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FINANCIAL ANALYSIS AND AN UPDATE FOR PRIVATE HIGHER EDUCATION AND OTHER NOT-FOR-PROFIT ORGANIZATIONS

JUNE 30, 2014

BROWNEDWARDS
certified public accountants

TRINITY COLLEGE

FINANCIAL ANALYSIS AND AN UPDATE FOR PRIVATE HIGHER EDUCATION AND OTHER NOT-FOR-PROFIT ORGANIZATIONS

June 30, 2014

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BROWNEDWARDS
certified public accountants

REPORT ON HIGHLIGHTS OF THE JUNE 30, 2014
FINANCIAL REPORT

To the Board of Trustees and Management of
Trinity College
Washington, D.C.

We have audited the financial statements of Trinity College as of and for the year ended June 30, 2014 and have issued our report thereon dated October 10, 2014. Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying supplemental information, Highlights of the June 30, 2014 Financial Report, is presented for purposes of additional analysis and is not a required part of the financial statements of Trinity College. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Brown, Edwards & Company, L.L.P.
CERTIFIED PUBLIC ACCOUNTANTS

Roanoke, Virginia
October 10, 2014

Your Success is Our Focus
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HIGHLIGHTS OF THE JUNE 30, 2014 FINANCIAL REPORT

Independent Auditor's Report

Our independent auditor's report is an unmodified opinion, also referred to as a "clean" opinion. This is the highest level of assurance that we can offer as certified public accountants on your financial statements. Our audit considers internal controls as a basis for designing appropriate audit procedures. However, we do not express an opinion on the effectiveness of internal controls.

Summary of Financial Highlights

For the year ended June 30, 2014, buoyed by significant and increasing non-operating contributions and very good investment returns, the College had an excellent overall **increase in total net assets of $14.8 million, or a 21.1% return on average net assets**. Operationally, while still strong and positive, the College experienced a reduction in the unrestricted operating surplus. Student-driven revenues decreased significantly, while operating expenses increased by only 1.9%. *Overall, another very good year and a tribute to management's fiscal stewardship given the many downward pressures on operating revenue, and the upward pressures on operating costs.* Key highlights include the following (additional detail is included on the following pages):

- **Total assets** *increased* by $15.3 million; there were fairly large increases in most asset categories offset by a small decrease in receivables.
- **Total liabilities** *increased* by $460,000, primarily related to increases in accounts payable and debt, offset by a large decrease in the interest rate swap liability.
- **Operating revenues** *decreased* by $2.3 million; primarily related to a decrease in net tuition and fees and a small decrease in gifts.
- **Operating expenses** *increased* by only $597,000, or 1.9%, with only modest changes in functional categories.
- The largest changes in **non-operating** activities were significant *increases* in gifts and private grants, investment return, and the change in the value of the interest rate swap.

Cash and cash equivalents at June 30, 2014 increased from the prior year by $7.2 million, as reflected in the statements of cash flows on page 8 of the financial report. Net cash provided by operating activities totaled $5.7 million. Net cash used in investing activities, which includes student loans activity, purchases of land, building, and equipment, and investment activity, totaled $5.0 million. Net cash provided by financing activities, which includes contributions restricted for long-term investment, proceeds from new debt, and debt principal payments, totaled $6.6 million.

Receivables and other assets, net of allowance for doubtful accounts, decreased from the prior year by $249,000 primarily related to the timing of requests for federal grant funds. Note 2 of the financial report provides some detail of the assets included in this line item on the financial statements.

Contributions receivable increased over the prior year by $1.1 million. The increase is primarily attributable to pledges received as part of the Second Century Campaign.

Summary of Financial Highlights (Continued)

Investments increased from the prior year by $5.4 million. The increase is partly attributable to investing $1 million of surplus cash. Note 4 of the financial report summarizes investment activity. Overall, College's **endowment investments** had an approximate total return of 16.1% as compared to 9.00% in the prior year, as reported by Wells Fargo. **Total investments**, which in addition to endowment investments also include operational funds substantially invested in fixed income vehicles, had an approximate total return of 5.9% based on average investments as compared to 3.0% in the prior year. Comparable indexes at the target asset allocations for the endowment for the fiscal year are as follows:

	Endowment Target Asset Allocation	**2014**	**2013**
Equities:			
Russell 1000 Growth	20.0%	26.9%	17.1%
Russell 1000 Value	20.0	23.8	25.3
Russell Midcap	15.0	26.9	25.4
MSCI EAFE	10.0	23.6	18.6
	65.0		
Fixed income:			
Barclays U.S. Aggregate	35.0	4.4	(0.7)
	100.0%		
Estimated total return using the above asset allocation for the entire year		18.1%	13.9%

	Approximate Total Asset Allocation	**2014**	**2013**
Equities:			
Russell 1000 Growth	4.8%	26.9%	17.1%
Russell 1000 Value	3.4	23.8	25.3
Russell Midcap	2.2	26.9	25.4
Russell 2000	1.3	23.6	24.2
Russell 2000	4.7	25.2	21.5
MSCI EAFE	4.4	23.6	18.6
	20.8		
Fixed income:			
Barclays U.S. Aggregate	79.2	4.4	(0.7)
	100.0%		
Estimated total return using the asset allocation for the entire year		8.7%	2.5%

Land, buildings, and equipment increased during the year by $1.0. This results from additions of $2.1 million, net of depreciation and disposals for the current year of $1.1 million. Note 5 of the financial report summarizes land, buildings, and equipment.

Summary of Financial Highlights (Continued)

Funds held in trust by others increased by $803,000. This increase is largely attributable to a good year in the financial markets this year versus the prior year. Note 6 of the financial report summarizes funds held in trust by others.

Accounts payable and accrued expenses increased by $150,000 primarily due to the timing of processing invoice payments.

Interest rate swap decreased by $1.1 million due to the refinancing of debt at the end of the fiscal year, which involved the retirement of the previously held interest rate swap agreement and the addition of two new interest rate swap agreements. The valuation of interest rate swap agreements is based on the expected future interest rates as compared to current interest rates.

Debt increased by $1.3 million, which is the result of net addition to debt outstanding as a result of the refinancing of existing debt and the addition of new debt for the construction of the new academic center, net of scheduled principal payments (including capital leases) in the current year of $671,000. Note 7 of the financial report summarizes debt.

Net assets, which are summarized in Note 8, changed during the year ended June 30, 2014 as follows:

	In Millions
Unrestricted	$ 3.8
Temporarily restricted	10.1
Permanently restricted	0.9
	$ 14.8

This represents a 21.1% return on average net assets versus a 25.7% return in the prior year.

