REVIEW OF THE ANNUAL FINANCIAL AUDITS

OF FLORIDA ATLANTIC UNIVERSITY

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INTRODUCTION

My comments refer to the Annual Financial Audits for the years ending June 30, 2003 through June 30, 2008 prepared by administration of Florida Atlantic University and the Auditor General of the State of Florida. The Tables included in this document were compiled from those documents. Any errors that might have existed in those documents may also be reflected in this Review.

FUNDAMENTALS OF FUND ACCOUNTING

In order to understand the overall financial condition of any institution of higher learning in the United States, one must be aware that the accounting principles applied to the finances of such an institution involve distinct, but interrelated, entities called "funds." Each fund has a self-balancing set of assets, liabilities, and a fund balance. One must examine all of the funds of an institution in order to assess its financial status.

An analogy to fund accounting is the following. Suppose that your assets consisted of five bank accounts, each with $10,000 in it as of a certain date. Your net worth, if you had no debts, would then be $50,000 and would remain unaffected by moving funds from one bank account to another. Similarly, assets are often moved between funds of a college. Consequently, the Tables included in this document utilize the net assets in all of the funds of Florida Atlantic University.

There are different types of funds. "Unrestricted" funds are those solely under the control of the institution's governing board. These are the funds which allow the institution flexibility in addressing its various needs. Although there may be some "restrictions" placed on the use of unrestricted funds, these "restrictions" normally refer only to resolutions of the governing board which may be rescinded at any time by action of that board. While Endowment Funds are Restricted Funds, Funds Functioning as Endowment funds such as Quasi-Endowment Funds are Unrestricted funds since they have merely been designated Funds Functioning as Endowment by the Board of Trustees.

By contrast, “restricted” funds are resources which have external, legally binding restrictions placed upon their use. For example, a government grant (minus any indirect cost in the award, which can be treated as unrestricted revenue) can only be expended for the purpose for which it was awarded. Similarly, gifts sometimes carry legally binding stipulations restricting their usage. Thus, an institution’s administration and governing board are not at liberty to use restricted funds except for stated purposes. However, in some cases, even these funds can be expended for activities which free up unrestricted funds.

Investment in Capital Assets Net of Related Debt are classified separately from Unrestricted and Restricted Funds and are considered to be resources generally not available for other uses by an institution.

You may wish to refer to Chapter 2, Fund Accounting, of the *Budget Handbook for Association Leaders in Higher Education Units*, which I wrote for the National Education Association. That Chapter expands upon the prior comments and illustrates them for a fictitious college.

REPORTING ENTITY

The Financial Audits present information about Florida Atlantic University as well as its discretely presented component units, the Florida Atlantic University Foundation, Inc. and the Florida Atlantic University Research Corporation, Inc. Both of these component units are described on pages 15 and 16 of the 2008 Financial Audit.

TABLE 1: STATEMENT OF NET ASSETS

Table 1 was constructed from the Statement of Net Assets in each annual Audit (see, for example, page 11 of the 2008 Audit). The Total Net Assets of Florida Atlantic University increased each year from $400,795,247 as of June 30, 2003 to $709,653,731 as of June 30, 2008. The Unrestricted Net Assets increased from $33,563,437 as of June 30, 2003 to $73,456,329 as of June 30, 2008. In addition, on page 27 of the 2008 Audit, the administration noted that the total liability for compensated absences payable was $22,190,330 as of June 30, 2008, of which the current portion was $1,260,358, "the amount expected to be paid in the coming fiscal year."
"Although the University expects the liability to be funded primarily from future appropriations, generally accepted accounting principles do not permit the recording of a receivable in anticipation of future appropriations."

What this means is that in reality the Noncurrent liability for compensated absences will not be paid from current unrestricted reserves. Hence the Unrestricted Funds available to the University are effectively more than $20 million larger than the stated amount of $73,456,329 as of June 30, 2008.

