues participation in the University’s group medical plan.

Pursuant to the provisions of ASC 715-60, *Defined Benefits Plans – Other Post-Retirement*, and 715-20, *Defined Benefit Plans – General*, net periodic pension costs, other than service costs, and other post-retirement related changes are reflected in the consolidated statements of activities as a net change in net assets without donor restrictions apart from operating expenses. The University amortizes a portion of these costs each year and reports these amounts into other components of net periodic pension cost. Amounts amortized and the changes in balances of unamortized costs are as follows:

	Beginning Balance of Unamortized Amounts	Amount Amortized into Net Periodic Benefit Costs	Current Year Gains/Losses	Ending Balance of Unamortized Amounts
Net (gains) losses	\$ 9,899,133	\$ (1,292,307)	\$ 1,764,389	\$ 10,371,215
Prior service costs	(4,473,432)	4,473,432	-	-

In fiscal year 2021, the University expects to recognize as net periodic benefit approximately \$1,399,000 and \$-0- of previously unamortized net gain and net prior service costs, respectively.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 12—Benefit plans (continued)

The status of the University's accrued post-retirement benefit cost at June 30, 2020 and 2019 are as follows:

	<u>2020</u>	<u>2019</u>
Reconciliation of benefit obligation:		
Obligation at beginning of year	\$ 6,773,790	\$ 7,456,747
Service cost including expenses	6,780	9,219
Interest cost	193,364	248,824
Actuarial loss (gain)	1,764,389	(434,564)
Benefit payments and actual expenses	<u>(455,319)</u>	<u>(506,436)</u>
Obligation, end of year	8,283,004	6,773,790
Reconciliation of fair value of plan assets:		
Employer contributions	455,319	506,436
Benefit payments and estimated expenses	<u>(455,319)</u>	<u>(506,436)</u>
Fair value of plan assets, end of year	<u>-</u>	<u>-</u>
Funded status, end of year	<u>\$ 8,283,004</u>	<u>\$ 6,773,790</u>

Amounts recognized in the consolidated statements of financial position are as follows:

	<u>2020</u>	<u>2019</u>
Current liabilities	\$ (491,868)	\$ (522,250)
Noncurrent liabilities	<u>(7,791,136)</u>	<u>(6,251,540)</u>
	<u>\$ (8,283,004)</u>	<u>\$ (6,773,790)</u>

Net periodic post-retirement benefit cost recognized during fiscal year 2020 and 2019 are as follows:

	<u>2020</u>	<u>2019</u>
Service cost	\$ 6,780	\$ 9,219
Interest cost	193,364	248,824
Amortization of prior actuarial loss	1,292,307	1,401,804
Amortization of prior service gain from plan amendment	<u>(4,473,432)</u>	<u>(5,849,751)</u>
	<u>\$ (2,980,981)</u>	<u>\$ (4,189,904)</u>

The University used a weighted average discount rate of 2.23% and 3.18% to determine the post-retirement benefit obligation at June 30, 2020 and 2019, respectively. An average discount rate of 3.18% and 3.93% was used to determine the net periodic benefit cost for fiscal years 2020 and 2019, respectively. The decrease in the discount rate from 3.18% to 2.23% increased the accrued post-retirement liability by approximately \$1,509,000.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 12—Benefit plans (continued)

In determining the net periodic benefit cost, the assumed pre-Medicare health care cost trend rate was 6.5% for fiscal year 2020, declining gradually to 4.5%. There is no trend on the post Medicare benefits as the HRA values are now capped. These health care cost trend rate assumptions have a significant effect on the amount of the obligation and periodic cost reported. For example, an increase in the assumed health care cost trend rate by one percentage point in each year would increase the amount of the obligation at June 30, 2020 by \$986,000 and the aggregate of service cost and interest cost components of net periodic post-retirement benefit cost for the year then ended by \$26,000. Alternatively, a decrease in the assumed health care cost trend rate by one percentage point in each year would decrease the obligation at June 30, 2020 by \$833,000 and the aggregate of service cost and interest cost components of net periodic post-retirement benefit cost for the year then ended by \$22,000.