Gross tuition and fees decreased during the year by $1.4. This was primarily attributable to a decrease in the number of full time equivalent students netted with a 2.0% Board-approved undergraduate tuition and fees increase from the prior year. **Net tuition and fees from graduate programs decreased by $750,000. Net tuition and fees** decreased during the year ended June 30, 2014 by $2.2 million. This was the net result of the gross tuition and fee decrease and a $741,000 increase in financial aid. The College's tuition discounts can be summarized and compared to Moody's Investors Service and Standard & Poor's (fiscal 2013 median for small private institutions) and Brown Edwards' client median as follows:

	Rating Agencies		Brown Edwards' Client Median	Trinity College	
	S & P "BBB")	Moody's "Baa")	2014	2014	2013
Non-funded			43.3%	29.6%	27.4%
Funded			7.1	1.5	1.3
Total tuition discount	34.2%	39.7%	50.4%	31.1%	28.7%

Most institutions in all the benchmarks must discount much more significantly to attract student than the College. The College's discount rates are more in line with similar urban institutions.

Summary of Financial Highlights (Continued)

Operating expenses increased by only $597,000. (The consumer price index for the year ended June 30, 2014 was 2.1%; and the Higher Education Price Index was 3.0%.) Salaries, wages, and benefits totaled 64.6% and 63.1% of operating expenses for the years ended June 30, 2014 and 2013, respectively.

Change in net assets from unrestricted operating activities represents the College's unrestricted operating surplus (deficit) during the year. For the years ending June 30, 2014 and 2013, the change was $2.9 million and $5.3 million, respectively. The drop from the prior year was the result of a decrease in unrestricted operating revenues and slightly higher operating expenses.

The **temporarily restricted change in net assets from operating activities** was $(270,000) and $238,000 for the years ended June 30, 2014 and 2013, respectively.

The **non-operating income** section of the statement of activities represents contributions of a capital nature and other restricted contributions, including promises to give, investment income, investment return, net of amount available to support current operations, and the change in value of split-interest agreements.

Below is a summary of some of the College's financial strengths and challenges:

Financial strengths:

- A seasoned management team and Board focused on achieving ***financial equilibrium***
  (Financial equilibrium is defined as simultaneously maintaining balanced financial operations that include funding for capital additions, depreciation expense and deferred maintenance, preserving physical assets, maintaining the purchasing power and continuing to grow the endowment, and nourishing the human resources of the College.)
- An ideal urban location and a strong reputation that translate into marketability and the ability to attract students.
- Generating a strong positive change from operations and total activities, good cash reserves, and excellent cash flow generated from operating activities.
- A financial transformation has taken place at the College over the past five plus years, which has positioned the College well with the necessary financial wherewithal to move institutional initiatives forward within reason.

Financial challenges:

- Utilizing the College's financial strength to carrying out key strategic initiatives to 1) protect what has built over the past several years and 2) continue to position the College for long-term sustainability.
- Continuing to grow expendable (unrestricted and temporarily restricted net assets, less plant assets net of related long-term debt) financial reserves for key institutional needs, e.g. mission-driven strategic initiatives, technological improvements, deferred maintenance, campus improvements, etc.
- Continuing to grow the endowment and increasing the amount per FTE student.
- Continuing to strategically manage debt while funding important institutional initiatives.

BROWNEDWARDS
certified public accountants

REPORT ON FINANCIAL ANALYSIS

To the Board of Trustees and Management of
Trinity College
Washington, D.C.

We have prepared, from information derived from the financial statements of Trinity College (the "College") for the years ended June 30, 2010 through 2014 the ratio and trend analysis. The analysis uses selected financial position and operating ratios developed by leading consultants to the higher education industry, a major credit rating agency, and the U.S. Department of Education. We have selected these ratios as a concise group of important indicators and trends that can be used, through analysis and informed decision making, to help facilitate the sustainability of small liberal arts colleges and universities.

The information provided herein is not audited and no assurance is provided for its accuracy as an indicator of financial strength or weakness. These financial ratios and analysis are not intended to be all inclusive. Consequently, this report should be read in conjunction with the financial statements of the College and other analysis. This analysis is intended solely for the use of Management and governing body of Trinity College and is not intended to be, and should not be, used by anyone other than the specified parties. We encourage Management and the Trustees to consider the information and trends in conjunction with the College's strategic plan. All strategic plans are different as the missions and goals of each college or university are different.

We would be pleased to meet with you and discuss how these indicators relate to specific events of the past few years and how planned events are likely to affect the indicators going forward. Using this information in this manner is considered by many to be an excellent tool for weaving desired financial goals into the non-financial goals of a college or university.

Brown, Edwards & Company, L.L.P.
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Roanoke, Virginia
October 10, 2014

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TRINITY COLLEGE
TREND ANALYSIS

INTRODUCTION TO THE TREND ANALYSIS

Trinity College is very similar in financial size to many other colleges in the Southeast The College's operations, like most of its peers, is tuition dependent (net tuition and fees and auxiliary revenue) with student-driven revenue making up a large percent of total operating revenue. Income derived from the endowment for the purpose of supporting annual operations is an important but not a large portion of the operating revenue budget on a continuous basis. However, a significant portion of the expendable net assets, a major factor in assessing financial strength and liquidity in higher education, consists of accumulated net appreciation on endowment investments. Of course, while the investment markets have been bullish in recent years, they can turn unstable which can impact the trend analysis significantly.

Enrollment has increased dramatically during this trend period, although down in 2014. Accordingly, net tuition and fees have also increased even with higher tuition discounting. There have been increases in all operating expense categories over the past five years. Many of these issues can be seen in most colleges of similar size, financial strength, and mission. Most other institutions of similar size are struggling mightily to maintain and increase enrollment, and are paying much more in financial aid to accomplish this.

The major factors facing higher education over the recent and next few years have been and will continue to be pressure on tuition and other revenue (demographic shifts, competition, less government funding), uncertainty in investment markets, and rising costs (for ever-changing technologies, managing increased regulations, etc). These factors make it even more important to fairly assess financial strength and growth potential in developing strategic plans.

