

## REPORT HIGHLIGHTS

FINANCIAL STATEMENT AUDIT

### Subject

The University of Arizona 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*.



2005

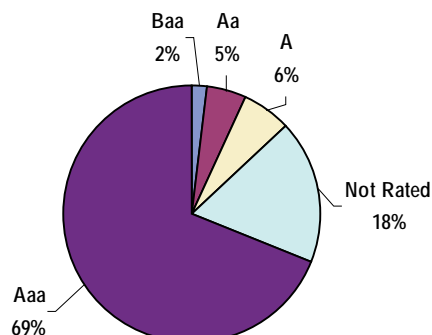
Year Ended June 30, 2005

## University Implements New Financial Reporting Standard

During fiscal year 2005, the University implemented Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures*. This reporting standard requires the University to disclose its investment policies and any investment and deposit risks related to credit risk, custodial credit risk, concentration of credit risk, foreign currency risk, and interest rate risk. The deposits and investments 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 Moody's Investors Service. A significant portion, or 69 percent, of the University's debt securities that were subject to credit risk received the highest ratings assigned by Moody's as shown in the chart below.

Credit Risk of Investments  
 As of June 30, 2005  
 Moody's Investors Service Ratings



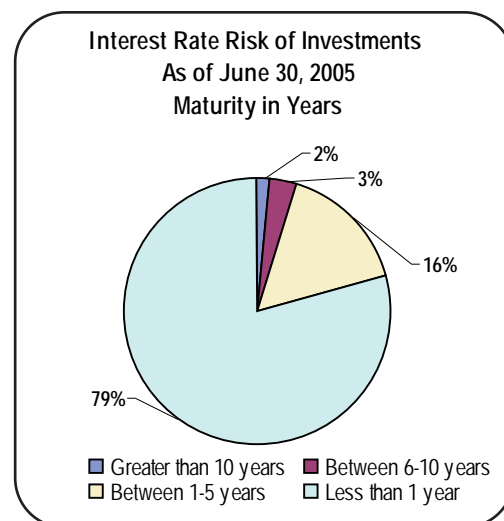
**Custodial credit risk:** This is the risk that a government will not be able to recover deposits if a depository financial institution fails, or recover the value of an investment in the possession of an outside party if the counterparty to a transaction fails.

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 had \$17.7 million of total deposits and investments that were exposed to custodial credit risk.

**Concentration of credit risk:** This is the risk of loss attributed to the magnitude of a government's investment in a single issuer. Governments must generally disclose, by amount and issuer, investments in any one issuer that represents 5 percent or more of total investments. At June 30, 2005, the University had 16 percent invested in securities issued by the Federal National Mortgage Association, 16 percent in securities issued by the Federal Home Loan Bank, and 6 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 deposit or investment type the balances of deposits and investments exposed to foreign currency risk. At June 30, 2005, the University held investments in two international mutual funds, representing 13 percent of the University's total endowment portfolio.

**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 segmented time distribution method of disclosure, as it is most consistent with the University's method of identifying and managing this risk. A significant portion, or 79 percent, of the University's debt securities that were subject to interest rate risk had a maturity of less than 1 year as shown in the chart to the right.



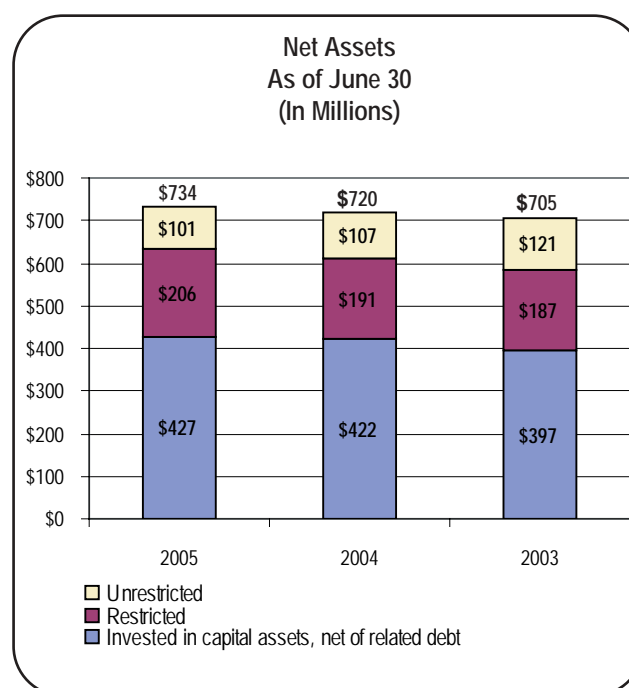
## Condensed Financial Information

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 University's component units are not included in the condensed financial information that follows.

