



CHAPMAN UNIVERSITY AND AFFILIATES

Consolidated Financial Statements

May 31, 2020

(With Comparative Financial Information as of May 31, 2019)

(With Independent Auditors' Report Thereon)

CHAPMAN UNIVERSITY AND AFFILIATES

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KPMG LLP
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Independent Auditors' Report

The Board of Trustees
Chapman University:

The Board of Regents
Brandman University:

We have audited the accompanying consolidated financial statements of Chapman University and Affiliates (the University) as of May 31, 2020, which comprise the consolidated statement of financial position as of May 31, 2020, and the related consolidated statements of activities and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles; 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 these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the University as of May 31, 2020, and the changes in their net assets and their cash flows for the year then ended, in accordance with U.S. generally accepted accounting principles.



Other Matter

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying Supplementary Schedule of Financial Responsibility Data as of and for the year ended May 31, 2020 is presented for purposes of additional analysis, as required by the US Department of Education, and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the financial responsibility schedule is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Report on Summarized Comparative Information

We have previously audited the University's 2019 consolidated financial statements, and we expressed an unmodified audit opinion on those consolidated financial statements in our report dated September 20, 2019. In our opinion, the summarized comparative information presented herein as of and for the year ended May 31, 2019 is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 24, 2020 on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the University's internal control over financial reporting and compliance.

KPMG LLP

November 24, 2020

CHAPMAN UNIVERSITY AND AFFILIATES
Consolidated Statement of Financial Position
May 31, 2020
(with comparative financial information as of May 31, 2019)

Assets	2020	2019
Current assets:		
Cash, cash equivalents, and restricted cash	\$ 144,699,000	101,002,000
Investments (notes 2 and 3)	—	9,348,000
Accounts receivable, less allowance for doubtful accounts of \$1,429,000 and \$948,000 in 2020 and 2019, respectively	6,820,000	7,053,000
Current portion of contributions receivable, net (note 4)	7,345,000	6,439,000
Current portion of notes receivable	128,000	172,000
Other current assets	7,983,000	7,230,000
Current assets held-for-sale (note 13)	<u>78,979,000</u>	<u>49,832,000</u>
Total current assets	<u>245,954,000</u>	<u>181,076,000</u>
Long-term assets:		
Notes receivable, less current portion and allowance for doubtful notes of \$504,000 and \$599,000 in 2020 and 2019, respectively	2,194,000	2,506,000
Contributions receivable, less current portion, net (note 4)	47,147,000	36,801,000
Long-term investments (notes 2 and 3)	418,594,000	419,216,000
Plant assets, net (note 5)	978,660,000	969,251,000
Other real property	54,000	54,000
Other long-term assets	<u>4,486,000</u>	<u>4,520,000</u>
Total long-term assets	<u>1,451,135,000</u>	<u>1,432,348,000</u>
Total assets	<u>\$ 1,697,089,000</u>	<u>1,613,424,000</u>
Liabilities and Net Assets		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 42,903,000	46,358,000
Deferred revenues and student deposits	21,462,000	20,983,000
Current portion of bonds and notes payable (note 6)	28,314,000	27,914,000
Other current liabilities	1,287,000	1,062,000
Current liabilities held-for-sale (note 13)	<u>46,694,000</u>	<u>33,105,000</u>
Total current liabilities	<u>140,660,000</u>	<u>129,422,000</u>
Long-term liabilities:		
Annuities payable, less current portion	1,756,000	1,882,000
Refundable loan programs	469,000	750,000
Bonds and notes payable, less current portion (note 6)	321,534,000	332,848,000
Liability related to interest rate swaps (notes 3 and 6)	—	7,500,000
Other long-term liabilities	<u>12,231,000</u>	<u>11,258,000</u>
Total long-term liabilities	<u>335,990,000</u>	<u>354,238,000</u>
Total liabilities	<u>476,650,000</u>	<u>483,660,000</u>
Net assets:		
Without donor restrictions (note 12)	938,820,000	864,831,000
With donor restrictions (note 12)	<u>281,619,000</u>	<u>264,933,000</u>
Total net assets	<u>1,220,439,000</u>	<u>1,129,764,000</u>
Total liabilities and net assets	<u>\$ 1,697,089,000</u>	<u>1,613,424,000</u>

See accompanying notes to consolidated financial statements.

CHAPMAN UNIVERSITY AND AFFILIATES

Consolidated Statement of Activities

Year ended May 31, 2020

(with summarized financial information for the year ended May 31, 2019)

	2020			2019 Total
	Without donor restriction	With donor restriction	Total	
Revenues, gains, and other support:				
Net tuition and fees (net of student financial aid of \$163,923,000 and \$148,272,000 in 2020 and 2019, respectively)	\$ 334,009,000	—	334,009,000	308,356,000
Endowment returns designated for operations	5,166,000	5,976,000	11,142,000	10,689,000
Other investment income	2,615,000	127,000	2,742,000	2,871,000
Private gifts, grants, and bequests	10,866,000	34,757,000	45,623,000	33,884,000
Auxiliary enterprises	45,100,000	—	45,100,000	49,006,000
Other sources	22,707,000	71,000	22,778,000	18,234,000
	86,454,000	40,931,000	127,385,000	114,684,000
Net assets transferred or released from donor restrictions	11,878,000	(11,878,000)	—	—
Total revenues, gains, and other support	432,341,000	29,053,000	461,394,000	423,040,000
Expenses:				
Educational and general:				
Instruction	191,559,000	—	191,559,000	183,934,000
Academic support	52,106,000	—	52,106,000	48,363,000
Student services	32,436,000	—	32,436,000	31,882,000
General institutional support	58,611,000	—	58,611,000	51,915,000
Total educational and general expenses	334,712,000	—	334,712,000	316,094,000
Auxiliary enterprises	39,647,000	—	39,647,000	39,962,000
Total expenses	374,359,000	—	374,359,000	356,056,000
Increase from operating activities	57,982,000	29,053,000	87,035,000	66,984,000
Nonoperating activities:				
Endowment returns, net of designation for operations	(3,127,000)	(3,297,000)	(6,424,000)	422,000
Realized loss on interest rate swap related to bonds	(127,000)	—	(127,000)	(1,587,000)
Building gifts released from restriction	8,703,000	(8,703,000)	—	—
Other-non-operating activity	4,208,000	(538,000)	3,670,000	58,000
Increase (decrease) from nonoperating activities	9,657,000	(12,538,000)	(2,881,000)	(1,107,000)
Discontinued operations:				
Change in net assets from discontinued operations	6,350,000	171,000	6,521,000	4,984,000
Change in net assets	73,989,000	16,686,000	90,675,000	70,861,000
Net assets, beginning of year	864,831,000	264,933,000	1,129,764,000	1,058,903,000
Net assets, end of year	\$ 938,820,000	281,619,000	1,220,439,000	1,129,764,000

See accompanying notes to consolidated financial statements.

