



REPORT OF INDEPENDENT AUDITORS AND
FINANCIAL STATEMENTS

UNIVERSITY OF SAN DIEGO

June 30, 2018 and 2017

Table of Contents

	PAGE
Report of Independent Auditors	1–2
Financial Statements	
Statements of financial position	3
Statement of activities – 2018	4
Statement of activities – 2017	5
Statements of cash flows	6
Notes to financial statements	7–31

Report of Independent Auditors

The Board of Trustees
University of San Diego

Report on the Financial Statements

We have audited the accompanying financial statements of University of San Diego, which comprise the statements of financial position as of June 30, 2018 and 2017, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of University of San Diego as of June 30, 2018 and 2017, and the changes in its net assets and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Moss Adams LLP

San Diego, California
October 17, 2018

University of San Diego
Statements of Financial Position
(In Thousands)

	June 30,	
	2018	2017
ASSETS		
Cash and cash equivalents	\$ 11,172	\$ 9,179
Short-term investments	138,163	112,764
Accounts and loans receivable, net	47,579	46,074
Other assets	6,439	5,819
Contributions receivable, net	32,686	26,190
Property, plant, and equipment, net	505,752	501,231
Long-term investments	638,040	585,334
	<u>638,040</u>	<u>585,334</u>
Total assets	<u>\$ 1,379,831</u>	<u>\$ 1,286,591</u>
LIABILITIES		
Accounts payable and accrued expenses	\$ 49,666	\$ 50,214
Deferred tuition revenue	19,493	18,238
Other liabilities	25,097	32,107
Bonds payable	154,160	157,481
Refundable advances	11,886	12,213
	<u>11,886</u>	<u>12,213</u>
Total liabilities	<u>260,302</u>	<u>270,253</u>
NET ASSETS		
Unrestricted	750,709	686,196
Temporarily restricted	180,621	145,905
Permanently restricted	188,199	184,237
	<u>188,199</u>	<u>184,237</u>
Total net assets	<u>1,119,529</u>	<u>1,016,338</u>
Total liabilities and net assets	<u>\$ 1,379,831</u>	<u>\$ 1,286,591</u>

University of San Diego
Statement of Activities
(In Thousands)

	Year Ended June 30, 2018			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
OPERATING				
Revenues and other additions:				
Tuition and fees	\$ 374,701	\$ -	\$ -	\$ 374,701
Less: tuition discounts and financial aid	(121,488)	-	-	(121,488)
Net tuition and fees	253,213	-	-	253,213
Sales and services of auxiliary enterprises	49,551	-	-	49,551
Grants and contracts	16,321	-	-	16,321
Contributions	4,381	11,684	2,372	18,437
Investment return distributed	7,271	9,761	-	17,032
Investment income	3,230	-	-	3,230
Other revenue	7,103	-	295	7,398
Total revenues	341,070	21,445	2,667	365,182
Net assets released from restrictions for operations	18,234	(18,234)	-	-
Total revenues and other additions	359,304	3,211	2,667	365,182
Expenses:				
Educational programs	182,773	-	-	182,773
Research	3,873	-	-	3,873
Athletics and recreation	17,696	-	-	17,696
Public service	6,473	-	-	6,473
Auxiliary enterprise expenses	43,082	-	-	43,082
Management and general expenses	73,418	-	-	73,418
Total expenses	327,315	-	-	327,315
Increase in net assets from operations	31,989	3,211	2,667	37,867
NON-OPERATING				
Investment income	26,096	21,380	20	47,496
Less: investment return distributed	(7,271)	(9,761)	-	(17,032)
Total non-operating investment return	18,825	11,619	20	30,464
Contributions for non-operating activities	-	29,005	-	29,005
Unrealized gain on interest rate swap	5,855	-	-	5,855
Net assets released from restriction - non-operating	9,215	(9,215)	-	-
Other non-operating changes	(1,371)	96	1,275	-
Increase in net assets from non-operating activities	32,524	31,505	1,295	65,324
INCREASE IN NET ASSETS	64,513	34,716	3,962	103,191
NET ASSETS				
Beginning of year	686,196	145,905	184,237	1,016,338
End of year	\$ 750,709	\$ 180,621	\$ 188,199	\$ 1,119,529

University of San Diego
Statement of Activities
(In Thousands)

	Year Ended June 30, 2017			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
OPERATING				
Revenues and other additions:				
Tuition and fees	\$ 351,214	\$ -	\$ -	\$ 351,214
Less: tuition discounts and financial aid	(109,800)	-	-	(109,800)
Net tuition and fees	241,414	-	-	241,414
Sales and services of auxiliary enterprises	48,608	-	-	48,608
Grants and contracts	16,574	-	-	16,574
Contributions	5,456	10,573	3,710	19,739
Investment return distributed	7,134	9,652	-	16,786
Investment income	562	-	-	562
Other revenue	6,045	-	303	6,348
Total revenues	325,793	20,225	4,013	350,031
Net assets released from restrictions for operations	22,644	(22,644)	-	-
Total revenues and other additions	348,437	(2,419)	4,013	350,031
Expenses:				
Educational programs	180,276	-	-	180,276
Research	3,685	-	-	3,685
Athletics and recreation	16,678	-	-	16,678
Public service	8,126	-	-	8,126
Auxiliary enterprise expenses	43,010	-	-	43,010
Management and general expenses	69,386	-	-	69,386
Total expenses	321,161	-	-	321,161
Increase in net assets from operations	27,276	(2,419)	4,013	28,870
NON-OPERATING				
Investment income	38,208	31,119	1	69,328
Less: investment return distributed	(7,134)	(9,652)	-	(16,786)
Total non-operating investment return	31,074	21,467	1	52,542
Contributions for non-operating activities	-	(144)	-	(144)
Unrealized gain on interest rate swap	11,346	-	-	11,346
Net assets released from restriction - non-operating	1,627	(1,627)	-	-
Other non-operating changes	1,076	(1,301)	225	-
(Decrease) increase in net assets from non-operating activities	45,123	18,395	226	63,744
(DECREASE) INCREASE IN NET ASSETS	72,399	15,976	4,239	92,614
NET ASSETS				
Beginning of year	613,797	129,929	179,998	923,724
End of year	\$ 686,196	\$ 145,905	\$ 184,237	\$ 1,016,338

University of San Diego
Statements of Cash Flows
(In Thousands)

