The Audit Process

Independent Auditors' Reports on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards were issued for all financial reports. The combined financial statements, as well as the financial statements for each institution, the Commission, and the Council can be viewed on the Commission's website at http://www.hepc.wvnet.edu/finance.

Summary of Financial Results

A summary of the financial information for the System is provided in this section. As a point of reference, the dollar amounts numbers are presented in thousands.

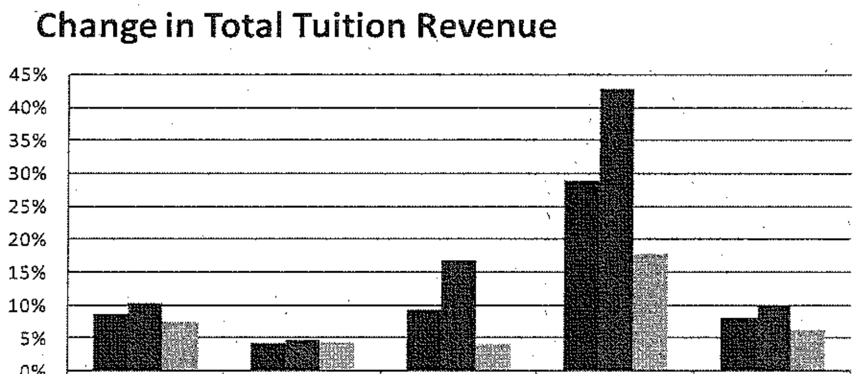
Net Assets

Net assets are the total assets less the total liabilities of the System. The net assets of the System increased in fiscal year 2011 by $10.6 million. This follows an increase of $27.8 million in fiscal year 2010.The change in FY 2011 approximates the increase in capital assets net of depreciation. As noted in the chart below, other changes were offset by the increase in the OPEB liability. Much of the change in assets and liabilities in FY 2010 was a result of transfers from four-year institutions.

	FY 2010	FY 2011	Change
Net assets	156,391	167,024	10,633
Capital assets - net	119,241	129,645	10,404
Current cash and cash equivalents	66,160	70,424	4,264
Accounts Payable	3,600	2,947	(653)
Appropriations due from primary government	7,663	8,560	897
Debt service obligation	9,779	8,795	(984)
Noncurrent cash and cash equivalents	2,497	3,673	1,176
OPEB liability	9,015	16,424	7,409

Tuition and Fee Revenue

Primarily as a result of enrollment growth, total student tuition and fee revenues net of the scholarship allowance increased $1.8 million in fiscal year 2011. The $4.4 million increase in gross tuition and fees revenues was offset by a $2.6 million increase in the scholarship allowance. Over the past five years the percent increase in the scholarship allowance has exceeded the percent increases in gross and net tuition and fees because more federal and State financial aid has been available to students.



	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
Gross Tuition and Fee Revenues	8%	4%	9%	29%	8%
Scholarship Allowance	10%	5%	17%	43%	10%
Net Tuition and Fee Revenues	7%	4%	4%	18%	6%

Operating Expenses

Operating expenses increased $14.7million over FY 2010. Total salaries and wages increased as a result of new faculty lines required to serve a growing student population, successful grant activity and limited salary increases provided during the year. Scholarships and Fellowships expenses increased because students received additional federal and state financial aid. Investments in institutional facilities and equipment resulted in additional depreciation expense.

Operating Expenses (in 000s)			
	FY 2010	**FY 2011**	**Change**
Salaries and Wages	$61,768	$66,770	$5,002
Benefits	22,743	22,966	223
Supplies and Other Services	43,283	44,025	742
Utilities	1,920	2,238	318
Student Financial Aid- Scholarships and Fellowships	37,894	44,947	7,053
Depreciation	5,011	6,109	1,098
Loan Cancellations and write-offs	39	280	241

Operating Expenses Percent Increases					
	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
Salaries and Wages	5.22%	8.87%	8.16%	3.84%	8.10%
Benefits	-5.49%	26.43%	8.00%	39.30%	0.98%
Supplies and Other Services	3.91%	-8.18%	20.77%	22.53%	1.71%
Utilities	2.95%	0.73%	-17.02%	11.56%	16.56%
Scholarships and Fellowships	3.97%	18.07%	39.64%	53.55%	18.61%
Depreciation	8.37%	7.03%	5.24%	34.20%	21.91%

Other Post Employment Benefits

Beginning in Fiscal Year 2008, the System adopted GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions*. This statement provides standards for the measurement, recognition, and reporting of other postemployment benefit (OPEB) expenditures, assets, and liabilities. To address the issues raised by this Statement, the legislature created a postemployment trust fund for all State agencies. The System participates in this multiple employer cost-sharing plan, administered by the Public Employee's Insurance Agency (PEIA).