Other changes in plan assets and benefit obligations recognized in net assets without donor restriction:

	<u>2020</u>	<u>2019</u>
Net gain	\$ 1,764,389	\$ (434,564)
Amortization of net gain	(1,292,307)	(1,401,804)
Amortization of prior service cost	<u>4,473,432</u>	<u>5,849,751</u>
Total recognized net assets without donor restriction	<u>4,945,514</u>	<u>4,013,383</u>
Total recognized in net periodic benefit cost and net assets without donor restriction	<u>\$ 1,964,533</u>	<u>\$ (176,521)</u>

The following post-retirement benefit payments, which reflect expected future service, as appropriate, are expected to be paid, net of the estimated Medicare prescription drug subsidies expected to be received:

Years Ending June 30,

2021	\$ 492,000
2022	481,000
2023	469,000
2024	480,000
2025	490,000
2026-2030	<u>2,389,000</u>
	<u>\$ 4,801,000</u>

Note 13—Line of credit

The University had an unsecured line of credit on June 30, 2020 and 2019 for \$1,500,000 with First Texas Bank, Georgetown, at the bank's prime rate. The line of credit expires annually on June 30th. The University has obtained approval to renew this line of credit through June 30, 2021. The University did not draw on this line of credit in either fiscal year 2020 or 2019.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 14—Nature and amount of net assets with donor restrictions

Net assets with donor restrictions are available for the following purposes at June 30:

	<u>2020</u>	<u>2019</u>
Subject to expenditure for specified purpose:		
Scholarships	\$ 36,808,636	\$ 39,348,132
Professorships and faculty development	38,556,861	40,506,038
Plant	3,408,012	3,861,391
Academic support	5,842,456	6,409,925
Annuities and living trusts	112,276	137,455
Other	10,271,072	10,203,325
Restricted for use in future periods	<u>60,600,491</u>	<u>64,646,040</u>
	<u>155,599,804</u>	<u>165,112,306</u>
Restricted in perpetuity:		
General operations	28,850,319	28,512,952
Scholarships	41,066,303	38,665,309
Professorships and faculty development	23,888,916	23,789,274
Plant	1,547,045	1,547,046
Academic support	14,384,858	12,861,006
Annuities and living trusts	4,918,864	5,072,314
Other	<u>5,540,168</u>	<u>6,607,662</u>
	<u>120,196,473</u>	<u>117,055,563</u>
Total with donor restriction	<u>\$ 275,796,277</u>	<u>\$ 282,167,869</u>

Note 15—Functional expenses

Expenses by function and nature consist of the following for the year ended June 30, 2020:

	<u>Salary and Wages</u>	<u>Benefits</u>	<u>Other Operating Expense</u>	<u>Depreciation</u>	<u>Interest</u>	<u>COVID-19 Campus Readiness Expenses and Student Aid</u>	<u>Grand Total</u>
Instructional services	\$ 12,368,209	\$ 3,826,084	\$ 5,230,522	\$ 1,874,857	\$ 120,583	\$ 3,620	\$ 23,423,875
Student services	5,828,598	1,866,190	3,395,550	629,048	40,458	5,964	11,765,808
Auxiliary services	186,357	64,608	6,304,421	1,607,357	103,378	-	8,266,121
Institutional support	8,855,656	2,749,506	1,261,824	614,870	39,546	52,632	13,574,034
Scholarships (HEERF)	-	-	-	-	-	606,725	606,725
Grand total	<u>\$ 27,238,820</u>	<u>\$ 8,506,388</u>	<u>\$ 16,192,317</u>	<u>\$ 4,726,132</u>	<u>\$ 303,965</u>	<u>\$ 668,941</u>	<u>\$ 57,636,563</u>

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 15—Functional expenses (continued)

During the year ended June 30, 2020, the University was awarded \$1,213,450 in grant funding from the Higher Education Emergency Relief Fund (“HEERF”) through the Coronavirus Aid, Relief, and Economic Security (the “CARES Act”), of which \$906,725 was recognized and included in government grants with donor restrictions on the consolidated statements of activities. The University disbursed the entire amount of HEERF Part A funding directly to enrolled students for expenses related to the disruption of campus operations due to the COVID-19 pandemic during the same fiscal year. As a result, the \$606,725 is shown as a separate operating expense called “scholarships” on the accompanying consolidated statements of activities for the year ended June 30, 2020. The University also received \$300,000 of HEERF Part B funding, which was applied against a portion of the amount refunded to students for room and board as a result of the campus closing due to the COVID-19 pandemic. The total refunds to students for auxiliary services was approximately \$2,300,000 and is presented as a reduction in auxiliary enterprises operating revenue on the accompanying consolidated statements of activities for the year ended June 30, 2020. A separate column was added to the functional expense table above specifically for COVID-19 related expenses, which include the Part A HEERF funds used for scholarships and other campus readiness expenses.