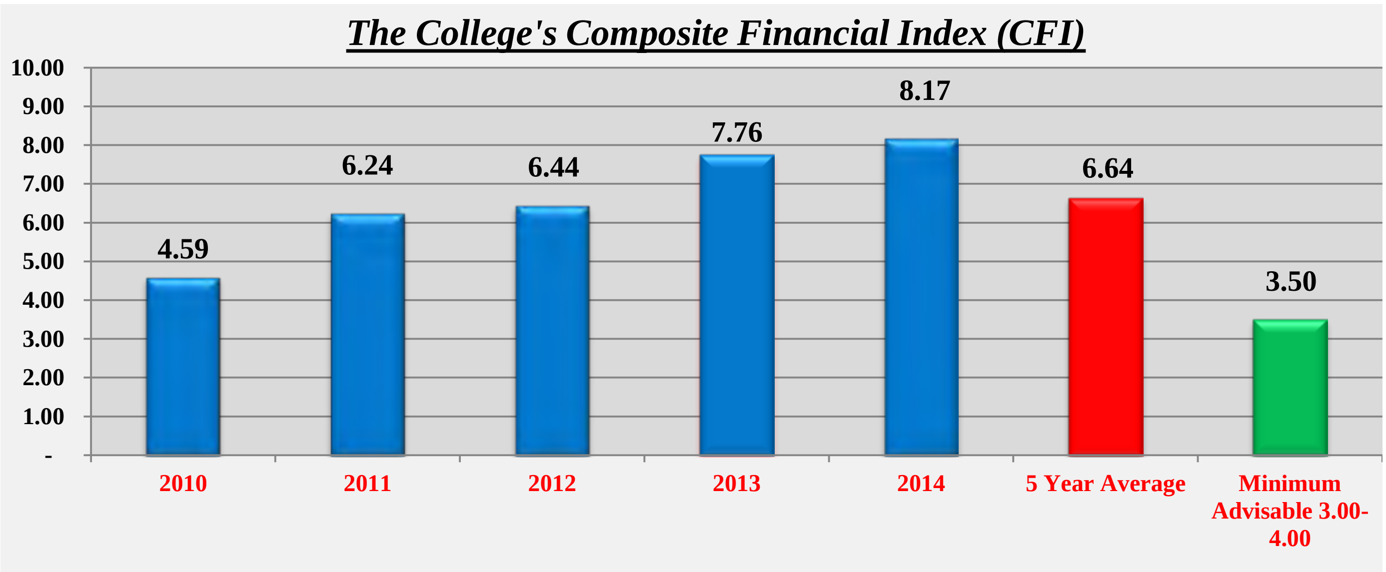
The following trends give further insight into factors that affect the financial strength of the College. (*The Moody's and S&P median ratios throughout this analysis are for fiscal year 2013 as they are the most recent available which is inherent with most benchmarking data.*) ***None of the ratios consider additional debt incurred after year end.***

Composite Financial Index

Brown Edwards provides the College with many ratios as a value-added part of the audit process, but we place a greater focus on the Composite Financial Index (CFI). CFI is a combination of four financial metrics that **measures the overall financial health of the Institution**. To fully understand CFI, it is important to understand its components which are indicators of specific areas of financial strengths and weaknesses and can provide you with important insights as to where to focus your efforts for improvement and transformation. A more detailed discussion of the CFI can be found at the end of this trend analysis.

<u>Composite Financial Index</u> (Continued)

The College's CFI trend is as follows:



The Brown Edwards' CFI group median, institutions all very similar in size and within reasonable geographic proximity to the College, was 5.59 in 2014 and 5.13 in 2013; the CFI median for the top 10 was 7.00 in 2014. The College was in the Brown Edwards top 10.

Our Analysis & Comments on Your CFI

The trend of the College's CFI is remarkable and very strong, averaging over 6.00 and peaking in 2014. It follows the College's strong performance from operations with a slight pause in 2012 related to the financial markets dip. After a difficult financial period dating up through fiscal 2009, the College has consistently been well above the minimum advisable range and has moved to a very healthy position of financial strength.

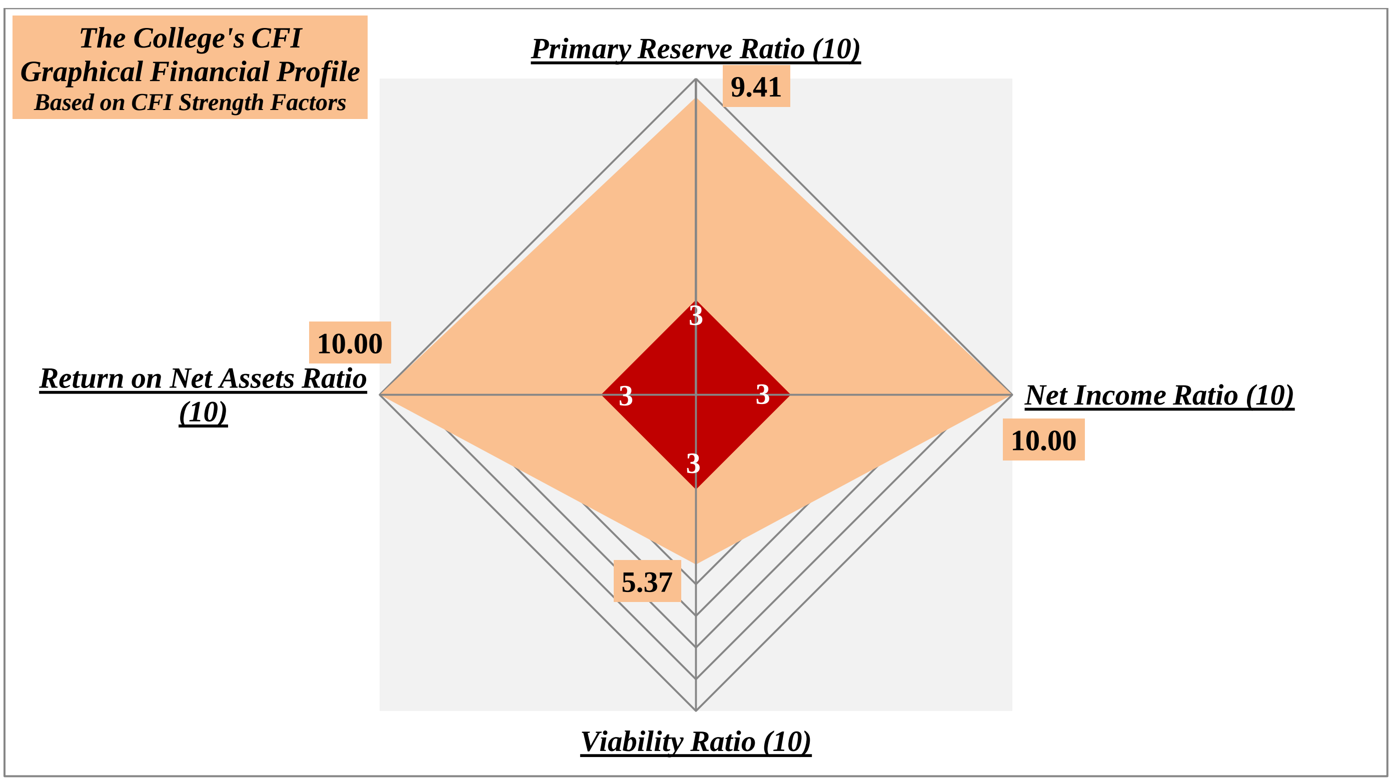
Although the College's strength is operational, be mindful that seventy percent of the input into the CFI calculation is based on accumulated financial wealth on the balance sheet, or expendable net assets. A large portion of expendable net assets is the accumulated net appreciation on endowment investments. Net appreciation rises and falls with the financial markets. The volatility in the financial markets suggests that management and the Board look at the CFI over more than one year. In addition, the operating size of the College, measured in terms of total operating expenses, has increased over the past five years. This increase demands higher expendable net asset levels to maintain the strength of financial position. Even considering this, the College's expendable net assets relative to operating expenses are currently very good.

