McKendree University

Independent Auditor’s Report and Consolidated Financial Statements

June 30, 2019 and 2018

McKendree University
June 30, 2019 and 2018

Contents

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Independent Auditor's Report

The Board of Trustees
McKendree University
Lebanon, Illinois

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of McKendree University (the "University"), which comprise the consolidated statements of financial position as of June 30, 2019 and 2018, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the University'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 University'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 June 30, 2019 and 2018, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As discussed in Note 2 to the consolidated financial statements, in 2019, the University adopted new accounting guidance, Accounting Standards Update (ASU) 2016-14, *Not-For-Profit Entities* (Topic 958): *Presentation of Financial Statements of Not-For-Profit Entities*. Our opinion is not modified with respect to this matter.

The accompanying consolidated financial statements have been prepared assuming the University will continue as a going concern. As discussed in Note 21, the University has suffered recurring decreases in net assets without donor restriction, which raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 21. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

Other Matters

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying supplementary information, including the schedule of expenditures of federal awards required by Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards,* as listed in the table of contents, is presented for purposes of additional analysis 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 information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 20, 2020, on our consideration of the University’s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the University’s internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the University’s internal control over financial reporting and compliance.

BKD, LLP

St. Louis, Missouri
March 20, 2020

McKendree University

Consolidated Statements of Financial Position

June 30, 2019 and 2018

	2019	2018
Assets		
Cash	$ 736,882	$ 134,135
Accounts receivable, net of allowance: 2019 - $2,089,778 and 2018 - $3,775,640	3,574,274	3,289,508
Contributions receivable, net of allowance: 2019 - $639,536 and 2018 - $295,140	6,920,832	1,672,463
Student loans receivable, net of allowance: 2019 - $464,125 and 2018 - $477,390	381,619	428,202
Investments	39,050,345	35,614,635
Prepaid expenses and other assets	232,049	319,090
Property and equipment, net	57,411,775	61,286,395
Total assets	$ 108,307,776	$ 102,744,428
Liabilities		
Outstanding checks in excess of bank balance	$ 177,572	$ 83,860
Accounts payable	850,053	739,132
Annuities payable	848,563	862,518
Accrued liabilities	3,043,087	3,471,851
Notes payable to bank	12,755,910	11,148,602
Deferred revenue	1,651,928	1,450,464
Federal student loans funds payable	159,452	163,435
Long-term debt and capital lease obligation, net	30,072,171	31,504,263
Total liabilities	49,558,736	49,424,125
Net Assets		
Without donor restrictions	9,105,723	12,096,255
With donor restrictions	49,643,317	41,224,048
Total net assets	58,749,040	53,320,303
Total Liabilities and Net Assets	$ 108,307,776	$ 102,744,428

McKendree University
Consolidated Statements of Activities
June 30, 2019 and 2018

	2019		
	Without Donor Restrictions	With Donor Restrictions	Total
Operating Revenue			
Tuition and fees, net of scholarships allowances:			
2019 - $24,852,958	$ 26,400,931	$ -	$ 26,400,931
Government grants	304,068	-	304,068
Private gifts and grants	1,181,260	7,624,141	8,805,401
Investment return, net	137,487	2,032,109	2,169,596
Other income	1,180,850	10,418	1,191,268
Sales and services of auxiliary enterprises	9,422,382	-	9,422,382
Net assets released from restrictions	1,247,399	(1,247,399)	-
Total operating revenue	39,874,377	8,419,269	48,293,646
Operating Expenses			
Salaries and wages	16,948,654	-	16,948,654
Benefits	4,885,295	-	4,885,295
Purchased services	5,396,141	-	5,396,141
Facility and occupancy	3,271,320	-	3,271,320
Travel, conference and events	2,105,923	-	2,105,923
Licenses and fees	1,268,335	-	1,268,335
Materials and supplies	1,882,249	-	1,882,249
Other	947,360	-	947,360
Depreciation and amortization	3,671,687	-	3,671,687
Interest	1,448,198	-	1,448,198
Bad debt expense	1,039,747	-	1,039,747
Loss on extinguishment of debt	-	-	-
Total operating expenses	42,864,909	-	42,864,909
Change in Net Assets	(2,990,532)	8,419,269	5,428,737
Net Assets, Beginning of Year	12,096,255	41,224,048	53,320,303
Net Assets, End of Year	$ 9,105,723	$ 49,643,317	$ 58,749,040

McKendree University

Consolidated Statements of Activities (Continued)

June 30, 2019 and 2018

	2018		
	Without Donor Restrictions	With Donor Restrictions	Total
Operating Revenue			
Tuition and fees, net of scholarships allowances:			
2018 - $24,148,835	$ 27,601,011	$ -	$ 27,601,011
Government grants	162,335	2,000	164,335
Private gifts and grants	426,039	1,778,010	2,204,049
Investment return, net	310,205	2,649,369	2,959,574
Other income	482,605	171,281	653,886
Sales and services of auxiliary enterprises	10,025,375	-	10,025,375
Net assets released from restrictions	1,686,650	(1,686,650)	-
Total operating revenue	40,694,220	2,914,010	43,608,230
Operating Expenses			
Salaries and wages	17,851,001	-	17,851,001
Benefits	5,047,714	-	5,047,714
Purchased services	5,155,014	-	5,155,014
Facility and occupancy	3,812,948	-	3,812,948
Travel, conference and events	2,123,074	-	2,123,074
Licenses and fees	991,076	-	991,076
Materials and supplies	2,236,732	-	2,236,732
Other	228,459	-	228,459
Depreciation and amortization	3,791,451	-	3,791,451
Interest	1,464,051	-	1,464,051
Bad debt expense	825,862	-	825,862
Loss on extinguishment of debt	328,697	-	328,697
Total operating expenses	43,856,079	-	43,856,079
Change in Net Assets	(3,161,859)	2,914,010	(247,849)
Net Assets, Beginning of Year	15,258,114	38,310,038	53,568,152
Net Assets, End of Year	$ 12,096,255	$ 41,224,048	$ 53,320,303

McKendree University

Consolidated Statements of Cash Flows

Years Ended June 30, 2019 and 2018

	2019	2018
Operating Activities		
Change in net assets	$ 5,428,737	$ (247,849)
Items not requiring (providing) operating cash flows		
Depreciation	3,652,166	3,755,351
Amortization of debt issuance cost	19,521	36,100
Loss on extinguishment of long-term debt	-	328,697
Provision for losses on accounts receivable	685,155	846,816
Provision for losses on contributions and student loans receivables	354,592	(21,033)
Noncash gifts	(568,647)	(567,008)
Contributions restricted for long-term investments	(870,635)	(212,422)
Investment income restricted for long-term investments	(113,377)	(67,846)
Net realized and unrealized gains on investments	(1,369,762)	(2,214,936)
Loss on disposal of property and equipment	26,294	-
Actuarial gains on annuity obligations	10,702	(24,975)
Change in cash surrender value of life insurance policies	1,466	269
Changes in		
Accounts receivable	(935,204)	1,979,983
Student loans receivable	39,982	(23,373)
Contributions receivable	(5,631,077)	494,257
Prepaid expenses and other assets	87,041	59,544
Accounts payable	142,810	112,745
Accrued expenses and federal student loans fund payable	(472,961)	(13,038)
Deferred revenue	201,464	(138,707)
Net cash provided by operating activities	688,267	4,082,575
Investing Activities		
Purchase of property and equipment	(779,354)	(938,803)
Proceeds from sale of property and equipment	171,342	-
Purchase of investments	(11,123,535)	(9,426,572)
Proceeds from sale of investments	10,505,349	8,781,392
Net cash used in investing activities	(1,226,198)	(1,583,983)