	Years Ended June 30,	
	2018	2017
OPERATING ACTIVITIES		
Changes in net assets	\$ 103,191	\$ 92,614
Adjustments to reconcile changes in net assets to net cash provided by operating activities:		
Depreciation and net amortization	16,842	15,998
Net amortization of bond premiums/discount and debt issuance cost	(139)	(139)
Net provision for losses on receivables	345	(15)
Net realized and unrealized gain on long-term investments	(43,481)	(63,233)
Net unrealized gain on interest rate swap	(5,855)	(11,346)
Contributions restricted for long-term investments	(3,926)	(4,111)
Contributions restricted for investment in property, plant, and equipment	(29,005)	144
Proceeds from sale of donated securities	2,441	378
Changes in operating assets and liabilities:		
Accounts and loans receivable	(3,174)	(1,102)
Other assets	(620)	1,244
Contributions receivable	(6,496)	1,696
Accounts payable and accrued expenses	(548)	2,725
Deferred tuition revenue	1,255	3,170
Other liabilities	(1,155)	(800)
Net cash provided by operating activities	<u>29,675</u>	<u>37,223</u>
INVESTING ACTIVITIES		
Proceeds from maturities/sales of investments	313,588	305,454
Purchases of investments	(353,276)	(325,609)
Purchase of property, plant, and equipment	(21,363)	(19,258)
Net cash used in investing activities	<u>(61,051)</u>	<u>(39,413)</u>
FINANCING ACTIVITIES		
Principal payments on bonds payable	(3,182)	(3,129)
Advances for government loan funds	(327)	(196)
Net disbursements of student loans	1,324	673
Contributions restricted for long-term investments	3,926	4,111
Contributions restricted for investment in property, plant, and equipment	29,005	(144)
Proceeds from sale of securities restricted for long-term investment or assets	2,623	727
Net cash provided by financing activities	<u>33,369</u>	<u>2,042</u>
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	1,993	(148)
CASH AND CASH EQUIVALENTS		
Beginning of year	<u>9,179</u>	<u>9,327</u>
End of year	<u>\$ 11,172</u>	<u>\$ 9,179</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid for interest	<u>\$ 7,437</u>	<u>\$ 7,449</u>

Note 1 – Nature of Operation and Significant Accounting Policies

The University of San Diego (the “University”) is an independent Catholic university chartered in 1949 under the nonprofit public benefit corporation law and is governed by its Board of Trustees (the “Board”). In 1972, the San Diego College for Women merged with the University of San Diego College for Men, forming the University. The University includes a College of Arts and Sciences and six professional schools: the School of Business Administration; the Shiley-Marcos School of Engineering; the School of Leadership and Education Sciences; the School of Law; the Philip Y. Hahn School of Nursing and Health Science; and the Joan B. Kroc School of Peace Studies.

Financial statement presentation – The University classifies its net assets as unrestricted, temporarily restricted, and permanently restricted based upon the following criteria:

- Unrestricted net assets represent expendable funds available for operations that are not otherwise limited by donor restrictions.
- Temporarily restricted net assets consist of contributed funds subject to specific donor-imposed restrictions, which are contingent upon a specific performance of a future event or a specific passage of time before the University may spend the funds.
- Permanently restricted net assets are subject to irrevocable donor restrictions requiring that the assets be maintained in perpetuity, primarily for generating investment income to fund current operations.

Revenue recognition

Tuition and fees – Student tuition and fees are recorded as revenue in the year during which the related academic services are rendered. Student tuition and fees received in advance of services to be rendered are recorded as deferred tuition revenue.

Contributions – Contributions of cash, unconditional pledges, and other assets are recorded as revenue in the period received and are classified as permanently restricted, temporarily restricted, or unrestricted based on donor stipulations. Contributions whose restrictions are met in the same period they are received are recorded as revenue in temporarily restricted net assets and as net assets released from restrictions. Unconditional pledges with terms greater than one year are initially recorded at fair value based on their estimated future cash flows. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met. Gifts of assets other than cash are recorded at their estimated fair value.

Grants and contracts – Revenues from grants and contracts are reported as increases in unrestricted net assets as allowable expenditures under such agreements are incurred.

Sales and services of auxiliary enterprises – Revenues from supporting services, such as student housing, dining facilities, and the bookstore, are recorded at the time of delivery of a product or service. Amounts received in advance of services to be rendered are recorded as deferred revenue.

University of San Diego

Notes to Financial Statements

Note 1 – Nature of Operation and Significant Accounting Policies (continued)

Operating activities – Operating revenue and expenses consist of those items attributable to the University's academic programs, research conducted by the academic departments, and auxiliary operations. The amount computed under the endowment spending policy of the investment pool and all investment income earned by investing cash in excess of daily requirements are used to support current operations. Contribution revenues with restrictions for long-lived assets are recorded under non-operating activities.

Cash and cash equivalents – The University considers liquid investments, which fund the daily operating activities of the University and have a maturity of three months or less at the date of purchase, to be cash equivalents. The University is required to keep separate bank accounts for certain funding received, including the Perkins Student Loan Fund Program. Balances in these accounts totaled approximately \$3,108,000 and \$2,141,000 as of June 30, 2018 and 2017, respectively.

Concentration of credit risk – Financial instruments that potentially subject the University to concentrations of credit risk consist principally of cash deposits at financial institutions and investments in marketable securities. At times, balances in the University's cash and investment accounts exceed Federal Deposit Insurance Corporation (FDIC) or Securities Investors Protection Corporation (SIPC) limits.

Student loans and accounts receivables and other receivables are due from a variety of sources concentrated primarily in the western United States. In addition, the University's students receive a substantial amount of support from state and federal student financial assistance programs which are subject to audit by governmental agencies. A significant reduction in the level of this support, if this were to occur, could have an adverse effect on the University's programs and activities.

Accounts and loans receivable – Receivables are recorded net of an allowance for doubtful accounts. The allowance is based on historical experience and management's evaluation of receivables at the end of each year.

Interest rate swap – In conjunction with the University's November 2005 issuance of variable-rate demand revenue bonds, refunded in July 2015 with the issuance of the 2015 variable rate revenue bonds, the University entered into an interest-rate swap agreement with a financial institution counterparty. The purpose of this agreement is to swap the variable rate on underlying debt for a fixed rate of 3.513 percent for a period of 40 years. The University entered into the agreement to manage the risk associated with the cash flows attributable to interest payments on the debt and does not use this instrument for speculative purposes. The instrument's fair value and changes therein are reported in the University's unrestricted net assets. The value of the swap instrument represents the estimated receivable of or payable by the University to cancel the agreement at the reporting date, which is based on option pricing models that consider risks and market factors.

Note 1 – Nature of Operation and Significant Accounting Policies (continued)

The unrealized gain for the change in the swap agreement's fair value was approximately \$5,855,000 and \$11,346,000 for the years ended June 30, 2018 and 2017, respectively. The value of the swap instrument is a payable of approximately \$21,276,000 and \$27,131,000 recorded in other liabilities at June 30, 2018 and 2017, respectively.

Refundable advances – The University serves as an agent for the federal government in administering the Perkins Student Loan Fund Program and the Nursing Faculty Loan Program. Amounts received in conjunction with these programs are recorded as refundable advances in the statements of financial position. Disbursements made to students in accordance with the federal program requirements are recorded as student loans receivable. Included in accounts and loans receivable at June 30, 2018 and 2017 are student loans receivable of approximately \$13,499,000 and \$14,694,000, respectively, related to these programs.

