

Northeastern University
Consolidated Financial Statements
June 30, 2019 and 2018

Northeastern University

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June 30, 2019 and 2018

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Report of Independent Auditors

To the Board of Trustees of Northeastern University

We have audited the accompanying consolidated financial statements of Northeastern University and its subsidiaries, which comprise the consolidated statements of financial position as of June 30, 2019 and 2018, and the related consolidated statements of activities for the year ended June 30, 2019, and of cash flows for the years ended June 30, 2019 and 2018.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the 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.

Auditors' Responsibility

Our responsibility is to express an opinion on the consolidated 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 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 our 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, we consider internal control relevant to the Company'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 Company'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 Northeastern University and its subsidiaries as of June 30, 2019 and 2018, and the changes in their net assets for the year ended June 30, 2019 and their cash flows for the years ended June 30, 2019 and 2018 in accordance with accounting principles generally accepted in the United States of America.



Emphasis of Matter

As discussed in Note 2 to the consolidated financial statements, the University changed the manner in which it presents net assets and reports certain aspects of its financial statements as a not-for-profit entity in 2019. Our opinion is not modified with respect to this matter.

Other Matter

We previously audited the consolidated statement of financial position as of June 30, 2018, and the related consolidated statements of activities and of cash flows (the statement of activities is not presented herein) for the year then ended, and in our report dated October 15, 2018, we expressed an unmodified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying summarized financial information as of June 30, 2018 and for the year then ended is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

PricewaterhouseCoopers LLP

Boston, Massachusetts
October 7, 2019

Northeastern University
Consolidated Statements of Financial Position
June 30, 2019 and 2018

(in thousands of dollars)

| | 2019 | 2018 |
|--|---------------------|---------------------|
| Assets | | |
| Cash and cash equivalents | \$ 338,203 | \$ 239,389 |
| Accounts and other receivables, net | 87,927 | 56,489 |
| Prepays and other assets | 49,414 | 32,301 |
| Pledges receivable, net (Note 5) | 103,653 | 88,264 |
| Student and other loans receivable, net | 25,520 | 30,023 |
| Investments (Notes 4 and 6) | 1,273,068 | 1,113,170 |
| Property, plant and equipment, net (Note 7) | <u>1,543,666</u> | <u>1,431,637</u> |
| Total assets | <u>\$ 3,421,451</u> | <u>\$ 2,991,273</u> |
| Liabilities and Net Assets | | |
| Liabilities | | |
| Accounts payable and accrued liabilities | \$ 163,835 | \$ 155,515 |
| Accounts payable on construction projects | 30,688 | 28,869 |
| Deferred revenue and student deposits | 193,038 | 63,630 |
| Refundable advances | 39,828 | 36,227 |
| Interest rate swap agreement (Notes 4 and 9) | 49,219 | 36,458 |
| Capital lease obligation (Note 8) | 22,857 | 24,222 |
| Bonds and notes payable (Notes 4 and 9) | <u>898,029</u> | <u>852,363</u> |
| Total liabilities | <u>1,397,494</u> | <u>1,197,284</u> |
| Net assets | | |
| Without donor restrictions (Note 12) | 1,427,755 | 1,279,216 |
| With donor restrictions (Note 12) | <u>596,202</u> | <u>514,773</u> |
| Total net assets | <u>2,023,957</u> | <u>1,793,989</u> |
| Total liabilities and net assets | <u>\$ 3,421,451</u> | <u>\$ 2,991,273</u> |

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

Northeastern University
Consolidated Statement of Activities
Year Ended June 30, 2019
(with summarized financial information for the year ended June 30, 2018)

| <i>(in thousands of dollars)</i> | Without Donor Restrictions | With Donor Restrictions | 2019 | 2018 |
|--|----------------------------------|----------------------------|---------------------|---------------------|
| Operating | | | | |
| Revenues and other support | | | | |
| Tuition and fees (after financial aid of \$352,663 in 2019 and \$338,994 in 2018) | \$ 998,077 | \$ - | \$ 998,077 | \$ 919,187 |
| Contributions available for operations | 3,862 | 17,148 | 21,010 | 31,424 |
| Auxiliary enterprises | 151,668 | - | 151,668 | 146,161 |
| Sponsored support | 123,049 | - | 123,049 | 108,337 |
| Indirect cost recovery | 31,418 | - | 31,418 | 31,223 |
| Endowment spending available for operations (Note 13) | 16,101 | 12,205 | 28,306 | 25,401 |
| Other investment return available for operations | 15,899 | - | 15,899 | 7,366 |
| Other | 35,744 | - | 35,744 | 37,377 |
| Total operating revenues | <u>1,375,818</u> | <u>29,353</u> | <u>1,405,171</u> | <u>1,306,476</u> |
| Net assets released for operations | <u>25,701</u> | <u>(25,701)</u> | <u>-</u> | <u>-</u> |
| Total operating revenues and other support | <u>1,401,519</u> | <u>3,652</u> | <u>1,405,171</u> | <u>1,306,476</u> |
| Expenses | | | | |
| Salary and benefits | 714,390 | - | 714,390 | 670,671 |
| Other operating expenses | 445,883 | - | 445,883 | 425,391 |
| Depreciation | 69,359 | - | 69,359 | 63,741 |
| Interest | 39,824 | - | 39,824 | 39,093 |
| Total operating expenses (Notes 7, 9 and 15) | <u>1,269,456</u> | <u>-</u> | <u>1,269,456</u> | <u>1,198,896</u> |
| Increase in net assets from operating activities | 132,063 | 3,652 | 135,715 | 107,580 |
| Nonoperating | | | | |
| Contributions | 3,917 | 87,404 | 91,321 | 40,681 |
| Contributions available for operations | (3,862) | (17,148) | (21,010) | (31,424) |
| Endowment and other investment return (Note 4 and 13) | 52,581 | 25,726 | 78,307 | 72,315 |
| Endowment spending available for operations (Note 13) | (16,101) | (12,205) | (28,306) | (25,401) |
| Other investment return available for operations | (15,899) | - | (15,899) | (7,366) |
| Change in annuity and life income funds | - | (2,224) | (2,224) | 128 |
| Other nonoperating changes | 9,137 | - | 9,137 | - |
| Net realized and change in unrealized (loss)/gain on interest rate swap agreement (Note 9) | (17,073) | - | (17,073) | 6,822 |
| Net assets released from restrictions and other transfers | <u>3,776</u> | <u>(3,776)</u> | <u>-</u> | <u>-</u> |
| Change in net assets | 148,539 | 81,429 | 229,968 | 163,335 |
| Net assets at beginning of year | <u>1,279,216</u> | <u>514,773</u> | <u>1,793,989</u> | <u>1,630,654</u> |
| Net assets at end of year | <u>\$ 1,427,755</u> | <u>\$ 596,202</u> | <u>\$ 2,023,957</u> | <u>\$ 1,793,989</u> |

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

Northeastern University
Consolidated Statements of Cash Flows
Years Ended June 30, 2019 and 2018

