*The Understandability of Financial Statements*
*Presented by Emil Haeflinger*
*at the Illinois Community College Trustees Association's*
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Community college financial statements *are* different to understand, but to be an effective board member you need to understand what they mean, how they are put together and what they can do for you. This is not to say that you, as a board member, need to understand every number and nuance behind them, but they should be your guide to assure financial stability for your particular institution.

The comments which follow are an attempt to provide the basics of what you need to know about your institution's "numbers". Keep in mind to form the basis of these comments, eight one liners are offered which tie the remaining comments together -- these are common and important in any business!

1. What are the *financial drivers?*
2. What are the *controllable numbers?*
3. What are the *time frames* to work within?
4. What are the *lag times* that have to be worked within?
5. What are the *policies* that guide the direction of the institution?
6. What are the *links* between decisions that are made?
7. What are the *accountability standards* and reports that can guide decisions?
8. What are the *predictors* of problems or variances (i.e. benchmarks)?

Let's now look at each of these *examples*:

1. What are the *financial drivers*?
    a. Financial drivers are both revenue and expenses -- i.e. taxes, tuition, apportionment are the biggest revenue drivers; salaries, benefits and capital are the largest expenditure drivers.
    b. Trends locally, statewide and nationally influence all of these.

2. What are the *controllable numbers*?
    a. Of the items listed above, tuition and salaries are the most controllable.
    b. Interestingly, though, tuition rates can influence enrollment, and enrollments influence apportionment. Salaries and benefits are some to extent controllable but also influence morale/staffing/recruitment/quality/ enrollments.
    c. Know how each relate to each other and keep in mind there is a balancing act between all of these.

3. What are the *time frames* to work within?
   a. Enrollments today influence apportionment two years hence.
   b. Salary increases today may influence hiring progress in the future.
   c. Changes in benefit plans cannot be too frequent / if they are, the rates will rise even higher than your experience rating.

4. What are the *lag times* that have to be worked within?
   a. Enrollments today influence apportionment two years hence.
   b. Energy usage spikes influence rates for the next 11 months.
   c. Benefits costs in one year influence rates and run off reserves for several years to come.
   d. Tax levies made in one year don't result in cash until the next unless borrowing is involved, and then interest expenses are realized for years into the future.

5. What are the *policies* that guide the direction of the institution?
   a. Tax levies can be accrued and recognized in the year made *or* received.
   b. Deferred expenses can be recognized or accrued as to when due.
   c. Contracts made need to be factored into cash flow projections to recognize consequences.

6. What are the *links* between decisions that are made?
   a. Tuition increases can influence enrollments.
   b. Marketing can sometimes have only a temporary impact.
   c. Cutting maintenance costs can have long-term effects.
   d. Expansion of facilities will not only have staffing effects but other operational demands (i.e., bricks and motor costs money, long term).

7. What are the *accountability standards* and reports that can guide decisions?
   a. Recognition of tax revenues, future contracts and liabilities are dictated by the AICPA (i.e. your external auditors). Make sure you agree with them.
   b. The ICCB rules require compliance of recognition could be at stake.
   c. Construction records need to be monitored and projects closed out adequately.

8. What are the *predictors* of problems or variances (i.e. the benchmarks)?
    a. Define major problems that need corrected - make them into goals and factor them into the previous seven key "one-liners".
    b. Define predictors of future problems and factor these the same way. (Monitor these throughout the year and include them in each major decision).

These sound tough and may be confusing, but that is what the administration is for!

Remember:

The Board's responsibility is -- to make sure the right things are done!

The Administration's responsibility is -- to make sure things are done right!

To insure your responsibility has been fulfilled depend on:

1. Your external auditors -- not only their fiscal report but the report on internal controls.
2. The development and dependence on a finance committee to monitor and understand the above. Not everyone on the Board is financially savvy -- don't get caught in the trap that everyone can and should be.
3. Challenge your administration to answer the above questions and report on them at least quarterly.
4. Lastly, make sure your fiduciary bond is up to date and adequate.

Understandability of financial statements is, as illustrated above, dependent on a lot of work, and trust in your fellow board members, your auditors and your administrators. Also, remember that each institution has different answers to the points above. (A personal comment from years of experience with great boards -- if *you* do your homework and plan ahead you won't embarrass anyone publicly, including yourselves.) Ask the "big" questions!