(Continued)

McKendree University

Consolidated Statements of Cash Flows (Continued)

Years Ended June 30, 2019 and 2018

	2019	2018
Financing Activities		
Payments to annuitants	$ (92,742)	$ (99,761)
Proceeds from annuitants	-	8,680
Net borrowings on notes payable	378,297	792,038
Gross payments on MAP note payable	(2,793,989)	(4,681,462)
Gross borrowings on MAP note payable	4,023,000	2,296,752
Extinguishment of long-term debt	-	(7,302,671)
Payments on long-term debt	(876,767)	(515,224)
Payment of debt issuance cost	-	(142,081)
Proceeds from issuance of long-term debt	-	7,550,000
Payments on capital lease obligation	(574,845)	(543,250)
Increase (decrease) in outstanding checks in excess of bank balance	93,712	(234,511)
Proceeds from contributions restricted for long-term investment	870,635	212,422
Proceeds from investment income restricted for long-term investment	113,377	67,846
Net cash provided by (used in) financing activities	1,140,678	(2,591,222)
Increase (Decrease) in Cash	602,747	(92,630)
Cash, Beginning of Year	134,135	226,765
Cash, End of Year	$ 736,882	$ 134,135

Additional Cash Payment Information

	2019	2018
Interest paid	$ 1,462,061	$ 1,456,830

McKendree University
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Organization

McKendree University (the "University") is a private, co-educational college, providing students with both a liberal arts education and the preparation necessary for success in their chosen fields. The University was incorporated as a not-for-profit organization in January 1839, under the laws of the state of Illinois. The University, located in Lebanon, Illinois, also offers courses at Scott Air Force Base and other locations in Southern Illinois and Radcliff, Kentucky.

Basis of Accounting

The following organization is consolidated into the financial statement of the University:

- McKBearcat LLC, a wholly-owned entity, was formed in 2012 to purchase the 114-acre golf course adjacent to the University owned property in Lebanon, Illinois. McKBearcat LLC ceased operations in February 2017.

The University's consolidated financial statements are prepared on the accrual basis of accounting in conformity with generally accepted accounting principles (GAAP) in the United States of America. All significant intercompany transactions and accounts have been eliminated.

Classification of Net Assets

Net assets, revenues, gains and losses are classified based on the existence or absence of donor restrictions.

Net assets without donor restrictions are available for use in general operations and not subject to donor restrictions. The governing board has designated, from net assets without donor restrictions, net assets for an operating reserve and board-designated endowment.

Net assets with donor restrictions are subject to donor restrictions. Some restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity.

Revenue Recognition and Deferred Revenue

The University recognizes revenues from tuition and fees in the fiscal year in which the educational programs are conducted. Summer session tuition fees billed in the current fiscal year for future year's programs are reported as deferred revenue. Revenue from tuition, room and board and other fees that are billed in advance are deferred and recognized over the periods to which the fees relate.

Functional Classification of Expenses

The costs of supporting the various programs and other activities are reported by natural classification on the Consolidated Statement of Activities and by function in Note 16. Certain costs have been allocated among the program and supporting categories based on a variety of cost allocation methods including time and effort and square footage.

Accounts Receivable

Accounts receivable are stated at the amount billed plus any accrued and unpaid interest. Student accounts receivable are ordinarily due at the start of each semester. Non-student accounts receivable are due 30 days after the issuance of the invoice. Accounts that are unpaid after the due date bear interest at 1½ percent per month. Payments of accounts receivable are applied to the earliest unpaid invoices unless a specific term is indicated.

The University provides an allowance for doubtful accounts, which is based upon a review of outstanding receivables, historical collection information and existing economic conditions. All accounts or portions thereof deemed to be uncollectible or to require an excessive collection cost are written off to the allowance for doubtful accounts.

Student Loans Receivable

Student loans receivable consist of amounts due from the Federal Perkins Loan Program and the Wagner Loan Program, a non-federal loan program, for former and current students. The carrying amount of student loans receivable is reduced by a valuation allowance that reflects management's best estimate of amounts that will not be collected. The allowance for doubtful accounts is based on management's assessment of the collectability of specific student loans receivable and the aging of the student loans receivable.

Investments and Investment Return

Investments in equity securities having a readily determinable fair value and in all debt securities are carried at fair value. Other investments are valued at the lower of cost (or fair value at time of donation, if acquired by contribution) or fair value. Investment return includes dividend, interest and other investment income; realized and unrealized gains and losses on investments carried at fair value; and realized gains and losses on other investments, less external and direct internal investment expenses. Investment return that is initially restricted by donor stipulation and for which the restriction will be satisfied in the same year is included in net assets with donor restriction and then released from restriction. Other investment return is reflected in the Consolidated Statements of Activities as with or without donor restriction based upon the existence and nature of any donor or legally imposed restrictions.

The University maintains pooled investment accounts for its endowments. Investment income and realized and unrealized gains and losses from securities in the pooled investment accounts are allocated to the individual endowments based on the relationship of the fair value of the interest of each endowment to the total fair value of the pooled investments accounts, as adjusted for additions to or deductions from those accounts.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation. Depreciation is charged to expense using the straight-line method over the estimated useful life of each asset. Assets under capital lease obligations and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives. The University capitalizes net interest expense on funds used during construction of major projects during the construction period. The estimated useful lives for each major depreciable classification of property and equipment are as follows:

Furnishings and equipment	3-10 years
Buildings and improvements	5-40 years

Long-Lived Asset Impairment

The University evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimated future cash flows expected to result from the use and eventual disposition of the asset are less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value. No asset impairment was recognized during the years ended June 30, 2019 and 2018.

Annuity Agreements

The University utilizes the actuarial method to record the liability for its annuity agreements. Assets are recorded at fair value at date of receipt, and a liability is recorded based on the present value of the agreement utilizing the life expectancy tables as set forth in the Internal Revenue Code. On an annual basis, an adjustment is made to the liability to record an actuarial gain or loss based on the donor’s revised life expectancy. Upon termination of the agreement, the values are transferred to the appropriate net asset classification, in accordance with the wishes of the donor.

Contributions

Contributions are provided to the University either with or without restrictions placed on the gift by the donor. Revenues and net assets are separately reported to reflect the nature of those gifts – with or without donor restrictions. The value recorded for each contribution is recognized as follows:

Nature of the Gift	Value Recognized
Conditional gifts, with or without restriction	
Gifts that depend on the University overcoming a donor-imposed barrier to be entitled to the funds	Not recognized until the gift becomes unconditional, *i.e.* the donor-imposed barrier is met
Unconditional gifts, with or without restriction	
Received at date of gift – cash and other assets	Fair value
Received at date of gift – property, equipment and long-lived assets	Estimated fair value
Expected to be collected within one year	Net realizable value
Collected in future years	Initially reported at fair value determined using the discounted present value of estimated future cash flows technique

In addition to the amount initially recognized, revenue for unconditional gifts to be collected in future years is also recognized each year as the present-value discount is amortized using the level-yield method.

