

**MINNESOTA STATE COLLEGES AND UNIVERSITIES  
BOARD OF TRUSTEES  
Agenda Item Summary Sheet**

**Finance and Facilities Committee**

**Date:** January 21, 2014

**Title:** FY2013 and FY2012 Audited Financial Statements

**Purpose (check one):**

- |   |   |   |
|---|---|---|
| <input type="checkbox"/> Proposed<br>New Policy or<br>Amendment to<br>Existing Policy | <input type="checkbox"/> Approvals<br>Required by<br>Policy | <input type="checkbox"/> Other<br>Approvals |
| <input type="checkbox"/> Monitoring /<br>Compliance                                   | <input checked="" type="checkbox"/> Information             |   |

**Brief Description:**

The purpose of this Board report is to present to the Finance and Facilities Committee of the Board of Trustees the audited financial statements for the Minnesota State Colleges and Universities (MnSCU) for the years ending June 30, 2013 and 2012. These financial statements were prepared by the Finance division of the system office with the assistance of the campus Finance departments and have been audited by the firm of CliftonLarsonAllen LLP.

The MnSCU system audit, Revenue Fund audit, and the thirteen individual college and university audits, received unmodified opinion letters from the respective audit firms. There were no reported material weaknesses and only two reported significant deficiencies in internal control, both at the campus level. The opinion letters provide the Board and other users of the financial statements with assurance that the information is accurate and reliable in all material respects.

**Scheduled Presenter(s):**

Laura King, Vice Chancellor – Chief Financial Officer

**BOARD OF TRUSTEES  
MINNESOTA STATE COLLEGES AND UNIVERSITIES  
*INFORMATION ITEM***

**FY2013 and FY2012 Audited Financial Statements**

**BACKGROUND**

The purpose of this Board report is to present to the Finance and Facilities Committee of the Board of Trustees the audited financial statements for the Minnesota State Colleges and Universities (MnSCU) for the years ending June 30, 2013 and 2012. These financial statements were prepared by the Finance division of the system office with the assistance of the campus Finance departments and have been audited by the firm of CliftonLarsonAllen LLP. This is the fourth year with CliftonLarsonAllen LLP as the system auditor. These statements were presented to the Audit Committee by the Finance division and CliftonLarsonAllen LLP, at the December 3, 2013 Audit Committee meeting.

**AUDIT RESULTS**

The MnSCU system audit, Revenue Fund audit, and the thirteen individual college and university audits, received unmodified opinion letters from the respective audit firms. In addition, there were no reported material weaknesses and only two reported significant deficiencies in internal control, both at the campus level. The opinion letters provide the Board and other users of the financial statements with assurance that the information is accurate and reliable in all material respects.

The three external audit firms, CliftonLarsonAllen LLP, Kern DeWenter Viere, Ltd., and Baker Tilly Virchow Krause, LLP, presented their respective results of audits, including audit opinions, internal control matters and other required communications at the December 3, 2013 Audit Committee meeting.

The Revenue Fund and the thirteen individual college and university financial statements have been incorporated into the MnSCU system financial statements along with the financial statements of the unaudited colleges. The Audit Committee recommended release of the audited statements, a motion that was passed by the full Board of Trustees at the December 3, 2013 meeting.

All audited financial reports will be available on the system's website at:  
<http://www.finance.mnscu.edu/accounting/financialstatements/index.html>

The MnSCU system financial report for fiscal years 2013 and 2012 is presented in accordance with Statement No. 35 *Basic Financial Statements – and Management’s Discussion and Analysis – for Public Colleges and Universities* as established by the Governmental Accounting Standards Board (GASB). The system’s financial information is presented in one column form as a “Business Type Activity”. The resources are governed by the governmental fund based principles and continue to be accounted for in the general, special revenue, enterprise, agency, and revenue funds. Fund level information can be found in the financial statement supplemental schedules contained in a separate report (unaudited) titled “*Supplement to the Annual Financial Report for the year ended June 30, 2013.*” This supplemental report also contains financial statements for each college and university.

All university foundations plus the Century College Foundation and Fergus Area College Foundation are separately included in the related institutions’ financial reports and the system’s financial report. Reporting standards require the inclusion of component entities if found to be “significant” to the primary organization. The foundations and their auditors are very cooperative in adjusting their audit schedules in order to conform to the system’s financial reporting audit schedule.