Functional expense classifications – Expenses, including certain allocated expenses, are reported in major categories: educational programs, research, athletics and recreation, public service, auxiliary enterprise expenses, and management and general expenses. Auxiliary enterprises include, among others, student residence and board, food services, and the bookstore.

Management and general expenses consist of general institutional support including expenses for fundraising. The University incurred fundraising expenses in the amount of approximately \$8,465,000 during the year ended June 30, 2018, including approximately \$6,015,000 in personnel expenses and approximately \$2,450,000 in other expenses. The University incurred fundraising expenses in the amount of approximately \$8,401,000 during the year ended June 30, 2017, including approximately \$6,074,000 in personnel expenses and approximately \$2,327,000 in other expenses. These expenses were incurred to support campaigns promoting charitable contributions including gifts directed toward the University's endowment and capital projects.

Earnings on permanently restricted endowments – Assets of the University's individual endowment funds (the "Funds") are generally maintained in pooled investment portfolios. Interest, dividends, and gains and losses in the investment pool are allocated on a monthly-average basis to the Funds in proportion to each Fund's relative share in the investment pool, and are recorded in the Fund which is authorized to expend the earnings. The earnings on permanently restricted endowments are primarily recorded as temporarily restricted, in accordance with donor stipulations. In certain unique situations, a Fund's earnings may be recorded as permanently restricted or unrestricted, in accordance with donor stipulations. Accumulated unspent earnings are reinvested and retained in the Funds to protect them against inflation over the long term.

Expiration of donor-imposed restrictions – The expiration of a donor-imposed restriction on net assets is recognized in the period in which the restriction expires and at the time the related resources are reclassified to unrestricted net assets. Net assets are released from donor restrictions by incurring expenses satisfying the restricted purposes, by occurrences of events specified by the donors, or by the change of restrictions specified by the donors. Restrictions on gifts of cash or other assets received for the acquisition of long-lived assets are released when the long-lived assets are placed into service.

University of San Diego

Notes to Financial Statements

Note 1 – Nature of Operation and Significant Accounting Policies (continued)

Fair value of financial instruments – Fair value is defined as 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. The University classifies certain of its assets and liabilities based upon the established fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1 – Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities that the University has the ability to access at the measurement date;

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

Level 3 – Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

Investments measured using the net asset value per share (or its equivalent) practical expedient are not classified in the fair value hierarchy. The following describes these investments:

Assets held at Net Asset Value (NAV) – Valuations based on fair value using the NAV per share (or its equivalent) of such investment funds as a practical expedient for fair value. The University has estimated the fair value of these funds by using the NAV provided by the fund's managers.

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 categorization of assets and liabilities within the hierarchy is based upon the pricing transparency and does not necessarily correspond to the University's perceived risk of the assets and liabilities.

The University has various processes and controls in place to ensure that fair value is reasonably estimated. The Finance Office, under supervision of the Vice President for Finance and Chief Financial Officer, sets the valuation policies and is responsible for the determination of fair value. Securities classified within Level 3 investments are based on valuations provided by external investment managers. The Investment Committee, in conjunction with the external investment advisors, monitors and analyzes the valuations of the investments four times during the academic year. The Investment Committee reports to the Board of Trustees. The valuations consider variables such as financial performance of the investment, recent sales prices of investments, and other pertinent information.

Although the University uses its best judgment in determining the fair value of financial instruments, there are inherent limitations in any methodology. Future confirming events could affect the estimates of fair value and could be material to the financial statements. These events could also affect the amount realized upon liquidation of the instruments.

Note 1 – Nature of Operation and Significant Accounting Policies (continued)

Investments, in general, are subject to various risks including credit, interest, and overall market volatility risks. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in values of investment securities will occur in the near term and such changes could materially affect the amounts reported in the financial statements.

Use of estimates – The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Income taxes – The University is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code (IRC) and Section 23701(d) of the California Revenue and Taxation Code.

The University has no unrecognized tax benefits or liabilities as of June 30, 2018 and 2017. The University files an exempt organization return and applicable unrelated business income tax return in the U.S. federal jurisdiction and with the California Franchise Tax Board.

Recently issued accounting standards – In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-02, *Leases (Topic 842)*. This guidance requires the recognition of rights and obligations arising from lease contracts, including existing and new arrangements, as assets and liabilities on the statement of financial position. The guidance is effective for annual reporting periods beginning after December 15, 2018. Management is currently evaluating the impact this will have on the University's future financial statements.

In August 2016, FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statement for Not-for-Profit Entities*. This guidance revises the not-for-profit reporting model. The guidance streamlines and clarifies net asset reporting, provides flexibility regarding the definition of reported operating subtotals, and imposes new reporting requirements related to expenses. The guidance is effective for fiscal years beginning after December 15, 2017. Management is currently evaluating the impact this will have on the University's future financial statements.

In June 2018, FASB issued ASU 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. The ASU was issued to provide clarification to not-for-profit entities as they adopt ASU 2014-09, *Revenue from Contracts with Customers*, specifically as it relates to grants and contracts and distinguishing between reciprocal (exchange) transactions and nonreciprocal (contributions) transactions. The guidance is effective for fiscal years beginning after June 15, 2018. Management is currently evaluating the impact this will have on the University's future financial statements.

University of San Diego

Notes to Financial Statements

Note 2 – Investments

Investments are reported at their fair values. The University follows a spending rule for its endowment funds, which provides for regular increases in spending while preserving the long-term purchasing power of the endowment. Earnings available for spending are shown in operating income, and the balance as non-operating income.

The University pools certain investments from the various net asset categories. Interest, dividends, and gains and losses in the investment pool are all distributed to the appropriate net asset category. Distributions are based upon the carrying value of the various net asset categories' assets when pooled, and adjusted for purchases or gifts specifically identified to a given net asset category.

Investments consist of the following at June 30 (in thousands):

	<u>2018</u>	<u>2017</u>
Cash and cash equivalents	\$ 38,410	\$ 43,718
Fixed income	93,092	58,319
Equities	256	226
Real estate	14,939	13,818
Pooled investments	<u>629,506</u>	<u>582,017</u>
Total	<u>\$ 776,203</u>	<u>\$ 698,098</u>

Pooled investments consist of the following at June 30 (in thousands):

Cash and cash equivalents	\$ 13,962	\$ 18,909
Fixed income	86,915	73,264
Equities	285,405	276,544
Real assets	40,586	34,248
Marketable alternatives	109,922	102,956
Non-marketable alternatives	<u>92,716</u>	<u>76,096</u>
Total	<u>\$ 629,506</u>	<u>\$ 582,017</u>

University of San Diego
Notes to Financial Statements

Note 2 – Investments (continued)

Investment return – The following schedule summarizes investment income and its classification in the statements of activities for the years ended June 30, 2018 and 2017 (in thousands):