When a donor stipulated time restriction ends or purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the Consolidated Statements of Activities as net assets released from restrictions. Absent explicit donor stipulations for the period of time that long-lived assets must be held, expirations of restrictions for gifts of land, buildings, equipment and other long-lived assets are reported when those assets are placed in service. Gifts and investment income that are originally restricted by the donor and for which the restriction is met in the same time period are recorded as revenue with donor restrictions and then released from restriction.

Government Grants

Support funded by grants is recognized as the University meets the conditions prescribed by the grant agreement, performs the contracted services or incurs outlays eligible for reimbursement under the grant agreements. Grant activities and outlays are subject to audit and acceptance by the granting agency and, as a result of such audit, adjustments could be required.

Income Taxes

The University is exempt from income taxes under Section 501 of the Internal Revenue Code and a similar provision of state law. However, the University is subject to federal income tax on any unrelated business taxable income. The University files tax returns in the U.S. federal jurisdiction. With a few exceptions, the University is no longer subject to U.S. federal examinations by tax authorities for years before 2016.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues, expenses, gains, losses and other changes in net assets during the reporting period. Estimates related to allowances for various receivables are reflected in each specific footnote. Actual results could differ from those estimates.

Risks and Uncertainties

The University's investments are exposed to various risks, such as interest rate, market and credit. Due to the level of risk associated with certain investments and the level of uncertainty related to changes in the value of investments, it is at least possible that changes in values of investment securities in the near term would materially affect the amounts reported in the Consolidated Financial Statements.

Contingencies and Litigation

The University is subject to other claims and lawsuits that arose primarily in the ordinary course of its activities. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the financial position, change in net assets and cash flows of the University. Events could occur that would change this estimate materially in the near term.

Revisions

Certain revisions have been made to the 2018 endowment footnote to remove amounts that were not following the investing and spending policies of the endowment. These revisions did not have an impact on the financial statements.

Accounting Pronouncements and Future Changes in Accounting Principle

The Financial Accounting Standards Board (FASB) issues Accounting Standards Updates (ASU) that are applicable to and have an impact on the University's Consolidated Financial Statements. The University evaluates and implements pronouncements by the effective fiscal year end date or prior if early adoption is permitted and deemed appropriate. The adoption of certain ASUs is pending further evaluation as noted.

Under Evaluation:

- ASU No. 2014-09, *Revenue from Contracts with Customers* (Topic 606), requires that the recognition of revenue from customer contracts be determined using a principles-based framework. This ASU was issued in May 2014 and is effective for the fiscal year 2020.
- ASU No. 2016-02, *Leases* (Topic 842), increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the Consolidated Statement of Financial Position and disclosing key information about leasing arrangements. This ASU was issued in February 2016 and is effective for the fiscal year ended 2022.
- ASU No. 2016-18, *Statement of Cash Flows* (Topic 230), requires presentation of the total change in cash, cash equivalents, restricted cash and restricted cash equivalents for the period of the statement of cash flows. This ASU was issued in November 2016 and is effective for the fiscal year 2020.
- ASU No. 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*, clarifies and improves the scope and accounting guidance in ASU No. 2014-09 related to revenue recognition for grants and contributions. The definition of an exchange transaction and the criteria for evaluating whether contributions are unconditional or conditional have been clarified. This ASU was issued in June 2018 and is effective for the fiscal year 2020.

Note 2: Changes in Accounting Principles

In 2019, the University adopted the following Accounting Standards Update (ASU):

Presentation of Financial Statements of Not-For-Profit Entities

ASU 2016-14, *Not-For-Profit Entities* (Topic 958): *Presentation of Financial Statements of Not-For-Profit Entities*. A summary of the changes is as follows:

<u>Consolidated Statements of Financial Position and Consolidated Statements of Activities</u>

- The Consolidated Statements of Financial Position and Consolidated Statements of Activities distinguish between two new classes of net assets – those without donor-imposed restrictions and those with. This is a change from the previously presented three classes of net assets and changes in net assets – unrestricted, temporarily and permanently restricted.

<u>Notes to the Consolidated Financial Statements</u>

- Expenses are reported by both nature and function in one location for 2019.
- Enhanced quantitative and qualitative disclosures provide additional information useful in assessing liquidity and cash flows available to meet operating expenses for one-year from the date of the Consolidated Statement of Financial Position.
- Amounts and purposes of Board of Trustees designations as of the end of the year are disclosed.

This change had no impact on previously reported total change in net assets.

Fair Value Measurements

ASU 2018-13, *Fair Value Measurement* (Topic 820), which changes the disclosure requirements for fair value measurement including removing the amounts and reasons for transfers between Levels 1 and 2, the policy for timing of transfers between levels, the valuation processes for Level 3 fair value measurements and the changes in unrealized gains and losses for the period included in earnings for recurring Level 3 fair value measurements. Modifications required as a result of this ASU include disclosure of transfers in and out of Level 3 and purchases and issues of Level 3 assets and liabilities, additional disclosures around investments in certain entities that calculate net asset value and clarify requirements to communicate information about the uncertainty in measurement as of the reporting date. Certain additional disclosures are required as a result of this standard that relate to Level 3 fair value measurements. This change had no impact on previously reported total change in net assets.

Note 3: Liquidity and Availability

The University regularly monitors the availability of resources required to meet its operating needs and other contractual commitments, while also striving to maximize the investment of its available funds. For purposes of analyzing resources available to meet general expenditures over a 12-month period, the University considers all expenditures related to its ongoing activities of instruction and public service as well as the conduct of services undertaken to support those activities to be general expenditures.

At June 30, 2019, the University's financial resources as follows:

	Financial Assets	
	At year end	Available for Next 12 Months of Operations
Cash, net of outstanding checks in excess of bank balance	$ 559,310	$ -
Accounts receivable, net	3,574,274	3,009,175
Contributions receivable, net	6,920,832	605,270
Student loans receivable, net	381,619	-
Investments	39,050,345	1,272,678
	$ 50,486,380	$ 4,887,123

The University also has lines of credit available to meet short-term cash needs. See Note 11 for information about these arrangements.