CHAPMAN UNIVERSITY AND AFFILIATES

Consolidated Statement of Cash Flows

Year ended May 31, 2020

(with comparative financial information for the year ended May 31, 2019)

	<u>2020</u>	<u>2019</u>
Cash flows from operating activities:		
Change in net assets	\$ 90,675,000	70,861,000
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Noncash contributions of property, life insurance policies, and investments	(4,605,000)	(3,175,000)
Proceeds from sale of gifts of investments	2,235,000	1,662,000
Contributions restricted for long-term investment	(15,024,000)	(18,954,000)
Net realized and unrealized loss (gain) on investments	600,000	(5,354,000)
Net realized gain on sale or disposition of property, plant, and other assets	(8,000)	(170,000)
Net unrealized gain on current assets held-for-sale	(1,999,000)	—
Realized loss on interest rate swap related to bonds	127,000	1,587,000
Depreciation	38,194,000	34,714,000
Actuarial loss (gain) on annuity obligations	221,000	(112,000)
Amortization of discounts and premiums on bonds payable	(914,000)	(914,000)
Decrease (increase) in accounts receivable	455,000	(2,087,000)
(Increase) in other assets	(623,000)	(829,000)
Decrease (increase) in contributions receivable	(11,251,000)	2,132,000
(Decrease) increase in accounts payable, accrued liabilities, and other liabilities	(2,059,000)	3,571,000
(Decrease) in annuities payable	(348,000)	(26,000)
(Increase) in net assets from discontinued operations	(6,521,000)	(4,984,000)
Net cash provided by operating activities	<u>89,155,000</u>	<u>77,922,000</u>
Cash flows from investing activities:		
Proceeds from sales and maturities of investments	96,548,000	115,276,000
Purchases of investments	(87,199,000)	(82,545,000)
Purchases of plant assets	(44,008,000)	(86,445,000)
Disbursements of loans to students	(311,000)	(239,000)
Repayments of loans from students	668,000	963,000
Net cash used in investing activities	<u>(34,302,000)</u>	<u>(52,990,000)</u>
Cash flows from financing activities:		
Proceeds from contributions restricted for long-term investments	15,024,000	18,954,000
Payments of notes, bonds payable, and interest rate swaps	(26,180,000)	(9,640,000)
Net cash (used in) provided by financing activities	<u>(11,156,000)</u>	<u>9,314,000</u>
Net increase in cash, cash equivalents, and restricted cash	43,697,000	34,246,000
Cash, cash equivalents, and restricted cash at beginning of year	<u>101,002,000</u>	<u>66,756,000</u>
Cash, cash equivalents, and restricted cash at end of year	\$ <u><u>144,699,000</u></u>	<u><u>101,002,000</u></u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for interest, net of amounts capitalized of \$24,000 and \$965,000 for 2020 and 2019, respectively	\$ 13,335,000	13,106,000
Supplemental schedules of noncash investing and financing activities:		
Contributions of property for plant assets	\$ 2,298,000	1,447,000
Contributions of life insurance policies	94,000	68,000
Contributions of investments	2,213,000	1,660,000

See accompanying notes to consolidated financial statements.

CHAPMAN UNIVERSITY AND AFFILIATES

Notes to Consolidated Financial Statements

May 31, 2020

(with comparative financial information as of May 31, 2019)

(1) Summary of Significant Accounting Policies and Other Matters

(a) Organization

Chapman University and its consolidated affiliates, which include Brandman University, Chapman University Charitable Giving LLC, Chapman University Enterprises, Inc., CBE Educational Services Company, Inc., and Chapman University Foundation (collectively, the University), are not-for-profit coeducational institutions of higher learning and taxable corporations primarily located in Orange County, California.

(b) Basis of Accounting

The accompanying consolidated financial statements are presented using the accrual basis of accounting.

(c) Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Chapman University and its affiliates. All significant intercompany balances and transactions have been eliminated in consolidation.

(d) Donor-Imposed Restrictions

All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received that are designated for future periods or are restricted by the donor for specific purposes are reported as donor-restricted support. When restrictions are met, net assets with donor restriction are reclassified to without donor restriction net assets and recorded as net assets released from restrictions in the accompanying consolidated statement of activities. Donor-restricted contributions whose restrictions are met within the fiscal year received are reported as support without donor restriction.

(e) Promises to Give

Unconditional promises to give that are expected to be collected within one year are recorded as contributions receivable at their estimated net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded as a contribution receivable at the present value of their estimated future cash flows. The discounts on those amounts are computed using a rate that is commensurate with the risks involved and applicable to the years in which the promises are received. Amortization of the discounts is included in contribution revenue. Conditional promises to give are not included as support until such time as the conditions are substantially met.

(f) Cash, Cash Equivalents, and Restricted Cash

The University considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents, except for those that have been purchased with donor-restricted funds or designated by the University as endowments, which are considered to be long-term investments and restricted cash.

Amounts included in restricted cash represent those required to be set aside by an agreement with donors restricted for specific projects or purposes which range from construction to loan funds.

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Notes to Consolidated Financial Statements

May 31, 2020

(with comparative financial information as of May 31, 2019)

The following table provides a reconciliation of cash, cash equivalents, and restricted cash reported within the statement of financial position and statement of cash flows.

	<u>2020</u>	<u>2019</u>
Cash and cash equivalents	\$ 119,175,000	79,118,000
Restricted cash	<u>25,524,000</u>	<u>21,884,000</u>
Total cash, cash equivalents, and restricted cash	<u>\$ 144,699,000</u>	<u>101,002,000</u>

(g) Plant Assets

Plant assets are stated at cost or estimated fair value at date of donation, net of accumulated depreciation. Depreciation is computed on a straight-line basis over the estimated useful lives of buildings and improvements (15 to 40 years) and equipment (3 to 10 years).

Contributed plant assets are recorded at fair value at the date of donation. If donors stipulate how long the assets must be used, the contributions are recorded as support with donor restrictions and are reclassified to net assets without donor restrictions when the stipulation ends. In the absence of such stipulations, contributions of property and equipment are recorded as support without donor restrictions.