Expenses by function and nature consist of the following for the year ended June 30, 2019:

	<u>Salary and Wages</u>	<u>Benefits</u>	<u>Other Operating Expense</u>	<u>Depreciation</u>	<u>Interest</u>	<u>Grand Total</u>
Instructional services	\$ 12,050,882	\$ 3,590,053	\$ 6,269,157	\$ 1,699,025	\$ 139,992	\$ 23,749,109
Student services	5,584,355	1,672,290	3,582,947	593,847	48,930	11,482,369
Auxiliary services	226,323	87,584	6,642,867	1,515,999	124,911	8,597,684
Institutional support	8,554,646	3,123,110	1,182,068	580,241	47,809	13,487,874
Grand total	<u>\$ 26,416,206</u>	<u>\$ 8,473,037</u>	<u>\$ 17,677,039</u>	<u>\$ 4,389,112</u>	<u>\$ 361,642</u>	<u>\$ 57,317,036</u>

Allocation of Certain Expenses – The consolidated statements of activities present expenses by functional classification. The University’s primary program services are instruction and student services. Expenses reported as institutional support and auxiliary services are incurred in support of these primary program services. Uncapitalized plant expenses are allocated to the specific operating expense lines that the expenses relate to. Depreciation, interest expense, the cost of operation and maintenance of plant facilities, and general plant expenses are allocated to functional categories based on building square footage dedicated to that specific function.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 16—Liquidity and availability of resources

The following table reflects the University's financial assets as of June 30, with reductions for amounts not available for general use because of contractual or donor-imposed restrictions within one year of the consolidated statements of activities.

	<u>2020</u>	<u>2019</u>
Financial assets:		
Cash and cash equivalents	\$ 29,213,874	\$ 37,223,150
Student receivables, net	34,079	57,136
Unconditional promise receivable, net	4,583,801	3,667,579
Investment income	1,516	41,616
Other receivables	592,495	478,322
Investments	<u>289,110,284</u>	<u>296,183,512</u>
Total financial assets at year-end	323,536,049	337,651,315
Less assets unavailable for general expenditures within one year:		
Receivable due in more than one year	(190,155)	(194,485)
Bond funds reserved for construction	(2,681,190)	(8,610,869)
Restricted investment	(7,325,149)	(7,747,456)
Perpetual and term endowments and accumulated earnings subject to appropriations beyond one year	(270,802,291)	(280,312,678)
Unmarketable investment	(3,600,020)	(3,600,020)
Restricted by donors with purpose restrictions	<u>(4,446,223)</u>	<u>(4,249,547)</u>
Financial assets available to meet cash needs for general expenditures within one year	<u>34,491,021</u>	<u>32,936,260</u>
Available board designated endowments	25,943,031	26,993,877
Available line of credit	<u>1,500,000</u>	<u>1,500,000</u>
Financial assets available to meet cash needs for general expenditures within one year with board approval	<u>\$ 61,934,052</u>	<u>\$ 61,430,137</u>

As part of the University's liquidity management plan, it structures its financial assets to be available as its obligations come due. Cash in excess of daily requirements is invested in the University's short-term pooled investment fund. For purposes of analyzing resources available to meet general expenditures over a 12-month period, the University considers all expenditures related to its ongoing activities of instruction, student services, and auxiliary services as well as the conduct of services undertaken to support those activities to be general expenditures. Student loans receivables are not considered available for general expenditures as principal and interest on these loans are used solely to make new loans and are therefore not available to meet current operating needs.