The administration also stated on page 4 of the 2008 Audit that "The changes in net assets that occur over time indicate improvement or deterioration in the

University's financial condition." Clearly the substantial increase in Net Assets for the Florida Atlantic University indicates that its financial health has been improving.

On page 3 of the 2008 Financial Audit the administration reported that Net Assets grew by $163.4 million during fiscal 2008, "resulting primarily from the acquisition of the Harbor Branch Oceanographic Institute."

On page 9 of the 2008 Audit it states that as of June 30, 2008 the University had $121.8 million in outstanding bonds and capital leases, representing a decrease of $4.7 million, or 3.7 percent, from the prior fiscal year."

Note from Table I that Investment in Capital Assets, Net of Related Debt, has increased dramatically from June 30, 2003 to June 30, 2008, by over $240 million in just 5 years.

The second part of Table 1 presents the same data as the first part, but for the two Component Units. As the Table demonstrates, Total Net Assets have increased from $117,754,358 as of June 30, 2003 to $227,199,600 as of June 30, 2008. In addition, Unrestricted Funds have increased from $8,238,264 as of June 30, 2003 to $14,610,718 as of June 30, 2008.

Nearly all of the Net Assets of the Component Units were held by the Florida Atlantic University Foundation, which as of June 30, 2008 had Net Assets of $226,825,916 (see page 37 of the 2008 Audit) while the remaining Component Unit had Net Assets of only $373,684.

TABLE 2 , STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

Table 2 presents this data for the six year period fiscal 2003 through fiscal 2008. The 2007-08 data comes from page 12 of the 2008 Audit. Table 1 shows that there had been an increase in Net Assets for the University itself each year covered by Table 2.

Note that Depreciation averaged about $19 million per year. Depreciation is not a cash expenditure but rather a reduction in the value of capital assets.

In fiscal 2005 moneys received for Federal and State student financial aid was transferred from Operating Revenues (hence the decrease in Federal Grants and Contracts under Operating Revenues) to NonOperating Revenues (hence the new category of Federal and State Financial Aid which jumped from 0 in fiscal 2004 to $25,149,076 in fiscal 2005). These changes, caused by the adoption of GASB 33, did not affect the bottom line. They merely changed the categories under which the revenues and expenses were listed, not the net amount of revenue received. See pages 9 and 23 of the 2005 Financial Audit for a fuller explanation.

Also there is a large one year increase in Scholarships and Fellowships expenses between fiscal 2004 and fiscal 2005 that is not explained. However in the 2006 Financial Audit on pages 8 and 23 (Note 2) it stated that "In prior fiscal years, the University reported Federal Family Education Loan (FFEL) program transactions in the Current Funds-Restricted. The FFEL program activities are considered custodial loans, meaning they represent funds held by the University as custodian for others. These type of funds are typically reported in an Agency Fund. Accordingly, for the 2005-06 fiscal year, the University began reporting FFEL program transactions in the Agency Funds. Agency funds are not included in the University's statement of revenues, expenses and changes in

net assets." This explains at least some of the decrease in the expense category Scholarships and Fellowships between fiscal 2005 and fiscal 2006.
During fiscal 2008, the increase in Net Assets was an impressive $163,410,741.

Note that I listed the Operating Expenses by functional classifications while the administration listed them by "natural classification", i.e. by "Compensation and Employee Benefits", etc. on page 12 of the 2008 Audit. The same total of $388,457,334 for Operating Expenses is found on page 35 of the 2008 Audit where it is broken down by functional classifications of Instruction, etc. In my opinion, the functional classification is more useful for trend analysis.

