Financial Statement
Issues—MD&A

FOCUS
Virginia Tech

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Management’s Discussion & Analysis—Required Elements

Contained in GASB 34, paragraphs 8 through 11, as amended by GASB 37, paragraphs 4 and 5

Key considerations

– Required *supplementary* information
– Objective and easily readable analysis of *financial* activities
– Based on *currently known* facts, decisions, or conditions…
Management’s Discussion & Analysis—Required Elements

– Comparison to prior year required but emphasis is on current year

– Charts and graphs encouraged to enhance understandability

– Emphasis is on institution rather than component units (CU)

- Professional judgment determines whether CU are discussed; if appropriate MD&A should refer reader to CU separately issued financial statements…
Management’s Discussion & Analysis—Required Elements

- Brief discussion of basic financial statements—but only “government-wide” statements

  - Statement of net assets
  - Statement of revenues, expenses, and changes in net assets
    - Statement of cash flows is a fund financial statement
  - Encouraged to report only the most relevant information and avoid “boilerplate”...
Management’s Discussion & Analysis—Required Elements

– Information presented *should be confined* to following topics

  Condensed financial information related to

  – Total assets, distinguishing between capital and other assets
  – Total liabilities, distinguishing between long-term and other liabilities...
Management’s Discussion & Analysis—Required Elements

– Total net assets, distinguishing between amounts invested in capital assets, net of related debt / restricted amounts / unrestricted amounts
– Program revenues by major source
– General revenues by major source
– Total revenues
– Program expenses, minimally by function…
Management’s Discussion & Analysis—Required Elements

– Total expenses
– Surplus / deficiency *before* additions to permanent & term endowments, special & extraordinary items, and transfers
– Contributions
– Special and extraordinary items
– Changes in net assets
– Ending net assets…
Management’s Discussion & Analysis—Required Elements

Analysis of overall financial position and results of operations

- Indication whether financial position has improved or deteriorated as a result of operations

Reasons for significant changes from prior year should be explained; amount or percentage change by itself is not sufficient...
Management’s Discussion & Analysis—Required Elements

- Analysis of net assets and reasons for significant changes in amounts
  - Whether restrictions significantly affect the availability of resources for future use

- Description of significant capital asset or debt activity
  - Including discussion of commitments, changes in debt rating, and any debt limitations…
Management’s Discussion & Analysis—Required Elements

Description of currently known facts, decisions, or conditions expected to have significant effect on

- Financial position
  - Net assets
- Results of operations including
  - Revenues
  - Expenses
  - Other changes in net assets
Management’s Discussion & Analysis—Required Elements

– Footnote a to paragraph 11 of GASB 34 (as amended by GASB 37) specifies that information not relating to the required topics *should not be included* in MD&A

  May be provided elsewhere

– Letter of transmittal

– Other forms of supplementary information (i.e., *other supplementary information*)
Financial Statements Reviewed

- Christopher Newport University (2009)
- George Mason University (2010)
- James Madison University (2010 unaudited)
- Norfolk State University (2009)
- University of Mary Washington (2009)
- Virginia Community College System (2009)
- Virginia Tech (2010) •
Global Observations

Not covered in any MD&A reviewed
– Explanation of depreciation
– Explanation of scholarship allowance
– Explanation of interest expense versus interest capitalized

Several institutions discussed changes in treatment for the current fiscal year to explain a variance and indicated that they didn’t restate the prior year…
Too little discussion of reasons behind numbers changes from year to year
- In most cases the specific category of change was identified but there was no discussion of the reasons for the change

Found typos and misspellings in the majority (but not all) institutions’ MD&A
Institution A

Opens with a description of the institution’s rise to national prominence, discusses its inclusion in the state’s CAFR, and describes its governing board.

Includes a fairly lengthy description of the GASB statements governing financial reporting and goes on to describe new statements issued...
Institution A

Includes a statement that “debt incurred, but not yet expended for capital assets, is not included as a component of invested in capital assets, net of related debt”

– Statement probably is not needed for MD&A but, if it appears, should indicate where it is reported…
Institution A

- Refers to state appropriations and capital appropriations in multiple places but doesn’t differentiate—EVERYONE DOES THIS!
  - Should use terms “state operating appropriation” or “state appropriation for operations” and “state capital appropriation”

- References research as if it’s separate from academic—academic includes instruction, research, and public service...
Institution A

- Refers to E&G but does not explain the term and what it includes.

- Defines operating expenses as expenditures.
  - With introduction of depreciation this term no longer applies when discussing expenses.

- Factual error suggesting that largest expense growth is in student aid—not true either as amount or percentage...
Institution A

- Includes coverage of statement of cash flows
- Closes with a good discussion of the economic outlook
- Also includes good discussion of relevant information from component unit
- Appropriately discusses endowment performance, ranking in NSF R&D study, current debt ratings, and capital campaign progress
Institution B

- MD&A not labeled unaudited
- Opens with description of the institution’s operations, its special recognition for accomplishments of its alumni, its inclusion in the state’s CAFR, and its board and how they’re appointed
- Includes a description of the GASB statements governing financial reporting and inclusion of component units...
Institution B

Includes a statement that “debt incurred, but not yet expended for capital assets, is not included as a component of invested in capital assets, net of related debt”

Explains that unrestricted net assets can be used at discretion of the board to support mission but does not detail what the mission is (i.e., teaching/learning, research, and public service)…
Institution B

- References expenditures as part of operating expenses
- References functional expense categories but identifies a couple functions that should be included in academic support
- Discusses the reclassification of FICA taxes from fringe to salaries & wages – Did not restate prior year numbers…
Institution B

- Good use of tables and charts
- Inclusion of list of completed capital projects is a nice element—much better than narrative listing
- Includes coverage of statement of cash flows
- Economic outlook discussion references expected reduction in general fund appropriation
  - Only okay if known before opinion date…
Institution B

Discussion references practice of not automatically filling vacant positions in response to financial challenges

- Implies that some positions were filled
- Yet economic analysis section indicates that a hiring freeze is being continued into next fiscal year

Overall, good discussion of steps taken to respond to reductions of state support.
Institution C

Includes a description of the GASB statements governing financial reporting and inclusion of component units.