### **Summary of Financial Results**

Fiscal year 2013 operating results yielded a slight decrease in financial position at June 30, 2013, with a \$2.0 million net operating revenue deficit, compared to a prior year net operating revenue surplus of \$62.9 million.

- Net position increased \$91.1 million or 4.6 percent; most of the increase was due to fiscal year 2013 capital appropriation revenue of \$88.5 million that funded capital asset investment, preservation and replacement.
- Income before other revenues, expenses, gains or losses, also termed “net operating revenue,” decreased from a surplus of \$62.9 million in fiscal year 2012 to a deficit of \$2.0 million in fiscal year 2013. This net operating revenue deficit is the net of \$1,889.8 million of operating and non-operating revenues less \$1,891.8 million of operating and non-operating expenses.
- Capital appropriation revenue of \$88.5 million plus other capital asset related revenue combined with the \$2.0 million net operating revenue deficit generated a change in net position of \$91.1 million in fiscal year 2013, a decrease from the \$121.5 million change in net position generated in fiscal year 2012.

### **Statements of Net Position**

The primary driver of change within the statements of net position between June 30, 2013 and 2012 is capital asset development and renewal activity related to the system’s 27 million plus square feet of academic and administrative buildings.

- New construction in progress of \$175.8 million was the primary factor increasing the capital assets balance, net of depreciation, by \$91.6 million.

- Capital asset financing came primarily from \$88.5 million of capital appropriation and \$77.4 million of new long-term debt.
- Net position (e.g., net worth) increased \$91.1 million including a \$72.9 million increase in net investment in capital assets.

### **Statements of Revenues, Expenses and Changes in Net Position**

Fiscal year 2013 operating expenses of \$1,857 million averaged \$5.1 million per day when divided by 365 days. Looking at the operating expense number in relation to liquid assets, the system's \$883.1 million of unrestricted cash and equivalents plus unrestricted investments would be adequate to cover approximately 5.7 months of expenses, an improvement of 0.1 months from fiscal year 2012.

- Revenue sources funding operations included \$553.2 million of state appropriation; \$837.2 million of student payments, net of scholarship allowance; \$459.5 million of federal and state grants; and \$39.9 million of other revenue.
- Expenses supporting operations included \$1,251.6 million of compensation, \$225.1 million of purchased services (utilities, enterprise and other IT support, etc.), \$145.6 million of supplies, \$107.9 million of depreciation, and other expenses of \$161.6 million.

### **Measuring, Monitoring and Improving Financial Health: Composite Financial Index (CFI) and Financial Health and Compliance Indicators**

The Composite Financial Index calculation uses four financial ratios and assigns a specific weighting to each factor in computing a single, composite measure of financial health. This CFI calculation methodology is used by the Higher Learning Commission as a gauge of member institutions' financial health. Without detailing the actual calculation methodology, financial ratio values are converted into strength factors which in turn are weighted to allow summing of the four components into a single, composite value.

Institutions may have differing values across the four component ratios but still have equivalent overall financial health as indicated by similar composite scores. This approach allows easy comparisons of relative financial health across different institutions. Looking at the composite scores, *Strategic Financial Analysis for Higher Education* suggests a composite value of 1.0 is equivalent to very little financial health, in the for-profit world it could perhaps be viewed as a "going-concern" threshold value, while a composite value of 3.0 is considered to signify relatively strong financial health, an organization with moderate capacity to deal with adversity or invest in innovation and opportunity. CFI scores greater than 3.0 represent increasingly stronger financial health.

The December's Audit Committee meeting included a high-level discussion of CFI, and the system's Annual Financial Report for the Years Ended June 30, 2013 and 2012 included much of the CFI information that follows within the Management Discussion and Analysis section of the report.

**Summary CFI Ratios for Fiscal Year 2013 and Fiscal Year 2012**

The MnSCU system’s financial ratios and other measures presented below are generally consistent with prior years’ presentations. The focus this year is on the four financial ratios used in computing CFI. All system ratios are computed using financial data taken from the accrual financial statements.