The recognition of OPEB expenditures, assets and liabilities has created a substantial burden for institutions across the System and Fund. The FY2011 $7.4 million increase in the liability is equal to 24 percent of the System's unrestricted assets. It is anticipated that the System will continue to be billed about the same amount annually for the near term future unless legislation is passed to deal with the problem. It should be noted that currently there is no penalty for nonpayment of the invoices submitted by PEIA. Nor is there any direct correlated benefit to paying the invoices.

Analysis: Ratios and Financial Information

The purpose of this section is to provide a summary and analysis of the data included in the System's financial statements. Only financial information is provided; therefore, this information should be combined with key performance indicators in other areas such as academics, and student and faculty satisfaction to acquire a more complete understanding of institutional strength.

To ascertain the financial health of a college, four questions should be asked:

- Are resources sufficient and flexible enough to support the mission?
- Does financial asset performance support the strategic direction?
- Do operating results indicate the institution is living within available resources?
- Is debt managed strategically to advance the mission?

To answer these questions, objective financial data should be analyzed within the context of the institutions' strategic plans. These plans are often influenced by the political and economic environment within which the institutions operate.

To address the four questions listed above, a financial analysis is presented using the Composite Financial Index (CFI) and several other ratios.[2]The CFI calculation uses the primary reserve, net operating revenues, viability and return on net assets ratios. These ratios are converted into strength factors which in turn are weighted to allow summing of the four resulting ratio scores into a single, composite value. The strength factors are limited to a scale of -4 to 10.

[2]The CFI methodology is described in the *Strategic Financial Analysis for Higher Education* (Sixth Edition), jointly developed and sponsored by Prager, Sealy & Co., LLC, KPMG, LLP and BearingPoint., Inc.

Weights are applied to the strength factors depending upon the amount of capital debt. The primary reserve ratio and viability ratio are measures of financial condition based on expendable net assets. The net operating revenues ratio measures an institution's ability to live within its means on a short term basis. The return on net assets assesses a school's capacity to generate overall return against all net resources. The viability ratio was not computed for institutions with an insignificant level of debt.

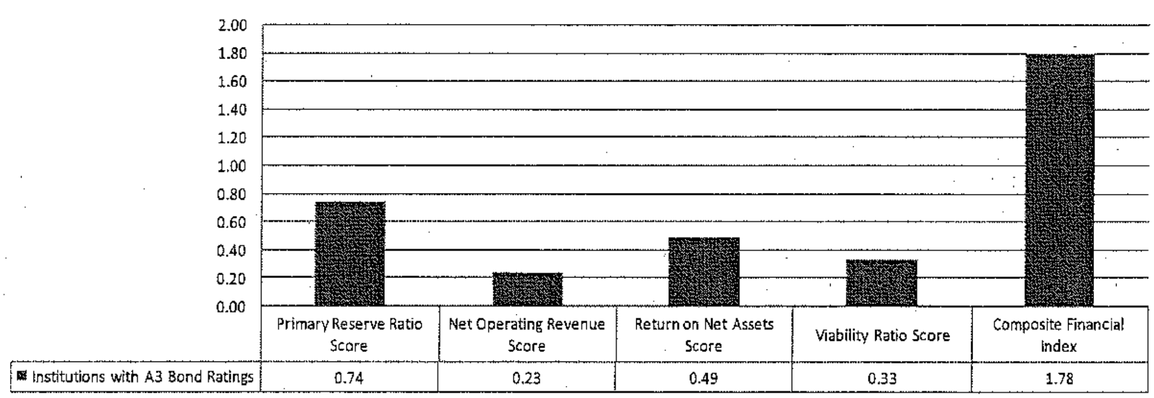
Composite Financial Index Weights (Percent)		
Ratio	Institutions with Significant Debt	Institutions without Significant Debt
Primary Reserve	35	55
Net Operating Revenue	10	15
Return on Net Assets	20	30
Viability	35	

Other ratios were calculated to provide additional insight into the schools' financial health. Because the CFI primary reserve indices for some institutions were relatively low, the number of days cash on hand was determined additionally. The age of the physical plant for each institution was estimated to assess the physical resources available to advance the schools' missions.

