

REPORT HIGHLIGHTS
 FINANCIAL STATEMENT AUDIT

University Implements New Financial Reporting Standard

Subject

Arizona State University issues financial statements annually. The University is responsible for preparing financial statements, maintaining strong internal controls, and demonstrating accountability for its use of public monies. As the auditors, our job is to determine whether the University has met its responsibilities.

Our Conclusion

The information in the University's financial statements is fairly stated in all material respects and the financial statements can be relied upon. This information is also incorporated in the State of Arizona's *Comprehensive Annual Financial Report*.

During fiscal year 2005, the University implemented Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures*. This reporting standard results in the University's disclosure of investment policies and any investment and deposit risks related to credit quality risk, custodial risk, concentration risk, foreign currency risk, and interest rate risk. The deposits and investments of the University are subject to all of these risks, which are described in greater detail below.

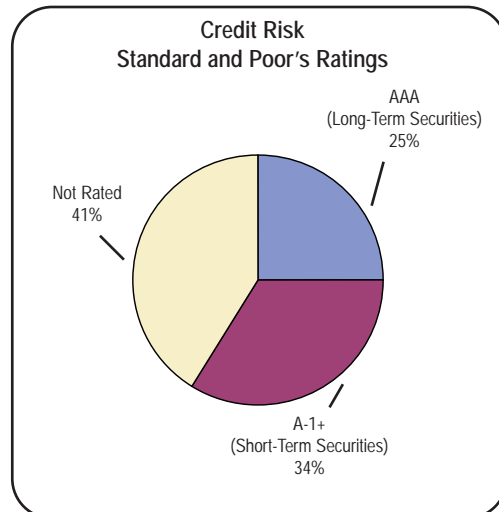
Credit risk: This is the risk that an issuer of a debt security will not fulfill its obligations. Governments must disclose the credit quality ratings of investments in most debt securities. The University obtained credit quality ratings from Standard and Poor's Ratings Service. The University's investments received the highest ratings assigned by Standard and Poor's. The unrated securities held by the University represent its share of various pooled investment funds, the largest being the State of Arizona Local

Government Investment Pool.

Custodial risk: This is the risk that a government will not be able to recover deposits if a depository financial institution fails, or recover the value of an investment in the possession of an outside party if the transaction fails. Governments must disclose deposits and investments subject to this risk by type and fair value, and describe how they are held. At June 30, 2005, the University's deposits and investments totaled \$413.2 million, with \$1.1 million exposed to custodial credit risk as one deposit was uncollateralized.

Concentration risk: This is the risk of loss attributed to the magnitude of a government's investment in a single issuer. Government's must generally disclose, by amount and issuer, investments in any one issuer that represent 5 percent or more of total investments. At June 30, 2005, the University had 24 percent invested in securities issued by the Federal National Mortgage Association, 15 percent in securities issued by the Federal Home Loan Bank, and 9 percent in securities issued by the Federal Home Loan Mortgage Corporation.

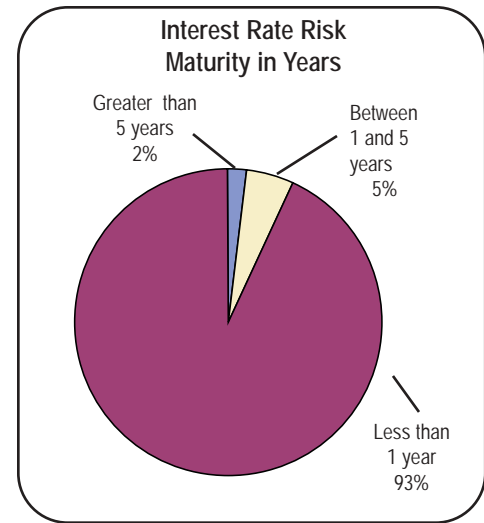
Foreign currency risk: This is the risk that changes in exchange rates will adversely affect the fair value of a deposit or investment. Governments must disclose by currency denomination and type the balances of deposits and investments exposed to foreign currency risk. At June 30, 2005, the University endowment investments of \$76.2 million included international investments totaling \$23.6 million, with 73 percent in equity investments, 4 percent in fixed income investments, and 23 percent in other marketable and nonmarketable investments.



2005

Year Ended June 30, 2005

Interest rate risk: This is the risk that changes in interest rates will adversely affect the fair value of an investment in debt securities. The University uses the weighted average maturity (WAM) method of disclosure, as it is most consistent with the University's method of identifying and managing this risk. A significant portion, or 93 percent, of the University's debt securities that were subject to interest rate risk had a WAM of less than one year as shown in the chart to the right.