Note 4: Accounts Receivable

Accounts receivable as of June 30 were:

	2019	2018
Student accounts	$ 5,420,022	$ 6,843,240
Business partner accounts	224,207	50,203
Federal and state accounts	19,823	168,205
Other	-	3,500
	5,664,052	7,065,148
Less allowance for doubtful accounts	2,089,778	3,775,640
Accounts receivable, net	$ 3,574,274	$ 3,289,508

Note 5: Contributions Receivable

Contributions receivable are recognized at the net present value of the contribution calculated using a discount rate of 3.25 percent at June 30, 2019, and 2.91 percent at June 30, 2018. An allowance between 5 and 15 percent, depending on size of pledge and experience with the donor, is recognized for uncollectible contributions. Contributions receivable, less discounts for present value on long-term pledges and related allowances for uncollectible receivables at June 30, are summarized as follows:

	June 30, 2019		
	Without Donor Restrictions	With Donor Restrictions	Total
Contributions receivable	$ 115,662	$ 8,587,020	$ 8,702,682
Unamortized discount	(26,071)	(1,116,243)	(1,142,314)
	89,591	7,470,777	7,560,368
Allowance	(17,267)	(622,269)	(639,536)
Contributions receivable, net	$ 72,324	$ 6,848,508	$ 6,920,832

	June 30, 2018		
	Without Donor Restrictions	With Donor Restrictions	Total
Contributions receivable	$ 25,199	$ 1,999,548	$ 2,024,747
Unamortized discount	(699)	(56,445)	(57,144)
	24,500	1,943,103	1,967,603
Allowance	(3,675)	(291,465)	(295,140)
Contributions receivable, net	$ 20,825	$ 1,651,638	$ 1,672,463

Anticipated timeline of receipt of receivable is summarized as:

	2019	2018
Receivable in less than one year	$ 1,739,988	$ 782,915
Receivable in one to five years	3,815,715	1,225,762
Receivable in greater than five years	3,146,979	16,070
	8,702,682	2,024,747
Less allowance for doubtful accounts	639,536	295,140
Less unamortized discount	1,142,314	57,144
Total contributions receivable, net	$ 6,920,832	$ 1,672,463

At June 30, 2019, the University had not received any conditional promises to give.

Note 6: Student Loans Receivable

At June 30, student loans included on the Consolidated Statements of Financial Position consisted of the following:

	2019	2018
Wagner loans	$ 742,311	$ 773,193
Federal Perkins loans	103,433	126,241
Other	-	6,158
	845,744	905,592
Less allowance for doubtful accounts	464,125	477,390
Accounts receivable, net	$ 381,619	$ 428,202

The Wagner Loan is a University sponsored program funded by an endowed gift to support students entering the ministry. The program includes a forgiveness option, where loans to students are forgiven after serving a specified period in service to the community. Management estimates that approximately half of all loans will be forgiven. New loans awarded were $13,295 and $56,904 in fiscal years 2019 and 2018, respectively.

On September 30, 2017, the Federal Perkins Loan Program expired when it was not extended by the U.S. Congress. Students did not receive new loans after that date unless the student had received a disbursement before October 1, 2017 for the 2017-2018 award year. Under current federal guidelines, the University will continue to service existing Perkins Loans through a third-party administrator.

Note 7: Investments

Total investments for the fiscal years ended June 30 are as follows:

	2019		2018	
	Cost	Fair Value	Cost	Fair Value
Money market funds	$ 3,111,086	$ 3,111,117	$ 1,485,479	$ 1,484,347
Equities	20,338,954	24,889,673	19,629,287	23,801,390
Fixed income	9,337,929	9,899,221	9,363,847	9,532,242
Hedge funds	27,245	27,578	70,392	100,650
Real estate and other	925,866	1,122,756	498,659	696,006
Total investments	$ 33,741,080	$ 39,050,345	$ 31,047,664	$ 35,614,635

Assets and liabilities measured and reported at fair value are classified and disclosed within one of the following categories:

Level 1

Quoted prices (unadjusted) in active markets for identical assets or liabilities as of the measurement date. An active market is one in which transactions occur with sufficient frequency and volume to provide pricing information on an ongoing basis. Market price data is generally obtained from exchange or dealer markets.

Level 2

Pricing inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the same term of the assets. Inputs are obtained from various sources including market participants, dealers and brokers using a market approach.

Level 3

Pricing inputs are unobservable and include situations where there is little, if any, market activity for the fair value of the assets or liabilities.

Inputs are used in applying the various valuation techniques and broadly refer to the assumptions that market participants use to make valuation decisions, including assumptions about risk. Inputs may include price information, volatility statistics, specific and broad credit data, liquidity statistics, and other factors. A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Furthermore, the fair value hierarchy does not correspond to a financial instrument's relative liquidity in the market or to its level of risk. The University assumes that any transfers between levels occur at the beginning of any period.

Following is a summary of the University's investments carried at fair value as of June 30:

	2019			
	Fair Value	**Level 1**	**Level 2**	**Level 3**
Money market funds	$ 3,111,117	$ 3,111,117	$ -	$ -
Equities	24,889,673	24,798,505	91,168	-
Fixed income	9,899,221	9,887,313	11,908	-
Hedge funds	27,578	-	27,578	-
Real estate and other	1,122,756	-	13,437	1,109,319
Total investments	$ 39,050,345	$ 37,796,935	$ 144,091	$ 1,109,319

	2018			
	Fair Value	**Level 1**	**Level 2**	**Level 3**
Money market funds	$ 1,484,347	$ 1,484,347	$ -	$ -
Equities	23,801,390	23,725,004	76,386	-
Fixed income	9,532,242	9,518,985	13,257	-
Hedge funds	100,650	-	100,650	-
Real estate and other	696,006	-	42,189	653,817
Total investments	$ 35,614,635	$ 34,728,336	$ 232,482	$ 653,817

Transfers to Level 3

The University holds 42.82 acres of land (formerly the Locust Hills Golf Course) as investment property. The 2012 purchase of the 110.43 acres and buildings contained therein, was made using board-designated endowed funds. McKBearcat, LLC was established to operate the facility. That facility was closed in 2017. A portion of the course (67.61 acres and all buildings on that land) was sold in April 2019 to a related party. The remaining holding is classified as a portion of the board-designated endowment. The amount transferred into Level 3 for the land was $428,000 for 2019.

In 2018, $198,255 was purchased and transferred into Level 3 for contributions to a 457 Plan.

Note 8: Endowment

The University's endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The *Illinois Uniform Prudent Management of Institutional Funds Act* (UPMIFA) governs the management and investment of funds held by not-for-profit corporations and other institutions. Absent donor stipulations to the contrary, the statutory guidelines contained in UPMIFA relate to the prudent management, investment and expenditure of donor-restricted endowment funds without regard to the original value of the gifts. However, UPMIFA contains specific factors that must be considered prior to making investment decisions or appropriating funds for expenditure.

The Board of Trustees' interpretation of its fiduciary responsibilities for donor-restricted endowment funds under Laws of the State of Illinois, including UPMIFA, is to preserve intergenerational equity to the extent possible by prudently managing, investing and spending from the endowment funds. This principle holds that future endowment beneficiaries should receive at least the same level of economic support that the current generation receives. As a result of this interpretation, the University classifies as donor-restricted net assets the unappropriated portion of (a) the original value of gifts donated to a true endowment fund; (b) the original value of subsequent gifts to a true endowment fund; and (c) accumulations to a true endowment fund made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. Unspent appropriations related to donor-restricted endowment funds are classified as net assets with donor restrictions until the amounts are expended by the University in a manner consistent with the donor's intent.

The Board of Trustees determines the appropriate amount to withdraw from endowment and similar funds on an annual basis to provide support for operations with prudent concern for the long-term growth in the underlying assets as well as the specific factors detailed in UPMIFA.