The *FY 2010 U.S. Public College and University Medians* published by Moody's Investors Service was utilized to provide benchmark data for comparison purposes. The report includes median ratios for each rating category.

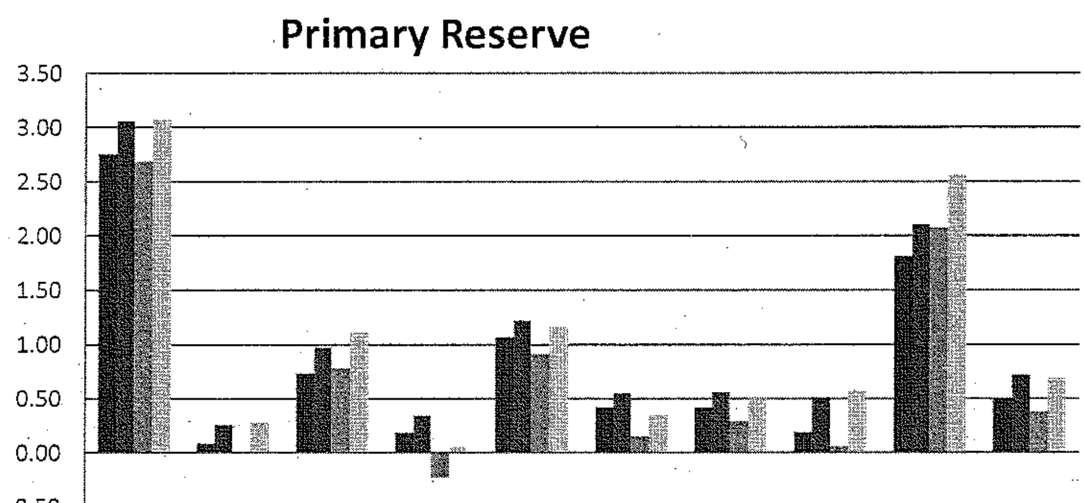
The rating category A3 was used because the characteristics of the related institutions are similar to those of the System's institutions. It should be noted that Moody' reviews many additional institutional characteristics such as management performance, market factors to determine their ratings. The CFI strength factors were applied to the Moody's median ratios to derive scores for the rating.

Moody's Ratios



Primary Reserve Ratio

The primary reserve ratio used to calculate the primary reserve score is determined by dividing expendable net assets into expenses and applying the appropriate strength factor. The results indicate that amounts held in reserve did not keep pace with increases in expenditures for most of the colleges. The increased OPEB liability was a major factor in the reduction of all of the schools' primary reserves except for Eastern West Virginia Community and Technical College and West Virginia Northern Community College. Excluding the OPEB liability, Blue Ridge Community and Technical College, Bridgemont Community and Technical College, Eastern West Virginia Community and Technical College, Southern West Virginia Community and Technical College and Northern West Virginia Community and Technical College experienced increases in reserves as a percentage of operating expenses. The primary reserve score for the majority of the institutions was below the scores calculated for the schools included in the Moody's report. The scores calculated for Bridgemont Community and Technical College, Kanawha Valley Community and Technical College, New River Community and Technical College and Southern West Virginia Community and Technical College are significantly less than the scores calculated from the Moody's data.



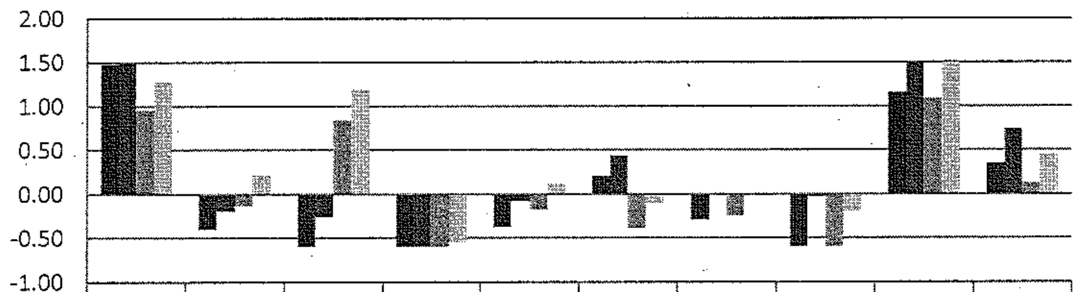
	BRCTC	BCTC	EWVCTC	KVCTC	MCTC	NRCTC	PCTC	SWVCTC	NWVCC	WVUP
FY 2010	2.76	0.09	0.73	0.19	1.07	0.43	0.42	0.19	1.81	0.50
FY 2010 Without OPEB	3.06	0.26	0.98	0.35	1.22	0.55	0.56	0.51	2.11	0.72
FY 2011	2.69	-0.01	0.78	-0.23	0.91	0.15	0.30	0.06	2.07	0.38
FY 2011 Without OPEB	3.07	0.27	1.11	0.06	1.16	0.35	0.51	0.58	2.56	0.69