*Note: Higher values are deemed better for all ratios presented. The Supplement to the Annual Financial Report will be available to view individual college and university financial statements.*

<http://www.finance.mnscu.edu/accounting/financialstatements/yearendstatements/index.html>

The fiscal year 2013 CFI of 2.26 went down compared to 2012’s CFI of 2.78.

The following table provides reference benchmarks for individual components of the CFI for achieving a total CFI score of 3.0, and illustrates the system, college and university average composite scores.

	<u>Weight</u>	<u>Benchmark</u>	<u>System</u>	<u>2 Yr</u>	<u>4 Yr</u>
Primary Reserve	35%	1.05	0.91	0.81	0.90
Viability	35%	1.05	0.90	1.16	0.60
Net Operating Revenue	10%	0.30	(0.01)	(0.07)	0.02
Return on Net Position	<u>20%</u>	<u>0.60</u>	<u>0.46</u>	<u>0.48</u>	<u>0.41</u>
Composite Financial Index (CFI)	100%	3.00	2.26	2.38	1.93

**CFI Ratio Variability across Colleges and Universities**

There is considerable variability in individual 2013 CFI financial ratio values across the 31 colleges and universities. The following tables, which exclude foundations, highlight the broad range in the results:

	<u>High</u>	<u>Low</u>	<u>Median</u>
Primary Reserve – <i>resource availability</i>	1.52	0.20	0.77
Viability – <i>debt coverage</i>	3.05	0.41	0.98
Net Operating Revenue – <i>surplus or deficit</i>	0.43	(0.40)	(0.05)
Return on Net Position – <i>asset stewardship</i>	<u>2.00</u>	<u>(0.43)</u>	<u>0.35</u>
Composite Financial Index (CFI)	4.73	0.39	2.47

The financial values have been divided into quartiles so to illustrate the range of scores. Individual colleges and universities could be placed in several quartiles based on the individual values in each measure.

Midpoint of Quartiles	<u>1st</u>	<u>2nd</u>	<u>3rd</u>	<u>4th</u>
Primary Reserve – <i>resource availability</i>	1.28	0.89	0.67	0.38
Viability – <i>debt coverage</i>	2.39	1.33	0.85	0.55
Net Operating Revenue – <i>surplus or deficit</i>	0.26	0.00	(0.11)	(0.31)
Return on Net Position – <i>asset stewardship</i>	1.35	0.50	0.24	(0.16)
Composite Financial Index (CFI)	4.19	3.04	1.89	0.85

**Other Financial Measures**

There are additional financial metrics which are used to measure, monitor, and improve the financial condition of each college and university.

The Board required budget reserve ratio compares prior year general fund cash-basis operating revenues to that portion of the general fund’s end-of-year cash balance that has been designated as a special reserve amount. The systemwide figure of 7 percent for fiscal year 2013 represents a reserve balance of \$100.0 million, an increase of \$0.2 million, from fiscal year 2012. All of the colleges and universities report budget reserves within the Board policy expectation.

In fiscal year 2013, 20 of the system’s 31 colleges and universities generated negative net operating revenues using a generally accepted accounting principles measurement; this compares to 10 colleges and universities in fiscal year 2012. Of the 20 colleges and universities with negative net operating revenue in fiscal year 2013, only two also had negative net operating revenue in fiscal years 2012 and 2011. The significant number of institutions reporting net operating losses is attributed principally to the use of fund balance as a part of a budget strategy. Ongoing operating deficits negatively impact the ability of this institution to maintain normal operations under adverse economic circumstances and to implement new strategic initiatives. Negative unrestricted net position generally indicates a college or university has experienced ongoing operating deficits. No college or university reported a negative unrestricted net position.

	<u>FY2013</u>		<u>FY2012</u>		<u>FY2011</u>	
	<u>#</u>	<u>%</u>	<u>#</u>	<u>%</u>	<u>#</u>	<u>%</u>
<b>Net operating revenue loss*</b>	20	65	10	32	3	10
<b>Negative unrestricted net position</b>	0	0	0	0	0	0
<b>Board reserves below 3%</b>	0	0	0	0	0	0

\* As shown in financial statements on line titled “Income (loss) before other revenues, expenses, gains, or losses.”