The composition of net assets by type of endowment fund at June 30 was:

	2019		
	Without Donor Restrictions	With Donor Restrictions	Total
Board-designated endowment funds	$ 2,176,497	$ -	$ 2,176,497
Donor restricted endowment funds			
Original donor-restricted amount and amounts required to be maintained in perpetuity by donor	-	24,527,163	24,527,163
Accumulated gains	-	7,974,343	7,974,343
Total endowment funds	$ 2,176,497	$ 32,501,506	$ 34,678,003

	2018		
	Without Donor Restrictions	With Donor Restrictions	Total
Board-designated endowment funds	$ 2,737,370	$ -	$ 2,737,370
Donor restricted endowment funds			
Original donor-restricted amount and amounts required to be maintained in perpetuity by donor	-	22,351,103	22,351,103
Accumulated gains	-	8,376,516	8,376,516
Total endowment funds	$ 2,737,370	$ 30,727,619	$ 33,464,989

Changes in endowment net assets for the years ended June 30 were:

	2019		
	Without Donor Restriction	With Donor Restrictions	Total
Endowment net assets, beginning of year	$ 2,737,370	$ 30,727,619	$ 33,464,989
Investment return, net	110,001	1,712,013	1,822,014
Contributions	-	847,273	847,273
Other transfers	(670,874)	313,650	(357,224)
Appropriation of endowment assets for expenditure	-	(1,099,049)	(1,099,049)
Endowment net assets, end of year	$ 2,176,497	$ 32,501,506	$ 34,678,003

	2018		
	Without Donor Restriction	With Donor Restrictions	Total
Endowment net assets, beginning of year	$ 3,414,120	$ 28,384,027	$ 31,798,147
Investment return, net	298,223	2,496,044	2,794,267
Contributions	-	383,607	383,607
Other transfers	(962,000)	49,577	(912,423)
Appropriation of endowment assets for expenditure	(12,973)	(585,636)	(598,609)
Endowment net assets, end of year	$ 2,737,370	$ 30,727,619	$ 33,464,989

Other transfers represents activity determined to either not be following the investing and spending policies (decreases) or were following investing policies (increases). These transfers did not impact net asset classifications in the consolidated statement of activities.

The University's endowment consists of approximately 190 individual funds providing long-term support of scholarships, institutional financial aid and other long-term financial needs of the University.

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level the University is required to retain as a fund of perpetual duration pursuant to donor stipulation or UPMIFA. At June 30, 2019 and 2018, funds with original gift values of $251,220 and $251,150, fair values of $177,673 and $168,237, and deficiencies of $73,547 and $82,913, respectively, were reported in net assets with donor restrictions. These deficiencies resulted from unfavorable market fluctuations that occurred shortly after investment of new restricted contributions and continued appropriation for certain purposes that was deemed prudent by the governing body.

The University has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs and other items supported by its endowment while seeking to maintain the purchasing power of the endowment. Endowment assets include those assets of donor-restricted endowment funds the University must hold in perpetuity or for donor-specified periods, as well as those of board-designated endowment funds. Under the University's policies, endowment assets are invested in a manner that is intended to produce results that meet or exceed the annual spending rate plus all fees and costs incurred in managing the investments while assuming a moderate level of investment risk. The University expects its endowment funds to provide an average rate of return of approximately 10 percent annually over time. Actual returns in any given year may vary from this amount.

To satisfy its long-term rate of return objectives, the University relies on a total return strategy in which investment returns are achieved through both current yield (investment income such as dividends and interest) and capital appreciation (both realized and unrealized). The University targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

The University has a policy (the spending policy) of appropriating for expenditure each year 4 percent of its endowment fund's average fair value over the prior three years through the December preceding the year in which expenditure is planned. In establishing this policy, the University considered the long-term expected return on its endowment. This is consistent with the University's objective to maintain the purchasing power of endowment assets held in perpetuity or for a specified term, as well as to provide additional real growth through new gifts and investment return. The University spending policy does not permit spending from underwater endowment funds.

Note 9: Property and Equipment

Property and equipment at June 30 consists of:

	2019	2018
Land	$ 1,725,975	$ 2,533,903
Buildings and improvements	89,827,940	89,575,042
Furnishings and equipment	16,188,691	18,039,588
Construction in progress	190,651	30,067
	107,933,257	110,178,600
Less accumulated depreciation	50,521,482	48,892,205
	$ 57,411,775	$ 61,286,395

Total depreciation expense for 2019 and 2018 was $3,652,167 and $3,755,351, respectively.

Note 10: Annuities Payable

The University has been the recipient of several gift annuities which require future payments to the donor or their named beneficiaries. The assets received from the donor are recorded at fair value. The University has recorded a liability at June 30, 2019 and 2018, of $848,563 and $862,518, respectively, which represents the present value of the future annuity obligations. The liability has been determined using a discount rate of 3.0 percent and 3.4 percent at June 30, 2019 and 2018, respectively.

Note 11: Notes Payable to Bank

The University maintains a $12,000,000 revolving bank line of credit that expires on December 24, 2022, and is collateralized by an investment account. At June 30, 2019 and 2018, there was $11,526,899 and $11,148,602, respectively, borrowed against this line. Interest, which varies with the bank's prime rate, was 4.00 percent and 3.75 percent on June 30, 2019 and 2018, respectively, and is payable quarterly.

The University also maintains a $3,000,000 revolving bank line of credit that expires on December 23, 2022, and is collateralized by an investment account. At June 30, 2019 and 2018, there was $1,229,011 and $0, respectively, borrowed against this line. Interest, which varies with the bank's prime rate, was 4.00 percent and 3.75 percent on June 30, 2019 and 2018, respectively, and is payable quarterly.

In connection with the notes payable to bank, the University is required, among other things, to maintain a ratio of debt service coverage in excess of 1.2 to 1.0. This particular covenant is only required to be calculated annually. The bank has formally approved noncompliance with this requirement. In consideration for the waiver, the University has agreed to pledge additional property as collateral on the debt, engage the services of a financial consultant and submit a plan to achieve certain financial targets including budget and cash flow information to the lender.

Note 12: Long-Term Debt

	2019	2018
Residential Facilities Revenue Bonds (McKendree University) Series 2010 of the state of Illinois, Southwestern Illinois Development Authority; 3.10% interest per annum due twice annually through December 30, 2030 (A)	$ 5,697,338	$ 6,172,116
Revenue Bonds (McKendree University) Series 2017 of the county of St. Clair, Illinois (B)	7,190,000	7,550,000
Mortgage note payable to bank; fixed interest rate of 4.0%; principal and interest payments of $8,230 due quarterly through July 1, 2028 (C)	253,494	275,717
Capital lease obligation, payable monthly at amounts ranging from $97,623 to $115,863; lease term expires January 2037 (D)	16,712,032	17,286,877
Mortgage note payable to bank; variable interest rate currently at 3.50%; principal and interest payments due monthly through April 27, 2026 (E)	463,245	483,012
	30,316,109	31,767,722
Less unamortized debt issuance costs	243,938	263,459
	$ 30,072,171	$ 31,504,263

(A) On December 30, 2010, the University issued $14,000,000 in the county of St. Clair, Illinois Residential Facilities Revenue Bonds (McKendree University) Series 2010 under a trust indenture between the state of Illinois, Southwestern Illinois Development Authority and Busey Bank, formerly TheBANK of Edwardsville. The Bonds were amended in November 2016 which modified the interest rate and eliminated the requirement of a debt reserve fund. The bonds are maturing in 2030 with an interest rate of 3.10 percent and are for the purpose of acquiring, constructing, furnishing and equipping an approximately 75,000 square foot residence hall located on University property in Lebanon, Illinois. Unamortized debt issuance costs based on an imputed interest rate of 3.47 and 3.20 percent were $115,909 and $126,061 at June 30, 2019 and 2018, respectively.