(h) Impairment of Long-lived Assets and Long-lived Assets to Be Disposed of

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows (undiscounted and without interest) expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. During 2020, there were no events or changes in circumstances indicating that the carrying amount of long-lived assets may not be recoverable.

(i) Investment Valuation

In accordance with U.S. generally accepted accounting principles, the University reports investments at fair value based upon a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

Level I Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities.

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(with comparative financial information as of May 31, 2019)

Level II Inputs of other than that quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. This includes quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, or inputs that are derived principally from or corroborated by observable market data.

Level III Inputs are unobservable for the asset or liability. Unobservable inputs reflect the University's own assumptions about the assumptions that market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

(j) Fair Value of Financial Instruments

The University did not elect fair value accounting for any asset or liability that is not currently required to be measured at fair value.

Fair value of the University's financial instruments is determined using the estimates, methods, and assumptions as set forth below. See note 3 for further information regarding investments and their fair value.

(i) Cash Equivalents, Accounts and Other Receivables, Accounts Payable, and Accrued Expenses

Fair value approximates book value due to the short maturity of these instruments.

A reasonable estimate of the fair value of student loans extended under government loan programs has not been made as the loans can only be assigned to the U.S. government or its designees.

(ii) Contributions Receivable

Contributions receivable are reported based on the discounted value of estimated cash flows. The discount rate is estimated based upon a risk-free rate of return. The book value approximates fair value.

(iii) Interest Rate Swaps

Fair value of the University's swap agreements are estimated based on observable inputs, such as relevant interest rates that reflect assumptions market participants would use in pricing the instruments. These inputs fall within Level II of the fair value hierarchy. Fair value of the swap agreements was a liability of \$7,500,000 as of May 31, 2019. During the fiscal year ended May 31, 2020, the swap agreements were terminated by paying \$7,650,000 to fully settle the contracts.

(iv) Alternative Investments

Alternative investments, such as private equity interests, are recorded based on valuations provided by the general partners or external investment managers. As these generally are investments without a ready market to compare, the inputs into the determination of fair value require significant judgment. Due to the inherent uncertainty of these estimates, these values may

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(with comparative financial information as of May 31, 2019)

differ materially from the values that would have been used had a ready market for these investments existed. Management reviews and evaluates the valuations and has determined that the valuation methods and assumptions result in reasonable estimates of fair value. Refer to note 3 for fair value determination.

(v) *Annuities Payable*

The carrying amount of annuity and trust obligations approximates fair value as the instruments are recorded at the estimated net present value of future cash flows.

(k) *Income Taxes*

The University and affiliates, with the exception of Chapman University Enterprise, Inc., are exempt from taxation under Section 501(c)(3) of the Internal Revenue Code and Section 23701d of the California Revenue and Taxation Code and are generally not subject to federal or state income taxes. However, the University is subject to income taxes on any net income that is derived from a trade or business regularly carried on, and not in furtherance of the purposes for which it was granted exemption. No income tax provision has been recorded as the net income, if any, from any unrelated trade or business, in the opinion of management, is not material to the consolidated financial statements taken as a whole.

(l) *Use of Estimates*

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(m) *Fund-Raising Expenses*

The accompanying consolidated statements of activities include fund-raising expenses of \$17,152,000 and \$15,214,000 for the years ended May 31, 2020 and 2019, respectively, as a component of general institutional support.

(n) *Comparative Data*

The consolidated financial statements include prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation conformity with U.S. generally accepted accounting principles. Accordingly, such information should be read in conjunction with the University's consolidated financial statements as of and for the year ended May 31, 2019, from which the summarized information was derived.

(o) *Functional Expenses*

Expenses that can be specifically identified with a specific program or supporting service are charged directly to the related program or supporting service. Expenses that are associated with more than one program or supporting service are allocated based on an evaluation made by management.

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(with comparative financial information as of May 31, 2019)

(p) Reclassifications

The University has reclassified certain amounts relating to its prior period results to conform to its current year presentation. These reclassifications have not changed the results of operations of prior periods.

(q) Net Assets – Basis of Presentation

Net Assets, revenue, expenses, gains, and losses are classified based on the existence or absence of donor or grantor imposed restrictions. The definitions used to clarify and report net assets are as follows:

Net Assets without Donor Restrictions – Net assets that are not subject to donor imposed stipulations and are available for use in general operations or are part of what's invested in property, plant and equipment (net of related debt). However, the governing board may designate any of these funds for specific purposes (i.e., specific purpose reserves or endowments).

Net Assets with Donor Restrictions – Net assets subject to donor imposed stipulations (1) that will be met either by actions of the University or the passage of time or (2) that are to be permanently maintained by the University. Generally, the donors of these assets permit the University to use all or part of the income earned on related investments for general or specific purposes.

(r) Liquidity and Availability

The following table reflects the University's financial assets as May 31, 2020 available for general expenditures within one year. Financial assets are considered unavailable when illiquid or not convertible to cash within one year. Other considerations of non-liquid assets are perpetual endowments and accumulated earnings net of appropriations within one year, amounts restricted by donors for nonoperating activities, amounts limited by the University's Board of Trustees and student loans receivable. The University considers investment income without donor restrictions, appropriated earnings from donor-restricted and board-designated endowments, contributions without donor restrictions and contributions with donor restrictions for current operating activities to be available to meet cash needs for general expenditures. For purposes of analyzing resources available to meet general expenditures over a one year period, the University considers all expenditures related to its

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Notes to Consolidated Financial Statements

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(with comparative financial information as of May 31, 2019)

ongoing mission-related activities as well as the conduct of services undertaken to support those activities to be general expenditures.

	<u>2020</u>	<u>2019</u>
Financial assets available to meet general expenditures over the next 12 months:		
Cash and cash equivalents	\$ 38,637,000	45,310,000
Current investments	—	9,348,000
Current accounts receivable, net	6,820,000	7,053,000
Current notes receivable, net	128,000	172,000
Current assets held-for-sale	<u>16,037,000</u>	<u>14,038,000</u>
Total financial assets available to meet general expenditures over the next 12 months	<u>61,622,000</u>	<u>75,921,000</u>
Financial assets not available for general expenditures over the next 12 months:		
Cash and cash equivalents	\$ 106,062,000	55,692,000
Long term investments	418,594,000	419,216,000
Plant assets	978,660,000	969,251,000
Contributions receivable, net	54,492,000	43,240,000
Long term notes receivable, net	2,194,000	2,506,000
Current assets held-for-sale	62,942,000	35,794,000
Other assets	<u>12,523,000</u>	<u>11,804,000</u>
Total financial assets not available for general expenditures over the next 12 months	<u>1,635,467,000</u>	<u>1,537,503,000</u>
Total financial assets	<u>\$ 1,697,089,000</u>	<u>1,613,424,000</u>