(in thousands of dollars)

| | 2019 | 2018 |
|---|-------------------|-------------------|
| Cash flows from operating activities | | |
| Cash received from student-related revenues | \$ 1,129,875 | \$ 1,063,692 |
| Cash received from sponsored programs | 125,512 | 125,994 |
| Cash received from donors | 26,317 | 20,848 |
| Proceeds from sale of contributed securities | 2,591 | 2,861 |
| Cash received from endowment and other investment income | 10,789 | 1,602 |
| Cash received from auxiliary enterprises other than student housing | 4,991 | 6,656 |
| Cash received from other income | 178,997 | 36,434 |
| Cash paid to employees and vendors | (1,158,039) | (1,086,942) |
| Interest and other payments | (45,025) | (46,645) |
| Net cash provided by operating activities | <u>276,008</u> | <u>124,500</u> |
| Cash flows from investing activities | | |
| Acquisition of property, plant and equipment | (180,757) | (135,193) |
| Acquisition of business | (9,045) | - |
| Decrease in deposits with trustees | - | 23,268 |
| Proceeds from sale or maturities of investments | 499,557 | 226,667 |
| Purchases of investments | (592,909) | (292,988) |
| Student loans and other loans issued | (1,319) | (3,648) |
| Proceeds from student and other loans | 5,569 | 5,741 |
| Proceeds from sale of property | 4,879 | 1,813 |
| Net cash used in investing activities | <u>(274,025)</u> | <u>(174,340)</u> |
| Cash flows from financing activities | | |
| Increase in refundable advances | 3,601 | 99 |
| Interest and dividends restricted for long-term investments | 715 | 723 |
| Payment to annuitants and life income funds | (1,081) | (967) |
| Contributions for long-term investments | 42,695 | 8,354 |
| Proceeds from sale of restricted contributed securities | 4,105 | 4,952 |
| Payments on capital lease obligation | (1,365) | (1,299) |
| Net proceeds from issuance of long-term debt | 70,349 | - |
| Payments on bonds and notes payable | (22,188) | (24,232) |
| Net cash provided by/ (used in) financing activities | <u>96,831</u> | <u>(12,370)</u> |
| Increase/ (Decrease) in cash and cash equivalents | 98,814 | (62,210) |
| Cash and cash equivalents | | |
| Beginning of the year | <u>239,389</u> | <u>301,599</u> |
| End of the year | <u>\$ 338,203</u> | <u>\$ 239,389</u> |
| Supplemental non-cash financing disclosures | | |
| Proceeds from issuance of debt | \$ 68,315 | - |
| Use of proceeds to refund debt | (68,315) | - |

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

Northeastern University

Notes to Consolidated Financial Statements

June 30, 2019 and 2018

1. Background

Founded in 1898, Northeastern University (“the University” or “Northeastern”) is one of the largest private urban universities in North America. It is a world leader in experiential education, an academic approach that integrates academic study and professional work to ensure a more powerful learning experience. The University is also a leader in the production of use-inspired research that meets societal needs. Northeastern grants associate, bachelor, master and doctoral degrees. The University attracts students from all 50 states within the United States and more than 125 countries, with campuses in Boston, Charlotte, Seattle, the San Francisco Bay Area, Toronto, Vancouver, and London.

2. Summary of Significant Accounting Policies

The significant accounting policies followed by the University are set forth below.

Basis of Presentation

The accompanying consolidated financial statements have been prepared on the accrual basis and in accordance with the reporting standards for not-for-profit organizations and include the University and its subsidiaries, the most significant of which includes a research institute and the New College of the Humanities based in the United Kingdom.

Generally Accepted Accounting Principles (“GAAP”) require classification of net assets and revenues, expenses, gains and losses, based on the existence or absence of donor restrictions. The categories, net assets without donor restrictions and net assets with donor restrictions, are defined as follows:

Net Assets Without Donor Restrictions – Net assets available for general use and not subject to donor-imposed stipulations. Net assets without donor restrictions may be designated for specific purposes by management or the Board of Trustees.

Net Assets With Donor Restrictions - Net assets subject to donor-imposed restrictions. Some donor-imposed restrictions are temporary in nature that may or will be met either by the passage of time or the events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity.

Revenues are reported as increases in net assets without donor restrictions unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in net assets without donor restrictions. Net realized and change in unrealized gains and losses on investments and other assets or liabilities are reported as increases or decreases in net assets without donor restrictions unless their use is restricted by explicit donor stipulation or by law.

Unconditional promises to give (“Pledges”) are recognized as donor restricted revenues in the period received. Pledges are recorded at the present value of expected future cash flows. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Gifts of noncash assets are recorded at their market value at the date of contribution.

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The University has received beneficial interests in irrevocable charitable remainder trusts, for which the University does not serve as the trustee. For these trusts, the University recorded its beneficial interest in those assets as contributions revenue and pledges receivable at the present value of the expected future cash inflows. Trusts are recorded at the date the University has been notified of the trust's existence and sufficient information regarding the trust has been accumulated to form the basis for an accrual. Changes in the value of these assets are recorded as a nonoperating change in the valuation of pledges receivable in net assets with donor restrictions.

Expirations of donor-imposed restrictions on net assets are reported as reclassifications between the applicable classes of net assets in the statement of activities. Gifts with donor-imposed restrictions, which are reported as donor restricted revenues, are released to net assets without donor restrictions when used for an expenditure that satisfies the donor-imposed restriction. Gifts restricted for the purchase of land, buildings and equipment are reported as donor restricted nonoperating revenues and are released to net assets without donor restrictions when the assets are placed into service.

Revenues

Revenues are recognized when control of the promised goods or services is transferred to our customers, in an amount that reflects the consideration the University expects to be entitled to in exchange for those goods or services.

Tuition and fees are derived from students participating in degree programs as well as lifelong learning programs. Tuition is recognized ratably over the academic period of the course or program offered based on time elapsed and financial aid awarded to students reduces the amount of revenue recognized. The University's individual schools have various billing and academic cycles and the majority of our programs are designed to be completed within the fiscal year. Tuition and fees and auxiliary revenues received in advance of services to be rendered are recorded as deferred revenue and student deposits which totaled \$48,498,000 and \$60,573,000 respectively, at June 30, 2019 and 2018.

Scholarships applied to tuition and fees reflect student financial aid funded by the University's operating budget, restricted endowment funds, and federal and state assistance programs. Compensation of students for services provided and tuition benefits for employees are presented as expenses.

The University receives sponsored support from governmental and private sources. Sponsored support primarily consists of contribution revenue, which is recognized when qualifying expenditures are incurred. Sponsored support for which restrictions are met in the same year are reflected in revenues without donor restrictions. Federally funded operating grants and contracts for the years ended June 30, 2019 and 2018 were \$137,917,000 and \$122,110,000, respectively, including indirect costs of \$28,982,000 and \$28,783,000, respectively. Total conditional contributions remaining to be recognized from sponsors at June 30, 2019 equated to \$175,680,000 and primarily relate to support to be received from the federal government. Other sponsored support is considered exchange arrangements, and revenue under these agreements is recognized based on the University's fulfillment of the contract, which is typically based on costs incurred or the achievement of milestones.

Funding received in advance of recognition is recorded as refundable advances. Included in refundable advances at June 30, 2019 and 2018 are \$9,324,000 and \$5,949,000 respectively, of sponsored receipts, that have not been expended but generally are within next year. Indirect cost

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recoveries by the University on U.S. Government contracts and grants are based upon a negotiated rate and are recorded in revenues without donor restrictions.

Auxiliary enterprises include the operation of student housing and dining services, the daycare center and managed properties and are recognized ratably over the period during which the services are provided. Student housing and dining revenues received in advance of services to be rendered are recorded as deferred revenue and student deposits and are reflected above with those deposits related to tuition and fees.

Other revenues are recognized at the point in time goods or services are provided. During fiscal 2019, the University entered into a parking arrangement with a third party. The University received an upfront payment for which deferred revenue of \$144,168,000 was recorded for the year ended June 30, 2019. Deferred revenue recorded will be recognized on a straight-line basis over the fifty year term of the parking arrangement and reflected in other revenues.