(B) On December 19, 2017, the University issued $7,550,000 in the county of St. Clair, Illinois Revenue Bonds (McKendree University) Series 2017 under a trust indenture with St. Clair County, Illinois maturing in 2033 with interest rates determined on an annual basis not to exceed 3.5 percent for the purposes of: (1) refunding and refinancing of the Series 2004 and 2012 outstanding revenue bonds; and (2) paying certain costs of issuing the bonds. Interest rates on the bonds in effect at June 30, 2019 and 2018, were 3.10 percent and 2.20 percent, respectively. Unamortized debt issuance costs based on an imputed interest rate of 2.86 percent and 1.23 percent were $128,029 and $137,398 at June 30, 2019 and 2018, respectively.

(C) On June 27, 2013, the University obtained a note payable of $370,000 secured by mortgaged property in Lebanon, Illinois. The property includes two apartment buildings which the University purchased for $462,805 in February 2013 to use for student housing. The note payable has a fixed interest rate of 4.00 percent, with quarterly payments of $8,230 in principal and interest through July 1, 2028.

(D) On January 18, 2017, the University entered into a capital lease for the use of eight apartment buildings. The lease term expires in January 2037.

(E) On June 1, 2015, the University purchased property adjacent to the University's Radcliff, Kentucky campus by entering into a three-month mortgage with the anticipation of doing renovation work and refinancing the full amount following the renovations. On April 27, 2016, the University entered into a mortgage to pay the remaining portion over 10 years with monthly principal and interest payments of $3,050 through May 2023 and $3,144 through maturity. The mortgage has a 3.50 percent interest rate through May 2023 and 4.00 percent interest rate through maturity.

In connection with both the Series 2010 and Series 2017 bonds, the University is required, among other things, to maintain a ratio of debt service coverage in excess of 1.2 to 1.0. This particular covenant is only required to be calculated annually. The bank has formally approved noncompliance with this requirement. In consideration for the waiver, the University has agreed to pledge additional property as collateral on the debt, engage the services of a financial consultant and submit a plan to achieve certain financial targets including budget and cash flow information to the lender.

Aggregate annual maturities of long-term debt payments and capital lease obligations at June 30, 2019, are:

	Long-Term Debt (Exc. Lease)	Capital Lease Obligation
2020	$ 898,325	$ 1,199,320
2021	920,072	1,210,840
2022	941,815	1,222,360
2023	963,492	1,233,880
2024	985,820	1,245,400
Thereafter	8,894,553	17,148,767
	$ 13,604,077	23,260,567
Less amount representing interest		6,548,535
Present value of future minimum lease payments		$ 16,712,032

Property and equipment include the following property under capital lease at June 30:

	2019	2018
Building and leasehold improvements	$ 18,078,004	$ 18,078,004
Less accumulated depreciation	2,259,751	1,355,850
	$ 15,818,253	$ 16,722,154

Note 13: Net Assets with Donor Restrictions

Net assets with donor restriction are available for the following purposes or periods:

	2019	2018
Subject to expenditure for a specified purpose		
Capital construction	$ 8,514,310	$ 6,845,087
Building maintenance	26,947	22,668
Athletic programs	-	368,154
Student activities	-	60,215
Educational programs	-	23,639
Promises to give, the proceeds from which have been restricted by donors for:		
Capital construction	2,006,721	1,445,607
Educational programs	547	30,767
Scholarship	14,199	45,101
Beneficial interests in charitable trusts held by others		
Scholarship	312,966	26,606
Educational programs	484,741	490,859
	11,360,431	9,358,703
Subject to the passage of time		
Beneficial interests in charitable trusts held be others	280,334	311,367
Assets held under split interest agreements	634,693	602,119
Promises to give that are not restricted by donor but which are unavailable for expenditure until due	4,866,353	224,240
	5,781,380	1,137,726

	2019	2018
Subject to appropriation and expenditure when a specified event occurs		
Scholarship	$ 6,657,780	$ 6,566,273
Loans to students	649,862	1,316,960
Educational programs	422,347	365,498
Building maintenance	244,354	127,785
	7,974,343	8,376,516
Subject to University's investment spending policy		
Scholarship	18,326,585	17,476,917
Loans to students	3,258,544	2,089,544
Educational programs	2,286,489	2,328,970
Building maintenance	477,872	287,435
Underwater endowments	177,673	168,237
	24,527,163	22,351,103
Total endowments	32,501,506	30,727,619
Total net assets with donor restrictions	$ 49,643,317	$ 41,224,048

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of other events specified by donors.

Note 14: Net Assets Released from Restriction

Net assets were released from donor restriction by incurring expenses satisfying the restricted purpose or by occurrence of other events specified by the donor.

	2019	2018
Scholarships disbursed	$ 1,238,032	$ 668,911
Programmatic purpose completed	9,367	1,017,739
	$ 1,247,399	$ 1,686,650

Note 15: Board-Designated Net Assets

Net assets without donor restrictions designated by the Board of Trustees for long-term investment totaled $2,176,496 and $1,960,062 at June 30, 2019 and 2018, respectively.

Note 16: Expenses

The University reflects expenses by natural classification in the Consolidated Statements of Activities for the years ended June 30, 2019 and 2018. For additional disclosure, the following schedule of expenses by natural classification and functional source for the year ended June 30, 2019, is presented.

	2019						
	Program Activities				Supporting Activities		
	Instruction	Public Service	Academic Support	Student Services	Institutional Support	Auxiliary Enterprises	Total Expense
Salaries and wages	$ 7,722,452	$ 217,306	$ 624,954	$ 4,291,576	$ 3,879,584	$ 135,451	$ 16,871,323
Benefits	1,416,230	45,281	115,699	965,626	2,067,170	247,749	4,857,755
Purchased services	203,879	64,723	21,971	589,964	810,411	1,625,878	3,316,826
Facility and occupancy	41,942	855	63,150	876,131	526,266	251,571	1,759,915
Travel, conference and events	126,910	21,367	62,886	1,559,708	266,178	64,400	2,101,449
Licenses and fees	74,745	13,566	233,961	89,821	855,401	250	1,267,744
Materials and supplies	127,905	61,256	142,521	722,646	432,517	15,535	1,502,380
Other	9,850	-	169	383,210	548,700	-	941,929
Depreciation and amortization	201,412	3,429	-	50,579	170,358	1,701,572	2,127,350
Interest	16,835	-	-	-	807,710	623,653	1,448,198
Bad debt expense	640,094	-	-	-	361,243	38,410	1,039,747
Chargebacks	13,726	430	4,787	(19,137)	133,815	2,038	135,659
	10,595,980	428,213	1,270,098	9,510,124	10,859,353	4,706,507	37,370,275
Allocation of operations and maintenance	1,554,254	312,111	369,172	1,122,536	1,160,887	975,674	5,494,634
Total expenses	$ 12,150,234	$ 740,324	$ 1,639,270	$ 10,632,660	$ 12,020,240	$ 5,682,181	$ 42,864,909
	2018						
Total expenses	$ 14,396,992	$ 382,885	$ 1,552,441	$ 13,489,805	$ 10,617,286	$ 3,416,670	$ 43,856,079

Institutional support includes fundraising expenses of $961,713 in 2019. For comparative purposes, fundraising expenses for 2018 were $1,019,005.