Net Operating Revenue

The increase or decrease in net assets resulting from on-going operations is divided into the revenues from on-going operations to determine the net operating ratio. This ratio is used to determine the Primary Reserve Ratio Score.

The OPEB expense significantly reduced the net operating revenue for all institutions. Excluding this expense, Blue Ridge Community and Technical College, New River Community and Technical College, Southern West Virginia Community and Technical College, and West Virginia University at Parkersburg experienced decreases in net operating revenues over FY 2010.The low operating results scores indicate that most of the institutions are not living within available resources.

Net Operating Revenue

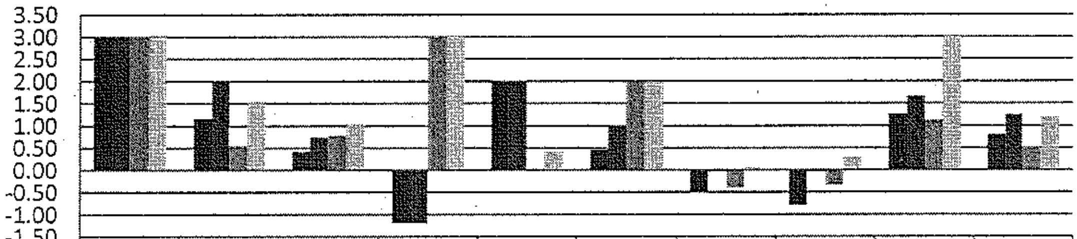


	BRCTC	BCTC	EWVCTC	KVCTC	MCTC	NRCTC	PCTC	SWVCTC	NWVCC	WVUP
FY 2010	1.48	-0.40	-0.60	-0.60	-0.37	0.20	-0.29	-0.60	1.16	0.35
FY 2010 Without OPEB	1.50	-0.19	-0.25	-0.60	-0.08	0.44	0.00	-0.03	1.50	0.74
FY 2011	0.96	-0.13	0.84	-0.60	-0.18	-0.39	-0.24	-0.60	1.10	0.13
FY 2011 Without OPEB	1.28	0.21	1.18	-0.54	0.12	-0.11	0.02	-0.20	1.50	0.45

Return on Net Assets

The return on net assets ratio is calculated by dividing the change in net assets by the beginning net assets. The resulting ratio is used to determine the return on net assets score. This score is influenced by institutional income, capital grants and gifts, and capital bond proceeds. Most of the institutions received capital funds during FY 2011. The significant OPEB expense increase limited the schools' scores. Most of the institutions' scores are well above the Moody's scores. The scores for Pierpont Community and Technical College and Southern West Virginia Community and Technical College were well below the Moody's averages. For the majority of institutions across the system, the performance of financial assets provides a sufficient level of support for their respective core missions.