<u>Composite Financial Index</u> (Continued)

Our Analysis & Comments on Your CFI (Continued)

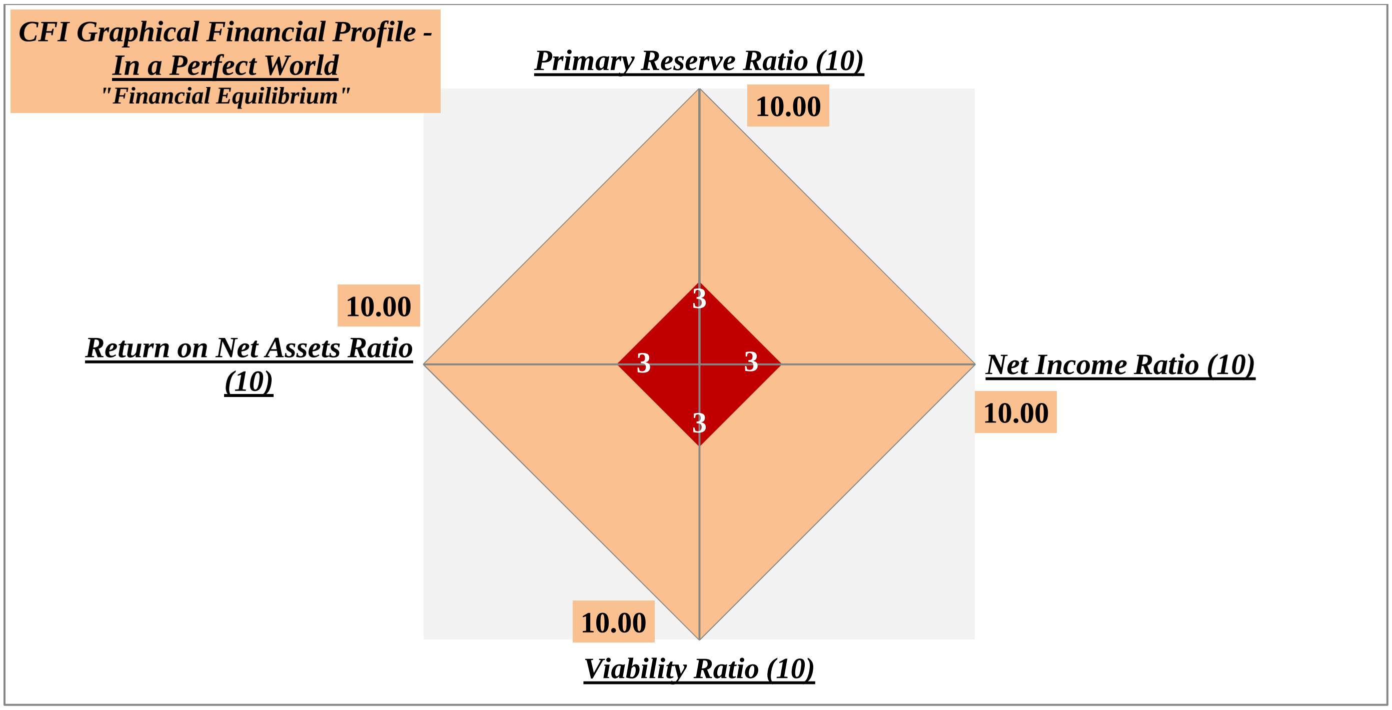
Overall, the College's CFI indicates a very financially healthy institution that is well capitalized and that has produced substantial returns on current activities as well as on total net assets. To analyze underlying strengths and areas to work on, **view the CFI Graphical Financial Profile diamond below** (which is *based on input ratio strength factors*). (The dark red inner diamond represents the desired minimum strength of three. The light outer diamond represents the maximum scale score of ten. Ideally, a goal is to have all College points outside the inner diamond and pushing toward the maximum outer diamond, which all the College's values are. Two of the College points are at maximum ten positions.) A summary of the College's scoring: **a) Primary reserve ratio** – Financial reserves relative to operating size (operating expenses) are excellent and very close to the top of the scale with a ratio of 1.25, or a 15-month reserve; **b) Net income ratio** – Operating returns continue to be very strong in 2014 at 8.45% (the minimum advisable range is 2% - 4% of unrestricted operating revenues); **c) Viability ratio** – Debt levels are presently reasonable given the current level of expendable net assets; and) **d) Return on net assets ratio** – The College has generated an outstanding overall return on net assets during the trend period, averaging an incredible 19.01%.

The College's current CFI and trend indicates that it has the financial resources to move robust strategic initiatives forward that will preserve the College's financial strength and continue to position it for long-term sustainability.