The University's Condensed Financial Information

The University's financial information is presented in three financial statements: Statement of Net Assets; Statement of Revenues, Expenses, and Changes in Net Assets; and Statement of Cash Flows.

The third category, unrestricted net assets, shows the net resources available to the University to fund other general operations. The summary below presents a condensed Statement of Net Assets as of June 30, 2005.

Statement of Net Assets

The Statement of Net Assets reports all assets and liabilities of the University using the accrual basis of accounting, which is similar to the accounting that most private-sector institutions use. Net assets, which is the difference between assets and liabilities, include three major categories. The first category, invested in capital assets, net of related debt, shows the University's equity in property, plant, and equipment. The next category, restricted net assets, shows the amount of net resources available for certain university expenditures. These net assets must be used for purposes determined by donors and external entities that have placed purpose restrictions on their use.

Statement of Net Assets As of June 30, 2005 (In Millions)

Assets	
Current	\$ 180
Noncurrent, other than capital	326
Capital assets, net	<u>1,246</u>
Total assets	<u>1,752</u>
Liabilities	
Current	103
Noncurrent	<u>812</u>
Total liabilities	<u>915</u>
Net Assets	
Invested in capital assets, net of related debt	572
Restricted	105
Unrestricted	<u>160</u>
Total net assets	<u>\$ 837</u>

Statement of Revenues, Expenses, and Changes in Net Assets

The Statement of Revenues, Expenses, and Changes in Net Assets presents the University's operating and nonoperating revenues and expenses, and the resulting change in net assets. Revenues and expenses are classified as operating if they relate to the University's primary activities, such as instruction, research, and public service. All other revenues and expenses, such as state appropriations and interest on indebtedness, are considered nonoperating. The change in net assets indicates whether the University's financial health has improved or deteriorated as a result of current-year operations. For the current year, the University's net assets showed a slight decrease of \$4 million. The summary to the right presents the University's revenues and expenses for the year ended June 30, 2005.

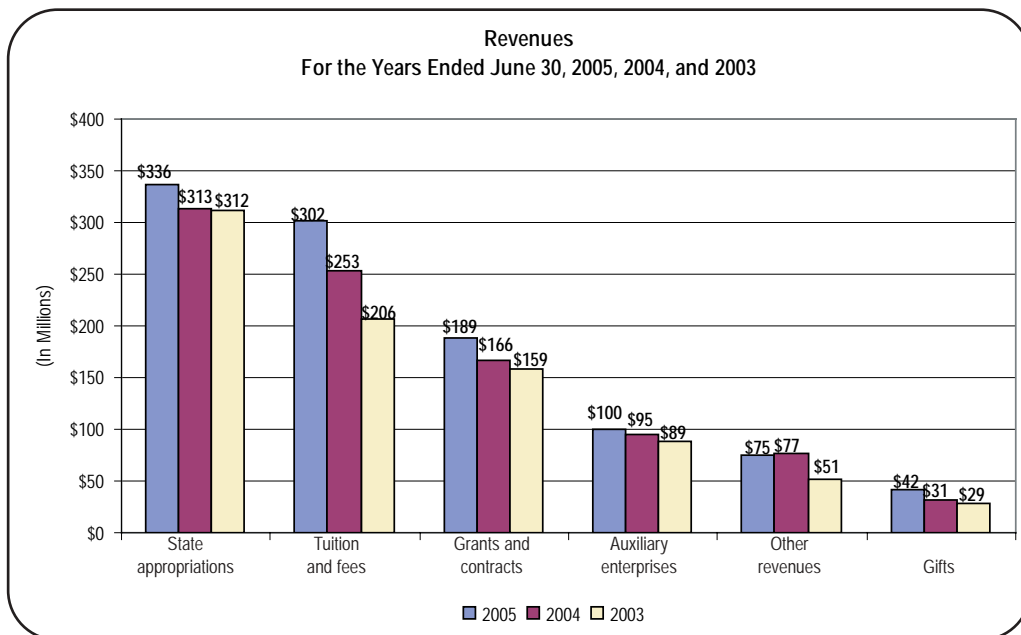
Revenues and Expenses For the Year Ended June 30, 2005 (In Millions)