Nonoperating activities include all contributions, endowment and other investment return, change in annuity and life income funds, other nonoperating changes, net realized and changes in unrealized gains or losses on interest rate swap agreements, and net assets released from restrictions and other transfers during the period used for current operations. Nonoperating activities also include the portion of the endowment return/(loss) in connection with the University's spending policy in excess of the amount appropriated and other investment return. Contributions available for operations received and spent in the same year are presented as reductions to nonoperating revenues and are reclassified to operating revenues. All other activities are classified as operating. Expenses incurred in carrying out the fundraising activities of the University, amounted to \$22,217,000 and \$22,234,000 for the years ended June 30, 2019 and 2018, respectively.

Certain 2018 amounts have been reclassified to conform to the current year presentation.

The financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the University's financial statements for the year ended June 30, 2018, from which the summarized information was derived.

Cash and Cash Equivalents

Cash and cash equivalents consist primarily of cash management accounts, money market funds and bonds with maturities when purchased of three months or less.

Most of the University's banking activity, including cash and cash equivalents, is conducted with several national banks with investment grade credit ratings. From time to time in the regular course of business deposit amounts exceed federal insurance limits. It is the University's policy to monitor these banks' financial strength and deposit balances on a daily basis and no losses have been experienced to date.

Accounts and Loans Receivable

Accounts receivable are stated net of allowance for doubtful accounts of \$9,488,000 and \$10,979,000 at June 30, 2019 and 2018, respectively. Loans receivable are stated net of allowance for doubtful accounts of \$687,000 at June 30, 2019 and 2018. Loans receivable are principally amounts due from students under Federally Sponsored Loan Programs, which are subject to significant restrictions; accordingly, it is not practical to determine the fair value of such amounts.

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The University records an allowance for doubtful accounts for student and other loans receivables including those under the Federal Perkins Loan Program. Management regularly assesses the adequacy of the allowance for credit losses by performing evaluations on the student loan portfolio, current economic environment, and level of delinquent loans. The allowance is adjusted based on the results of these evaluations. Loans disbursed under the Federal Perkins Loan Program are able to be assigned to the Federal government in certain nonrepayment situations. Management believes that this allowance at June 30, 2019 and 2018 is adequate to absorb credit losses inherent in the portfolio as of that date.

Investments

Investments include cash and cash equivalents which are designated for long-term investment by the University. They also include fixed income and equity portfolios with broadly defined investment strategies. Managers of these portfolios may utilize hedging strategies, invest in securities denominated in foreign currencies, or invest in options, futures, forward contracts, or other financial instruments whose value and performance are derived, at least in part, from the performance of an underlying asset or index and the creditworthiness of the counterparty to the transactions. The University also invests in a number of limited partnerships which sell securities short and which use leverage.

All investments are carried at estimated fair value.

Net investments return (loss) is reported in the statements of activities and consists of interest and dividends, realized and unrealized capital gains and losses, less external and direct internal investment expenses.

Gains and losses upon sale of certain investments are calculated using average cost at trade date.

Property, Plant and Equipment

Property, plant and equipment are stated at cost on the date of acquisition, net of accumulated depreciation. Plant assets donated to the University are stated at fair market value on the date of the gift, net of subsequent accumulated depreciation.

Depreciation is calculated using the straight-line method over the following estimated useful lives:

| | |
|--------------------------------|------------|
| Buildings | 50 years |
| Building improvements | 30 years |
| Furniture, equipment and books | 5–20 years |
| Software | 4–7 years |

Expenditures for maintenance and repairs are charged to operations as incurred; significant renewals and betterments are capitalized. Costs associated with construction of new facilities are reported as construction in progress until such projects are completed.

Conditional Asset Retirement Obligations

The University recognizes the fair value of a liability for legal obligations associated with asset retirements in the period in which the obligation is incurred. When the liability is initially recorded, the cost of the asset retirement obligation is capitalized by increasing the carrying amount of the related long-lived asset. The liability is accreted to its present value each period, and the capitalized cost associated with the retirement obligation is depreciated over the useful life of the related asset. Upon settlement of the obligation, any difference between the cost to settle the

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asset retirement obligation and the liability recorded is recognized as a gain or loss in the consolidated statement of activities.

The University recognized \$1,228,000 and \$1,196,000 of operating expenses related to the accretion of liabilities recorded for the years ended June 30, 2019 and 2018, respectively. Conditional asset retirement obligations of \$23,785,000 and \$23,438,000 at June 30, 2019 and 2018, respectively, are included in accounts payable and accrued liabilities on the consolidated statement of financial position.

Net Investment in Plant

Net investment in plant includes the net book value of all capital assets offset by outstanding liabilities associated with those capital assets. Capital assets include prepaid assets, and property, plant and equipment (net of accumulated depreciation). Outstanding liabilities include the conditional asset retirement obligation, accounts payable associated with construction projects, premiums, unamortized debt issuance costs and discounts on bonds and notes payables, capital lease obligation and outstanding bonds and notes payable, including amounts of the associated interest rate swap agreement.

Endowment

The endowment includes both donor-restricted funds and funds designated by the Board of Trustees ("the Board") to function as endowments. The net assets associated with endowment funds, including funds designated by the Board to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions in accordance with the laws of the Commonwealth of Massachusetts.

The Board has interpreted the Massachusetts Uniform Prudent Management of Institutional Funds Act ("UPMIFA" or "Act") for donor-restricted endowment funds as requiring the preservation of the original value of gifts, as of the gift date, to donor-restricted endowment funds, absent explicit donor stipulations to the contrary. The University retains in perpetuity: (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund, if any. Collectively these amounts are referred to as the historic dollar value of the fund.

In accordance with the Act, the University considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: the duration and preservation of the fund; the purposes of the donor-restricted endowment fund; general economic conditions; the possible effect of inflation and deflation; the expected total return from income and the appreciation of investments; other resources available; and investment policies.

Net assets without donor restrictions include funds designated by the Board to function as endowments.

The University has adopted endowment investment and spending policies that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of endowment assets. To achieve 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 gains) and current yield (interest and dividends). The University expects its endowment funds, over time, to provide an average real rate of return of approximately 4% annually.

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The University's endowment spending policy is calculated using 4% of a sixty-month moving average of the endowment fund's market value. This amount is distributed to the appropriate funds and treated as operating revenue in the statement of activities. These distributions consist of dividends, interest and, if necessary, a portion of accumulated investment gains. The amount distributed each year is subject to the Board's approval. During both fiscal years 2019 and 2018, the full payout amount was distributed.

From time to time, certain donor-restricted endowment funds may have fair values less than the amount required to be maintained by donors or by law (underwater endowments). These deficits usually result from unfavorable market fluctuations that generally occur shortly after the investment of recently established endowments. The University has interpreted UPMIFA to permit spending from underwater endowments in accordance with prudent measures required under law.

There are no underwater endowment funds at June 30, 2019 and 2018.

Tax Status

The University and its subsidiaries are tax-exempt organizations as described in section 501(c)(3) of the Internal Revenue Code.

GAAP requires that the University evaluate tax positions taken by the University and recognize a tax liability (or asset) if the University has taken an uncertain position that more likely than not would not be sustained upon examination by the Internal Revenue Service. The University has analyzed the tax positions taken and has concluded that as of June 30, 2019, there are no significant uncertain tax positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the financial statements.

The Tax Cuts and Jobs Act (the "Act") was enacted on December 22, 2017. The Act impacts the University in several ways, including a new excise tax on executive compensation, increases to unrelated business taxable income ("UBTI") by the amount of certain fringe benefits for which a deduction is not allowed, changes to the net operating loss rules, repeal of the alternative minimum tax, and the computation of UBTI separately for each unrelated trade or business. Further, the Act reduces the US federal corporate tax rate and federal corporate unrelated business income tax rate from 35% to 21%. The overall impact of the Act remains uncertain and the full impact of the Act will not be known until further regulatory guidance is provided to assist the University with calculating income and excise tax liabilities. The University continues to evaluate the impact of tax reform on the organization.