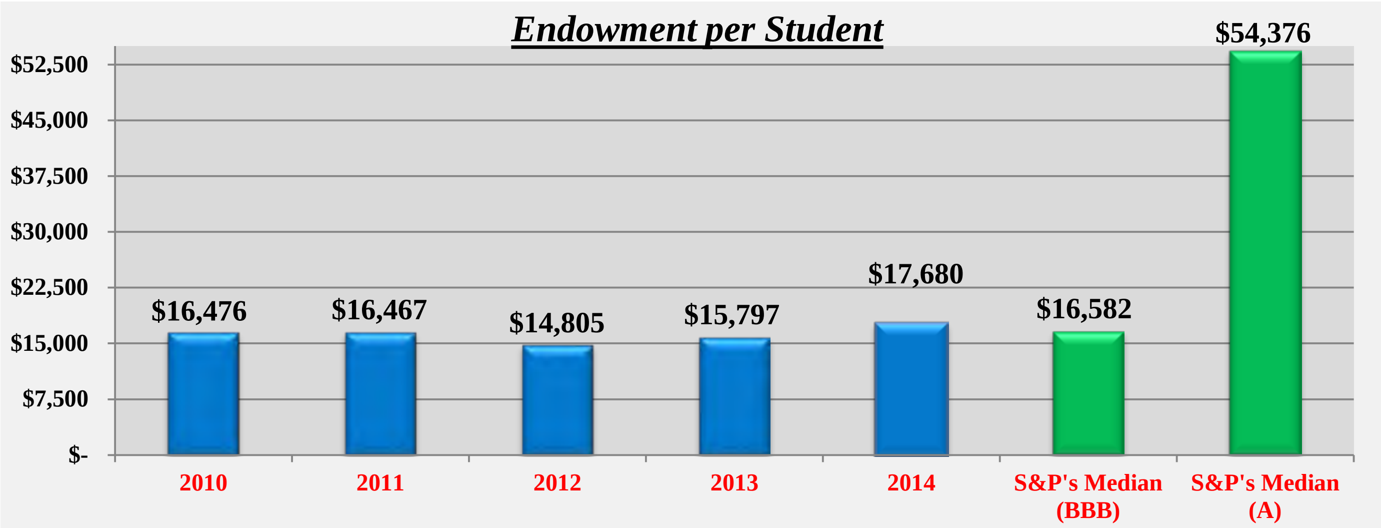
Composite Financial Index (Continued)

Our Analysis & Comments of Your CFI (Continued)



Endowment per Student

The **Endowment per Student Ratio** compares the market value of the endowment funds to the student enrollment (FTEs). **(Note that all references in this document to students and FTEs refers to undergraduate students only unless otherwise indicated.)** This ratio is an indicator of the institution's overall accumulated financial wealth.



The Brown Edwards' endowment per student group median was approximately $45,500 in 2014 and $39,000 in 2013; the endowment per student median for the top 10 was $58,500 in 2014.

Endowment per Student (Continued)

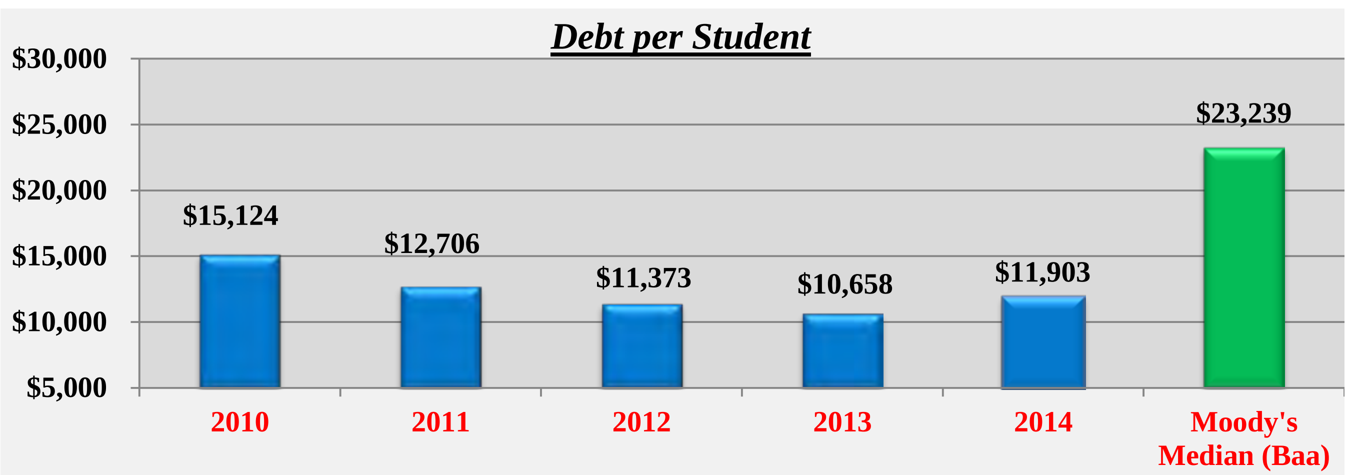
Our Analysis & Comment on Your Endowment per Student

The value of the College's endowment has grown over the trend period with a slight decrease in 2012 which was attributable to a drop in the financial markets. The College's total endowment has also increased over the trend period, however, undergraduate student enrollment has grown dramatically requiring a larger endowment to keep step with the per student amount. The College's endowment per student is now above the S&P median for institutions rated BBB.

Financial markets are currently higher, but no more certain as the overall economy continues to grow modestly and is susceptible to any of a number of potential disruptions. Endowment spending only makes up a small portion of total operating revenue, so one year changes are not as critical as long-term performance. The Brown Edwards group consists of more rural institutions that tend to have much larger endowments, which in turn must be utilized to subsidize tuition to maintain enrollment.

Strategically Managing Debt

Debt is a critical component of the resources available to an institution to fund capital projects. If used strategically and under a program designed to maximize the use of debt to achieve institutional goals, taking on additional debt increases the likelihood of an institution meeting its mission. Below is the College's **debt per student** trend. The trend is dramatically impacted by the substantial increase in enrollment during this period. Accordingly, even with relatively level amounts of debt, the per student amount has dropped significantly.



The Brown Edwards' debt per student group median was approximately $20,300 in 2014 and $19,100 in 2013; the debt per student median for the top 10 was $20,300 in 2014.