The University's governing board has designated a portion of its unrestricted resources for endowment and other purposes. These funds are invested for long-term appreciation and current income but remain available and may be spent at the discretion of the board. At May 31, 2020, the following amounts were designated for specific purposes by the board:

Quasi-endowment funds	\$ 214,559,000
Designated for capital assets	<u>72,673,000</u>
Total board-designated funds	<u>\$ 287,232,000</u>

The University has the long-standing practice of reporting its monthly projected cash flows for the entire fiscal year to the Finance and Budget Committee of the Board of Trustees. This report is designed to ensure that at any time the University has a minimum of \$20 million in cash available to address unknown or urgent claims. Further, while it is not the intention of the Board of Trustees to spend the

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(with comparative financial information as of May 31, 2019)

principle of its board-designated endowment, as of May 31, 2020 its market value was \$214,559,000 and could be made available if necessary.

(s) Change in Accounting Principle

During 2020, The University adopted the provisions of ASU 2016-18, Statement of Cash Flows (Topic 230). As a result, an additional disclosure is included in the footnotes that reconciles cash, cash equivalents, and restricted cash to the consolidated statement of cash flows.

(t) Current Environment

In March 2020, the World Health Organization declared the novel coronavirus (COVID-19) a pandemic. The outbreak of the disease has affected travel, commerce and financial markets globally, including in the United States. The continued spread of COVID-19 and its impact on social interaction, travel, economies and financial markets may adversely affect operations and financial condition, including, among other things, (i) the ability of the University to conduct its operations and/or the cost of operations, (ii) governmental and non-governmental funding, and (iii) financial markets impacting investments valuation and interest rates.

Commencing March 2020, undergraduate and graduate course instruction was conducted virtually and most students vacated the campus. The University granted refunds of \$14 million in fiscal year 2020 for housing and dining services not provided after March 2020. Students continued to meet their academic requirements for the remainder of the 2019 – 2020 academic year. In addition, the start of 2020-21 academic year will remain a virtual learning environment. While some faculty and staff are working on-campus to ensure continuity of essential operations, most faculty and staff have transitioned to remote work. As of May 31, 2020, there is such uncertainty over the progression of the virus and governmental emergency directives that there is no timetable for when instruction and campus operations will return to normal.

The COVID-19 pandemic has negatively affected national, state, and local economies and global financial markets, and the higher education landscape in general. While the financial impact on the University cannot be quantified at this time, the pandemic may have a material adverse effect on the current and future financial profile and operating performance of the University. The University continues to monitor the course of the pandemic and is prepared to take additional measures to protect the health of the University community and promote the continuity of its academic mission.

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(with comparative financial information as of May 31, 2019)

(2) Investments

Investments at May 31, 2020 and 2019 consist of the following:

	<u>2020</u>	<u>2019</u>
Money market funds	\$ 13,521,000	35,654,000
Equities	108,590,000	91,637,000
Fixed income and mutual funds	45,466,000	48,181,000
Real estate	26,000,000	41,100,000
Venture capital	29,185,000	22,602,000
Private equity	40,854,000	31,958,000
Mezzanine debt funds	270,000	662,000
Hedge funds	129,943,000	133,454,000
Real asset funds	19,822,000	18,588,000
Unitrust investments:		
Money market funds	173,000	202,000
Equities	2,999,000	2,666,000
Fixed income/mutual funds	1,659,000	1,604,000
Alternative investments	25,000	198,000
Real asset fund	87,000	58,000
Total investments	\$ <u>418,594,000</u>	<u>428,564,000</u>

Investment income consisted of the following for the years ended May 31, 2020 and 2019:

		<u>2020</u>	
	<u>Endowment</u>	<u>Other</u>	<u>Total</u>
Interest and dividends	\$ 6,167,000	2,660,000	8,827,000
Realized and unrealized gains (losses), net	517,000	83,000	600,000
Less investment expenses	<u>(1,966,000)</u>	<u>(1,000)</u>	<u>(1,967,000)</u>
Investment income, net	<u>\$ 4,718,000</u>	<u>2,742,000</u>	<u>7,460,000</u>
Operating	\$ 11,142,000	2,742,000	13,884,000
Nonoperating	<u>(6,424,000)</u>	<u>—</u>	<u>(6,424,000)</u>
Investment income, net	<u>\$ 4,718,000</u>	<u>2,742,000</u>	<u>7,460,000</u>

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		2019	
	Endowment	Other	Total
Interest and dividends	\$ 6,353,000	3,620,000	9,973,000
Realized and unrealized gains (losses), net	6,085,000	(731,000)	5,354,000
Less investment expenses	<u>(1,327,000)</u>	<u>(18,000)</u>	<u>(1,345,000)</u>
Investment income, net	<u>\$ 11,111,000</u>	<u>2,871,000</u>	<u>13,982,000</u>
Operating	\$ 10,689,000	2,871,000	13,560,000
Nonoperating	<u>422,000</u>	<u>—</u>	<u>422,000</u>
Investment income, net	<u>\$ 11,111,000</u>	<u>2,871,000</u>	<u>13,982,000</u>

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(3) Fair Values of Financial Instruments

The following tables summarize investment values by category of investment as of May 31, 2020 and 2019. Consistent with ASU 2015-07, investments measured at net asset value (NAV) are not classified in the fair value hierarchy.

	2020				
	Investments measured at NAV	Investments classified in the fair value hierarchy			
		(Level I)	(Level II)	(Level III)	Total
Pooled investments:					
Money market funds	\$ —	13,521,000	—	—	13,521,000
Equities:					
U.S. equities	—	20,989,000	—	—	20,989,000
Global equities	55,546,000	—	—	—	55,546,000
Emerging market equities	14,537,000	14,749,000	—	—	29,286,000
Fixed income	8,117,000	15,617,000	—	—	23,734,000
Fixed income mutual funds	—	21,732,000	—	—	21,732,000
Venture capital	29,185,000	—	—	—	29,185,000
Private equity	40,854,000	—	—	—	40,854,000
Mezzanine debt funds	270,000	—	—	—	270,000
Hedge funds	129,943,000	—	—	—	129,943,000
Real asset funds	—	19,822,000	—	—	19,822,000
Total pooled investments	278,452,000	106,430,000	—	—	384,882,000
Other investments:					
Equities	—	2,770,000	—	—	2,770,000
Fixed income-mutual funds	—	1,000	—	—	1,000
Real estate	—	—	26,000,000	—	26,000,000
Total other investments	—	2,771,000	26,000,000	—	28,771,000
Unitrust investments:					
Money market funds	—	173,000	—	—	173,000
Equities	—	2,999,000	—	—	2,999,000
Fixed income/mutual funds	—	1,530,000	127,000	—	1,657,000
Alternative investments	25,000	—	—	—	25,000
Real asset funds	87,000	—	—	—	87,000
Total unitrust investments	112,000	4,702,000	127,000	—	4,941,000
Total investments	\$ 278,564,000	113,903,000	26,127,000	—	418,594,000