Table 3 converts each of the Operating Expenses into a percentage of the total to see if trends can be discerned. Although there are some fluctuations from year to year, the largest change in any expense category was for scholarships and fellowships that increased from 13.96% of total expenses in fiscal 2004 to 26.71% in fiscal 2005 and then decreased the very next year to only 5.96%. As I stated before no explanation was given for the unusual one year increase in fiscal 2005 for Scholarships and Fellowships but the fiscal 2006 decreases was explained. The huge increase in that category for fiscal 2005 reduced the percentages for all other categories that year and hence distorted the trend analysis for all other expense categories. Overall, Scholarships and Fellowships decreased from 12.97% in fiscal 2003 to 5.84% in fiscal 2008. One might wish to ask the administration to explain these changes in the percentage of expenses for Scholarships and Fellowships over the 6 year period covered by Table 3.

Student Tuition and Fees, Net decreased slightly between fiscal 2006 ($81,421,230) and fiscal 2007 ($78,147,882). Was this due to a small decrease in enrollment? It then increased to $82,449,070 for fiscal 2008.

INFORMATION TECHNOLOGY-APPLICATION ACCESS CONTROL PROCEDURES: SIGNIFICANT DEFICIENCY

The auditors reported on page 6 of the 2007 Financial Audit that there was a significant deficiency in internal control over financial reporting. They did not believe that this was a "material weakness", .i.e " a significant deficiency, or combination of significant deficiencies , that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the University's internal control".

The significant deficiency was that "the University needed to strengthen its access control procedures related to the SCT Banner application, as described below" (see pages 1 and 2 of the 2007 Financial Audit for the details).

You might want to ascertain the current status of this issue.

THE FUTURE

The most recent information on which I based this report was the 2008 Financial Audit. Clearly there have been developments since then that have impacted the university financially. I want to offer two observations concerning the future.

1. The decrease in the value of investments held by the University and its Component Units which probably have occurred since June 30, 2008 may be at least partially reversed by the end of the 2008-09 fiscal year. The stock market has often been a predictor of the economy 6 – 9 months in the future. Thus by

June 30, 2009, it may reflect the opinion of investors as to what the economy will look like in the first or second quarter of 2010.

2. The stimulus plan can be the source of additional funding for the University through three mechanisms:

   A. Funding for the National Institutes of Health , the National Science Foundation, the Energy Department and NASA will be increased by $16 billion dollars under the stimulus package enacted into law. This increase in funds available from these granting agencies should result in an increase in grants received by the faculty of FAU.

   B. Student aid funds are increasing via an increase in Pell Grant Funding, Tuition Tax Credits and Work Study Funds. This should result in an increase in student enrolments and hence in tuition dollars received by FAU.

   C. The State Fiscal-Stabilization Fund of $53.6 billion should allow the State of Florida to reduce at least some of the cuts made to higher education funding.

CONCLUSIONS

Florida Atlantic University was in excellent shape financially as of June 30, 2008. Its Total Net Assets had increased from $400,795,247 as of June 30, 2003 to $709,653,731 as of June 30, 2008, of which $73,456,329 were Unrestricted Net Assets. In addition its component units had increased their Net Assets from $117,754,358 as of June 30, 2003 to $227,199,600 as of June 30, 2008, of which $14,610,718 were Unrestricted Net Assets.

TABLE 1
FLORIDA ATLANTIC UNIVERSITY
STATEMENT OF NET ASSETS

as of	30-Jun-03	30-Jun-04	30-Jun-05	30-Jun-06	30-Jun-07	30-Jun-08
Invested in Capital Assets, Net of Related Debt	$310,197,842	$348,442,846	$355,124,153	$395,998,662	$464,149,653	$551,910,570
Restricted for Expendable						
Debt Service	$89,070	$23,064	($85,801)	$48	$0	$0
Loans	$4,708,107	$4,717,667	$3,990,211	$4,465,229	$4,634,111	$4,594,529
Capital Projects	$48,123,201	$13,745,259	$14,691,355	$19,894,776	$21,462,629	$75,140,153
Other Restricted	$4,113,590	$13,517,015	$21,823,904	$8,067,705	$11,495,745	$4,552,150
Total Restricted Expendable	$57,033,968	$32,003,005	$40,419,669	$32,427,758	$37,592,485	$84,286,832
Unrestricted	$33,563,437	$34,842,128	$36,160,777	$40,170,254	$44,500,852	$73,456,329
TOTAL NET ASSETS	$400,795,247	$415,287,979	$431,704,599	$468,596,674	$546,242,990	$709,653,731