Return on Net Assets

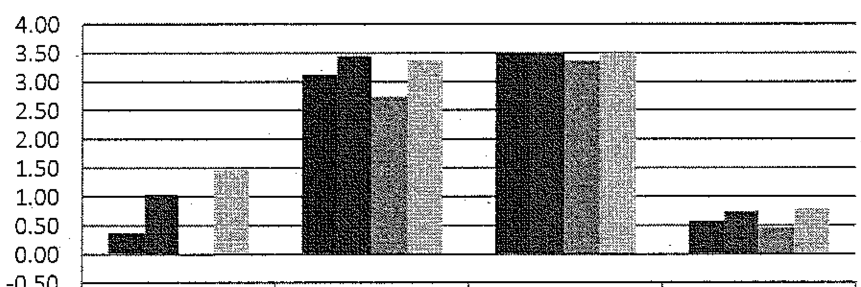


	BRCTC	BCTC	EWVCTC	KVCTC	MCTC	NRCTC	PCTC	SWVCTC	NWVCC	WVUP
FY 2010	3.00	1.17	0.42	-1.20	2.00	0.47	-0.48	-0.78	1.27	0.81
FY 2010 Without OPEB	3.00	2.00	0.74	-1.20	2.00	0.99	-0.03	-0.03	1.68	1.25
FY 2011	3.00	0.56	0.78	3.00	-0.02	2.00	-0.39	-0.34	1.12	0.51
FY 2011 Without OPEB	3.00	1.53	1.03	3.00	0.42	2.00	0.06	0.29	3.00	1.18

Viability

To determine the viability ratio of this calculation, expendable net assets are divided into capital project-related debt. This ratio was calculated for Bridgemont Community and Technical College, Mountwest Community and Technical College, New River Community and Technical College and Pierpont Community and Technical College because they had significant debt levels. The result of this calculation is used to determine the viability score for each institution. An institution's market position and capacity to raise fees to support debt service will influence its level of debt. Tuition and fee rates for resident students are limited; consequently, some institutions are not in a position to incur additional debt. Without the ability to incur debt, aging facilities are not renewed or replaced unless capital resources are provided from other sources.

Viability



	BCTC	MCTC	NRCTC	PCTC
FY 2010	0.38	3.12	3.50	0.58
FY 2010 Without OPEB	1.04	3.45	3.50	0.75
FY 2011	-0.03	2.75	3.36	0.46
FY 2011 Without OPEB	1.49	3.36	3.50	0.78

Composite Financial Index

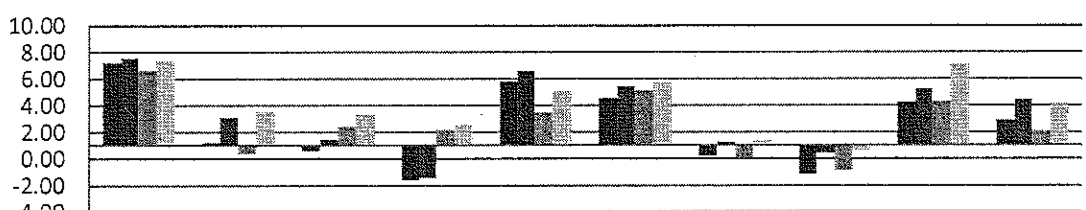
The four ratio scores were combined to determine the CFI. Because the impact of the OPEB expense and liability was substantial, the CFI was calculated with and without the OPEB information. [3]A composite value of 1.0 is equivalent to weak financial health. A value of 3.0 signifies relatively strong financial health and scores above 3.0 indicate increasingly stronger financial health

The CFI must be assessed in light of the strategic direction for each institution. Strong financial results are not beneficial unless resources are deployed effectively to advance mission specific goals and objectives. These indices are best used to track institutional performance, both historically and as a planning tool, over a long time horizon, rather than compare to other institutions as each institution is unique in terms of specific goals, objectives and funding composition.

For most of the institutions, the OPEB liability increase did not result in a lower CFI score. Bridgemont Community and Technical College, Eastern West Virginia Community and Technical College, Kanawha Valley Community and Technical College, New River Community and Technical College, Pierpont Community and Technical College, Southern West Virginia Community and Technical College, and West Virginia Northern Community College experienced an increase in the CFI calculated without the OPEB expense and liability. Southern West Virginia Community and Technical College has poor financial health.

The Composite Financial Indices for the institutions demonstrate that reserves are not sufficient and flexible enough to support the schools' missions. Operating results do not support the accumulation of adequate financial resources. The State support for capital projects and a low level of capital debt are reflected positively in the scores.