Use of Estimates

The preparation of consolidated financial statements in accordance with GAAP requires management to make estimates and assumptions that affect reported amounts and disclosures. Actual results may differ from these estimates.

Recently Adopted Accounting Pronouncements

On July 1, 2018, the University adopted Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers (Topic 606) and Other Assets and Deferred Costs—Contracts with Customers (Subtopic 340-40)*, which outlines a single comprehensive framework for revenue recognition across all industries and supersedes most existing revenue recognition guidance. In addition, ASU 2014-09 requires new and enhanced disclosures. These changes do not have a material impact on the University's financial statements and have been applied to the University's financial statements and footnotes on a modified retrospective basis.

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On July 1, 2018, the University adopted ASU No.2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*, which amends the accounting guidance related to (1) evaluating whether transactions should be accounted for as contributions or exchange transactions, and (2) determining whether a contribution is conditional. The University has evaluated and applied the guidance on a modified prospective basis to the financial statements and added the required additional revenue disclosures. The adoption of this standard did not have a significant impact on the University's financial statements.

On July 1, 2018, the University adopted ASU 2016-14, *Presentation of Financial Statements for Not-for-Profit Entities*. The guidance is intended to improve the net asset classification requirements and the information presented in the financial statements and notes about a not-for-profit entity's liquidity, financial performance, and cash flows. The main provision of this guidance includes the presentation of two classes of net assets versus the previously required three. The guidance also enhances disclosures for liquidity and expenses by both their natural and functional classifications. These changes are reflected in the University's financial statement and footnotes and have been applied retrospectively, where applicable.

On July 1, 2018, the University adopted ASU 2018-13 - *Fair Value Measurement (Topic 820): Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement*. Following this new guidance, the University is no longer required to disclose the amount of and reasons for transfers between Level 1 and Level 2 of the fair value hierarchy. For investments in certain entities that calculate net asset value, the requirement to disclose the estimated period of time over which the underlying assets might be liquidated is modified to only require disclosure if the investee has communicated the timing to the University or announced the timing publicly.

New Accounting Pronouncements

In January 2016, the FASB issued ASU 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*, which address certain aspects of recognition, measurement, presentation and disclosure of financial instruments. This guidance allows an entity to choose, investment-by-investment, to report an equity investment that neither has a readily determinable fair value, nor qualifies for the practical expedient for fair value estimation using NAV, at its cost minus impairment (if any), plus or minus changes resulting from observable price changes in orderly transactions for the identical or similar investment of the same issue. Impairment of such investments must be assessed qualitatively at each reporting period. Entities must disclose their financial assets and liabilities by measurement category and form of asset either on the face of the statement of financial position or in the accompanying notes. The ASU is effective for the University beginning in fiscal year 2020. The University is evaluating the impact of the new guidance on the financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases*, which, requires a lessee to recognize a right-of-use asset and a lease liability, initially measured at the present value of the lease payments, in its balance sheet. The guidance also expands the required quantitative and qualitative disclosures surrounding leases. This ASU is effective for the University beginning fiscal year 2020. The University is evaluating the impact of the new guidance on the financial statements.

In March 2017, the FASB issued final guidance on ASU 2017-07, *Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. Net benefit cost is currently reported as an operating expense. The amendment requirements the bifurcation of net benefit cost. The service cost component will be presented with other employee costs in operating expenses. The other components will be reported separately outside of operations, and will not be eligible for capitalization. The ASU is

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effective for the University beginning in fiscal year 2020. The adoption of the new guidance is not expected to have a material impact on the University's financial statements.

3. Available Resources and Liquidity

As of June 30, 2019, the following table shows the total financial assets held by the University and the amounts of those financial assets could readily be made available within one year of the Statement of Financial Position date to meet expenditures:

(in thousands of dollars)

| Financial assets available to meet general expenditures over the next 12 months | 2019 |
|--|-------------------|
| Cash and cash equivalents | \$ 338,203 |
| Accounts and other receivables, net | 87,927 |
| Pledges receivable due in 1 year or less available for expenditures | 11,239 |
| Forecasted endowment spending available for operations | 33,786 |
| Other investments not invested in the endowment | 181,476 |
| | <u>\$ 652,631</u> |

Northeastern regularly monitors liquidity required to meet its operating needs and other contractual commitments, while also striving to maximize the investment of its available funds. When reviewing available resources required to meet its expenditures over a 12-month period, the University considers all expenditures related to its ongoing activities.

In addition to financial assets available to meet expenditures over the next 12 months, the University operates with a balanced budget and anticipates collecting sufficient revenue to cover expenditures not covered by donor-restricted resources. Refer to the Consolidated Statements of Cash Flows which identify the sources and uses of the University's cash and show positive cash generated by operations for fiscal years 2019 and 2018.

Additionally, the University has quasi endowment assets of \$639,095,000 as of June 30, 2019. Although the University does not intend to spend from its quasi endowment funds other than amounts appropriated for general expenditures as part of its annual budget approval and appropriation process, amounts from its quasi endowment could be made available if necessary. However, these funds contain investments with lock-up provisions that reduce the total investments that could be made available (Please see Note 4 for disclosures about investments).

4. Fair Value Measurements

The University values its financial assets and liabilities at fair value in accordance with GAAP. GAAP defines fair value, establishes a framework for measuring fair value, and delineates the disclosures required about fair value measurements. Financial assets consist primarily of the endowment and other investments. Additionally, GAAP allows the University the use of estimates to fair value alternative investments at the measurement date using net asset values ("NAV") reported by the investment managers without further adjustment, provided that the University does not expect to sell the alternative investments at a value other than the NAV. The University performs due diligence procedures on its alternative investments to determine if the values recorded are appropriate.

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GAAP clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. The University uses valuation techniques to measure fair value on investments that maximize use of observable inputs and minimize the use of unobservable inputs. As a basis for considering assumptions, this standard establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

- Level 1 Valuations using quoted prices in active markets for identical assets or liabilities. Valuations of these products do not require a significant degree of judgment.
- Level 2 Valuations using observable inputs other than Level 1 prices such as quoted prices in active markets for similar assets or liabilities; quoted prices for identical or similar assets or liabilities in markets that are not active; broker or dealer quotations; or other inputs that are observable or can be corroborated by observable market data for substantially the same term of the assets or liabilities.
- Level 3 Valuations using unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

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The following table presents information about assets and liabilities that are measured at fair value on a recurring basis as of June 30, 2019, and indicates the fair value hierarchy utilized to determine such fair value:

| | Fair Value Measurements at the End of the Reporting Period Using | | | |
|--|--|---|---|--|
| | 6/30/2019 | Quoted Prices in Active Markets for Identical Assets Level 1 | Significant Other Observable Inputs Level 2 | Significant Unobservable Inputs Level 3 |
| <i>(in thousands of dollars)</i> | | | | |
| Beneficial interest in charitable remainder trust investments | \$ 4,498 | \$ - | \$ - | \$ 4,498 |
| Endowment investments | | | | |
| Cash equivalents | 73,852 | 73,852 | - | - |
| Fixed income | 78,307 | 78,307 | - | - |
| Domestic equity | 225,695 | 225,695 | - | - |
| International equity | 139,244 | 139,244 | - | - |
| Private equity at NAV (a) | 179,417 | - | - | - |
| Hedge funds at NAV (a) | 356,315 | - | - | - |
| Other alternative investments at NAV (a) | 21,762 | - | - | - |
| Total endowment investments | <u>1,074,592</u> | <u>517,098</u> | <u>-</u> | <u>-</u> |
| Other investments | | | | |
| Fixed income | 180,223 | 180,223 | - | - |
| Domestic equity | 1,253 | 1,253 | - | - |
| Auction rate securities and other | 17,000 | - | - | 17,000 |
| Total other investments | <u>198,476</u> | <u>181,476</u> | <u>-</u> | <u>17,000</u> |
| Total investments | <u>1,273,068</u> | <u>698,574</u> | <u>-</u> | <u>17,000</u> |
| Total assets | <u>\$ 1,277,566</u> | <u>\$ 698,574</u> | <u>\$ -</u> | <u>\$ 21,498</u> |
| Interest rate swap agreements – liability | \$ (49,219) | \$ - | \$ (49,219) | \$ - |
| Total liabilities | <u>\$ (49,219)</u> | <u>\$ -</u> | <u>\$ (49,219)</u> | <u>\$ -</u> |