Component Units
Statement of Net Assets

As of	30-Jun-03	30-Jun-04	30-Jun-05	30-Jun-06	30-Jun-07	30-Jun-08
Invested in Capital Assets, Net of Related Debt	$5,029,840	$5,026,199	$8,785,070	$11,227,963	$10,912,175	$11,125,901
Total Restricted	$104,486,254	$126,950,020	$151,305,594	$183,184,395	$205,959,518	$201,462,981
Unrestricted	$8,238,264	$10,040,683	$11,245,368	$2,008,008	$14,872,161	$14,610,718
TOTAL NET ASSETS	$117,754,358	$142,016,902	$171,336,032	$196,420,366	$231,743,854	$227,199,600

TABLE 2
FLORIDA ATLANTIC UNIVERSITY
STATEMENT OF REVENUES, EXPENDSES
AND CHANGES IN NET ASSETS

For fiscal year ended	30-Jun-03	30-Jun-04	30-Jun-05	30-Jun-06	30-Jun-07	30-Jun-08
REVENUES						
Operating Revenues						
Student Tuition and Fees, Net	$56,194,685	$68,908,035	$74,705,495	$81,421,230	$78,147,882	$82,449,070
Federal Grants and Contracts	$37,366,202	$42,765,434	$22,350,465	$32,954,554	$26,056,398	$28,489,510
State and Local Grants and Contracts	$10,312,039	$19,648,003	$4,554,662	$10,950,903	$15,191,142	$10,544,328
Nongovernmental Grants and Contracts	$29,970,970	$39,543,168	$60,927,290	$8,152,816	$7,968,185	$6,793,970
Sales and Services of Educational Dept.	$0	$0	$104,118	$230,515	$247,991	$394,597
Sales and Services of Auxiliary Enterprises	$25,265,263	$14,109,798	$14,087,871	$16,821,172	$18,774,466	$26,806,973
Interest on Loans Receivable	$68,709	$138,336	$122,442	$111,103	$115,418	$110,209
Other Operating Revenue	$15,030,708	$8,927,126	$23,151,276	$25,145,138	$23,298,022	$20,521,253
TOTAL OPERATING REVENUE	$174,208,576	$194,039,900	$200,003,619	$175,787,431	$169,799,504	$176,109,910
EXPENSES						
Instruction	$103,266,881	$115,950,561	$108,141,783	$112,944,164	$130,714,538	$135,092,265
Research	$26,240,608	$30,849,560	$28,377,618	$24,334,672	$23,825,240	$27,792,335
Public Services	$1,617,604	$2,959,446	$9,934,701	$9,964,680	$11,309,809	$8,803,646
Academic Support	$23,373,010	$27,990,512	$30,406,795	$30,713,788	$33,219,164	$35,556,796
Student Services	$24,199,618	$19,195,751	$20,446,425	$20,806,162	$19,130,622	$16,060,939
Institutional Support	$26,356,035	$26,470,316	$17,895,461	$42,767,704	$28,677,277	$41,612,823
Operation and Maintenance of Plant	$13,967,782	$14,762,979	$16,747,824	$18,769,081	$20,072,824	$21,421,604
Scholarships and Fellowships	$40,671,459	$46,998,967	$106,115,569	$20,818,136	$21,276,671	$22,671,411
Auxiliary Operations	$32,515,053	$34,626,913	$35,039,507	$48,818,183	$51,354,956	$55,537,451
Depreciation Expense	$20,354,782	$16,748,879	$17,912,835	$18,972,806	$19,898,483	$23,908,064
Loan Operating Expense	$311,337	$0	$6,306,042	$599,885	$152,557	$0
Other Operating Expenses	$754,891	$0	$0	$0	$0	$0
TOTAL OPERATING EXPENSES	$313,629,060	$336,553,884	$397,324,560	$349,509,261	$359,632,141	$388,457,334
OPERATING INCOME/LOSS	($139,420,484)	($142,513,984)	($197,320,941)	($173,721,830)	($189,832,637)	($212,347,424)
NONOPERATING REVENUES/EXPENSES						
State Appropriations	$127,483,829	$119,484,474	$148,830,036	$151,457,078	$179,747,848	$189,255,782
Federal and State Student Financial Aid	$0	$0	$25,149,076	$26,554,823	$25,537,384	$31,536,181
Investment Income, Net	$6,756,978	($1,080,646)	$2,259,692	$1,451,805	$4,426,210	$5,701,674
Other Nonoperating Revenue	$693,393	$0	$0	$0	$3,186,066	$2,141,010
Loss on Disposal of Capital Related Debt	$0	$0	$0	$0	($637,233)	($740,224)
Interest on Asset-Related Debt	($3,598,763)	($6,853,136)	($1,589,368)	($4,563,178)	($3,908,576)	($5,576,792)
Other Nonoperating Expenses	($3,529,380)	($284,959)	($479,461)	($2,848,299)	$0	$0
TOTAL NET NONOPERATING REVENUES	$127,806,057	$111,265,733	$174,169,975	$172,052,229	$208,351,699	$222,317,631
INCOME(LOSS) BEFORE OTHER REV	($11,614,427)	($31,248,251)	($23,150,966)	($1,669,601)	$18,519,062	$9,970,207
Capital Appropriations	$37,556,678	$41,910,712	$28,966,207	$37,269,721	$51,869,835	$101,050,584
Capital grants. Contracts, Donations	$8,623,686	$3,732,126	$10,699,524	$2,673,876	$7,346,337	$52,349,950
Fees for Capital Projects	$0	$98,145	($98,145)	$88,964	$0	$0
Loss on Disposal of Capital Assets	$0	$0	$0	($1,470,885)	$0	$0
Other Expenses	$0	$0	$0	$0	($88,918)	$40,000
TOTAL OTHER REVENUES	$46,180,364	$45,740,983	$39,567,586	$38,561,676	$59,127,254	$153,440,534
INCREASE (DECREASE) IN NET ASSETS	$34,565,937	$14,492,732	$16,416,620	$36,892,075	$77,646,316	$163,410,741