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	2019				
	Investments measured at NAV	Investments classified in the fair value hierarchy			
		(Level I)	(Level II)	(Level III)	Total
Pooled investments:					
Money market funds	\$ —	28,676,000	—	—	28,676,000
Equities:					
U.S. equities	—	8,099,000	—	—	8,099,000
Global equities	53,787,000	—	—	—	53,787,000
Emerging market equities	16,916,000	10,519,000	—	—	27,435,000
Fixed income	—	14,423,000	—	—	14,423,000
Fixed income mutual funds	—	24,410,000	—	—	24,410,000
Venture capital	22,602,000	—	—	—	22,602,000
Private equity	31,958,000	—	—	—	31,958,000
Mezzanine debt funds	662,000	—	—	—	662,000
Hedge funds	133,454,000	—	—	—	133,454,000
Real asset funds	—	18,588,000	—	—	18,588,000
Total pooled investments	259,379,000	104,715,000	—	—	364,094,000
Other investments:					
Cash and cash equivalents	—	6,978,000	—	—	6,978,000
Equities	—	2,316,000	—	—	2,316,000
Fixed income-mutual funds	—	9,348,000	—	—	9,348,000
Real estate	—	—	41,100,000	—	41,100,000
Total other investments	—	18,642,000	41,100,000	—	59,742,000
Unitrust investments:					
Money market funds	—	202,000	—	—	202,000
Equities	—	2,666,000	—	—	2,666,000
Fixed income/mutual funds	—	1,229,000	375,000	—	1,604,000
Alternative investments	198,000	—	—	—	198,000
Real asset funds	58,000	—	—	—	58,000
Total unitrust investments	256,000	4,097,000	375,000	—	4,728,000
Total investments	\$ 259,635,000	127,454,000	41,475,000	—	428,564,000
Interest rate swaps	\$ —	—	(7,500,000)	—	(7,500,000)
Total liabilities	\$ —	—	(7,500,000)	—	(7,500,000)

Money Market Funds – Investments in money market funds are classified as Level I, as they can be liquidated in the same day, representing the active and ready market for these assets.

U.S. Equities – Investments in U.S. equities are measured at fair value using quoted market prices. They are classified as Level I, as they are traded in active markets for which closing stock prices are readily available.

Global Equities – International Equity Funds – Investments in this category are classified at net asset value (NAV), as they are not traded actively; however, the fair value has been estimated using the NAV of this account. The exit frequency of this investment is monthly.

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Emerging Markets Equities – Investments in emerging markets equities that are classified as Level I are traded in active markets for which closing prices are readily available. Certain investments in emerging markets equities are classified as NAV as these investments have unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the asset.

Fixed Income – Investments that are classified in Level I are listed on national exchanges or over-the-counter markets and for which quoted market prices are available from sources such as financial publications, the exchanges, or the National Association of Securities Dealers Automated Quotations System. Certain investment in fixed income is classified as NAV as this investment has unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the asset.

Fixed Income Mutual Funds – Investments in fixed income mutual funds include investments in debt securities, U.S. government, and municipal obligations, are classified as Level I. Investments are classified in category Level II, when they use significant other observable inputs, particularly dealer market prices for comparable investment as of the valuation date as reflected on account statements issued by investment custodians.

Real Asset Funds – Investments in the real asset funds are measured at fair value using quoted market prices and classified as Level I, as they are traded in active markets for which prices are readily available.

Real Estate – Investments in real estate include commercial property holdings. Real estate investments are classified as Level II based on multiple sources of information such as appraisals and market comparables.

Alternative investments include hedge funds, venture capital, private equity, and mezzanine debt funds. These investments are classified NAV as these investments have unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the asset. As such, the University is unable to obtain independent valuations from market sources. Therefore, these investments are valued utilizing NAVs. Realized and unrealized gains and losses are reported in the consolidated statement of activities under the line item entitled “Endowment return designated for operations” and under nonoperating activities under the line item entitled “Endowment returns, net of designation for operations.”

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The following table summarizes the fair value measurements of investments that calculate NAV per share (or its equivalent) as of May 31, 2020:

<u>Category of investment</u>	<u>NAV in funds</u>	<u>Unfunded commitments</u>	<u>Redemption notice period (in days)</u>	<u>Days until exit</u>
Global equities	\$ 55,546,000	—	10–30	30–31
Emerging market equities	14,537,000	—	10–30	31–122
Fixed income	8,117,000	—	n/a	n/a
Venture capital	29,185,000	22,360,000	See below	See below
Private equity	40,854,000	63,396,000	See below	See below
Mezzanine debt funds	270,000	607,000	See below	See below
Hedge funds:				
U.S. equities	90,507,000	—	31–90	61–396
Global	23,381,000	—	10–75	30–214
Multi-strategy	16,055,000	—	44–65	122–761
Unitrust investments:				
Alternative investments	25,000	—	n/a	Daily
Real asset funds	87,000	—	n/a	Daily
	<u>\$ 278,564,000</u>	<u>86,363,000</u>		

The University holds certain investments in venture capital, private equity, and mezzanine debt funds in the amount of \$29,185,000, \$40,854,000, and \$270,000, respectively. These limited partnerships do not allow for periodic redemptions, but rather distributions are received through the liquidation of the underlying assets of the partnership. The University had no transfers between Level I, Level II, and Level III investments during the fiscal years ended May 31, 2020 or 2019.

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(4) Contributions Receivable

Contributions receivable include unconditional pledges that have been discounted at rates ranging from 0.92% to 7.75%. The following is a summary of the University's unconditional contributions receivable at May 31, 2020 and 2019:

	<u>2020</u>	<u>2019</u>
Unconditional contributions expected to be collected in:		
Less than one year	\$ 13,724,000	12,376,000
One to five years	31,899,000	23,678,000
More than five years	<u>28,345,000</u>	<u>26,441,000</u>
	73,968,000	62,495,000
Less:		
Unamortized discount	(11,416,000)	(12,361,000)
Allowance for uncollectible contributions	<u>(8,060,000)</u>	<u>(6,894,000)</u>
Total contributions receivable	\$ <u><u>54,492,000</u></u>	<u><u>43,240,000</u></u>

Conditional pledges for the University, which depend on the occurrence of specified future and uncertain events, approximated \$137,612,000 at May 31, 2020. Outstanding conditional pledges from related parties represent \$117,445,000 at May 31, 2020. The primary purpose of these conditional pledges is to support current and future programs at the University.