- a) Certain investments that are measured at fair value using the NAV per share (or its equivalent) as a practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

Excluded from the fair value hierarchy at June 30, 2019 are \$179,417,000 of private equity, \$356,315,000 of hedge funds and \$21,762,000 of other alternative investments for which fair value is measured at NAV per share using the practical expedient.

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The following table presents information about assets and liabilities that are measured at fair value on a recurring basis as of June 30, 2018, and indicates the fair value hierarchy utilized to determine such fair value:

| | 6/30/2018 | Fair Value Measurements at the End of the Reporting Period Using | | |
|--|--------------|--|---|---|
| | | Quoted Prices in Active Markets for Identical Assets Level 1 | Significant Other Observable Inputs Level 2 | Significant Unobservable Inputs Level 3 |
| <i>(in thousands of dollars)</i> | | | | |
| Beneficial interest in charitable remainder trust investments | \$ 4,153 | \$ - | \$ - | \$ 4,153 |
| Endowment investments | | | | |
| Cash equivalents | 78,342 | 78,342 | - | - |
| Fixed income | 60,041 | 60,041 | - | - |
| Domestic equity | 107,931 | 107,931 | - | - |
| International equity | 160,348 | 160,348 | - | - |
| Other investments | 20,067 | 20,067 | - | - |
| Private equity at NAV (b) | 143,048 | - | - | - |
| Hedge funds at NAV (b) | 254,959 | - | - | - |
| Other alternative investments at NAV (b) | 23,020 | - | - | - |
| Total endowment investments | 847,756 | 426,729 | - | - |
| Other investments | | | | |
| Fixed income | 246,515 | 246,515 | - | - |
| Domestic equity | 1,899 | 1,899 | - | - |
| Auction rate securities and other | 17,000 | - | - | 17,000 |
| Total other investments | 265,414 | 248,414 | - | 17,000 |
| Total investments | 1,113,170 | 675,143 | - | 17,000 |
| Total assets | \$ 1,117,323 | \$ 675,143 | \$ - | \$ 21,153 |
| Interest rate swap agreements – liability | \$ (36,458) | \$ - | \$ (36,458) | \$ - |
| Total liabilities | \$ (36,458) | \$ - | \$ (36,458) | \$ - |

- b) Certain investments that are measured at fair value using the NAV per share (or its equivalent) as a practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

Excluded from the fair value hierarchy at June 30, 2018 are \$143,048,000 of private equity, \$254,959,000 of hedge funds and \$23,020,000 of other alternative investments for which fair value is measured at NAV per share using the practical expedient.

All financial instruments are valued using a market approach involving identical or comparable assets or liabilities except for auction rate securities and the University's beneficial interest in charitable remainder trusts, which are valued using an income approach.

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At June 30, 2019, the change in the fair value of financial instruments valued using significant unobservable inputs (Level 3) is shown below:

| <i>(in thousands of dollars)</i> | Auction Rate Securities and Other | Beneficial Interest in Charitable Remainder Trust | Total |
|---|--|--|------------------|
| Fair value recorded at June 30, 2017 | \$ 17,221 | \$ 4,240 | \$ 21,461 |
| Sale | (221) | - | (221) |
| Unrealized losses | - | (87) | (87) |
| Fair value recorded at June 30, 2018 | 17,000 | 4,153 | 21,153 |
| Unrealized gains | - | 345 | 345 |
| Fair value recorded at June 30, 2019 | <u>\$ 17,000</u> | <u>\$ 4,498</u> | <u>\$ 21,498</u> |

The fair values of marketable domestic and international equities and fixed income instruments are determined generally based on quoted market prices in active markets. Alternative investments include private equity funds, hedge funds and other alternative investments. Private equity investments may consist of commitments in a limited partnership that invests in private companies or properties. Hedge funds may include investments that are publicly traded and may be subject to redemption restrictions.

At June 30, 2019, liquidity terms for investments consist of the following:

| <i>(in thousands of dollars)</i> | Within 30 Days | 31-60 Days Prior Written Notice | 61-90 Days Prior Written Notice | 91-180 Days Prior Written Notice | 181-365 Days Prior Written Notice | 1-5 Years | 6-10 Years | Total |
|----------------------------------|-----------------------|--|--|---|--|------------------|-------------------|---------------------|
| Cash equivalents | \$ 73,852 | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - | \$ 73,852 |
| Fixed income | 258,530 | - | - | - | - | - | - | 258,530 |
| Domestic equity | 226,948 | - | - | - | - | - | - | 226,948 |
| International equity | 139,244 | - | - | - | - | - | - | 139,244 |
| Private equity | - | - | - | - | - | - | 179,417 | 179,417 |
| Hedge funds | 146,342 | 38,171 | 2,088 | 47,930 | 84,864 | 35,731 | 1,189 | 356,315 |
| Other alternative investments | - | 21,762 | - | - | - | - | - | 21,762 |
| Other investments | - | - | - | - | - | - | 17,000 | 17,000 |
| | <u>\$ 844,916</u> | <u>\$ 59,933</u> | <u>\$ 2,088</u> | <u>\$ 47,930</u> | <u>\$ 84,864</u> | <u>\$ 35,731</u> | <u>\$ 197,606</u> | <u>\$ 1,273,068</u> |

The University is the beneficiary of various charitable remainder trusts held and administered by outside trustees. A receivable is recorded at the present value of the amount held by the trustees that is due to the University, which is calculated using the life expectancy of the beneficiaries. Valuations are reviewed annually by management by updating life expectancy of the beneficiaries, discount rates and the fair value of the underlying investments. The discount rates used for the years ended June 30, 2019 and 2018 ranges from 1.76% to 2.91% based on 10 year daily treasury yield curve rates.

The University's auction rate securities at June 30, 2019 and 2018 were determined to have a fair value of \$17,000,000, and were reflective of a \$3,000,000 discount. The auction rate securities are valued using the income approach, specifically a discounted cash flow analysis. This valuation methodology includes utilizing unobservable inputs such as offered quotes and comparability adjustments to arrive at the estimated fair value. The University performs ongoing due diligence to determine that the auction rate securities' fair value is reasonable.

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The estimated fair value of the interest rate swap agreement is based on an independent third party valuation. The fair value of swap instruments represents the estimated cost to the University to cancel the agreements at the reporting date. The University has performed due diligence on the fair value of its interest rate swap agreement to determine fair value at June 30, 2019 and 2018.