Includes a paragraph related to enrollment and admissions:
- Does not tie it specifically to financial results.
- Projects enrollment out to 2016!...
Institution C

Includes a statement that “debt incurred, but not yet expended for capital assets, is not included as a component of invested in capital assets, net of related debt”

Pretty vanilla presentation of data for summarized financial statements without calculated changes or percentages

Amounts in the narrative text include lots of zeros for thousands rather than rounding…
Institution C

- Good discussion of board’s debt policy (although 10 percent annual debt service limit seems high)

- Lengthy discussion of projects completed in past years while describing Virginia Higher Education Bond Referendum of 2002
  - Should cover only current projects

- Includes coverage of statement of cash flows...
Institution C

- Economic outlook section references Higher Education Restructuring Act but doesn’t tie it to financial results
- Repeats the reference to growing enrollment by 2016
  - Cannot include projected number of students

Institution D

- MD&A not labeled unaudited
- Opening paragraph references new GASB reporting model
- References GASB 39 to explain component unit treatment
- Refers to time restrictions when discussing restricted net assets
  - Time is an eligibility requirement, not a restriction…
Institution D

Condensed statement of net assets is good as a table but the narrative discussion only addresses the capital portion of the change.

Condensed SRECNA isn’t very condensed at all.

– Putting both revenues and expenses in same table makes it difficult to focus, appears too similar to actual SRECNA…
Institution D

Capital asset and debt administration section references future projects and their expected completion date

– Okay if they are already underway but not if they are not in progress

References a SCHEV calculation of debt service to expenditures (should be expenses) but does not indicate whether it’s good or bad or what the standard is
Institution D

- Economic outlook discussion is consistent with requirements
- Describes linkage to commonwealth’s health and directs readers to CAFR for information about commonwealth's economic outlook
- Good description of steps being taken by institution to manage difficult financial conditions
- Overall, the MD&A is too concise •
Institution E

- MD&A not labeled unaudited
- Opens with institutional profile section that is not appropriate for MD&A
  - Covers non-financial elements and doesn’t link them to financial considerations
- Includes a nice financial highlights section but clouds it a little by addressing non-financial aspects of some capital projects...
Institution E

- Discusses tuition increase and places it in context of impact
  - Goes on to discuss that it’s lower than other Virginia four-year institutions
- Not really relevant for MD&A
- Refers to time restrictions when discussing restricted net assets...
Institution E

- Capital asset and debt administration section is very detailed and would benefit from tables or lists.
- Uses several acronyms that probably are known on campus but not by the average reader of the financial statements.
- Includes a table for the condensed SRECNA and misclassifies scholarships and fellowships separately from E&G…
Institution E

- Does a nice job of discussing state operating appropriation and differentiating it from the capital appropriation
  - Still doesn’t label capital appropriation as state appropriation though
- Devotes nearly two full pages to the statement of cash flows
- Economic outlook discussion is very good but clouded with examples of research projects…
Institution E

Discusses the strategic plan and indicates a target for research growth

– Referencing a specific number (i.e., 70 percent) without indicating what it’s based on is problematic

– But it’s an interesting way to comply with requirement to limit discussion to known facts, decisions, or conditions •
Institution F

- MD&A not labeled unaudited
- Opens with a discussion of GASB financial reporting statements
- Good CU discussion and disclosure that it’s not addressed in the MD&A
- Excellent financial highlight section with four bullets of highly relevant information
  - Enrollment chart covers five fiscal years but should be limited to current and prior year...
Institution F

- Good discussion of condensed statement of net assets but would benefit from variance analysis
- Discussion of changes involving capital assets is very detailed—could benefit from table
- Condensed SRECNA discussion is too limited
- Nice charts but insufficient analysis of changes or percentages to explain difference between current and prior year...
Institution F

- Includes coverage of statement of cash flows
- Economic outlook includes good discussion of state appropriation changes and ARRA
- In-depth explanation of changes in tuition and fee rates coupled with quantification of revenue it will generate
- Discusses capital additions but does not discuss construction in progress or current commitments
Institution G

- Good discussion of component unit and mentions that it’s not addressed in MD&A
- Condensed statement of net assets with percentage variance information
- Nice bulleted explanation of the changes in assets and liabilities and the resulting impact on net assets…
Institution G

- Condensed SRECNA includes percentage variance information
- Supplemented with nice charts for both revenues and expenses identifying the major categories of each
- First institution to avoid use of “expenditures” when discussing operating expenses
- Bulleted list of changes in amounts between the two years…
Institution G

- Includes coverage of statement of cash flows
- Capital asset and debt administration section discusses major capital acquisitions from a component unit but does not explain the reason for the transaction
  - Also uses a number of acronyms
- No discussion of outstanding commitments
- Economic outlook discussion is too brief
Financial Statement Issues

Questions, Comments, and Reactions

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