### Statement of Net Assets

The Statement of Net Assets reports all of the University's assets and liabilities using the accrual basis of accounting, which is similar to the accounting that most private-sector institutions use. Net assets, 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 the use of those resources. The third category, unrestricted net assets, shows the net resources available to the University to fund other general operations.

Changes in net assets over time are one way to measure the University's financial health. As shown in the chart below, the University's financial position has remained relatively stable from fiscal years 2003 through 2005. Total net assets have increased from \$705 million as of June 30, 2003, to \$734 million as of June 30, 2005, or 4 percent over the 3-year period.



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

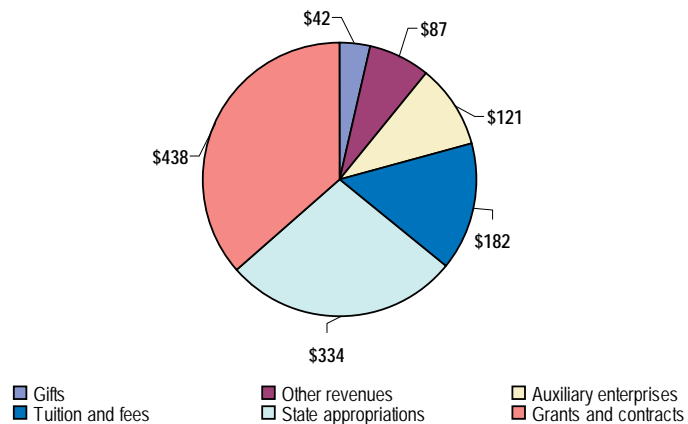
The Statement of Revenues, Expenses, and Changes in Net Assets presents the University's operating and nonoperating revenues and expenses, and the resulting change in net assets. The change in net assets indicates whether the University's financial health has improved or deteriorated as a result of current-year operations. For the current year, the University's net assets increased \$14 million.

### Revenues

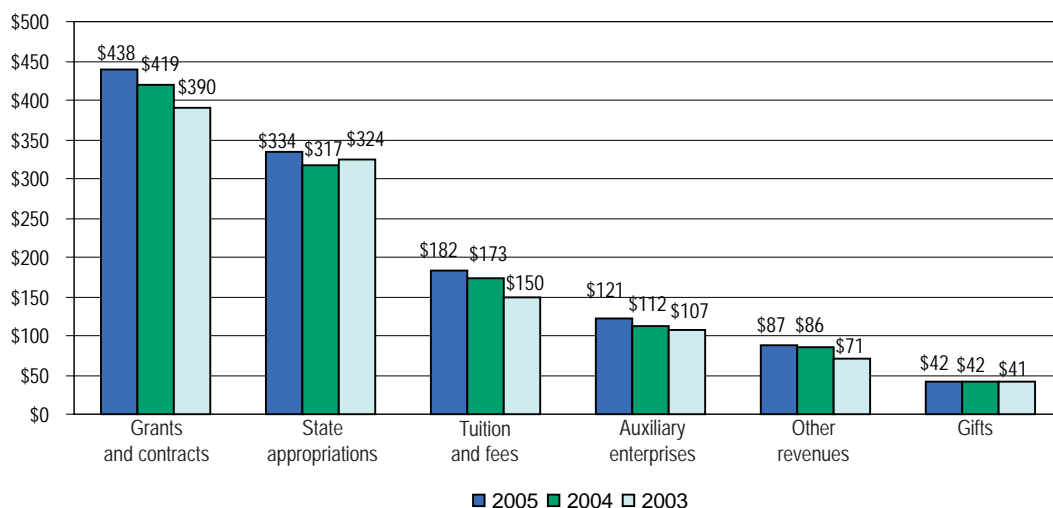
The chart to the right shows the components of the University's operating and nonoperating revenues for the year ended June 30, 2005. Grants and contracts, state appropriations, tuition and fees, and auxiliary enterprises comprise 89 percent of the University's total revenues. Between fiscal years 2003 and 2005, total revenues have increased by \$121 million, or 11 percent. As shown in the chart to the right, the change primarily resulted from

increases in grants and contracts and tuition and fees revenues. Grants and contracts revenues increased \$48 million, and tuition and fees revenues increased \$32 million during the period. These changes primarily resulted from increases in grants awarded to the University for research projects and increased rates for tuition and fees.