5. Pledges Receivable

Pledges receivable as of June 30 are expected to be realized in the following time periods:

| <i>(in thousands of dollars)</i> | 2019 | 2018 |
|--------------------------------------|-------------------|------------------|
| One year or less | \$ 31,940 | \$ 30,492 |
| Between one and five years | 68,843 | 48,438 |
| Greater than five years | <u>18,146</u> | <u>23,592</u> |
| | 118,929 | 102,522 |
| Less: Discount | (10,268) | (9,396) |
| Less: Allowance for doubtful pledges | <u>(5,008)</u> | <u>(4,862)</u> |
| | <u>\$ 103,653</u> | <u>\$ 88,264</u> |

At June 30, 2019, the University has a \$2,000,000 conditional pledge that is not reflected in the consolidated financial statements due to its conditional nature.

6. Investments

Investments, stated at fair value, held by the University at June 30 were as follows:

| <i>(in thousands of dollars)</i> | 2019 | 2018 |
|----------------------------------|---------------------|---------------------|
| Cash equivalents | \$ 73,852 | \$ 78,342 |
| Fixed income | 258,530 | 306,556 |
| Domestic equity | 226,948 | 109,830 |
| International equity | 139,244 | 160,348 |
| Private equity | 179,417 | 143,048 |
| Hedge funds | 356,315 | 254,959 |
| Other alternative investments | 21,762 | 23,020 |
| Other investments | <u>17,000</u> | <u>37,067</u> |
| | <u>\$ 1,273,068</u> | <u>\$ 1,113,170</u> |

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The unfunded commitments, consisting of commitments that the University has made to various private equity investments at June 30, 2019 are listed below. These funds may be called for a period to extend between one and fifteen years.

| <i>(in thousands of dollars)</i> | 2019 |
|----------------------------------|-------------------|
| Venture capital | \$ 106,621 |
| Real estate | 14,765 |
| Energy & commodities | <u>13,364</u> |
| | <u>\$ 134,750</u> |

7. Property, Plant and Equipment

Property, plant and equipment at June 30 consisted of the following:

| <i>(in thousands of dollars)</i> | 2019 | 2018 |
|----------------------------------|---------------------|---------------------|
| Land | \$ 28,498 | \$ 28,554 |
| Building and improvements | 1,894,749 | 1,756,507 |
| Capitalized lease | 37,928 | 38,410 |
| Furniture and equipment | 302,160 | 287,735 |
| Library books | 59,685 | 57,069 |
| Construction in progress | <u>49,870</u> | <u>34,395</u> |
| | 2,372,890 | 2,202,670 |
| Less: Accumulated depreciation | <u>(829,224)</u> | <u>(771,033)</u> |
| | <u>\$ 1,543,666</u> | <u>\$ 1,431,637</u> |

Depreciation expense amounted to \$69,359,000 and \$63,741,000 for the years ended June 30, 2019 and 2018, respectively, and is allocated in the consolidated statement of activities to functional expenses based on specific use of the related facilities. Operation, maintenance and security of plant expense totaled \$84,137,000 and \$83,633,000 for the years ended June 30, 2019 and 2018, respectively, and is allocated to functional expense categories in the consolidated statement of activities based on salary expense.

8. Capitalized Lease

The University commenced the residence hall lease in July 2001. The rent, over the 30-year term of the lease, is equal to the actual debt service plus customary fees payable with respect to the \$31,130,000 principal amount of the bonds issued to finance the building. The annual lease commitments for future years, principal plus interest, range from \$2,610,000 in 2020 to \$2,576,000 in 2032.

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Approximate future annual principal requirements as of June 30, 2019 are as follows:

| <i>(in thousands of dollars)</i> | Principal Payments |
|----------------------------------|-------------------------------|
| Year | |
| 2020 | \$ 1,433 |
| 2021 | 1,505 |
| 2022 | 1,581 |
| 2023 | 1,661 |
| 2024 | 1,744 |
| 2025-2032 | 14,933 |
| | <u>\$ 22,857</u> |

9. Bonds and Notes Payable

Bonds and notes payable consists of the following at June 30:

(in thousands of dollars)

| | Rate | Maturity | 2019 | 2018 |
|---|--------------|-----------------|-------------------|-------------------|
| Massachusetts Development Finance Agency | | | | |
| Series R (par value, \$89,615) | 4.50%-5.00% | 2019 | \$ - | \$ 68,315 |
| Series T-1 (par value, \$63,260) | 2.00%-5.00% | 2037 | 61,085 | 61,460 |
| Series T-2 (par value, \$66,315) | 3.00%-5.00% | 2037 | 64,140 | 64,515 |
| Series T-3 (par value, \$70,000) | Variable | 2019 | 67,850 | 68,225 |
| Series Y-1 (par value, \$38,280) | 5.00%-5.62% | 2029 | 25,260 | 26,910 |
| Series Y-2 (par value, \$25,545) | 5.00%-5.50% | 2024 | 8,720 | 9,935 |
| Series 2010A (par value, \$251,635) | 3.00%-5.00% | 2035 | 179,315 | 189,230 |
| Series 2012 (par value, \$54,385) | 4.00%-5.00% | 2035 | 54,385 | 54,385 |
| Series 2014A (par value, \$150,000) | 4.37%-5.25% | 2044 | 150,000 | 150,000 |
| Series 2018A (par value, \$61,005) | 3.00%-5.00% | 2034 | 61,005 | - |
| Taxable Revenue Bonds | | | | |
| Series 2010B (par value, \$75,460) | 3.35%-6.43% | 2035 | 57,855 | 61,010 |
| Series 2014B (par value, \$100,000) | 0.098%-5.28% | 2032 | 80,795 | 85,730 |
| Series 2018B (par value, \$70,415) | 4.12% | 2049 | 70,415 | - |
| Other Notes Payable | 2.50% | 2020 | 125 | 319 |
| | | | <u>880,950</u> | <u>840,034</u> |
| Add: Unamortized Premium on Bonds | | | 21,925 | 16,932 |
| Less: Unamortized Discount on Bonds | | | (3,152) | (2,903) |
| Less: Unamortized Issuance Cost on Bonds | | | (1,694) | (1,700) |
| | | | <u>\$ 898,029</u> | <u>\$ 852,363</u> |

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Approximate future annual principal requirements are below:

| <i>(in thousands of dollars)</i> | Principal Payments |
|----------------------------------|-------------------------------|
| Year | |
| 2020 | \$ 26,040 |
| 2021 | 27,085 |
| 2022 | 28,375 |
| 2023 | 29,785 |
| 2024 | 31,200 |
| Thereafter | 738,465 |
| | <u>\$ 880,950</u> |

The tables above reflect the contractual maturities of the debt agreements which were effective as of June 30, 2019.

On July 3, 2018, the University issued \$70,415,000 in US Bank National Association taxable bonds Series 2018B for the purpose of financing the Innovation Campus located on the Burlington, Massachusetts campus, various renovations on the main campus in Boston, Massachusetts, and other future capital projects. Principal payments commence in October 2044 with final tender in October 2048.

On July 25, 2018, the Massachusetts Development Finance Agency (“MDFA”) Series 2018A bonds were issued in the amount of \$61,005,000. The proceeds were used to refund MDFA Series R bond for \$68,315,000. The MDFA Series 2018A bonds were issued with an original issuance premium of \$9,261,000. Principal payments commence in October 2019 with final tender in October 2033.

Interest expense on bonds and notes payable totaled \$38,575,000 and \$37,775,000 for the years ended June 30, 2019 and 2018, respectively. Interest expense has been allocated to each functional expense category in the consolidated statement of activities based on specific identification. Total amounts paid in 2019 and 2018 were \$45,994,000 and \$45,109,000, respectively, to meet interest costs including settlement costs on the related interest rate swap agreement.

The University entered into an interest rate swap agreement on December 22, 2006 to manage the interest cost and variable rate risk associated with its Series T3 outstanding debt. The interest rate swap agreement was not entered into for trading or speculative purposes. Under the terms of the agreement, the University pays a fixed rate, determined at inception, to a third party who in turn pays the University a variable rate on these respective notional principal amounts.