Composite Financial Index



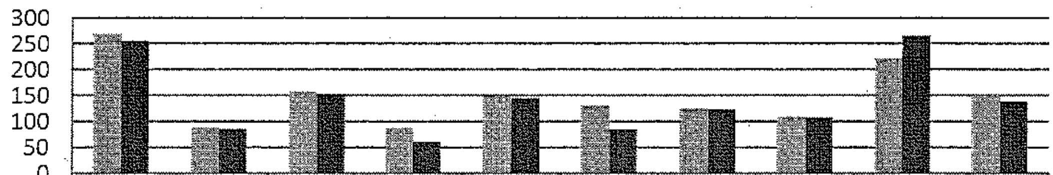
	BRCTC	BCTC	EWVCTC	KVCTC	MCTC	NRCTC	PCTC	SWVCTC	NWVCC	WVUP
FY 2010	7.23	1.24	0.56	-1.61	5.82	4.60	0.22	-1.18	4.25	2.94
FY 2010 Without OPEB	7.56	3.11	1.46	-1.45	6.59	5.48	1.28	0.44	5.29	4.44
FY 2011	6.65	0.39	2.40	2.17	3.46	5.12	0.13	-0.87	4.29	2.05
FY 2011 Without OPEB	7.35	3.51	3.32	2.51	5.06	5.74	1.37	0.67	7.06	4.09

[3] The OPEB liability and expenses related to the OPEB liability were eliminated from the data to calculate the CFI without OPEB amounts.

Number of Days Cash

The number of days cash ratio was calculated to provide additional liquidity analysis. This ratio is calculated by multiplying the institutions' June 30 cash balances by 365 and dividing the result into total expenses less deprecation and the OPEB expense. Data for discrete component units was not included in this calculation. The ratios for Blue Ridge Community and Technical College and the West Virginia Northern Community College are well above the ratios of other institutions. The Moody's median number of days cash ratios for institutions with A3 ratings is 60.

Number of Days Cash



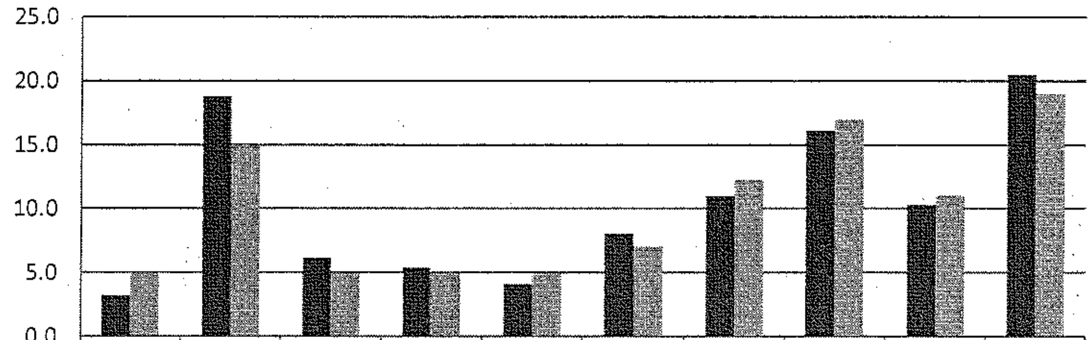
	BRCTC	BCTC	EWVCTC	KVCTC	MCTC	NRCTC	PCTC	SWVCTC	WVNCC	WVUP
FY 2010 Days Cash	269	89	158	88	148	131	125	110	222	152
FY 2011 Days Cash	256	86	154	62	145	85	124	109	266	139

Physical Plant Age

The physical plant age was calculated to estimate the adequacy of institutions' physical resources. This ratio is computed by dividing the annual depreciation expense by the accumulated depreciation. Generally, institutions that have received capital appropriations, borrowed funds or used institutional resources for capital projects reflect a lower physical plant age. The Moody's ratio for the A3 rating is 13.2. As mentioned above, institutional borrowing capacity is related to market position and the ability to increase fee revenues to pay debt service.

The ratios for new institutions are low because they do not own buildings or their facilities are relatively new. The physical plant age for Bridgemont Community and Technical College and West Virginia University at Parkersburg are aged.

Physical Plant Age



	BRCTC	BCTC	EWVCTC	KVCTC	MCTC	NRCTC	PCTC	SWVCTC	WVNCC	WVUP
■ FY 2010 Plant Age	3.2	18.8	6.1	5.4	4.1	8.1	11.0	16.1	10.3	20.5
▩ FY 2011 Plant Age	5.0	15.0	5.0	5.0	5.0	7.0	12.3	17.0	11.0	19.0

Conclusion

The continued expansion of the OPEB liability is a significant threat to the System's financial status. Although the colleges and universities under the System exhibit relatively strong financial health, the adequacy of financial resources at several institutions is a significant concern. Most of the schools do not demonstrate the ability to operate within the resources available to them. Because the facilities at a majority of the institutions are relatively new, their physical plant age is comparatively low.