

MANAGEMENT'S DISCUSSION AND ANALYSIS

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The discussion and analysis of Trinity Valley Community College's financial statements provides an overview of the College's financial activities for the year ending August 31, 2005. Please read it in conjunction with the independent auditor's reports, the College's basic financial statements, footnotes, schedules and supplemental information.

Trinity Valley Community College is a comprehensive community college providing both credit and non-credit courses. Courses are taught at the Athens campus, Palestine campus, Terrell campus, Kaufman Health Science Center, Texas Department of Criminal Justice, area high schools and through distance education. In order to maintain financial stability, the College strives to have adequate revenue streams to accumulate net assets to ensure sufficient funding to accomplish its mission.

FINANCIAL HIGHLIGHTS

For the year ending August 31, 2005:

- The College's net assets increased from \$31,386,922 in 2004 to \$32,998,068 in 2005.
- Cash increased from \$11,143,514 in 2004 to \$14,332,644 in 2005.
- The College issued a \$5.5 million general revenue bond for construction of a new technology building.

USING THIS REPORT

In December 1998, the Government Accounting Standards Board (GASB) released statement No. 33 "Accounting and Financial Reporting for Nonexchange Transactions" which revised the reporting of property tax revenue. In June 1999, GASB released statement No. 34 "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments". Changes in statement No. 34 require a comprehensive one-line look at the entity as a whole and capitalization of assets and depreciation. In November 1999, GASB issued statement No. 35 "Basic Financial Statements and Management's Discussion and Analysis for Public Colleges and Universities" which applies these standards to public colleges and universities. This annual report consists of a series of financial statements prepared in accordance with GASB 33, 34 and 35.

These financial statements differ significantly, in both the form and accounting principles utilized, from the College's financial statements issued prior to GASB 33, 34 and 35. Financial data is presented in a form similar to that used by corporations by providing information on the College as a whole. This presentation contrasts with financial statements prepared prior to implementation of GASB 33, 34 and 35 which focused on accountability of funds, i.e., current, auxiliary, endowment, loan and plant funds.

The annual financial report is presented in three sections: financial data, organizational data, and statistical data. The financial section includes the report of independent auditors, this management's discussion and analysis, the financial statements, notes to the financial statements, schedules, other reports, and supplemented information. The introductory section includes the College's principal officers and organization data. The statistical section includes selected unaudited data, generally presented in a multi-year basis.

FINANCIAL INFORMATION

There are three basic financial statements in this report:

- The Statement of Net Assets,
- The Statement of Revenues, Expenses, and Changes in Net Assets, and
- The Statement of Cash Flows.

The financial statements focus on the financial condition of the College, the results of operations, and cash flows of the College. These financial statements help our readers assess the College's financial health.

The Statement of Net Assets

The Statement of Net Assets includes all assets and liabilities. It is prepared under the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service to us, regardless of when cash is received or paid. This statement reflects the status of the College’s financial resources after the revenues and expenses have been recorded for the year.

The College’s net assets (the difference between assets and liabilities) is one indicator of the College’s financial health. Over time, increases or decreases in net assets is one indicator of the improvement or deterioration of the College’s financial health. Of course, other non-financial data such as enrollment levels and condition of facilities should also be considered in this assessment.

The following table reflects the condensed Statement of Net Assets. Please refer to the College’s Statement of Net Assets (page 15) for more complete detail.

Statement of Net Assets (Condensed)				
	<u>08/31/05</u>	<u>Restated 08/31/04</u>	<u>Increase (Decrease)</u>	<u>Percent Change</u>
Current assets	\$ 10,543,975	\$12,746,620	(\$2,202,645)	-17.3%
Noncurrent assets	6,505,755	934,793	5,570,962	596.0%
Capital assets – net	<u>23,844,054</u>	<u>19,829,348</u>	<u>4,014,706</u>	<u>14.8%</u>
Total assets	40,893,784	33,510,761	7,383,023	22.0%
Current liabilities	2,681,077	2,000,975	680,102	34.0%
Noncurrent liabilities	<u>5,214,639</u>	<u>122,864</u>	<u>5,091,775</u>	<u>4144.2%</u>
Total liabilities	7,895,716	2,123,839	5,771,877	271.8%
Net Assets:				
Invested in Capital Assets (net of related debt)	23,844,054	19,829,348	4,014,706	20.2%
Restricted	879,405	817,975	61,430	7.5%
Unrestricted	<u>8,274,609</u>	<u>10,739,599</u>	<u>(2,464,990)</u>	<u>-23.0%</u>
Total Net assets	\$32,998,068	\$31,386,922	\$ 1,611,146	5.1%

Current assets decreased approximately \$2.2 million during the year which primarily is a result of cash used in construction of campus facilities and acquisition of capital assets. Capital assets increased by approximately \$4 million. The increase in noncurrent assets is attributable to \$5.5 million in bond proceeds received at year end. Similarly, liabilities increased due to the newly acquired bond debt. Trinity Valley Community College continues to maintain a strong financial position. Its net assets increased by \$1,611,146, a 5.1% increase over last year’s net assets.