	2018			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Interest and dividends	\$ 7,059	\$ 3,039	\$ 20	\$ 10,118
Less: management fees	<u>(1,667)</u>	<u>(1,206)</u>	-	<u>(2,873)</u>
Net interest and dividends	5,392	1,833	20	7,245
Realized gain, net	8,624	7,247	-	15,871
Unrealized gain, net	<u>15,310</u>	<u>12,300</u>	-	<u>27,610</u>
Total	<u>\$ 29,326</u>	<u>\$ 21,380</u>	<u>\$ 20</u>	<u>\$ 50,726</u>
	2017			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Interest and dividends	\$ 5,645	\$ 3,243	\$ 1	\$ 8,889
Less: management fees	<u>(1,168)</u>	<u>(1,064)</u>	-	<u>(2,232)</u>
Net interest and dividends	4,477	2,179	1	6,657
Realized gain, net	7,610	6,670	-	14,280
Unrealized gain, net	<u>26,683</u>	<u>22,270</u>	-	<u>48,953</u>
Total	<u>\$ 38,770</u>	<u>\$ 31,119</u>	<u>\$ 1</u>	<u>\$ 69,890</u>

Note 3 – Fair Value of Financial Instruments

The University uses the following methods and assumptions to estimate the fair value for its assets and liabilities measured and carried at fair value in the financial statements:

Fixed-income securities – Investments in fixed-income securities are comprised of U.S. Treasury notes, mortgage-backed securities, municipal and corporate bonds, as well as global investment-grade debt securities denominated primarily in developed countries around the world. Fair value is based on quoted market prices for those traded with sufficient frequency.

Equities funds – Investments in equities funds include investments in securities traded in active markets for which closing prices are readily available. Investments in equities funds also include investments in index funds, which fair values may be based on the NAV of the fund.

Real estate – Investment in real estate includes various residential and commercial properties in San Diego, California. The University has estimated the real estate's fair value by using market comparables and third-party appraisals.

University of San Diego

Notes to Financial Statements

Note 3 – Fair Value of Financial Instruments (continued)

Real assets funds – Investments in real assets funds include funds, and funds of funds, which invest in various real assets. Fair value is based on quoted market prices for those traded on active markets. Several of these investments are either funds not actively traded in a public market or investments in limited partnerships, in which fair value is determined by the NAV of the funds as determined in good faith by the fund manager or general partner using the NAV as the practical expedient.

Alternative investments – Investments in alternatives include funds of funds, hedge funds, and private equity funds for which no active market exists. The University has estimated the investments' fair value by using the NAV provided by the funds' managers.

The University generally records alternative investments at NAV provided by the fund's managers, as the managers have the greatest insight into the investments of their fund and the related industry. The University assesses the NAV and takes into consideration events such as suspended redemptions, imposition of gates, restructuring, secondary sales, and investor defaults to determine if an adjustment is necessary. Additionally, asset holdings are reviewed within the investment manager's audited financial statements, as are interim financial statements and fund manager communications, for purposes of assessing valuation. The University's determination of fair value is based upon the best available information provided by the investment manager and may incorporate management assumptions and best estimates after considering a variety of internal and external factors. Such value generally represents the University's proportionate share of the partner's capital of the investment partnerships as reported by their general partners. For these investments, the University has determined, through its monitoring activities, to rely on the fair value as determined by the investment managers.

Beneficial interest in trust held by third parties – The University's beneficial interest in trust assets are valued at fair value using the quoted market prices of the underlying securities and discounted when appropriate. If a quoted market price is not available, fair value is determined using the net present value of future distributions the University expects to receive over the term of the agreements. See Note 5.

Interest-rate swap agreement – The fair value of the interest-rate swap agreement is the estimated amount the University would receive or pay to terminate the agreement at the reporting date, taking into consideration the current interest rates and creditworthiness of counterparties.

University of San Diego Notes to Financial Statements

Note 3 – Fair Value of Financial Instruments (continued)

The following table discloses by level the fair value hierarchy for assets and liabilities at June 30, 2018:

	(In Thousands)				
	Level 1	Level 2	Level 3	Assets Held at Net Asset Value (or Equivalent)	2018 Total
ASSETS					
Investment in:					
Cash and cash equivalents	\$ 52,372	\$ -	\$ -	\$ -	\$ 52,372
Fixed-income securities:					
Domestic debt securities	13,010	-	-	85,494	98,504
Government debt securities	15,131	-	-	-	15,131
Domestic and global securities	34,343	-	-	21,000	55,343
Global debt securities	-	-	-	11,029	11,029
Equities funds:					
Domestic equity securities	29,995	-	-	91,824	121,819
International equity securities	23,225	-	-	67,856	91,081
Emerging market equity securities	8,519	-	-	42,387	50,906
Inflation sensitive equities	21,855	-	-	-	21,855
Real estate	-	14,939	-	-	14,939
Real assets funds	25,194	-	-	15,392	40,586
Marketable alternatives:					
Absolute return hedge funds	-	-	-	38,162	38,162
Long/short hedge funds	-	-	-	50,344	50,344
Diversifying hedge funds	-	-	-	21,416	21,416
Non-marketable alternatives:					
Venture capital	-	-	-	25,252	25,252
Domestic private equity	-	-	-	18,812	18,812
International private equity	-	-	-	8,021	8,021
Distressed debt	-	-	-	10,072	10,072
Diversifiers private equity	-	-	-	614	614
Energy and resources	-	-	-	16,705	16,705
Real estate	-	-	-	13,240	13,240
	<u>223,644</u>	<u>14,939</u>	<u>-</u>	<u>537,620</u>	<u>776,203</u>
Beneficial interest in trust held by third parties	-	-	5,647	-	5,647
	<u>-</u>	<u>-</u>	<u>5,647</u>	<u>-</u>	<u>5,647</u>
Total fair value of assets	<u>\$ 223,644</u>	<u>\$ 14,939</u>	<u>\$ 5,647</u>	<u>\$ 537,620</u>	<u>\$ 781,850</u>
LIABILITIES					
Interest-rate swap agreement	<u>\$ -</u>	<u>\$ 21,276</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 21,276</u>

University of San Diego

Notes to Financial Statements

Note 3 – Fair Value of Financial Instruments (continued)

The following table discloses by level the fair value hierarchy for assets and liabilities at June 30, 2017:

	(In Thousands)				
	Level 1	Level 2	Level 3	Assets Held at Net Asset Value (or Equivalent)	2017 Total
ASSETS					
Investment in:					
Cash and cash equivalents	\$ 62,627	\$ -	\$ -	\$ -	\$ 62,627
Fixed-income securities:					
Domestic debt securities	24,524	-	-	51,626	76,150
Government debt securities	15,149	-	-	-	15,149
Domestic and global securities	29,117	-	-	-	29,117
Global debt securities	-	-	-	11,167	11,167
Equities funds:					
Domestic equity securities	35,244	-	-	85,092	120,336
International equity securities	21,218	-	-	62,868	84,086
Emerging market equity securities	24,384	-	-	23,475	47,859
Inflation sensitive equities	24,489	-	-	-	24,489
Real estate	-	13,818	-	-	13,818
Real assets funds	25,728	-	-	8,520	34,248
Marketable alternatives:					
Absolute return hedge funds	-	-	-	37,883	37,883
Long/short hedge funds	-	-	-	44,138	44,138
Diversifying hedge funds	-	-	-	20,935	20,935
Non-marketable alternatives:					
Venture capital	-	-	-	19,995	19,995
Domestic private equity	-	-	-	14,584	14,584
International private equity	-	-	-	9,324	9,324
Distressed debt	-	-	-	9,624	9,624
Energy and resources	-	-	-	13,852	13,852
Real estate	-	-	-	8,717	8,717
	<u>262,480</u>	<u>13,818</u>	<u>-</u>	<u>421,800</u>	<u>698,098</u>
Beneficial interest in trust held by third parties	<u>-</u>	<u>-</u>	<u>5,413</u>	<u>-</u>	<u>5,413</u>
Total fair value of assets	<u>\$ 262,480</u>	<u>\$ 13,818</u>	<u>\$ 5,413</u>	<u>\$ 421,800</u>	<u>\$ 703,511</u>
LIABILITIES					
Interest-rate swap agreement	<u>\$ -</u>	<u>\$ 27,131</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 27,131</u>

The following table discloses the summary of changes in the fair value of the beneficial interest in trust held by third parties as of June 30:

	2018	2017
Balance, beginning of year	\$ 5,413	\$ 5,398
Actuarial adjustment	<u>234</u>	<u>15</u>
Balance, end of year	<u>\$ 5,647</u>	<u>\$ 5,413</u>

University of San Diego
Notes to Financial Statements

Note 3 – Fair Value of Financial Instruments (continued)

The University recognizes all significant transfers between Levels 1, 2, and 3 at fair value at the end of the reporting period.

Net appreciation (depreciation) on investments and the actuarial adjustment for the beneficial interest in trusts in the above tables are reflected in the line “Investment income” and “Contributions,” respectively, in the statements of activities.

The following summarizes the investments by major class where NAV or its equivalent is used to measure fair value as of June 30, 2018:

	(In Thousands)		Redemption Frequency	Redemption Notice Period	Notes
	Fair Value	Unfunded Commitments			
Fixed-income securities:					
Domestic debt securities	\$ 85,494	N/A	1 – 90 days, with exception to those under gate limitations	1 – 60 days, with exception to those under gate limitations	(a)
Domestic and global securities	\$ 21,000	N/A	Daily	Daily	(a)
Global debt securities	\$ 11,029	N/A	Daily	Daily	(a)
Equities funds:					
Domestic equity securities	\$ 91,824	N/A	1 – 90 days, with exception to those under gate limitations	1 – 60 days, with exception to those under gate limitations	(a)
International equity securities	\$ 67,856	N/A	1 – 30 days, with exception to those under gate limitations	1 – 30 days, with exception to those under gate limitations	(a)
Emerging market equity securities	\$ 42,387	\$ 6,900	1 day - 24 months, with exception to those under gate limitations	1 – 184 days, with exception to those under gate limitations	(a)
Real assets funds	\$ 15,392	N/A	Monthly	15 days	(b)
Marketable alternatives:					
Absolute return hedge funds	\$ 38,162	N/A	3 – 36 months	60 – 90 days	(c)
Long/short hedge funds	\$ 50,344	N/A	3 – 36 months	45 – 90 days	(d)
Diversifying hedge funds	\$ 21,416	N/A	1 – 30 days	1 – 60 days	(e)

(continued)

University of San Diego

Notes to Financial Statements

Note 3 – Fair Value of Financial Instruments (continued)

(continued from above)

	(In Thousands)		Redemption Frequency	Redemption Notice Period	Notes
	Fair Value	Unfunded Commitments			
Non-marketable alternatives:					
Venture capital	\$ 25,252	\$ 17,430	N/A – Redeemable upon maturity	N/A	(f)
Domestic private equity	\$ 18,812	\$ 28,126	N/A – Redeemable upon maturity	N/A	(g)
International private equity	\$ 8,021	\$ 9,699	N/A – Redeemable upon maturity	N/A	(g)
Distressed debt	\$ 10,072	\$ 3,251	N/A – Redeemable upon maturity	N/A	(h)
Diversifiers private equity	\$ 614	\$ 9,430	N/A – Redeemable upon maturity	N/A	(i)
Energy and resources	\$ 16,705	\$ 15,152	N/A – Redeemable upon maturity	N/A	(j)
Real estate	\$ 13,240	\$ 14,385	N/A – Redeemable upon maturity	N/A	(k)
	<u>\$ 537,620</u>	<u>\$ 104,373</u>			

- (a) This category includes funds that consist of assets from several accounts which are blended together. These funds invest in U.S. debt and equities, international equities, as well as emerging markets. Less than 1 percent of the investments are not redeemable until liquidation by the fund manager.
- (b) This category includes an investment in one real assets fund. Underlying investments are primarily real estate holdings in the public property markets throughout North America, Europe, and Asia Pacific.
- (c) This category includes investments in various types of hedge funds using a total of 11 different fund managers. These funds are invested in absolute return strategies, including diversified arbitrage, event-driven arbitrage, and distressed funds. Less than 10 percent of the investments are not redeemable until liquidation by the fund manager. The remaining values are generally redeemable within one year, subject to certain gate limitations.
- (d) This category includes investments in various types of hedge funds using a total of 8 different fund managers. These funds are invested in long and short strategies in both U.S. and global common stocks. Less than 1 percent of the investments are not redeemable until liquidation by the fund manager. The remaining values are generally redeemable within one year, subject to certain gate limitations.
- (e) This category includes investments in various types of hedge funds using a total of 6 different fund managers. These funds are invested in diversifying strategies with lower correlation to equity markets, including global macro and trend-following funds. Values are generally redeemable within sixty days, subject to certain gate limitations.
- (f) This category includes investments in venture capital funds and funds of venture capital funds. Underlying investments are primarily private investments in early-stage companies.
- (g) This category includes investments in private equity funds and private equity funds of funds in the U.S. and outside of the U.S. whose mandates include leveraged buyouts and growth equity investments in companies.
- (h) This category includes investments in distressed debt funds and funds of funds. Underlying investments are primarily securities of companies or government entities that are already in default, under bankruptcy protection, or in distress and heading towards such a condition.
- (i) This category includes investments in diversifying funds, which use differentiated strategies and typically have low correlations to the rest of the portfolio.

Note 3 – Fair Value of Financial Instruments (continued)

- (j) This category includes funds, and a fund of funds, which invest in natural resources, commodities, and private energy in the U.S. and outside the U.S.
- (k) This category includes funds, and a fund of funds, which invest in private real estate in the U.S. and outside the U.S.