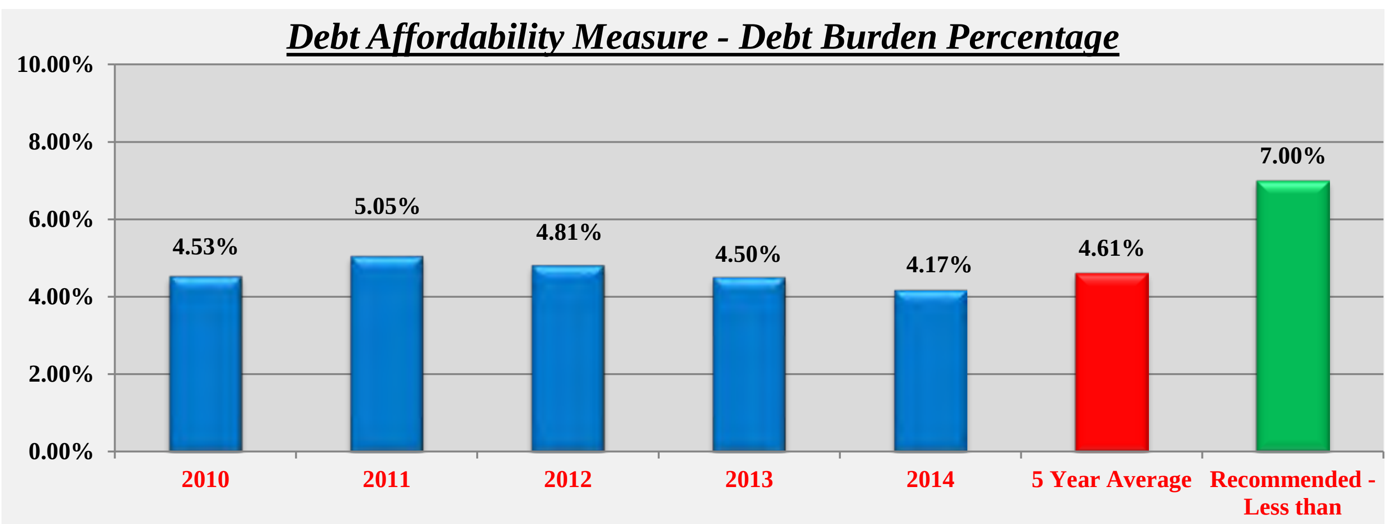
Strategically Managing Debt (Continued)

Critical to strategically managing debt is monitoring key components of a sound debt policy such as debt affordability and capacity measures. All but the financially weakest institutions should focus primarily on debt affordability, rather than debt capacity. **Debt affordability** highlights the concept that the institution's operating budget usually is the constraint limiting the incurrence of additional debt. This is in contrast to **debt capacity** which focuses solely on the institution's balance sheet; debt funding as a percentage of total capital. Balance sheet leverage generally is a limiting factor only for the less wealthy institutions since a weak balance sheet limits access to the capital markets. For most institutions, debt capacity is of interest primarily from a credit rating and peer comparison perspective. An organization should consider many factors in assessing its debt affordability and debt capacity including its strategic plan, market position, and alternative sources of funding. Some key ratios to provide a quantitative assessment of debt affordability and debt capacity are as follows:

Debt Affordability Measures

Debt Burden Percentage

This ratio measures the College's **debt service burden** (principal and interest) as a percentage of total operating expenses (which typically is a relatively stable base). The target for this ratio is intended to maintain long-term operating flexibility to finance existing requirements and new initiatives.



The Brown Edwards' debt burden percentage group median was approximately 7.20% in 2014.

Debt Service Coverage Ratio

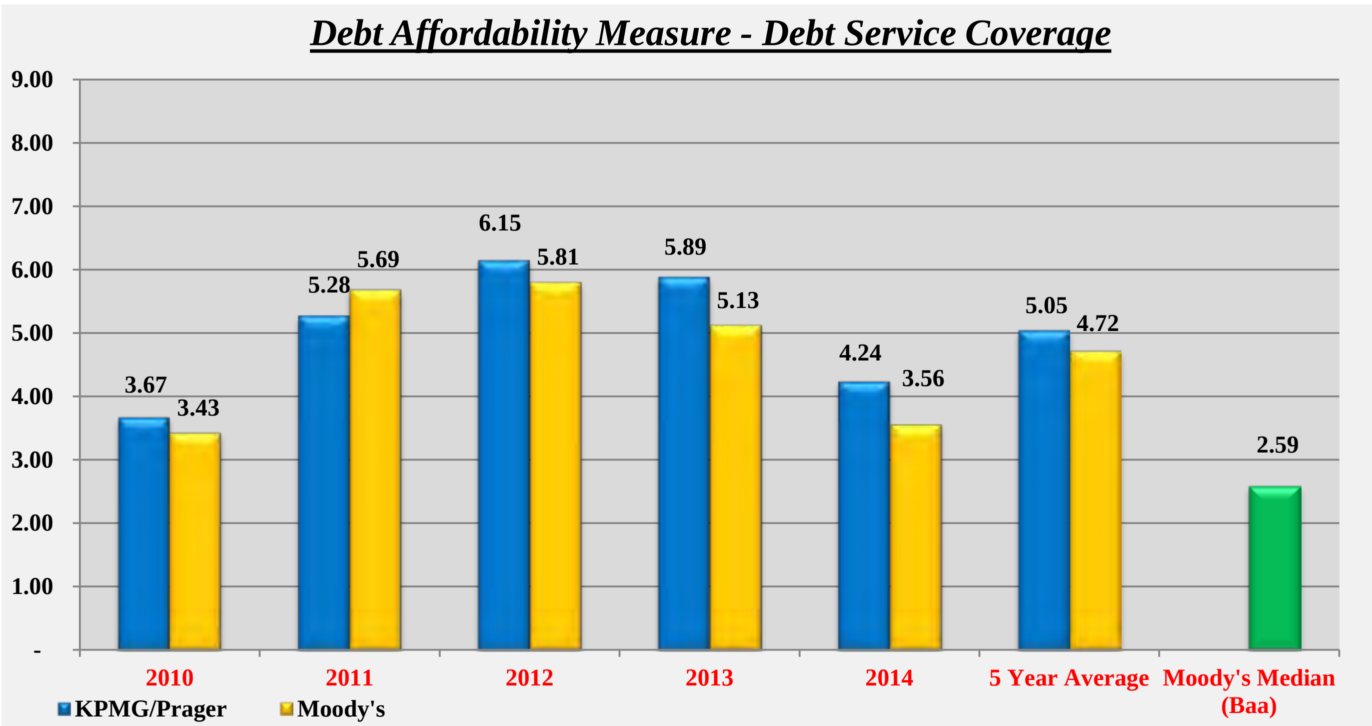
This ratio measures the College's ability to cover debt service requirements with revenues available for operations. The target established is intended to ensure that operating revenues are sufficient to meet debt service requirements and that debt service does not consume too large a portion of income. A high ratio is considered advantageous while a very low ratio or decreasing trend signifies financial difficulty.

There are several ways to calculate this ratio. The **KPMG/Prager debt service coverage ratio** is calculated by using the total change in unrestricted net assets (operating & non-operating) plus depreciation and interest divided by debt service (principal and interest). This ratio is significantly influenced by investment returns. The **Moody's ratio** is similar except that it uses the change in unrestricted operating net assets.