The University records the interest rate swap at fair value. Net payments or receipts under the swap agreement along with the change in fair value of the swap are included in the nonoperating section on the consolidated statement of activities.

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The University has applied guidance related to the *Disclosures about Derivative Instruments and Hedging Activity*. Under this guidance, the University is required to disclose the location and amounts of derivatives within the consolidated financial statements. The tables below depict the impact the derivative has on both the consolidated statements of financial position and consolidated statements of activities.

| <i>(in thousands of dollars)</i> | June 30, 2019 Fair Value | June 30, 2018 Fair Value |
|--|---|---|
| Interest rate swap agreement (liability) | \$ (49,219) | \$ (36,458) |

Net realized and unrealized (loss)/gain on the interest rate swap recorded in the consolidated statement of activities as nonoperating was as follows for the years ended June 30, 2019 and 2018:

| <i>(in thousands of dollars)</i> | 2019 | 2018 |
|----------------------------------|--------------------|-----------------|
| Realized loss | \$ (4,312) | \$ (5,534) |
| Change in unrealized (loss)/gain | <u>(12,761)</u> | <u>12,356</u> |
| | <u>\$ (17,073)</u> | <u>\$ 6,822</u> |

The following schedule presents the notional principal amounts and fair value of the University's interest rate swap agreement at June 30, 2019:

| <i>(in thousands of dollars)</i> | | | | | |
|----------------------------------|---------------------|-------------------|------------------------|---|------------------------------------|
| Bond Issue | Counterparty | Trade Type | Notional Amount | Date Expiration October 1, | Fair Value at June 30, 2019 |
| MDFA Series T | AIG | Swap | \$ 203,500 | 2037 | \$ (49,219) |

There is no collateral posting requirement for the University related to the swap with AIG.

The University maintained a line of credit in the aggregate amount of \$50,000,000 for which there was no amount outstanding for the years ended June 30, 2019 and 2018.

On October 1, 2019, the Massachusetts Health and Educational Facilities Authority Revenue Bonds, Series Y-1 and Y-2 were redeemed for the amounts of \$7,470,000 and \$23,530,000, respectively. The University financed the \$31,000,000 redemption utilizing its line of credit.

10. Retirement Plan

The University sponsors a retirement plan under which full-time faculty and staff may elect to contribute an amount of their eligible compensation up to the Internal Revenue Service published limit toward the purchase of contracts with Teachers Insurance and Annuity Association of America and College Retirement Equities Fund and/or Fidelity Management Trust Company. After two years of employment, the University contributes 10% of each participant's eligible compensation to each participant's account providing that the participant contributes a minimum of 5% of eligible compensation to the plan. The cost of the University's contribution to this plan was \$33,499,000 and \$31,505,000 for the years ended June 30, 2019 and 2018, respectively.

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11. Post-Retirement Medical Plan

The University sponsors a post-retirement medical plan under which faculty and staff who are 55 years of age and have at least 10 years of service can participate. Under the plan, retirees can contribute 50% of the premium for the medical plan selected. The plan is provided for pre-Medicare coverage and such coverage terminates at age 65. Spouses and dependent children may elect coverage under the plan by contributing 100% of the premium. Spouses are eligible until they are able to participate in Medicare and dependent children until age 26.

For the year ended June 30, 2019 and 2018, net periodic post-retirement medical benefits cost includes the following:

| <i>(in thousands of dollars)</i> | 2019 | 2018 |
|----------------------------------|-----------------|-----------------|
| Service cost | \$ 781 | \$ 803 |
| Interest cost | 470 | 447 |
| | <u>\$ 1,251</u> | <u>\$ 1,250</u> |

Changes in the post-retirement medical benefit obligations are as follows:

| <i>(in thousands of dollars)</i> | 2019 | 2018 |
|---|------------------|------------------|
| Benefit obligations at beginning of year | \$ 12,792 | \$ 14,303 |
| Service cost | 781 | 803 |
| Interest cost | 470 | 447 |
| Participant contributions | 551 | 583 |
| Actuarial loss (gain) | 476 | (1,828) |
| Benefits paid | <u>(1,503)</u> | <u>(1,516)</u> |
| Benefit obligations at end of year | <u>\$ 13,567</u> | <u>\$ 12,792</u> |

These costs are allocated to the functional expense categories in the statement of activities based on salary expense. The accrued post-retirement benefit obligation in the table above is included in accounts payable and accrued liabilities on the consolidated statement of financial position. The plan does not hold assets and is funded as benefits are paid.

For measurement purposes, the assumed annual rate of increase in the per capita cost of covered medical benefits was 6.00% for the year ending June 30, 2019, graded down ratably until reaching an ultimate medical trend rate of 3.50% for fiscal year 2027 and thereafter. The discount rate used to determine the accumulated benefit obligation is 2.96% and 3.82% as of June 30, 2019 and 2018, respectively. The discount rate used to determine the net periodic post-retirement benefit cost is 3.82% and 3.23% for the years ended June 30, 2019 and 2018, respectively. The cumulative amount in net assets without donor restrictions related to unamortized gains is \$143,000 as of June 30, 2019.

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Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plan. A one-percentage point change in assumed health care cost trend rates would have the following effect:

| <i>(in thousands of dollars)</i> | 2019 | 2018 |
|---|-------------|-------------|
| Impact of 1% increase in health care cost trend | | |
| on interest cost plus service cost during the past year | \$ 171 | \$ 151 |
| on accumulated post-retirement benefit obligation | 1,117 | 1,009 |
| Impact of 1% decrease in health care cost trend | | |
| on interest cost plus service cost during the past year | (149) | (132) |
| on accumulated post-retirement benefit obligation | (999) | (905) |

Expected future benefit payments and cash contributions to the plan are as follows:

| <i>(in thousands of dollars)</i> | Future Benefit Payments |
|----------------------------------|--|
| Year | |
| 2020 | \$ 1,048 |
| 2021 | 974 |
| 2022 | 911 |
| 2023 | 914 |
| 2024 | 952 |
| 2025-2029 | 5,923 |
| | <u>\$ 10,722</u> |

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12. Net Assets

The University's net assets are summarized as follows as of June 30:

| <i>(in thousands of dollars)</i> | 6/30/2019 | | |
|---|---------------------------------------|------------------------------------|---------------------|
| | Without Donor Restrictions | With Donor Restrictions | Total |
| Operating funds | | | |
| Net invested in plant | \$ 599,216 | \$ - | \$ 599,216 |
| Other unrestricted | 189,444 | - | 189,444 |
| Donor restricted for: | | | |
| Instruction and academic administration | - | 42,611 | 42,611 |
| Research | - | 11,876 | 11,876 |
| Scholarships, fellowships and other aid | - | 21,449 | 21,449 |
| Capital construction and maintenance | - | 3,593 | 3,593 |
| Other programs | - | 25,510 | 25,510 |
| Total operating funds | <u>788,660</u> | <u>105,039</u> | <u>893,699</u> |
| Endowment and life income funds: | | | |
| Quasi endowment funds | 639,095 | - | 639,095 |
| Donor restricted for : | | | |
| Instruction and academic administration | - | 203,646 | 203,646 |
| Research | - | 35,656 | 35,656 |
| Scholarships, fellowships and other aid | - | 210,309 | 210,309 |
| Capital construction and maintenance | - | 2,654 | 2,654 |
| Other programs | - | 25,923 | 25,923 |
| Life income funds | - | 12,975 | 12,975 |
| Total endowment and life income funds | <u>639,095</u> | <u>491,163</u> | <u>1,130,258</u> |
| Total net assets | <u>\$ 1,427,755</u> | <u>\$ 596,202</u> | <u>\$ 2,023,957</u> |