TABLE 3
FLORIDA ATLANTIC UNIVERSITY
EXPENSES AS PERCENTAGES

For fiscal year ended	30-Jun-03	30-Jun-04	30-Jun-05	30-Jun-06	30-Jun-07	30-Jun-08
Instruction	32.93%	34.45%	27.22%	32.32%	36.35%	34.78%
Research	8.37%	9.17%	7.14%	6.96%	6.62%	7.15%
Public Services	0.52%	0.88%	2.50%	2.85%	3.14%	2.27%
Academic Support	7.45%	8.32%	7.65%	8.79%	9.24%	9.15%
Student Services	7.72%	5.70%	5.15%	5.95%	5.32%	4.13%
Institutional Support	8.40%	7.87%	4.50%	12.24%	7.97%	10.71%
Operation and Maintenance of Plant	4.45%	4.39%	4.22%	5.37%	5.58%	5.51%
Scholarships and Fellowships	12.97%	13.96%	26.71%	5.96%	5.92%	5.84%
Auxiliary Operations	10.37%	10.29%	8.82%	13.97%	14.28%	14.30%
Depreciation Expense	6.49%	4.98%	4.51%	5.43%	5.53%	6.15%
Loan Operating Expense	0.10%	0.00%	1.59%	0.17%	0.04%	0.00%
Other Operating Expenses	0.24%	0.00%	0.00%	0.00%	0.00%	0.00%
TOTAL OPERATING EXPENSES	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%