The Statement of Revenues, Expenses, and Changes in Net Assets

The Statement of Revenues, Expenses, and Changes in Net Assets presents the revenues earned and expenses incurred during the year. The activities of the College are classified as either operating or non-operating.

GASB 33, 34, and 35 accounting requirements significantly impact the determination and classification of *operating* and *non-operating* revenues for public colleges. Operating revenues are activities that generate income that result from “exchange transactions”, i.e., payments received for the college’s services. This definition of operating revenues requires several major changes in the accounting preparation and presentation of financial statements for community colleges.

Perhaps the most significant change is that state appropriations and ad valorem tax revenues, while budgeted for operations, are considered non-operating revenue because these revenues do not meet the above mentioned definition for operating revenue.

Two other changes are notable as well:

- The reporting of tuition and fees and auxiliary (housing, food service and bookstore) revenue is *net of discounts*. Discounting is the practice of accepting less than the stated charge for tuition, fees, room, board and/or books in payment for the goods and services provided. Common terminology for methods of discounting are: “institutional scholarships” when self-funded by the institution, “waivers” and/or “exemptions” when state mandated, “financial aid” and “allowances”. Prior to GASB 34 and 35, reporting gross tuition and fee revenue, and reporting an offsetting expense as “scholarships and financial aid” was the generally acceptable accounting treatment for public colleges and universities. GASB 34 and 35 now require the reporting of scholarship/financial aid as a deduction (discount) from revenue; and
- The utilization of long-lived assets, referred to as capital assets, is reflected in the financial statement as depreciation expense, which allocates the cost of an asset over its expected useful life. Prior to 2004-2005, library books were recommended but not required to be depreciated. However, the Texas Higher Education Coordinating Board’s position has changed and now states that library books shall be depreciated beginning with the 2004-2005 year. For purposes of this report amounts have been restated to reflect the accumulated depreciation for library books through fiscal year 2004.

Due to the above accounting treatments and especially since state appropriations and ad valorem taxes are two of the three primary sources of revenue (state appropriations, tuition and fees, and property taxes), it is likely to be typical to have an *operating loss* on the Statement of Revenues, Expenses, and Changes in Net Assets.

There are additional basic transactions that affect the levels of revenues and expenses:

Revenues:

- Enrollment levels directly affect tuition and fee revenues and auxiliary (housing, food service, and bookstore) sales, services and fee revenues.
- The State of Texas contributes a significant portion of the College revenues through state appropriations. Thus, the economic health and budget priorities of the State may directly affect revenues.
- The College derives a significant amount of grant and student financial aid from the Federal and State governments. Again, changes in their budget priorities may affect revenues.
- Increases or decreases in property tax valuations and property tax rates will affect tax revenues.
- Investment income is affected by changes in interest rates, the stock market, etc.

Expenses:

- Enrollment levels may directly affect expenses by increasing or decreasing the resources required to support the students.
- The implementation of new programs or additional services within the existing functional expense categories directly affects the level of services required and resources needed.
- Economic factors, such as changes in prices caused by inflation or changes in energy prices, will impact operating costs.

The following table reflects the condensed Statement of Revenues, Expenses and Change in Net Assets. Please refer to the College’s Statement of Revenues, Expenses and Change in Net Assets (page 17) for more complete detail.