(5) Plant Assets

Plant assets at May 31, 2020 and 2019 consist of the following:

	<u>2020</u>		
	<u>Cost</u>	<u>Accumulated depreciation</u>	<u>Net</u>
Land	\$ 181,915,000	—	181,915,000
Buildings and improvements	860,712,000	(181,045,000)	679,667,000
Equipment	254,411,000	(156,300,000)	98,111,000
Construction in progress	<u>18,967,000</u>	<u>—</u>	<u>18,967,000</u>
	\$ <u><u>1,316,005,000</u></u>	<u><u>(337,345,000)</u></u>	<u><u>978,660,000</u></u>

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	2019		
	Cost	Accumulated depreciation	Net
Land	\$ 185,748,000	—	185,748,000
Buildings and improvements	788,877,000	(158,425,000)	630,452,000
Equipment	234,994,000	(140,948,000)	94,046,000
Construction in progress	59,005,000	—	59,005,000
	<u>\$ 1,268,624,000</u>	<u>(299,373,000)</u>	<u>969,251,000</u>

(6) Long-Term Debt Obligations

(a) Bonds and Notes Payable

Long-term debt consists of bonds payable and loans payable. Bond payable issued through the California Educational Facilities Authority (CEFA), and associated interest rates and maturities at May 31, 2020 and 2019 are as follows:

	2020		
	Interest rates	Maturity dates	Principal amount
Bonds payable:			
Series 2017 A Bonds	1.4%–3.8%	2041–2042	\$ 102,035,000
Series 2017 B Bonds	4.0%	2046–2047	37,650,000
Series 2015	4.0%–5.0%	2044–2045	106,445,000
Series 2011	5.0%	2030–2031	69,220,000
			<u>315,350,000</u>
Plus unamortized premiums			17,498,000
			<u>332,848,000</u>
Notes payable:			
Bank of America Term Loan	LIBOR plus 0.52%	2020–2021	10,500,000
Bank of America Term Loan	LIBOR plus 0.52%	2020–2021	6,500,000
			<u>17,000,000</u>
Total bonds and notes payable			<u>\$ 349,848,000</u>

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	2019		
	<u>Interest rates</u>	<u>Maturity dates</u>	<u>Principal amount</u>
Bonds payable:			
Series 2017 A Bonds	1.4%–3.8%	2041–2042	\$ 105,270,000
Series 2017 B Bonds	4.0%	2046–2047	37,650,000
Series 2015	4.0%–5.0%	2044–2045	108,570,000
Series 2011	5.0%	2030–2031	<u>73,860,000</u>
			325,350,000
Plus unamortized premiums			<u>18,412,000</u>
Bonds payable			<u>343,762,000</u>
Notes payable:			
Bank of America Term Loan	LIBOR plus 0.52%	2020–2021	10,500,000
Bank of America Term Loan	LIBOR plus 0.52%	2020–2021	<u>6,500,000</u>
Notes payable			<u>17,000,000</u>
Total bonds and notes payable			<u>\$ 360,762,000</u>

Bonds and notes payable at May 31, 2020 are due as follows:

Year ending May 31:	
2021	\$ 28,314,000
2022	10,835,000
2023	11,290,000
2024	11,770,000
2025	12,285,000
Thereafter	<u>258,770,000</u>
Total principal	333,264,000
Unamortized premium	<u>16,584,000</u>
	<u>\$ 349,848,000</u>

The CEFA agreements contain covenants relating to maintenance of the University, insurance, and other general terms.

Pursuant to the terms of the California Educational Facilities Authority Series 2015 and Series 2017 A and B Bonds indenture, investments include \$0 and \$6,788,000 of bond proceeds, which were held by independent trustees at May 31, 2020 and 2019, respectively.

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Total interest expense was \$13,359,000 and \$14,070,000 for the years ended May 31, 2020 and 2019, respectively, net of amount capitalized.

(b) Interest Rate Swaps

As part of the issuance of the 2008 Bonds, the University entered into an interest rate swap agreement that calls for fixed rates of 3.162%, 3.121%, and 3.212% in exchange of a monthly variable rate of USD-LIBOR-BBA for the Series 2008 A, B, and C Bonds, respectively. There was no cash exchanged at the time of acquisition. The swap entered into by the University covering the previously paid off 2008 Series A Bonds expires October 2036, and the swaps covering the 2008 B and C Bonds expire as of October 2026.

During the fiscal year ended May 31, 2020 there was no outstanding liability as the interest rate swap agreements were paid off. The resulting loss of \$127,000 was reported in the consolidated statement of activities.

(7) Commitments and Contingencies

(a) Lease Commitments

The University has commitments related to operating leases for building facilities and equipment at May 31, 2020 and 2019. All operating leases are noncancelable and expire on various dates through 2026.

Minimum future rental payments under noncancelable operating lease agreements at May 31, 2020 are summarized as follows:

Fiscal year ending May 31:	
2021	\$ 284,000
2022	214,000
2023	159,000
2024	139,000
2025	<u>134,000</u>
Total minimum lease payments	\$ <u><u>930,000</u></u>

Total rent expense was \$366,000 and \$465,000 for the years ended May 31, 2020 and 2019, respectively.

(b) Contingencies

The University is subject to certain loss contingencies, such as litigation, arising in the normal conduct of its educational activities. In the opinion of management, the liability, if any, for such contingencies will not have a material effect on the University's financial position.

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(8) Retirement Plan

The University has a defined contribution retirement plan. Employees working at least 20 hours a week are eligible to participate in the plan after 90 days of employment. The University contributes 3% of each employee's eligible annual salary, as defined by the plan. Eligible employees may contribute up to 6% of their eligible salary and the University matches their contributions. The University's total contribution to the plan was \$10,600,000 and \$9,846,000 for the years ended May 31, 2020 and 2019, respectively.

(9) Related Parties

The University is a recipient of generous support and commitments from many of its constituencies, which are considered related parties and include members of the Board of Trustees, Board of Governors, President's Cabinet, other advisory boards, and councils, as well as the administration. As a result of irrevocable commitments, a significant number of contributions are expected to be received from related parties in the future. Outstanding contributions receivable from related parties represent \$39,156,000 and \$25,374,000 as of May 31, 2020 and 2019, respectively.