Note 17: Operating Leases

Non-cancellable operating leases primarily for equipment and buildings and commitments for building usage expire in various years through 2032. Total rental expense incurred for years ended June 30, 2019 and 2018, were $1,078,163 and $1,265,376, respectively. Future minimum lease payments at June 30, 2019, were:

2020	$ 744,468
2021	696,238
2022	687,128
2023	689,593
2024	599,527
Thereafter	3,414,946
	$ 6,831,900

Note 18: Pension Plan

The University has a defined contribution pension plan covering substantially all employees, which allows for both employee and employer contributions. The University contribution consists of contributing a flat 8 percent of employee’s eligible compensation, if the employee contributes at least 5 percent. Effective for any new employees enrolling in the plan after September 1, 2018, the University contribution match was reduced to 5 percent of employee’s eligible compensation. The University’s contribution to the plan was $1,058,601 and $1,139,045 for 2019 and 2018, respectively.

Note 19: Health Insurance

The University maintains an elective Health Reimbursement Arrangement for the benefit of its employees. Under this arrangement, the University receives health insurance premium contributions from its employees and purchases health care insurance for them. The employee is responsible for either the first $1,000 or first $3,000 of covered expenses annually. The purchased insurance plan has a stop-loss high deductible limit of $5,000 annually. The balance of any eligible expenses incurred up to the $5,000 deductible amounts is paid directly to the provider of services rendered to the employee by a third-party administrator on behalf of the University from accumulated health insurance premiums. The University’s liability is limited by the $5,000 stop loss coverage. At June 30, 2019 and 2018, the claims paid on behalf of employees under this provision were $496 and $90,271, respectively.

Beginning January 1, 2018, the University moved to a self-insured health insurance model through the EIIA Higher Education Benefit Trust. Employees select a deductible of $1,000, $3,000 or $5,000. The University contributes monthly to a reserve in the trust held for the University. A third party administrator draws from the trust to pay all eligible claims. There are two types of stop loss coverage to limit the University’s liability. The plan includes a specific stop loss coverage for claims that exceed $75,000 per covered individual. Additionally, the plan includes an aggregate stop loss coverage for total claims that exceed 125 percent of expected claims in the calendar year. At June 30, 2019 and 2018, the actual claims paid on behalf of employees under the self-insured plan were $867,298 and $534,157, respectively, and the balance in the trust was $142,473 and $14,037, respectively.

Note 20: Related Party Transactions

Due to the composition of the University's Board of Trustees, with members being drawn from local, public and private organizations, it is inevitable that transactions will take place with organizations in which a member of the board may have an interest. All transactions involving organizations in which a member of the board may have an interest are conducted in accordance with the University's board policies, financial regulations and normal procurement procedures, which require individuals to declare any interest.

At June 30, 2019 and 2018, the net present value of related party contributions receivable prior to allowance considerations were $6,941,127 and $1,145,447, respectively. In addition, at June 30, 2019, approximately 80 percent of total gross contributions receivable were from two related parties and at June 30, 2018 approximately 49 percent of total gross contributions receivable were from one related party.

For the year ended June 30, 2019, approximately 80 percent of all contribution revenue were from two related parties.

Note 21: Management's Consideration of Going Concern Matters

The University incurred a decrease of net assets without donor restriction of approximately $2,991,000 in 2019 and has diminished operating reserves. As a result, the University is in technical default of a debt covenant as described in Notes 11 and 12. The lender may, at its option, give notice to the University that amounts are immediately due and payable. As of March 6, 2020, the bank has formally approved noncompliance with this requirement. In consideration for the waiver, the University has agreed to pledge additional property as collateral on the debt, engage the services of a financial consultant and submit a plan to achieve certain financial targets including budget and cash flow information to the lender.

The University's reoccurring decreases of net assets without donor restrictions and default of the debt covenants raises substantial doubt about the University's ability to continue as a going concern. The University is currently negotiating to stabilize its lender relationship by establishing certain internal operating and management plans. The University is also evaluating various revenue generating opportunities, selectively increasing certain fees and continuing to monitor operating expenses. However, there can be no assurance that the University will be successful in achieving its objectives.

The accompanying consolidated financial statements have been prepared assuming that the University will continue as a going concern; however, the above conditions raise substantial doubt about the University 's ability to do so. The consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classifications of liabilities that may result should the University be unable to continue as a going concern.

Note 22: Subsequent Events

There has been significant volatility in the investment markets both nationally and globally since June 30, 2019, resulting in an overall decline in certain market segments which has resulted in a substantial decline in the value of the University's investment portfolio.

Subsequent events have been evaluated through March 20, 2020, which is the date the consolidated financial statements were available to be issued.

Supplementary Information

McKendree University

Schedule of Expenditures of Federal Awards

Year Ended June 30, 2019

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-Through Entity Identifying Number	Passed Through to Subrecipients	Total Federal Expenditures
U.S. Department of Education				
Student Financial Assistance Cluster				
Federal Supplemental Educational Opportunity Grants	84.007	None	$ -	$ 159,243
Federal Work-Study Program	84.033	None	-	188,548
Federal Perkins Loan Program	84.038	None	-	126,241
Federal Pell Grant Program	84.063	None	-	3,028,881
Federal Direct Student Loans	84.268	None	-	14,892,845
Teacher Education Assistance for College and Higher Education Grants	84.379	None	-	7,416
Total Student Financial Assistance Cluster			-	18,403,174
National Science Foundation				
University of Illinois / Division of Chemistry: Disciplinary Research Programs	47.409	None	-	6,893
			$ -	$ 18,410,067

The accompanying notes are an integral part of this Schedule.

McKendree University

Notes to Schedule of Expenditures of Federal Awards

Year Ended June 30, 2019

Notes to Schedule

1. This accompanying schedule of expenditures of federal awards (the "Schedule") includes the federal awards activity of McKendree University and under a program of the federal government for the year ended June 30, 2019. The accompanying notes are an integral part of this Schedule. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of McKendree University, it is not intended to and does not present the financial position, changes in net assets or cash flows of McKendree University.

2. Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Negative amounts shown on the Schedule represent adjustment or credits made in the normal course of business to amounts reported as expenditures in prior years. McKendree University has elected not to use the 10 percent de minimis indirect cost rate allowed under the Uniform Guidance.

3. The federal loan program listed subsequently are administered directly by McKendree University, and balances and transactions relating to these programs are included in McKendree University's financial statements. Loans outstanding at the beginning of the year and loans made during the year are included in the federal expenditures presented in the Schedule. The balance of loans outstanding at June 30, 2019, consists of:

CFDA Number	Program Name	Outstanding Balance at June 30, 2019
84.038	Federal Perkins Loan Program	$ 103,433

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Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of the Financial Statements Performed in Accordance with *Government Auditing Standards*

Independent Auditor's Report

The Board of Trustees
McKendree University
Lebanon, Illinois

We have audited, 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, the consolidated financial statements of McKendree University ("University"), which comprise the consolidated statement of financial position as of June 30, 2019, and the related consolidated statements of activities and cash flows for the year then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated March 20, 2020, which contained an *Emphasis of Matters* section for the adoption of a new accounting standard and going concern consideration.