Note 4 – Accounts and Loans Receivable

The following is a summary of receivables at June 30 (in thousands):

	<u>2018</u>	<u>2017</u>
Student loans receivable	\$ 36,654	\$ 37,978
Other receivables	6,993	7,039
Student accounts receivable for tuition and fees	<u>10,614</u>	<u>7,394</u>
	54,261	52,411
Less allowance for doubtful accounts	<u>(6,682)</u>	<u>(6,337)</u>
Total	<u>\$ 47,579</u>	<u>\$ 46,074</u>

The University's student loans receivable consist of institutional and federally-sponsored loans due from both current and former students. Student loans and allowance for student loan doubtful accounts at June 30 are as follows (in thousands):

Institutional loans	\$ 23,155	\$ 23,284
Federally-sponsored loans	<u>13,499</u>	<u>14,694</u>
	36,654	37,978
Less allowance for doubtful accounts	<u>(6,156)</u>	<u>(5,823)</u>
Total	<u>\$ 30,498</u>	<u>\$ 32,155</u>

Institutional loans are funded by donor funds restricted for student loan purposes. Federally-sponsored loans are funded by advances to the University primarily under the Federal Perkins Loan Program (the "Program"). Loans to students under the Program are subject to mandatory interest rates and significant restrictions, and loans issued under the Program can be assigned to the federal government in certain non-repayment situations. In these situations, the federal portion of the loan balance is guaranteed.

Amounts received under the Program are ultimately refundable to the federal government in the event the University no longer participates in the Program and, accordingly, have been reported as refundable advances in the statements of financial position. As of October 1, 2017, under Federal law, the University may no longer award new Perkins Loans to undergraduate students and may not make subsequent disbursements to undergraduate students after June 30, 2018. As of July 1, 2017, the University may not disburse Perkins loans to graduate students.

University of San Diego

Notes to Financial Statements

Note 4 – Accounts and Loans Receivable (continued)

The University provides home mortgage financing assistance to certain faculty. Notes receivable amounting to approximately \$2,373,000 and \$2,604,000 were outstanding at June 30, 2018 and 2017, respectively, and are collateralized by deeds of trust on properties concentrated in the region surrounding the University. No allowance for doubtful accounts has been recorded against these loans based on their collateralization and nature of the loans as forgivable. So long as there is no event of default as described in the promissory note, loans are forgiven over a five-year period. These amounts are included in other receivables in the summary of receivables tables above.

Note 5 – Contributions Receivable

Contributions receivable are expected to be received in the following periods at June 30 (in thousands):

	2018	2017
Unconditional pledges:		
Less than one year	\$ 2,490	\$ 3,187
One to five years	11,703	3,320
More than five years	39,056	33,423
	<u>53,249</u>	<u>39,930</u>
Less present value discount (3.4 percent at June 30, 2018 and 2.4 percent at June 30, 2017)	(13,822)	(9,249)
Less allowance for uncollectibility	<u>(12,388)</u>	<u>(9,904)</u>
Net pledges receivable	27,039	20,777
Split-interest agreements - more than five years	<u>5,647</u>	<u>5,413</u>
Total	<u>\$ 32,686</u>	<u>\$ 26,190</u>

At June 30, 2018, an outstanding pledge from two donors represented 36 percent of the University's gross pledges. At June 30, 2017, 34 percent of the University's gross pledges was due from one donor.

Split-interest agreements are comprised of unitrusts and charitable gift annuities. The Finance Office, under the supervision of the Vice President for Finance and Chief Financial Officer, determines the fair value measurement policies and procedures for split-interest agreements. These policies and procedures are reassessed annually to determine if the current valuation techniques are still appropriate. At that time, the unobservable inputs used in the fair value measures are evaluated and adjusted, as necessary, based on current market conditions and other third-party information.

Type	(In Thousands) Fair Value at June 30, 2018	Valuation Technique	Significant Unobservable Inputs	Range of Input Value
Beneficial interests in trust held by third parties	\$ 5,647	Discounted Cash Flow	Discount Rate Life Expectancy	3.4% 4 to 35 years

Note 5 – Contributions Receivable (continued)

To determine the fair value of unitrust assets, the University determines net present value using a discount percentage and donor data. For charitable gift annuities, the assets are recorded at fair value and a liability is then recorded for the amount of the annuity payments based on the life of the donor. A decrease in the discount rate, a shorter life expectancy, and an increase in the fair value of the underlying assets will increase the recorded fair value of the unitrust; this change in fair value is recorded into revenue for the given year.

Note 6 – Property, Plant, and Equipment

Property, plant, and equipment consist of the following at June 30 (in thousands):

	2018	2017
Land and improvements	\$ 58,819	\$ 51,088
Buildings and improvements	554,572	539,429
Furniture, equipment, and capital leases	23,187	21,511
Library resources	53,276	52,762
Construction in progress	12,735	18,451
	702,589	683,241
Less accumulated depreciation	(200,899)	(186,072)
	501,690	497,169
Art collection	4,062	4,062
Total	\$ 505,752	\$ 501,231

Property, plant, and equipment are stated at cost if purchased, or fair value at the date of donation, and are depreciated on a straight-line basis over their appropriate estimated useful lives. The estimated useful lives by asset type are 50 years for buildings; 40 years for building improvements and library resources; 7 years for furniture, equipment, and technology upgrades; and 3 years for capital lease assets. Depreciation expense totaled approximately \$16,842,000 and \$15,998,000 for the years ended June 30, 2018 and 2017, respectively.

The art collection consists of various pieces of donated and purchased artwork, antique furniture, and artifacts whose value is expected to increase over time and, therefore, is not depreciated.

University of San Diego

Notes to Financial Statements

Note 7 – Employee Benefits

The University has a retirement healthcare program that pays a specified fixed amount to supplement the medical insurance payments made by retirees of the University. The University has internally designated specific investments toward covering this obligation.

The following table sets forth the amount of obligation and assets as of June 30 (in thousands):

	<u>2018</u>	<u>2017</u>
Fair value of designated assets	\$ 4,723	\$ 4,576
Post-retirement benefit obligation	<u>4,716</u>	<u>4,574</u>
Over funded	<u>\$ 7</u>	<u>\$ 2</u>

The designated assets are included in short-term investments and the benefit obligation is included in accounts payable and accrued expenses in the statements of financial position.

The following table sets forth benefit costs and benefits paid (in thousands):

Benefit costs	\$ 35	\$ 32
Benefit payments	172	171
Contributions	142	579
Weighted-average assumptions:		
Discount rate	5.0%	5.0%
Expected return on plan assets	8.0%	8.0%

The University uses an actuarial measurement date of June 30 to determine benefit measurements as of the same date of the current year. The discount rate is the estimated rate at which the obligation for benefits could effectively be settled. The expected return on plan assets reflects the average rate of earnings that the University estimates will be generated on the assets of the plan.

The University has a defined-contribution retirement plan (the “Plan”) which covers all benefit-eligible employees. For the participating employees, the University contributes 12 percent of the employees’ eligible compensation to the Plan. Both the employee and University contributions are employee-directed into various funding vehicles as provided by the plan sponsor. The University’s related expense was approximately \$16,919,000 and \$16,391,000 for the years ended June 30, 2018 and 2017, respectively.