## Financial Health and Compliance Indicators

The system has developed financial administration and financial health monitoring measures that are utilized to track patterns and trends at each of the colleges and universities. The measures are in support of board policy and board procedure.

**Board Policy 7.3** Part 1. includes the expectation that:

*“ It is the policy of the Board of Trustees to provide sound financial administration to safeguard the resources of the State of Minnesota, the system, the colleges and universities and the constituencies they serve. Effective financial administration will facilitate monitoring and improving managerial performance and evaluating the financial effects of management decisions.*

**Board procedure 7.3.16** includes the statement in Part 1

*“Financial Administration policy, effective financial administration will facilitate monitoring, improving managerial performance and evaluating the financial effects of management decisions. The Board of Trustees will be periodically updated on the administration and financial management of the system.”*

Management, working with the college and university chief financial officers, has developed a financial monitoring and compliance protocol in order to support policy and procedure expectations. Each measure is defined in procedure along with the data elements, the triggers and the management consequences for tripping the performance measure. The measures, and the implementation elements were defined in consultation with all the colleges and university CFOs.

There are seven measures; four with a short term – financial administration focus and three with a long term – financial health focus. The four short term measures requires monthly/quarterly reporting for a period if any of the measures triggered.

- Repair and replacement expenditures per square foot (-three-year moving average) of at least \$1.00 per square foot.
- Overdraft in a local bank account during the fiscal year.
- MnSCU to MAPS (SWIFT) reconciliation (including adjustments).
- Timely and complete bank reconciliation (including adjustments).

There are 3 long term measures which the procedure requires the preparation of a financial recovery plan if certain thresholds are triggered.

- Negative accrual based net operating revenue ("Income (Loss) Before Other Revenues, Expenses, Gains or Losses").
- Low accrual primary reserve level.
- Low Composite Financial Index (CFI) score.

Based upon 2013 financial statements, eight colleges and one university have been asked to work with the system office in the preparation of a financial recovery plan. The goal of the plans is to help colleges and universities get back to financial/operational health. The plans often have a multi-year horizon. This matter has the chancellor's awareness and is a part of his annual discussion with the responsible presidents.

## **2014 OUTLOOK**

The leadership at the colleges and universities is working aggressively to manage the revenue and expense outlook during challenging times. The schools are operating with very thin margins as cost pressures build in compensation and operating inflation. The 2014 enrollment outlook requires focused planning, targeting enrollment growth strategies and expanded retention and student success efforts. The colleges and universities are reporting stable, but thin reserves as protection against enterprise risk.

Strategic enrollment management and strong program development are key to successful year.

## **CONCLUSION**

Minnesota State Colleges and Universities maintained a sound financial position in fiscal year 2013, despite systemwide tuition freezes and significant increases to compensation expense. The system maintained a relatively strong financial position in fiscal year 2013, as measured by the \$91.1 million increase in net position. The system continues to rely heavily on state operating appropriation support to implement new programs tailored to the needs of the state's workforce, to maintain ongoing operations, and to devise the innovative strategies necessary to successfully manage the future challenges presented by a weak economy and a constantly evolving higher education marketplace.

The state, national and global economies are beginning to overcome the impacts of a significant recession throughout fiscal years 2013 and 2012. However, while in the years prior to 2011, increases in the general unemployment rate has resulted in increases in enrollment, the opposite occurred in fiscal years 2013 and 2012. Overall enrollment levels at the colleges and universities have decreased 2.3 percent, and 2.8 percent, and increased 1.6 percent in fiscal years 2013, 2012 and 2011, correspondingly. Enrollment forecasts in 2014 and 2015 are stable or slightly declining compared to 2013. It is expected that enrollment will once again moderate as the state's unemployment rate declines. The system's colleges and universities have aggressively managed class sizes, course offerings, and hours of operations in order to serve as many students as possible.

In the spring of 2013, the state legislature approved an increase in appropriation sufficient to fund a systemwide tuition freeze for the upcoming biennium. In the 4 years prior to fiscal year 2013, state appropriation revenue was reduced, although reductions were somewhat offset with one-time federal stimulus funds totaling \$79.2 million in fiscal years 2010 and 2011. System leadership has worked tirelessly to minimize tuition increases and the detrimental impact of cost cutting on the system's approximately 4,000 educational programs



and 420,000 students; both efforts are aimed squarely at limiting the negative impacts of state reductions on students.