Operating Revenues	
Tuition and fees	\$ 302
Grants and contracts	189
Sales and services	127
Other	<u>5</u>
Total operating revenues	<u>623</u>
Nonoperating Revenues	
State appropriations	336
Other	<u>85</u>
Total nonoperating revenues	<u>421</u>
Total revenues	<u>\$1,044</u>
Operating Expenses	
Educational and general	\$ 851
Auxiliary enterprises	91
Depreciation	<u>71</u>
Total operating expenses	<u>1,013</u>
Nonoperating Expenses	
Interest on indebtedness	23
Other	<u>12</u>
Total nonoperating expenses	<u>35</u>
Total expenses	<u>\$1,048</u>

Revenues

Between fiscal years 2003 and 2005, total revenues of the University have increased by \$198 million, or 23 percent. As shown in the chart below, the change primarily resulted from increases in tuition and fees and grants and contracts. Tuition and fees revenues

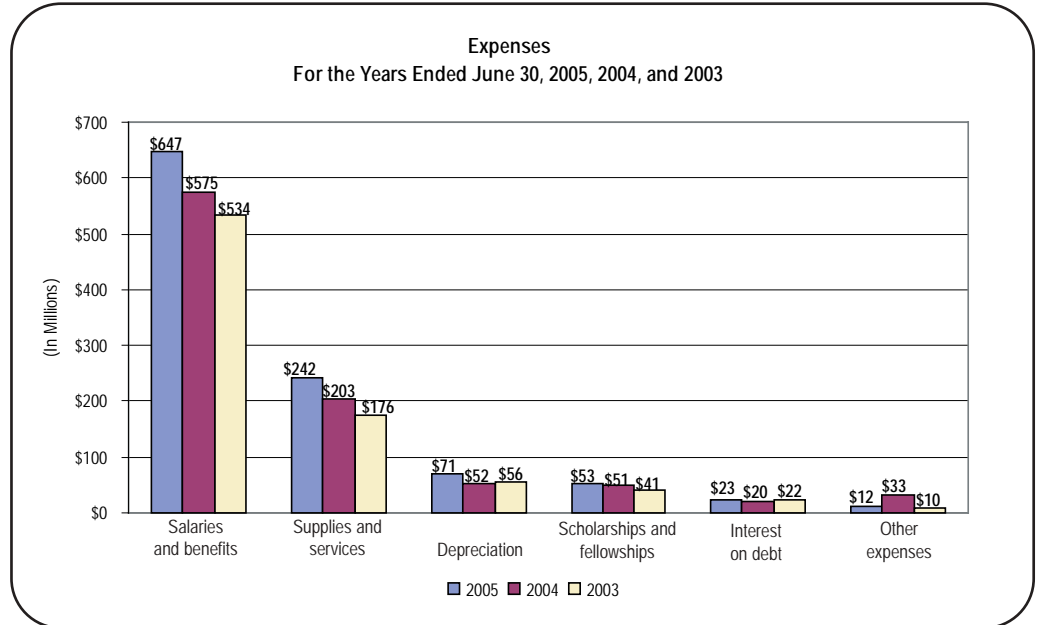
increased \$96 million, and grants and contracts revenues increased by \$30 million during the period. These changes primarily resulted from increased charges for tuition and fees and increases in grants awarded to the University.



Expenses

Between fiscal years 2003 and 2005, total expenses of the University have increased \$209 million, or 25 percent. As shown in the chart below, the change primarily resulted from increases in salaries and benefits and supplies and services expenses. Salaries and

benefits increased \$113 million and supplies and services increased \$66 million during the period. These changes primarily resulted from rising employee benefit costs, increases in information technology expenses for many of the colleges, increases in instruction delivery related to initiatives to decrease freshman class sizes, and increased services provided to students.



TO OBTAIN MORE INFORMATION

A copy of the full report can be obtained by calling
(602) 553-0333



or by visiting our Web site at:
www.azauditor.gov

Contact person for this report:
Jay Zsorey

Statement of Cash Flows

The Statement of Cash Flows provides information about cash receipts and cash payments during the year. This statement helps users assess the University's ability to generate net cash flows to meet its obligations as they come due and the need for external financing. The table to the right shows the net cash flows from each of the University's major activities for the year ended June 30, 2005.

Cash Flows For the Year Ended June 30, 2005 (In Millions)

Cash Flows from:	
Operating activities	\$(339)
Noncapital financing activities	365
Capital and related financing activities	(8)
Investing activities	<u>4</u>
Net increase in cash and cash equivalent investments	<u>\$ 22</u>