Internal Control Over Financial Reporting

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

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did identify a certain deficiency in internal control, described in the accompanying schedule of findings and questioned costs as item 2019-001 that we consider to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The University's Response to Findings

The University's response to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. The University's response was not subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we express no opinion on it.

Purpose of this Report

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

BKD, LLP

St. Louis, Missouri
March 20, 2020

BKD
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Report on Compliance for Each Major Federal Program and Report on Internal Control Over Compliance

Independent Auditor's Report

The Board of Trustees
McKendree University
Lebanon, Illinois

Report on Compliance for the Major Federal Program

We have audited McKendree University's ("University") compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on the University's major federal program for the year ended June 30, 2019. The University's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the University's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the University's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of the University's compliance.

Opinion on the Major Federal Program

In our opinion, McKendree University complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2019.

Other Matters

The results of our auditing procedures disclosed an instance of noncompliance that is required to be reported in accordance with the Uniform Guidance and which is described in the accompanying schedule of findings and questioned costs as item 2019-002. Our opinion on the major federal program is not modified with respect to this matter.

The University's response to the noncompliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs and/or corrective action plan. The University's response was not subjected to the auditing procedures applied in the audit of compliance, and accordingly, we express no opinion on the response.

Report on Internal Control Over Compliance

Management of McKendree University is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the University's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the University's internal control over compliance.

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

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

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

BKD, LLP

St. Louis, Missouri
March 20, 2020

McKendree University
Schedule of Findings and Questioned Costs
Year Ended June 30, 2019

Summary of Auditor's Results

Financial Statements

1. The type of report the auditor issued on whether the financial statements audited were prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) was:

   ☒ Unmodified ☐ Qualified ☐ Adverse ☐ Disclaimer

2. The independent auditor's report on internal control over financial reporting disclosed:

   Significant deficiency(ies)? ☐ Yes ☒ None reported

   Material weakness(es)? ☒ Yes ☐ No

3. Noncompliance considered material to the financial statements was disclosed by the audit? ☐ Yes ☒ No

Federal Awards

4. The independent auditor's report on internal control over compliance for major federal awards programs disclosed:

   Significant deficiency(ies)? ☐ Yes ☒ None reported

   Material weakness(es)? ☐ Yes ☒ No

5. The opinion expressed in the independent auditor's report on compliance for major federal awards was:

   ☒ Unmodified ☐ Qualified ☐ Adverse ☐ Disclaimer

6. The audit disclosed findings required to be reported by 2 CFR 200.516(a)? ☒ Yes ☐ No

7. The University's major program was:

Cluster/Program	CFDA Number
Student Financial Assistance Cluster:	
Federal Supplemental Educational Opportunity Grants	84.007
Federal Work-Study Program	84.033
Federal Perkins Loan Program	84.038
Federal Pell Grant Program	84.063
Federal Direct Student Loans	84.268
Teacher Education Assistance for College and Higher Education Grants	84.379

8. The threshold used to distinguish between Type A and Type B programs was $750,000.

9. The University qualified as a low-risk auditee? ☒ Yes ☐ No

McKendree University

Schedule of Findings and Questioned Costs (Continued)

Year Ended June 30, 2019

Findings Required to be Reported by *Government Auditing Standards*

Reference Number	Finding
2019-001	**Criteria or Specific Requirement** – The accuracy of the University's financial statements is dependent upon the proper function of internal control.
	Condition – The University did not have proper review processes in place during the year causing certain financial activity to require adjustments within the general ledger.
	Effect – Potential material misstatements in the financial statements could occur and not be detected and/or corrected in a timely manner.
	Cause – The University did not have proper controls in place to record and review certain receivable and payable activity.
	Recommendation – Management should review the procedures and policies to determine where additional review or reporting consideration is needed in evaluating completeness of accounts.
	Views of Responsible Officials and Planned Corrective Actions – Management understands the finding and will implement effective controls including system controls, documented policies and procedures and certified manual review of manual adjustments to student accounts.

Findings Required to be Reported by the Uniform Guidance

Reference Number	Finding
2019-002	**Student Financial Assistance Cluster, CFDA #84.063 – Federal Pell Grant Program, 84.268 – Federal Direct Loan Program, 84.033 – Federal Word-Study Program, 84.007 – Federal Supplemental Educational Opportunity Grants, 84.038 – Federal Perkins Loan Program, 84.379 – Teacher Education Assistance for College and Higher Education Grants, U.S. Department of Education 2018 – 2019 Program Year**

Criteria or Specific Requirement – Special Tests and Provisions – Gramm-Leach-Bliley Act (GLBA) – Securing Student Information. According to federal regulations, an institution is required to have a designated individual to coordinate the information security program, required to perform a risk assessment that addresses required areas regarding student information and required to document a safeguard for each risk identified through the risk assessment.

Condition – The University has not performed a formal risk assessment and documented safeguards for any risks.

Questioned Costs – None

Context – Through discussions with University personnel, the requirements of GLBA have not been met.

Effect – The University is not in compliance with the Gramm-Leach-Bliley Act requirements therefore, putting sensitive data at additional risk.

Cause – The Director of Information Technology had not taken on the role of GLBA coordinator nor had that role been assigned to anyone therefore, the required steps of performing a risk assessment that focuses on the required areas notes in 16 CFR 314.4 (b) and then documenting the safeguards that protects the University from identified risks has not occurred.

Identification as a Repeat Finding – N/A

Recommendation – We recommend the University review current roles, procedures and assessments and take the proper steps to be in compliance with the GLBA.

Views of Responsible Officials and Planned Corrective Actions – Management will review the assignment of the GLBA coordinator role and adjust job duties as needed to ensure the coordinator has capacity to perform the required duties. Duties of the GLBA coordinator will include documentation of safeguards in place and risks not mitigated through internal controls.

McKendree University
Summary Schedule of Prior Audit Findings
Year Ended June 30, 2019

Reference Number	Summary of Finding	Status
2018-001	**Criteria or Specific Requirement – Reporting** According to federal regulations, a Pell Grant should be awarded with a proper calculation based on a students' cost of attendance and expected family contribution. The University awarded students Pell grants based on an outdated cost of attendance calculation. Out of a population of 816 students who received a Pell award, a sample of 25 students were tested. An incorrect cost of attendance was used to calculate the Pell award for each student. Our sample was not and was not intended to be statistically valid.	**Resolved**

Finding 2019-001 (GAS)

Management has implemented internal controls, including

- limiting the number of active account combinations
- updating access to account combinations giving budget managers access to review of ledger activity, and
- identified reporting options within the enterprise system to better monitor both expense and receivable activity.

Management is currently updating and expanding on policy and procedure documentation for all business operations with anticipation completed by May 31, 2020.

Finding 2019-002 (SFA)

Management has realigned the Information Technology under the Daryl Hancock, Chief of Staff, allowing for some reassignment of University-wide assessment functions away from the Director of Information Technology. The GLBA coordinator role, which includes documentation of safeguards in place and risks not mitigated through internal controls, will remain with the George Kriss, Director of Information Technology.

Person responsible for Corrective Action Plan:

Marilee Kaye Montanaro, EdD, MBA
Vice President, Administration & Finance
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