(10) Annuities Payable

The University has legal title, either in the University's name or as trustee, to charitable remainder trusts. No significant financial benefit can be realized until the contractual obligations are released. The University also receives contributions in exchange for charitable gift annuity contracts.

The University uses an actuarial method of recording these annuities and trust liabilities using discount rates ranging from 1.2% to 9.8%. For charitable gift annuities and charitable remainder trusts, when a gift is received, the present value of future expected payments to the beneficiaries is recorded as a liability included in other current and long-term liabilities based upon life expectancy tables and discount rate assumptions, and the remainder is recorded as a contribution. Contribution revenue recognized from charitable gift annuities and charitable remainder trusts is classified as an increase in assets with donor restrictions net assets based on the existence or absence of time or use restrictions placed by the donor upon the University's interest in the assets. Annuity and trust assets are determined annually based on revised fair value, actuarial and earnings data, and the effect of terminated trusts and other agreements.

(11) Endowments

In approving endowment spending and related policies, as part of the prudent and diligent discharge of its duties, the Board of Trustees of the University, as authorized by the California law, has relied upon the actions, reports, information, advice, and counsel taken or provided by its duly constituted committees and duly appointed officers of the University, including University Counsel, and in doing so has interpreted the law to require the preservation of the historic dollar value of donor-restricted endowment funds, absent explicit donor direction to the contrary.

As a result of this interpretation, for accounting and financial statement purposes, the University classifies as donor-restricted net assets the historic dollar value of assets held as donor-restricted endowment, including any subsequent gifts and any accumulations to donor-restricted endowments made in accordance with the direction of the applicable gift instruments.

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Investment income and gains and losses on donor-restricted endowments are reported as an increase or decrease in net assets until those amounts are appropriated by the Board of Trustees.

Endowment net asset composition by type of funds as of May 31, 2020 and 2019 is as follows:

	2020		
	Without donor restrictions	With donor restrictions	Total
Donor-restricted endowments	\$ —	197,505,000	197,505,000
Board-designated endowments	214,559,000	—	214,559,000
Total	<u>\$ 214,559,000</u>	<u>197,505,000</u>	<u>412,064,000</u>

	2019		
	Without donor restrictions	With donor restrictions	Total
Donor-restricted endowments	\$ —	195,022,000	195,022,000
Board-designated endowments	211,284,000	—	211,284,000
Total	<u>\$ 211,284,000</u>	<u>195,022,000</u>	<u>406,306,000</u>

Changes in endowment net assets for the fiscal year ended May 31, 2020 are as follows:

	Without donor restrictions	With donor restrictions	Total
Endowment net assets at May 31, 2019	\$ 211,284,000	195,022,000	406,306,000
Investment return, net	2,039,000	2,679,000	4,718,000
Contributions	—	5,774,000	5,774,000
Appropriation of endowment assets for expenditure	(5,166,000)	(5,976,000)	(11,142,000)
Other changes:			
Additions, changes, and transfers	—	6,000	6,000
Transfers from operations to board-designated endowment funds	6,402,000	—	6,402,000
Change in endowment net assets	<u>3,275,000</u>	<u>2,483,000</u>	<u>5,758,000</u>
Endowment net assets at May 31, 2020	<u>\$ 214,559,000</u>	<u>197,505,000</u>	<u>412,064,000</u>

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Changes in endowment net assets for the fiscal year ended May 31, 2019 are as follows:

	<u>Without donor restrictions</u>	<u>With donor restrictions</u>	<u>Total</u>
Endowment net assets at May 31, 2018	\$ 198,710,000	195,361,000	394,071,000
Investment return, net	7,380,000	3,731,000	11,111,000
Contributions	—	1,984,000	1,984,000
Appropriation of endowment assets for expenditure	(4,705,000)	(5,984,000)	(10,689,000)
Other changes:			
Additions, changes, and transfers	160,000	(70,000)	90,000
Transfers from operations to board-designated endowment funds	9,739,000	—	9,739,000
Change in endowment net assets	<u>12,574,000</u>	<u>(339,000)</u>	<u>12,235,000</u>
Endowment net assets at May 31, 2019	<u>\$ 211,284,000</u>	<u>195,022,000</u>	<u>406,306,000</u>

(a) Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level required by the donor or law. The aggregated deficiencies of this nature for all donor-restricted endowment funds were \$349,000 and \$230,000 as of May 31, 2020 and 2019, respectively. These deficiencies resulted from unfavorable market fluctuations that occurred after the investment of permanently restricted contributions.

(b) Investment and Financial Objectives and Risk Parameters

The primary long-term investment objective of the endowment is to attain an average annual real total return (net of investment management fees) of at least 6% over the long term (a minimum five-year period). Real total return is the sum of capital appreciation (or loss) and current income (dividends and interest) adjusted for inflation by the consumer price index. The Investment Committee strives to achieve these objectives within acceptable risk levels.

Additionally, it is expected that the portfolio's annualized investment return exceeds a custom allocation index or total portfolio blended benchmark measured over a minimum five-year period. The custom blended benchmark consists of 17% Russell 3000, 13% Morgan Stanley Capital International (MSCI) Europe, Australia and Far East (EAFE) Index (net), 8% MSCI Emerging Markets Index (net), 15% Hedge Fund Research, Inc. (HFRI) Fund of Funds Diversified Index, 20% Blended Public Equities, 2% Morgan Stanley Capital International (MSCI) World Natural Resources Index, 2% Wells Fargo MLP Index, 8% Marketable Real Assets Benchmark, 11.2% Bloomberg (BBG) Barclays Intermediate Government Bond Index, 2.8% Bloomberg (BBG) Barclays Aggregate Bond Index, and 1% Bank of America Merrill Lynch (BofA ML) 91 day T-Bill. The primary financial objective of the endowment is to provide funds for the ongoing support of the operations of the University while providing for safety of principal through diversification of investments. Over the long term, this means providing a stream of

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relatively predictable, stable, and constant funding in support of annual budgetary needs, and preserving and enhancing the Endowment's real (inflation-adjusted) purchasing power, net of management expenses and spending.

The Endowment's investments shall also be diversified by asset class and within asset classes as well as by manager. The purpose of diversification is to provide reasonable assurance that no manager, asset class, or individual holding could have a disproportionate negative impact on the Endowment's aggregate results.