Statement of Revenues, Expenses and Changes in Net Assets (Condensed)				
	<u>2005</u>	<u>Restated 2004</u>	<u>Increase (Decrease)</u>	<u>Percent Change</u>
Operating Revenue				
Tuition and fees – net	3,321,684	3,290,105	31,579	1.2%
Grants and contracts	7,032,166	6,588,738	443,428	6.7%
Sales and Services of				
Educational Activities	385,374	361,678	23,696	6.6%
Auxiliary – net	2,093,808	2,156,776	(62,968)	-2.9%
Other	<u>182,480</u>	<u>319,273</u>	<u>(136,793)</u>	<u>-42.8%</u>
Total operating revenue	13,015,512	12,716,570	298,942	2.4%
Less Operating Expenses				
Instruction	11,579,615	11,559,234	20,381	0.2%
Public Service	347,022	303,787	43,235	14.2%
Academic Support	2,368,952	1,739,881	629,071	36.2%
Student Services	2,501,611	2,393,200	108,411	4.5%
Institutional Support	2,335,924	2,462,905	(126,981)	-5.2%
Plant Operations	2,689,687	2,289,962	399,725	17.5%
Scholarships**	2,891,367	2,790,309	101,058	3.6%
Auxiliary	2,973,737	3,078,751	(105,014)	-3.4%
Depreciation	<u>872,478</u>	<u>707,614</u>	<u>164,864</u>	<u>23.3%</u>
Total Operating Expenses	28,560,393	27,325,643	1,234,750	4.5%
Net Operating Income (Loss)	(15,544,881)	(14,609,073)	(935,808)	6.4%
Non Operating Revenue (Expenses)				
State Appropriations	12,187,632	12,193,672	(6,040)	0.0%
Property taxes	4,656,766	4,268,699	388,067	9.1%
Gifts	66,999	47,386	19,613	41.4%
Investment income	311,508	210,289	101,219	48.1%
Loss on Disposal of Assets	(66,878)	(88,891)	(22,013)	-24.8%
Insurance proceeds	0	233,259	(233,259)	-100.0%
Interest Expense	<u>0</u>	<u>0</u>	<u>0</u>	<u>0.0%</u>
Total non operating revenues	17,156,027	16,864,414	291,613	1.7%
Increase in Net Assets	1,611,146	2,255,341		
Net Assets – Beginning of Year	<u>31,386,922</u>	<u>30,510,225</u>		
Prior year adjustment		(1,378,644)	*accumulated depreciation/books	
Net Assets – End of Year	<u>\$32,998,068</u>	<u>\$31,386,922</u>	1,611,146	5.1%

**Note: In the above table, the terminology “scholarships” used under operating expenses are monies paid directly to students which were not included as a “discount” against tuition, fees, room, board and book revenues. (See paragraph on tuition discounting above.) The vast majority of these monies are Federal Financial Aid that flow from the U.S. Department of Education through the College to the students for their own use after educational costs have been paid.

In fiscal year 2005, operating revenue totaled \$13,015,512, an increase of 2.4% over the past year. Tuition and fee revenue increased by \$31,579 or 1%. However, adding back financial aid which paid for students’ tuition and fees (discounts for purposes of this annual report) results in a 2.3% increase. The small percentage increase in tuition and fee revenue is reflective of the College’s decision not to raise tuition and fee costs for fiscal year 2005. Student contact hour production increased approximately 2%. Increased federal and state financial aid to students is attributable to the increase in grant revenue. Sales and services of educational activities were up primarily due to the expansion of the distance education program. The decrease in other revenue is due to the previous year’s receipts of insurance proceeds for flood damage for contents at the Health Science Center.

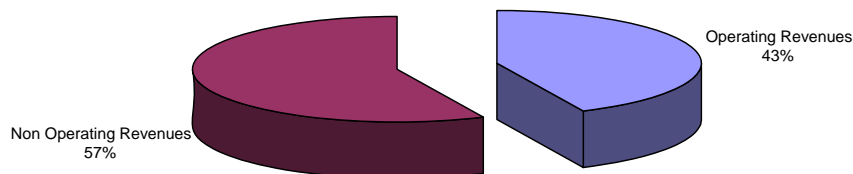
Non-operating revenue, the majority of which is state appropriations and property tax revenue, increased 1.7% from the previous year to \$17,156,027. State appropriations were essentially flat for the year while all other categories of revenue were up. Last year the College received insurance proceeds for flood damage to the Health Science Center. None were received for fiscal year 2005.

Fiscal year 2005 operating expenses totaled \$28,560,393, an increase of \$1,234,750, or 4.5% over the previous year. Salaries and employee fringe benefits, which represent the largest operating expense, increased due to additional personnel and annual pay increases. Increased expense can also be attributed to additional grant and scholarship aid.