<u>Strategically Managing Debt</u> (Continued)

Debt Affordability Measures (Continued)

Debt Service Coverage Ratio



The Brown Edwards' debt service coverage group medians were approximately 2.78 for KPMG/Prager and 1.93 for Moody's in 2014.

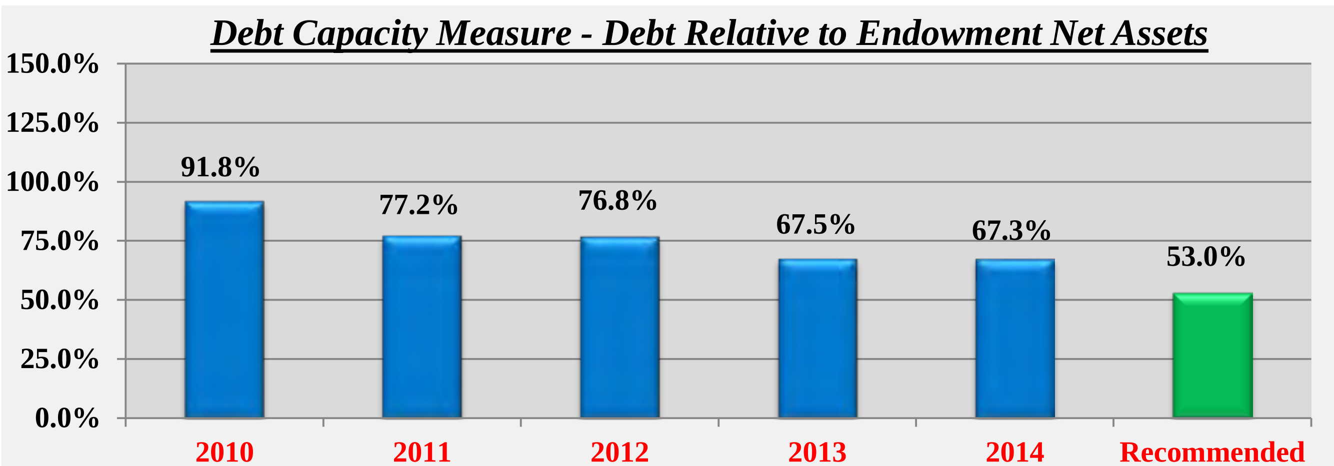
As one of its debt covenants, the College is required to meet a 1.10 cash flow to debt service ratio that is calculated more closely, but not exactly, to the KPMG's ratio. The College's cash flow to debt service ratio calculated in this fashion was 5.89.

Strategically Managing Debt (Continued)

Debt Capacity Measures

Debt Relative to Endowment Net Assets

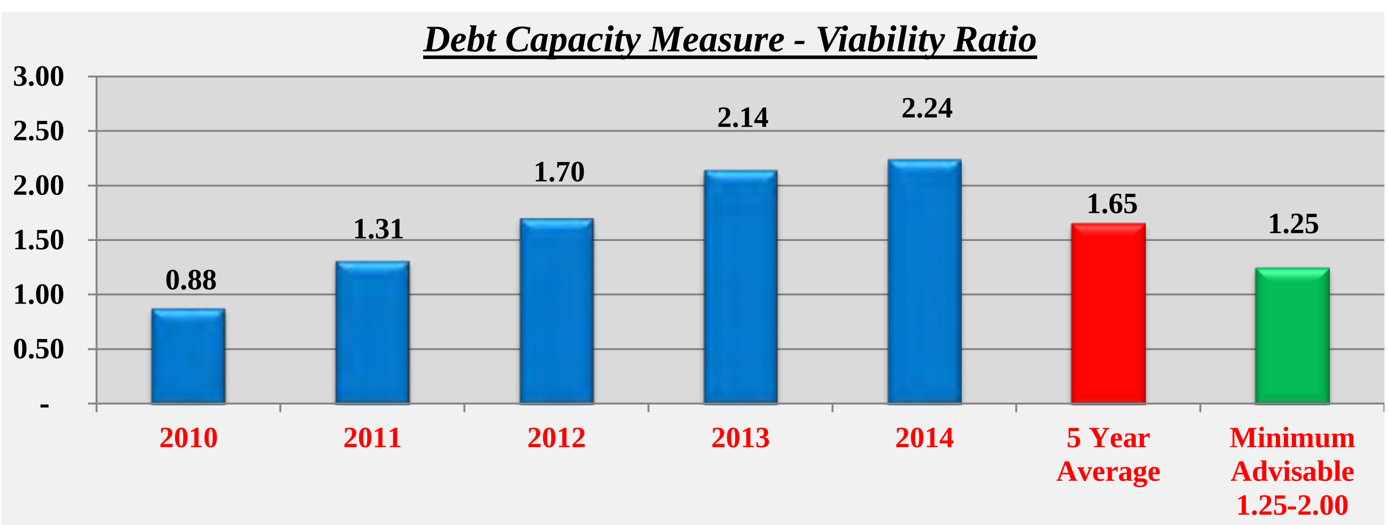
This is a simple measure of overall debt capacity and is benchmarked against the Cambridge Mean.



The Brown Edwards' debt relative to endowment net assets group median was approximately 49.4% in 2014.

Viability Ratio

This ratio, which is included in the CFI composite score, indicates one of the most basic determinants of financial health by measuring the medium to long-term health of the institution's balance sheet and debt capacity. Its purpose is to assess the availability of expendable net assets (unrestricted and temporarily restricted less plant assets net of related long-term debt) to cover debt should the institution need to settle its obligations as of the balance sheet date.



The Brown Edwards' viability ratio group median was 1.42 in 2014 and 1.21 in 2013; the viability ratio median for the top 10 was 2.05 in 2014.

<u>Strategically Managing Debt</u> (Continued)

Debt Capacity Measures

Other Debt Capacity Measures

Another debt capacity measure required as part of the College's debt covenants is that the College maintain no less than $11.0 million ($15.0 million in 2017 and forward) in "unencumbered unrestricted liquidity". This ratio is calculated by taking the sum of cash and cash equivalents and long-term investments and reducing it by restricted net assets (temporarily and permanently restricted less contributions receivable). The College exceeded the required amount significantly in 2014.