The changes in the federal financial aid program, in concert with the state and national economic conditions, has resulted in a substantial increase in federal financial aid participation by the system's students over the past three years. Reliance on state and federal financial assistance by current and future students is a state and national concern as affordability competes with the withdrawal of state support for public higher education. Further, the increased personal debt burden of today's students threatens participation and completion rates.

The continuing success of the system depends in part on a partnership with the state of Minnesota and its citizens. Preservation of the high quality, broadly accessible system of colleges and universities now available across the state will require continuing support from the state. The system leadership is committed to a statewide partnership with government, industry and the community to add to the prosperity of Minnesota. The system will also continue its aggressive management of costs and services to ensure efficient, effective operations on behalf of current and future students. The partnership enables the provision of accessible, high value, affordable higher education in accord with the economic and intellectual needs of the state. The state's continued support is critical to maintaining both affordability and access for students.

*Date Presented to Board of Trustees: January 21, 2014*

# Financial Performance Fiscal Year 2013 and 2012



Financial Statements of the system overall and select colleges  
and universities  
Finance and Facilities Committee  
Board of Trustees  
January 21, 2014

## Minnesota State Colleges and Universities

The Minnesota State Colleges and Universities system is an Equal Opportunity employer and educator.

### Agenda

- FY 2013 audited financial statements
- FY 2013 financial performance
- Composite Financial Index (CFI)
- Financial monitoring protocols
- FY 2014 outlook



## Fiscal Year 2013 Audited Financial Statements Results

- System statements
- 13 university and college statements
- Revenue fund
- “Clean” opinions
- No material weaknesses
- Two significant deficiencies (campus level)



## FY2013 System Financial Results are Stable

- Flat revenues with tight expense controls result in balanced college and university budgets
- System and college and university reserves stable but thinly funded
- College and university budget stress emerging in CFI calculations



## Changes in Net Position

FY 2013 vs. FY 2012 (\$ millions)

*(includes colleges, universities and system office)*

Revenue/(Expense)	FY2013	change	FY2012
Total revenues	\$1,889.8	\$10.7	\$1,879.1
Total expenses	(1,891.8)	(75.6)	(1,816.2)
Net operating revenue	(2.0)	(64.9)	62.9
Capital appropriation revenue	88.5	32.2	56.3
Other revenue, net	4.6	2.3	2.3
Change in Net Position	\$ 91.1	\$ (30.4)	\$ 121.5



## Changes in Net Operating Revenue

FY 2013 vs FY 2012 (\$ millions)

*(includes colleges, universities and system office)*

Revenue/(Expense)	FY2013	change	FY2012
Components and changes			
Revenue from students, net of financial aid	\$ 837.2	\$5.7	\$ 831.5
State appropriation revenue	653.2	1.9	651.3
Federal and state grant revenue	459.5	16.0	443.5
Compensation expense	(1,251.6)	(48.4)	(1,203.2)
All other revenues/(expenses), net	(600.3)	(40.1)	(560.2)
Net operating revenue	\$ (2.0)	\$(64.9)	\$ 62.9





## Statement of Net Position (\$ millions)

*(includes colleges, universities and system office)*

Assets, Liabilities and Net Position			
Fiscal Year	FY2013	FY2012	FY2011
Total assets	\$3,125.3	\$2,955.0	\$2,883.3
Total liabilities	\$1,042.6	\$963.4	\$1,013.2
Total net position	\$2,082.7	\$1,991.6	\$1,870.1

- Total assets increased each year due mainly to additional capital asset investments
- Total liabilities increased by 8 percent due primarily to new revenue bond issue of \$58M and \$19M in GO bonds.



## Statement of Revenues, Expenses and Changes in Net Position (\$ millions)

*(includes colleges, universities and system office)*

Revenues, Expenses and Net Position			
Fiscal Year	FY2013	FY2012	FY2011
Total revenues	\$1,982.8	\$1,938.3	\$2,050.3
Total expenses	\$1,891.8	\$1,816.8	\$1,904.0
Change in Net Position	\$91.0	\$121.5	\$146.3

- Total revenue increased by \$45 million due to \$32 million of additional capital appropriation along with \$17 million of additional state financial aid grants.
- Operating expenses increased by \$75 million, with \$48 million of that attributable to compensation, and \$9 million increase in financial aid paid to students.