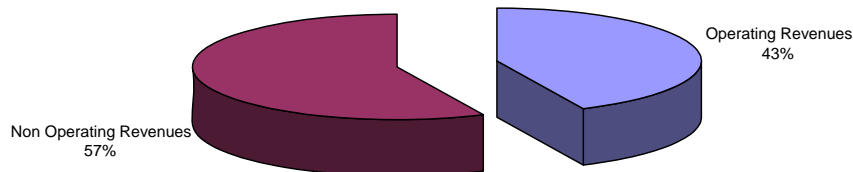
After deducting operating expenses from operating revenue, the College had a *net operating loss* of \$15,544,881. However, when combined with non-operating revenue of \$17,156,027 the College had a net increase in assets of \$1,611,146.

The following charts provide a graphic breakdown of total revenues by category for the fiscal years ending August 31, 2005 and August 31, 2004.

2005 Major Revenue Categories

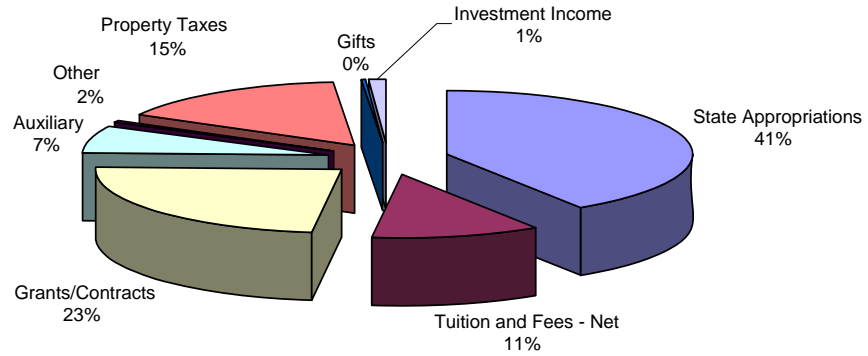


2004 Major Revenue Categories

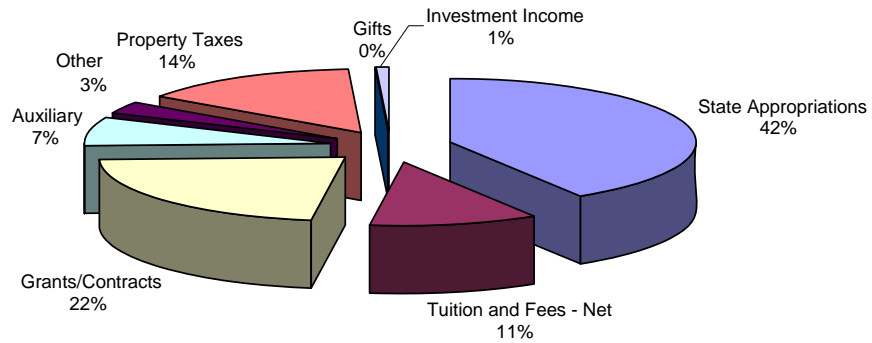


The following is graphic illustrations of revenues by source for the fiscal years August 31, 2005 and August 31, 2004:

2005 Revenue by Source

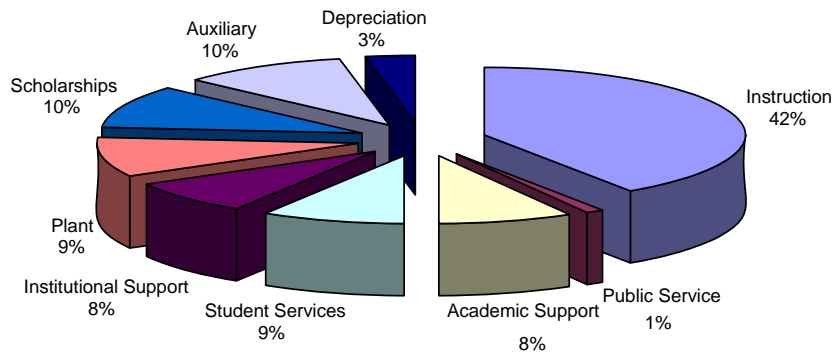


2004 Revenue by Source

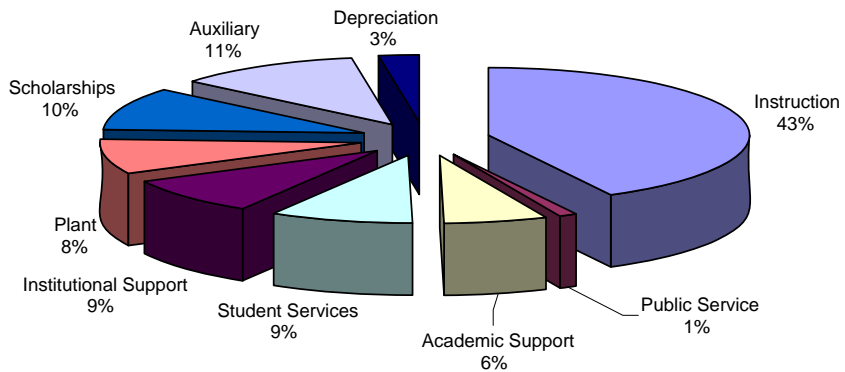


The following is graphic illustrations of operating expenses presented by functional classification for the fiscal years August 31, 2005 and August 31, 2004:

2005 Operating Expenses - Functional Classification

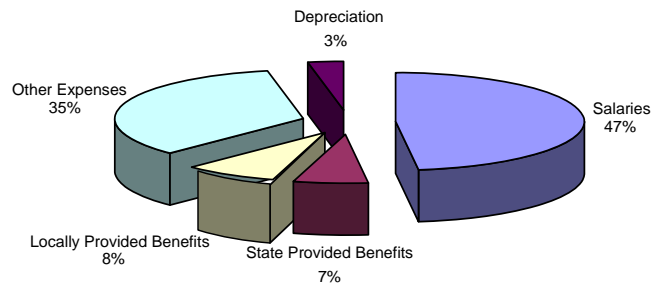


2004 Operating Expenses - Functional Classification

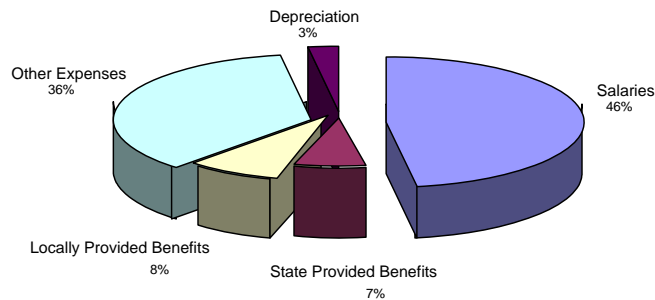


Operating expenses may also be presented by natural classification:

2005 Operating Expenses - Natural Classification



2004 Operating Expenses - Natural Classification



Operating Expenses (by natural classification)

	<u>2005</u>	<u>2004</u>	<u>Increase (Decrease)</u>	<u>% Change</u>
Salaries	\$13,712,558	\$12,968,938	\$ 743,620	5.7%
State Provided Benefits	\$ 1,863,941	\$ 1,861,203	\$ 2,738	0.1%
Local Provided Benefits	\$ 2,246,344	\$ 2,085,726	\$ 160,618	7.7%
Other Expenses	\$ 9,865,072	\$ 9,702,162	\$ 162,910	1.7%
Depreciation	\$ 872,478	\$ 707,614	\$ 164,864	23.3%
Total Expenses	\$28,560,393	\$27,325,643	\$ 1,234,750	4.5%

Statement of Cash Flows

Another way to assess the financial health of an institution is to look at the Statement of Cash Flows. Its primary purpose is to provide relevant information about actual cash receipts and cash payments during the period. It also helps users assess the institution's ability to generate future net cash flows, its ability to meet its obligations as they come due and whether or not there is a need for external financing.

Cash increased \$3,189,130 from 2004 resulting in a cash balance of \$14,332,644 as of August 31, 2005.

The following table reflects the condensed Statement of Cash Flows. Again, please refer to the College's Statement of Cash Flows (page 19) for complete details.

Statement of Cash Flows (Condensed)				
	<u>2005</u>	<u>2004</u>	Cash Increase (Decrease)	Percent Change
Net Cash provided (used) by:				
Operating activities	\$(12,594,510)	\$(11,668,469)	\$(926,041)	- 7.9%
Non-capital financing activities	14,924,437	14,540,575	383,862	2.6%
Capital and related financing activities	549,016	(1,639,573)	2,188,589	134.1%
Investing activities	<u>310,187</u>	<u>210,509</u>	<u>99,678</u>	<u>47.4%</u>
Net increase in cash	3,189,130	1,443,042	1,746,088	121.0%
Cash, beginning of the year	<u>11,143,514</u>	<u>9,700,472</u>		
Cash, end of the year	<u>\$14,332,644</u>	<u>\$ 11,143,514</u>		

Cash provided (used) by operating activities represents the difference in the incoming and outgoing cash for all educational and administrative activities (primarily receipts for tuition and fees, auxiliary services and grants and payments for salaries, goods and services and scholarships).