Endowment funds consist of donor-restricted endowments and board-designated endowments. Income from donor-restricted endowments is restricted for specific purposes and is not available for general expenditures, except for the amount that is available for annual appropriations in accordance with the board approved spending rate and with current year expenditures that meet the donor restrictions. Board-designated endowments totaling approximately \$26 million for June 30, 2020 and approximately \$27 million for June 30, 2019 are also subject to the board approved spending policy. The University does not intend to spend from the board-designated endowments other than the amounts appropriated for general expenditure in accordance with the spending policy; however, the amount of the board-designated endowments could be made available for cash liquidity needs with board approval.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 16—Liquidity and availability of resources (continued)

In addition to financial assets availability to meet general expenditure over the next 12 months, the University operates with a balanced budget and anticipates collecting sufficient revenue to cover general expenditures not covered by donor-restricted resources. Furthermore, the funds restricted by donors with purpose restrictions noted above are nonendowment funds and are also available for use in accordance with the donor restrictions for general expenditures in the following year. Lastly, the University has an unsecured \$1,500,000 line of credit available to meet cash flow needs in event of a liquidity need, as further described in Note 13.

Note 17—Deposits and deferred revenue

The activity and balances for deposits and deferred revenue from contracts with customers are shown in the following table:

	<u>Advance Tuition Payments</u>	<u>Student Deposit</u>	<u>Other</u>	<u>Total</u>
Beginning balance, June 30, 2018	\$ 2,188,799	\$ 509,523	\$ 49,700	\$ 2,748,022
Revenue recognized, deposits applied/forfeited	(2,188,799)	(255,095)	(213,089)	(2,656,983)
Payments received for future performance obligations	2,714,779	269,659	193,200	2,645,097
Balance, June 30, 2019	2,714,779	524,087	29,811	3,268,677
Revenue recognized, deposits applied/forfeited	(2,714,779)	(208,072)	(147,280)	(3,070,131)
Payments received for future performance obligations	3,650,694	308,600	202,341	4,161,635
Balance, June 30, 2020	<u>\$ 3,650,694</u>	<u>\$ 624,615</u>	<u>\$ 84,872</u>	<u>\$ 4,360,181</u>

Note 18—Disclosures about fair value of financial instruments

The estimated fair value amounts have been determined by the University using available market information and appropriate valuation methodologies. Considerable judgment is required in developing these estimates; however, no assurance can be given that the estimated values presented herein are indicative of the amounts that would be realized in a current market exchange. The use of different market assumptions and/or estimation methodologies could have a material effect on the estimated fair value amounts.

As of June 30, 2020 and 2019, the carrying amounts of the University's assets and liabilities which are considered to be financial instruments approximate their fair value except for student loans receivable (see Note 3) and the 2006 and 2017 notes payable (see Note 9). Based on the nature of the federal loan program and the privately contributed loan funds representing student loans receivable, such financial instruments may not be sold. Accordingly, determining fair value is not practical. The University's 2006 note payable totaled \$2,980,000 and \$3,180,000 and has an estimated fair value of \$2,980,000 and \$3,180,000 at June 30, 2020 and 2019, respectively. The 2006 note amount is valued using current market yields. The University's 2017 bonds payable totaled \$23,705,000 and \$24,115,000 and has an estimated fair value of \$26,327,249 and \$27,385,605 at June 30, 2020 and 2019, respectively.

SOUTHWESTERN UNIVERSITY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2020 AND 2019

Note 19—Commitments and contingencies

The University has contracts for the construction of University facilities, including residence halls, central plant, and athletic fields. At June 30, 2020, the remaining commitments under these contracts approximated \$711,011.

Note 20—Transactions with related parties

One member of the Board of Trustees of the University also serves as Vice Chairman of the Board of Trustees of a financial institution where the University has a significant banking relationship. Five voting members of the Board of Trustees also served as directors of a private foundation during the fiscal year where the University has an outstanding investment and loan. The University has a conflict of interest policy that is regularly updated by all members of the Board of Trustees. The relationship with the financial institution and the private foundation has been consistently reported as a conflict of interest. In all matters related to business decisions at the meetings of the Board of Trustees, the parties refrain from participating in any votes on these matters. The abstention is reflected in the official minutes of the meeting.

Note 21—Subsequent events

The University has evaluated subsequent events through October 5, 2020, the date when consolidated financial statements were available to be issued, and has determined there are no material subsequent events or transactions that would require additional disclosure in the University's consolidated financial statements.