University of San Diego Notes to Financial Statements

Note 8 – Lines of Credit

The University has a variable rate line of credit at a bank with a maximum borrowing limit of \$8,000,000; of which \$2,046,000 of the line has been earmarked for letters of credit related to insurance policies. The renewable line of credit is effective through February 1, 2019 and may be used for working capital purposes. There were no borrowings under this line at June 30, 2018 or 2017.

In 2010, the University obtained a line of credit for funding of a major campus sustainability project. The University converted the balance into a ten-year term loan effective September 30, 2010. The outstanding balance as of June 30, 2018 and 2017 was approximately \$2,317,000 and \$3,249,000, respectively, and is included in other liabilities in the statements of financial position.

The following table sets forth the University's payment requirements as of June 30, 2018 on the term loan (in thousands):

Years ending June 30,	
2019	\$ 991
2020	1,053
2021	<u>273</u>
Total	<u>\$ 2,317</u>

Note 9 – Lease Commitments

The University leases various types of equipment under leases that qualify as capital leases. The gross amount of equipment recorded as capital leases was approximately \$2,648,000 and \$2,083,000 at June 30, 2018 and 2017, respectively. Accumulated amortization for equipment recorded under capital leases was approximately \$1,109,000 and \$981,000 at June 30, 2018 and 2017, respectively. The amortization expense for these capital leases is included within the University's depreciation expense.

The following table sets forth the University's future minimum lease payments as of June 30, 2018 on capital lease obligations (in thousands):

Years ending June 30,	
2019	\$ 615
2020	435
2021	172
2022	111
2023	<u>16</u>
Total	<u>\$ 1,349</u>

University of San Diego

Notes to Financial Statements

Note 10 – Bonds Payable

Bonds payable consist of the following at June 30 (in thousands):

	<u>2018</u>	<u>2017</u>
2015 California Municipal Finance Authority Variable Rate Revenue Bonds (the "2015 Bonds"), with interest rates based on market conditions, varying between 1.373 and 2.283 percent during the year ended June 30, 2018, payable on April 1 and October 1 each year, maturing October 2045	\$ 89,895	\$ 90,535
	89,895	90,535
Unamortized original cost of issuance	<u>(167)</u>	<u>(208)</u>
	<u>89,728</u>	<u>90,327</u>
2012 California Municipal Finance Authority bonds (the "2012 bonds"), with an interest rate of 5 percent, payable on April 1 and October 1 each year, maturing October 2032	9,630	9,630
	9,630	9,630
Unamortized original issue premium	816	875
Unamortized original cost of issuance	<u>(133)</u>	<u>(143)</u>
	<u>10,313</u>	<u>10,362</u>
2011 A California Municipal Finance Authority bonds (the "2011 A bonds"), with interest rates varying between 5.00 and 5.25 percent, payable on April 1 and October 1 each year, maturing October 2028	17,910	17,910
	17,910	17,910
Unamortized original issue premium	649	712
Unamortized original cost of issuance	<u>(89)</u>	<u>(97)</u>
	<u>18,470</u>	<u>18,525</u>
2011 B California Municipal Finance Authority bonds (the "2011 B bonds"), with interest rates varying between 3 and 5 percent, payable on April 1 and October 1 each year, maturing October 2041	20,720	21,165
	20,720	21,165
Unamortized original issue premium	1,061	1,106
Unamortized original cost of issuance	<u>(145)</u>	<u>(151)</u>
	<u>21,636</u>	<u>22,120</u>

(continued)

University of San Diego
Notes to Financial Statements

Note 10 – Bonds Payable (continued)

(continued from above)

	2018	2017
2011 California Educational Facilities Authority revenue bonds (the "2011 bonds"), with interest rates varying between 3 and 5 percent, payable on April 1 and October 1 each year, maturing October 2022	8,155	9,560
	8,155	9,560
Unamortized original issue premium	402	473
Unamortized original cost of issuance	(103)	(122)
	8,454	9,911
1999 California Educational Facilities Authority revenue bonds (the "1999 bonds"), comprised of capital appreciation bonds with interest rates varying between 4.45 and 5.16 percent, with interest payable at the time they mature: Capital appreciation bonds, due October 2009 through October 2024	5,717	6,410
	5,717	6,410
Unamortized original issue discount	(31)	(34)
Unamortized original cost of issuance	(127)	(140)
	5,559	6,236
Total bonds payable	\$ 154,160	\$ 157,481

The 2015, 2012, 2011 A, 2011 B, 2011, and 1999 bonds are secured by the University's full faith and credit. The bond agreements place certain restrictive covenants on the University with which management believes the University has complied. Bond premiums, discounts, and issuance costs are amortized using the straight-line method over the life of the bonds, which approximates the interest method.

The estimated fair value of the University's bonds was approximately \$168,475,000 and \$174,457,000 at June 30, 2018 and 2017, respectively. Bonds payable are categorized as Level 2 within the fair value hierarchy discussed in Note 1. For the 2012, 2011 A, 2011 B, 2011, and 1999 bonds, the fair value was derived using estimated market prices on publicly-traded debt. The 2015 bonds are privately placed with a financial institution and management has determined the carrying value as of June 30, 2018 approximates the fair value of these bonds.

In July 2018, the University amended the terms of the 2015 Bonds with US Bank to restate the index used in the calculation of interest for the sole purpose of achieving future debt service savings. The current index used is 81 percent of LIBOR plus a credit spread of 67 basis points. The amended index is the SIFMA index plus a credit spread of 50 basis points. No other changes were made to the terms of the 2015 Bonds.

University of San Diego

Notes to Financial Statements

Note 10 – Bonds Payable (continued)

The following table sets forth the University's principal payment requirements as of June 30, 2018 on bonds payable for each of the next five years and thereafter (in thousands):

Years ending June 30,	2015 Bonds	2012 Bonds	2011 A Bonds	2011 B Bonds	2011 Bonds	1999 Bonds	Total
2019	665	-	-	475	1,480	651	3,271
2020	685	-	-	500	1,550	619	3,354
2021	710	-	-	525	1,625	588	3,448
2022	125	-	-	550	1,700	747	3,122
2023	125	-	-	575	1,800	707	3,207
Thereafter	87,585	9,630	17,910	18,095	-	2,405	135,625
	<u>\$ 89,895</u>	<u>\$ 9,630</u>	<u>\$ 17,910</u>	<u>\$ 20,720</u>	<u>\$ 8,155</u>	<u>\$ 5,717</u>	<u>\$ 152,027</u>

Note 11 – Net Assets

Temporarily restricted net assets are available for the following purposes at June 30 (in thousands):

	2018	2017
Educational programs	\$ 90,895	\$ 80,183
Scholarships	33,413	29,843
Athletics and recreation	2,131	627
Public service	10,785	9,556
Total program support	<u>137,224</u>	<u>120,209</u>
Management and general support	<u>43,397</u>	<u>25,696</u>
	<u>\$ 180,621</u>	<u>\$ 145,905</u>