## Statement of Revenues, Expenses and Changes in Net Position (\$ millions)

*(includes colleges, universities and system office)*

Revenues, Expenses and Net Position			
Fiscal Year	FY2013	FY2012	FY2011
Total revenues	\$1,982.8	\$1,938.3	\$2,050.3
Total expenses	\$1,891.8	\$1,816.8	\$1,904.0
Change in Net Position	\$91.0	\$121.5	\$146.3

- Total revenue increased by \$45 million due to \$32 million of additional capital appropriation along with \$17 million of additional state grants as part of financial aid streams.
- Operating expenses increased by \$75 million, with \$48 million attributable to compensation, along with \$9 million increase in financial aid paid to students.



## System Composite Financial Index

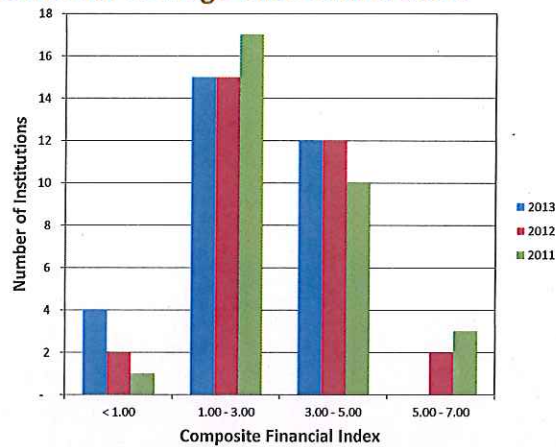
*(includes colleges, universities and system office results)*

### Components of CFI

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Return on Net Position	0.46	0.65	0.85
Net Operating Revenue	(0.01)	0.26	0.29
Primary Reserve	0.91	0.92	0.76
Viability	<u>0.90</u>	<u>0.95</u>	<u>0.80</u>
<b>CFI</b>	<b>2.26</b>	<b>2.78</b>	<b>2.70</b>



## Composite Financial Index Trends for College and Universities



## Composite Financial Index Variability in the Colleges and Universities

	2013 Averages		2012 Averages		2011 Averages	
	Colleges	Universities	Colleges	Universities	Colleges	Universities
Primary Reserve	0.81	0.90	0.82	0.92	0.71	0.71
Viability	1.16	0.60	1.17	0.67	1.13	0.52
Net Operating Revenue	(0.07)	0.02	0.13	0.38	0.26	0.32
Return on Net Position	<u>0.48</u>	<u>0.41</u>	<u>0.60</u>	<u>0.68</u>	<u>1.10</u>	<u>0.57</u>
CFI	2.38	1.93	2.72	2.65	3.20	2.12



## FY2013 Financial Summary

- CFI variability narrows amongst colleges & universities
- CFI trends have been fairly stable last three years
- System CFI improved in the two long term measurements
- Campuses displaying focused budgeting, planning and analysis



## Financial Monitoring Protocols

- Policy 7.3
- Procedure 7.3.16
- Seven measures
  - 4 short term – financial administration focus
  - 3 long term – financial health focus
- Monitoring, data, trigger and consequence agreed to by all CFOs
- Remedies include periodic certification, reports and/or workout plans





## FY2013 Monitoring Results

- 7 colleges and 1 university reported negative accrual based operating revenue two years running
- 6 colleges and 1 university reported CFI below 1.50 based on 2 year average or less than .5 in most recent year



## Monitoring Actions

- Procedure calls for certifications or financial recovery plan
- Monthly, quarterly, biannual reporting to VC- CFO office
- Goal is to help colleges and universities get back to financial/operational health
- Often a multi-year plan
- Issue has Chancellor's awareness



## FY2014 Outlook

- Colleges and universities managing revenue and expense outlook
- Very thin margins require focused planning
- Stable, but thin reserves provide some protection for enterprise risk
- Strategic enrollment management and strong program development are key to successful year