(c) Spending Policy

The Endowment is managed according to the "total return" concept, which envisions the sources of Endowment spending as being from interest, dividends, and realized capital gains, supplemented by recent donations and campaign gifts.

The University uses a moving average of market values to calculate its annual draw from the Endowment. For fiscal year 2019-20, the University targeted spending at 3.75% of the moving average of the Endowment's market value based on the previous 20-quarter-end portfolio market valuations.

The spending policy is reviewed periodically by the University's Finance and Budget Committee to determine whether the spending formula should be adjusted and whether the University's current policy objectives are being met.

In accordance with this policy, the Board of Trustees has authorized the following amounts for the years ended May 31, 2020 and 2019:

	<u>2020</u>	<u>2019</u>
Spending allocation per spending policy:		
Donor-restricted endowments	\$ 5,976,000	5,984,000
Board-designated endowments	<u>5,166,000</u>	<u>4,705,000</u>
Total endowment returns designated for operations	<u>\$ 11,142,000</u>	<u>10,689,000</u>

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(12) Net Assets

At May 31, 2020 and 2019, net assets consisted of the following:

	Consolidated	
	<u>2020</u>	<u>2019</u>
Without donor restrictions:		
Property, plant, and equipment	\$ 670,698,000	628,523,000
Board-designated quasi-endowment	214,559,000	211,284,000
Operations, scholarship and other	<u>53,563,000</u>	<u>25,024,000</u>
Total without donor restrictions	<u>\$ 938,820,000</u>	<u>864,831,000</u>
With donor restrictions for time or purpose:		
Unappropriated endowment earnings	\$ 62,782,000	66,080,000
Property, plant, and equipment	29,779,000	32,016,000
For educational and general programs	16,441,000	13,972,000
Financial aid	9,904,000	3,161,000
Research	<u>1,626,000</u>	<u>2,887,000</u>
Total with donor restrictions for time or purpose	<u>\$ 120,532,000</u>	<u>118,116,000</u>
With donor restrictions in perpetuity:		
Endowment	\$ 134,723,000	128,947,000
Pledges	18,879,000	10,678,000
Loan Funds	6,439,000	6,359,000
Annuity and life income funds	<u>1,046,000</u>	<u>833,000</u>
Total with donor restrictions in perpetuity	<u>\$ 161,087,000</u>	<u>146,817,000</u>

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(13) Discontinued Operation and Assets Held-For-Sale

On May 29, 2020, Chapman initiated a Change of Control Agreement that will divest control of Brandman University (the discontinued operation) to a separate accredited domestic educational institution in exchange for approximately \$137,000,000 when fully executed. The transaction is expected to be completed before the end of fiscal year 2021, and the discontinued operation will remain under control of Chapman University's Board of Trustee until that time.

The discontinued operation's assets and liabilities are presented in the consolidated statement of financial position as current assets held-for-sale and current liabilities held-for-sale, respectively. The discontinued operation's change in net assets is presented as a discrete line item in the consolidated statement of activities. No gain has been recognized as a result of the expected sale.

The University began to locate a buyer in fiscal year 2020 for a building previously classified under Plant assets. The value recorded in Current assets held-for-sale in the Statement of Financial Position for the related asset is \$16,037,000 and \$14,038,000 as of the year ended May 31, 2020 and 2019, respectively. The University is expecting a sale to be made prior to the end of fiscal year 2021.

(14) Functional Expenses by Natural Classification

Certain categories of expenses that are attributable to more than one program or supporting function are allocated based on various methods. Specifically, facilities, interest and depreciation are allocated among functional classifications based on usage of space and square footage. Information technology costs are allocated based on software usage and the overall employees in the various functional categories. All other costs are charged directly to the appropriate functional category.

Expenses by natural and functional classification for the year ended May 31, 2020, were as follows:

Functional expenses by natural classification (000's)							
	Instruction	Academic Support	Student Services	General Institutional Support	Auxiliary Enterprises	2020 Total	2019 Total
Salary and benefits	\$ 133,540	26,210	18,853	37,678	5,229	221,510	210,369
Facilities	12,818	9,577	3,113	6,403	14,337	46,248	39,867
Depreciation	18,824	6,057	2,872	3,560	6,881	38,194	34,714
Professional services	7,378	1,683	1,005	5,152	414	15,632	15,833
Promotion and advertising	364	334	1,068	1,958	15	3,739	3,926
Interest	4,312	1,376	681	853	6,137	13,359	14,070
Supplies	3,093	1,030	1,331	1,068	132	6,654	8,035
Other	11,230	5,839	3,513	1,939	6,502	29,023	29,242
Total	<u>\$ 191,559</u>	<u>52,106</u>	<u>32,436</u>	<u>58,611</u>	<u>39,647</u>	<u>374,359</u>	<u>356,056</u>

(15) Subsequent Events

The University has evaluated subsequent events from the date of the consolidated statement of financial position through November 24, 2020, the date on which the consolidated financial statements were issued.

SUPPLEMENTAL SCHEDULE

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Supplementary Schedule of Financial Responsibility Data

As of and for the year ended May 31, 2020

<u>Location in financial statements or related notes</u>	<u>Financial element</u>	<u>Amount</u>
Primary reserve ratio: Expendable net assets:		
Statement of financial position	Net assets without donor restrictions	\$ 938,820,000
Statement of financial position	Net assets with donor restrictions	281,619,000
Note 9, Related Parties	Unsecured related party receivable	39,156,000
Statement of financial position	Total property, plant, and equipment, net	978,660,000
Note 5, Property, Plant and Equipment	Construction in progress	18,967,000
Statement of financial position	Total long-term debt	321,534,000
Statement of financial position	Annuities with donor restrictions	1,756,000
Note, 12, Net Assets	Life income funds with donor restrictions	1,046,000
Note, 12, Net Assets	Net assets with donor restrictions: restricted in perpetuity	161,087,000
Primary reserve ratio: Expenses and losses:		
Statement of activities	Total expenses and losses without donor restrictions	374,359,000
Equity ratio: Modified net assets:		
Statement of financial position	Net assets without donor restrictions	938,820,000
Statement of financial position	Net assets with donor restrictions	281,619,000
Note 9, Related Parties	Unsecured related party receivable	39,156,000
Equity ratio: Modified assets:		
Statement of financial position	Total assets	1,697,089,000
Note 9, Related Parties	Unsecured related party receivable	39,156,000
Net income ratio:		
Statement of activities	Change in net assets without donor restrictions	73,989,000
Statement of activities	Total revenues and gains without donor restrictions	432,341,000

See accompanying independent auditors' report.