Net assets released from restrictions are as follows:

Purpose and time restricted	<u>\$ 18,234</u>	<u>\$ 22,644</u>
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University of San Diego
Notes to Financial Statements

Note 11 – Net Assets (continued)

Permanently restricted net assets are restricted to the following purposes at June 30 (in thousands):

	2018	2017
Revolving student loan funds from private sources	\$ 23,699	\$ 23,384
Investment in perpetuity, the income from which is expendable to support the following programs:		
Educational programs	108,339	107,576
Scholarships	48,442	42,939
Athletics and recreation	229	229
Public service	5,573	5,568
Total program support	162,583	156,312
Management and general support	1,917	4,541
	164,500	160,853
	\$ 188,199	\$ 184,237

Note 12 – Endowment

The state of California has adopted the Uniform Prudent Management of Institutional Funds Act (UPMIFA), the provisions of which apply to endowment funds existing or established after the date of adoption. The corpus of the fund subject to UPMIFA is classified as permanently restricted. The corpus represents the fair value of the original gifts as of the gift date and all subsequent gifts where the donor has indicated that the gift must be retained permanently. The value of assets in excess of original gifts in donor-restricted endowment funds is classified as temporarily restricted net assets until appropriated for expenditure by the University.

Spending policy – Spending is based on a total return strategy, which includes both appreciation and income. The University's spending allowance rate is 4 percent of the trailing three-year average of the endowment's fair value. The fair value is the sum of the endowment principal and the accumulated realized and unrealized earnings. In accordance with UPMIFA, the Board may expend so much of an endowment fund as the Board determines to be prudent for the uses and purposes for which the endowment fund is established, consistent with the goal of conserving the long-term purchasing power of the endowment fund.

Investment policy – The overall investment goal for the pooled endowment fund (the "Fund") is three-fold: (1) to provide a relatively predictable, stable, and constant return sufficient to meet the spending needs of the University; (2) to preserve and enhance the real (inflation adjusted) purchasing power of the Fund through active management; and (3) to increase the Fund through unspent income and gains, appreciated value, gifts, and other appropriate funds.

University of San Diego

Notes to Financial Statements

Note 12 – Endowment (continued)

The return objective for the Fund, measured over a full market cycle, shall be inflation plus 5.5 percent, after the payment of all investment-related fees. In addition, the Fund should experience no greater risk (volatility and variability of return) than that of the market; the market being defined as the Fund's relevant policy benchmarks. It is recognized that the achievement of a long-term, real return in excess of 5.5 percent per year will require a significant allocation to higher returning asset classes. To help moderate the volatility of the portfolio, the Fund will seek to achieve meaningful diversification across asset classes. In addition, the Fund will include significant allocations to asset classes that provide a meaningful hedge against deflation and inflation.

Endowment net assets – The following represents a description of the endowment net asset composition by type of fund as of June 30, 2018 (in thousands):

	2018			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
Donor-restricted endowment fund	\$ (14)	\$ 122,632	\$ 164,500	\$ 287,118
Board designated/quasi-endowment funds	242,880	-	-	242,880
Total endowment	<u>\$ 242,866</u>	<u>\$ 122,632</u>	<u>\$ 164,500</u>	<u>\$ 529,998</u>

The following represents a description of the endowment net asset composition by type of fund as of June 30, 2017 (in thousands):

	2017			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
Donor-restricted endowment fund	\$ (13)	\$ 109,891	\$ 160,853	\$ 270,731
Board designated/quasi-endowment funds	232,837	-	-	232,837
Total endowment	<u>\$ 232,824</u>	<u>\$ 109,891</u>	<u>\$ 160,853</u>	<u>\$ 503,568</u>

University of San Diego
Notes to Financial Statements

Note 12 – Endowment (continued)

As a result of market declines, the fair value of certain donor-restricted endowments was less than the historical cost value of such funds by approximately \$14,000 and \$13,000 at June 30, 2018 and 2017, respectively. These losses have been recorded as reductions in unrestricted net assets. Future gains will be used to restore this deficiency in unrestricted net assets before any net appreciation above the historical cost value of such funds increases temporarily restricted net assets.

The following represents the changes in endowment net assets for the year ended June 30, 2018 (in thousands):

	2018			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
Net endowment assets, beginning of year	\$ 232,824	\$ 109,891	\$ 160,853	\$ 503,568
Investment return:				
Investment income, net	1,523	1,828	-	3,351
Net appreciation	16,794	19,526	-	36,320
Total investment return	18,317	21,354	-	39,671
Contribution and other revenue	95	375	2,372	2,842
Appropriation and other expenditures	(7,328)	(9,028)	-	(16,356)
Other changes, including transfers	(1,042)	40	1,275	273
Net endowment assets, end of year	<u>\$ 242,866</u>	<u>\$ 122,632</u>	<u>\$ 164,500</u>	<u>\$ 529,998</u>

University of San Diego

Notes to Financial Statements

Note 12 – Endowment (continued)

The following represents the changes in endowment net assets for the year ended June 30, 2017 (in thousands):

	2017			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
Net endowment assets, beginning of year	\$ 203,124	\$ 89,754	\$ 156,919	\$ 449,797
Investment return:				
Investment income, net	1,805	2,174	-	3,979
Net appreciation	25,124	28,918	-	54,042
Total investment return	26,929	31,092	-	58,021
Contribution and other revenue	10	22	3,710	3,742
Appropriation and other expenditures	(6,013)	(9,608)	-	(15,621)
Other changes, including transfers	8,774	(1,369)	224	7,629
Net endowment assets, end of year	\$ 232,824	\$ 109,891	\$ 160,853	\$ 503,568

Note 13 – Commitments and Contingencies

Loan programs – The University participates in certain alternative loan programs. No assets or liabilities are recorded by the University for amounts loaned to students under these programs. The University is contingently liable for a portion of the outstanding loans, and the amount of the contingency was approximately \$1,269,000 and \$1,281,000 at June 30, 2018 and 2017, respectively.

Grants and contracts – Federal grant programs are subject to review by the grantor agencies, which could result in requests for reimbursement to grantor agencies for disallowed expenditures. Management believes it has adhered to the terms of its grants, and any disallowed expenditures resulting from such reviews would not have a material effect on the financial position of the University.

Legal – The University is party to certain legal actions arising in the ordinary course of business. In the opinion of management, liabilities, if any, under these actions will not have a material impact on its financial position.

Note 14 – Subsequent Events

Subsequent events are events or transactions that occur after the statement of financial position date, but before the financial statements are available to be issued. The University recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the statement of financial position, including the estimates inherent in the process of preparing the financial statements. The University's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the statement of financial position, but arose after the statement of financial position date and before the financial statements are available to be issued.

The University has evaluated subsequent events through October 17, 2018, which is the date the financial statements were available for issuance.