| <i>(in thousands of dollars)</i> | 6/30/2018 | | |
|---|---------------------------------------|------------------------------------|---------------------|
| | Without Donor Restrictions | With Donor Restrictions | Total |
| Operating funds | | | |
| Net invested in plant | \$ 542,288 | \$ - | \$ 542,288 |
| Other unrestricted | 263,937 | - | 263,937 |
| Donor restricted for: | | | |
| Instruction and academic administration | - | 44,264 | 44,264 |
| Research | - | 12,920 | 12,920 |
| Scholarships, fellowships and other aid | - | 20,048 | 20,048 |
| Capital construction and maintenance | - | 7,887 | 7,887 |
| Other programs | - | 20,651 | 20,651 |
| Total operating funds | <u>806,225</u> | <u>105,770</u> | <u>911,995</u> |
| Endowment and life income funds: | | | |
| Quasi endowment funds | 472,991 | - | 472,991 |
| Donor restricted for : | | | |
| Instruction and academic administration | - | 165,654 | 165,654 |
| Research | - | 23,912 | 23,912 |
| Scholarships, fellowships and other aid | - | 197,887 | 197,887 |
| Capital construction and maintenance | - | 2,588 | 2,588 |
| Other programs | - | 7,415 | 7,415 |
| Life income funds | - | 11,547 | 11,547 |
| Total endowment and life income funds | <u>472,991</u> | <u>409,003</u> | <u>881,994</u> |
| Total net assets | <u>\$ 1,279,216</u> | <u>\$ 514,773</u> | <u>\$ 1,793,989</u> |

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13. Endowment and Similar Net Assets

Changes in endowment and similar net assets for the fiscal year ended June 30, 2019:

| <i>(in thousands of dollars)</i> | Without Donor Restrictions | With Donor Restrictions | Total |
|---|---------------------------------------|------------------------------------|---------------------|
| Endowment and similar net assets at July 1, 2018 | \$ 472,991 | \$ 409,003 | \$ 881,994 |
| Total endowment return | 36,076 | 26,510 | 62,586 |
| Contributions | 55 | 68,374 | 68,429 |
| Endowment spending for operations and reinvestment | (16,101) | (12,205) | (28,306) |
| Other expenses and transfers | 146,074 | (519) | 145,555 |
| Endowment and similar net assets at June 30, 2019 | <u>\$ 639,095</u> | <u>\$ 491,163</u> | <u>\$ 1,130,258</u> |

Changes in endowment and similar net assets for the fiscal year ended June 30, 2018:

| <i>(in thousands of dollars)</i> | Without Donor Restrictions | With Donor Restrictions | Total |
|---|---------------------------------------|------------------------------------|-------------------|
| Endowment and similar net assets at July 1, 2017 | \$ 452,583 | \$ 380,738 | \$ 833,321 |
| Total endowment return | 37,023 | 30,954 | 67,977 |
| Contributions | 126 | 7,396 | 7,522 |
| Endowment spending for operations and reinvestment | (14,676) | (10,725) | (25,401) |
| Other expenses and transfers | (2,065) | 640 | (1,425) |
| Endowment and similar net assets at June 30, 2018 | <u>\$ 472,991</u> | <u>\$ 409,003</u> | <u>\$ 881,994</u> |

Endowment and similar net assets classified as net assets without donor restrictions include gifts without donor restrictions and other funds designated by the University as endowment for the long-term support of the University. Endowment and similar net assets consist of those funds designated by donors to be invested in perpetuity to provide a permanent source of income, including any accumulated income and appreciation as well as life income, annuities and trust funds (net of actuarial liability). Endowment and similar net assets are primarily used to fund scholarships and professorships.

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14. Lease Commitments and Contingencies

The University is subject to certain legal proceedings and claims which arise in the normal course of operations. In the opinion of management, the ultimate outcome of these actions will not have a material effect on the University's financial position.

The University leases property, plant and equipment under leases classified as operating. The annual operating minimum lease commitments for property rentals are approximated below:

| <i>(in thousands of dollars)</i> | Minimum Lease Commitments |
|----------------------------------|--|
| Year | |
| 2020 | \$ 45,413 |
| 2021 | 40,494 |
| 2022 | 39,071 |
| 2023 | 37,131 |
| 2024 | 33,615 |
| Thereafter | 219,686 |
| | <u>\$ 415,410</u> |

Total rental expense, including computer software licenses, for the University was \$61,379,000 and \$55,954,000 for the years ended June 30, 2019 and 2018, respectively.

The University has entered into contracts for various construction, maintenance and renovation projects for which a balance of \$44,941,000 is committed at June 30, 2019.

15. Functional and Natural Classification of Expenses

The financial statements report certain categories of expenses that are attributable to one or more program or supporting functions of the university. Expenses reported by functional categories include allocations of costs for operation and maintenance of plant, interest on indebtedness and depreciation and amortization expense. The University applies various methods to allocate costs among the program and support functions, the most significant of which is by the amount of building space utilized.

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Operating and non-operating expenses by functional and natural classification for the year ended June 30, 2019 are as follows:

| <i>(in thousands of dollars)</i> | Salary and benefits | Other operating expenses | Depreciation | Interest | Total |
|----------------------------------|----------------------------|---------------------------------|---------------------|------------------|---------------------|
| Instruction | \$ 346,397 | \$ 103,046 | \$ 18,005 | \$ 5,047 | \$ 472,495 |
| Research | 79,592 | 72,304 | 8,308 | 9,938 | 170,142 |
| Academic support | 112,507 | 74,560 | 7,863 | 5,561 | 200,491 |
| Student services | 64,722 | 64,452 | 6,191 | 1,406 | 136,771 |
| Institutional support | 91,773 | 45,486 | 13,988 | 2,207 | 153,454 |
| Auxiliary | 17,669 | 84,403 | 14,902 | 15,665 | 132,639 |
| Other | 1,730 | 1,632 | 102 | - | 3,464 |
| Total | <u>\$ 714,390</u> | <u>\$ 445,883</u> | <u>\$ 69,359</u> | <u>\$ 39,824</u> | <u>\$ 1,269,456</u> |

Operating and non-operating expenses by functional and natural classification for the year ended June 30, 2018 were as follows:

| <i>(in thousands of dollars)</i> | Salary and benefits | Other operating expenses | Depreciation | Interest | Total |
|----------------------------------|----------------------------|---------------------------------|---------------------|------------------|---------------------|
| Instruction | \$ 322,494 | \$ 104,169 | \$ 16,386 | \$ 5,241 | \$ 448,290 |
| Research | 76,194 | 62,778 | 7,659 | 8,114 | 154,745 |
| Academic support | 111,601 | 68,458 | 7,318 | 5,703 | 193,080 |
| Student services | 60,528 | 64,101 | 5,120 | 1,541 | 131,290 |
| Institutional support | 80,752 | 44,624 | 12,966 | 2,225 | 140,567 |
| Auxiliary | 17,320 | 79,975 | 14,189 | 16,269 | 127,753 |
| Other | 1,782 | 1,286 | 103 | - | 3,171 |
| Total | <u>\$ 670,671</u> | <u>\$ 425,391</u> | <u>\$ 63,741</u> | <u>\$ 39,093</u> | <u>\$ 1,198,896</u> |

16. Subsequent Events

The University has assessed the impact of subsequent events through October 7, 2019, the date the audited consolidated financial statements were issued, and has concluded that there were no such events that require adjustment to the audited consolidated financial statements or additional disclosure in the notes to the audited consolidated financial statement other than the event disclosed in Footnote 9.