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

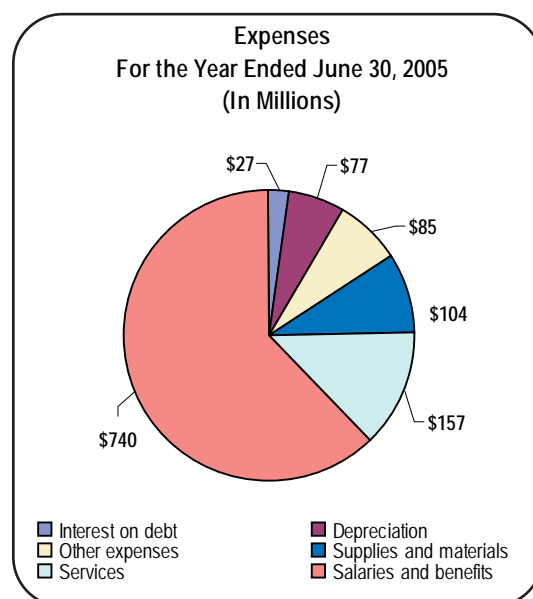


**Revenues**  
For the Years Ended June 30, 2005, 2004, and 2003  
(In Millions)



## Expenses

The chart to the right shows the components of the University's operating and nonoperating expenses for the year ended June 30, 2005. Salaries and benefits, services, supplies and materials, and other expenses comprise 91 percent of the University's total expenses. Between fiscal years 2003 and 2005, total expenses have increased \$141 million, or 13 percent. As shown in the chart below, the change primarily resulted from increases in salaries and benefits, services, and other expenses. Salaries and benefits increased \$78 million, other expenses increased \$25 million, and services increased \$22 million during the period. These changes primarily resulted from rising employee benefit costs, increased scholarship awards, and additional costs associated with the University's sponsored research activities.



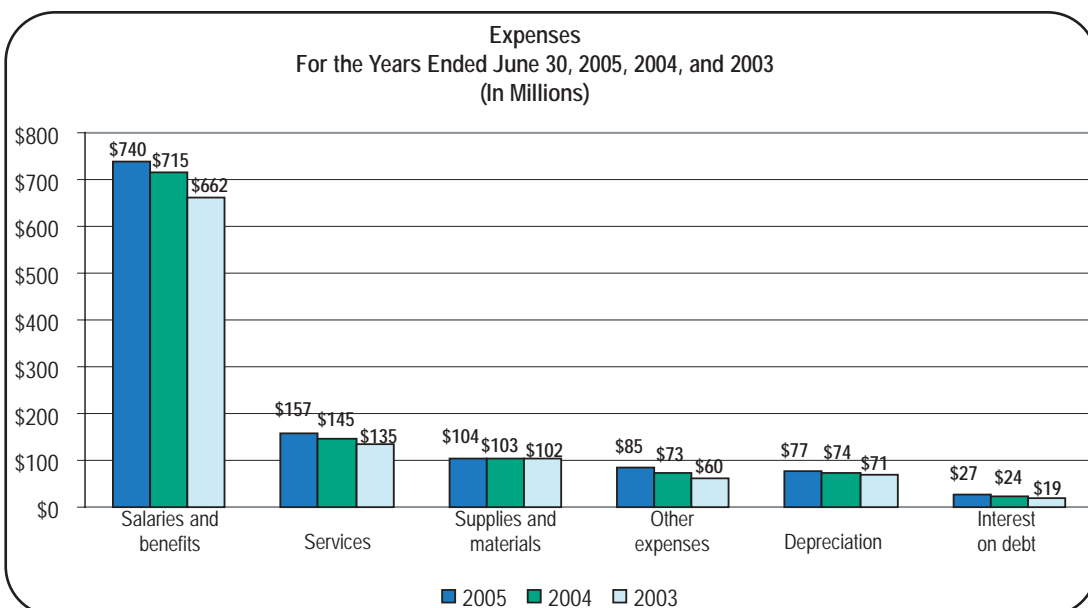
### TO OBTAIN MORE INFORMATION

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



or by visiting  
our Web site at:  
[www.azauditor.gov](http://www.azauditor.gov)

Contact person for  
this report:  
Rick Meyer



## 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	\$(318)
Noncapital financing activities	397
Capital and related financing activities	(219)
Investing activities	<u>162</u>
Net increase in cash and cash equivalents	<u>\$ 22</u>