Cash provided by non-capital financing activities represent state appropriations and collections for local ad valorem taxes.

Cash provided (used) in capital and related financing activities represent bond proceeds received and payments for acquisitions and construction of capitalized assets. For fiscal year 2005, the College received \$5.5 million in bond proceeds and paid out approximately \$4.9 million on construction and other capitalized assets.

Capital Asset and Debt Administration

Capital Assets

At August 31, 2005, the College had \$23,844,054 invested in capital assets, net of accumulated depreciation of \$9,616,977. This accumulated depreciation amount includes the prior year adjustment of \$1,378,644 to record depreciation on library books through fiscal year 2004. Details of these assets are shown below. Refer to Note 6 in the Notes to the Financial Statements (page 25) for further details.

Capital Assets				
	<u>08/31/05</u>	(Restated) <u>08/31/04</u>	Increase <u>(Decrease)</u>	Percent <u>Change</u>
Land	\$ 1,139,726	\$ 1,139,726	0	0
Library Books	2,384,967	2,347,559	37,408	1.6%
Construction in Progress	3,889,122	1,147,353	2,741,770	239.0%
Buildings	22,117,964	20,920,163	1,197,801	5.7%
Facility and Other Improvements	2,093,190	1,458,623	634,567	43.5%
Furniture, Machinery, Vehicles and Other Equipment	1,091,450	1,019,100	72,350	7.1%
Telecommunications and and Peripheral Equipment	<u>744,612</u>	<u>751,298</u>	<u>(6,686)</u>	<u>-0.9%</u>
Subtotal	33,461,032	28,783,822	4,677,210	16.2%
Accumulated Depreciation:	(9,616,977)	(8,954,474)	662,503	7.4%
Net Capital Assets	<u>\$ 23,844,055</u>	<u>\$ 19,829,348</u>	4,014,707	12.4%

During the year, capital assets acquisitions of \$4,954,062 (\$4.6 for building related projects) were added and capital assets in the amount of \$276,853 were removed. The net result, along with the change in accumulated depreciation for 2005 of \$662,503, is an increase in net capital assets of \$4,014,707.

The College stands committed to its facilities master plan in maintaining adequate physical resources to support its mission. In 2005, the College completed construction, except for some minor details, of the Learning Resource Center on the Terrell campus, at a cost of approximately \$3.3 million. This facility contains over 33,000 square feet and will provide eleven new classrooms, ten faculty offices, various conference and media rooms, and a new library. Additionally, the College recently completed an approximately 11,000 square foot, \$1.2 million athletic field house. The addition of this facility allows men and women's basketball teams to be housed under one gym, rather than two, and allows demolition of the old gym to make way for a new technology building.

Debt

This year, the College issued a \$5.5 million general revenue bond to aid in the construction of a new technology building. Refer to Note 7 in the Notes to the Financial Statements (page 27) for additional information regarding the bond. This is the first bond issue by the college in about forty years.

The technology building will provide twenty-four classrooms, seventeen faculty offices, and several conference rooms. Preparation of the site began in the summer of 2005 with an anticipated construction completion date of summer 2007.

FUTURE FINANCIAL AFFECTS

Trinity Valley Community College is committed to providing education and workforce development programs and services that meet individual and community needs. The ability to fulfill its mission is directly influenced by enrollment, state appropriations, and federal funding. Additionally, escalation of salaries, health care, utilities and unfunded state and federal mandates require continual fiscal oversight. The College will scrutinize potential avenues for additional revenue and will endeavor to keep operating costs at a minimum while striving to keep the price of education affordable for all students.

Historically, Trinity Valley Community College has been successful in maintaining low educational costs. Due to the continued uncertainty of the level of state funding for community colleges along with an anticipated upward trend in enrollment growth, the College foresees the need for increased revenue to fulfill the educational needs of the region. Tuition was raised \$5 per semester credit hour, a 33% increase, for the upcoming fiscal year 2005/2006.

To help meet the challenge, the College's Foundation was revitalized. It began a new Capital Campaign four years ago and the balance of the Foundation's fund at fiscal year end August 31, 2005, is \$1,201,404, an increase of \$335,861 over the previous year.

The campaign's overall goal seeks to strengthen scholarship endowment funds in hopes of providing some type of scholarship for every deserving student who desires a college education at Trinity Valley Community College.