Our Analysis & Comments on Debt Measurements

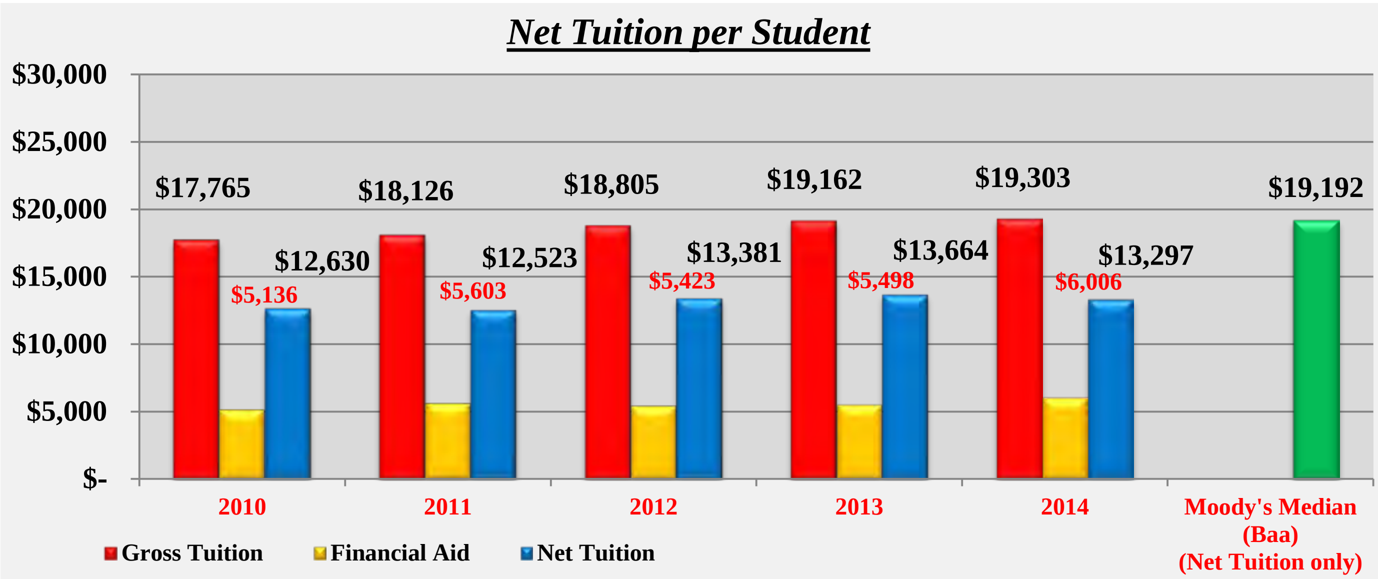
All the College's debt measurements have moved to much stronger positions during the last five years. The ratios indicate that the College, as compared to benchmarking medians and recommended targets, is in a very healthy debt position with available affordability and capacity. ***However, once again, the ratios only include debt at year end and do not include the full $15.0 million draw of the District of Columbia C Series 2014B Bonds or any other anticipated debt.***

Overall, the College is generating more than sufficient resources necessary to cover principal and interest payments on its debt. From a debt affordability standpoint, it is always important that management develop and closely manage budgets and financial plans with appropriate stress testing to assess potential vulnerabilities.

The College continues to maintain good overall financial flexibility to respond to its future potential capital needs with a capitalization ratio (total net assets divided by total assets) at about 77% (desirable range is 50% - 85%). ***The Brown Edwards capitalization ratio % group median was 76.3% in 2014***. This ratio further indicates that the College is appropriately leveraging its assets to potentially increase income and future financial wealth. The College's equity is comprised of a reasonable mix of financial assets (financial net asset ratio of about 77%) versus physical net assets which further indicates financial flexibility. ***The Brown Edwards financial net assets ratio % group median was 69.1% in 2014.*** Obviously managing all these factors to equilibrium is imperative and crucially important to the long-term success of the institution.

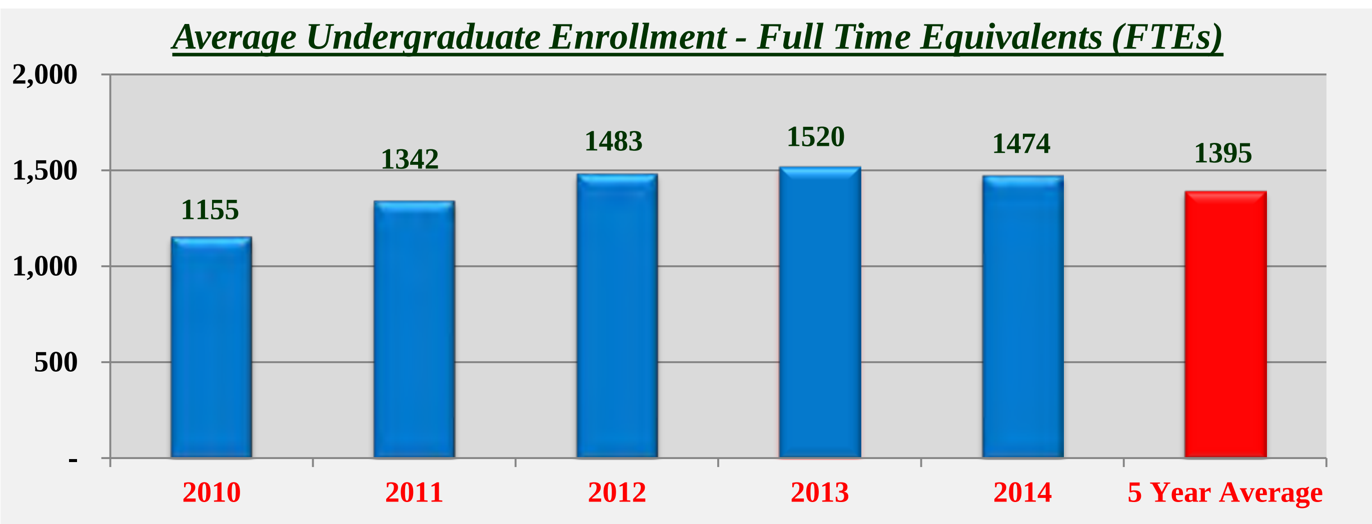
Net Tuition per Student

The **Net Tuition per Student Ratio** compares tuition and fee revenue, net of tuition discounts, to student enrollment (FTEs). This ratio indicates the average tuition paid per student.



The Brown Edwards' net tuition per student group median was $13,498 in 2014 (gross tuition $28,610; financial aid $14,682) and $13,324 in 2013; the net tuition per student median for the top 10 was $13,513 in 2014 (gross tuition $29,579; financial aid $16,422).

Although the financial aid cost of maintaining enrollment has continued to go up over the trend period, enrollment has increased steadily until 2014, contrary to the industry as a whole.



The Brown Edwards' enrollment FTE group median was 1317 in 2014 and 1275 in 2013; the enrollment FTE median for the top 10 was 1317 in 2014 and 1323 in 2013.

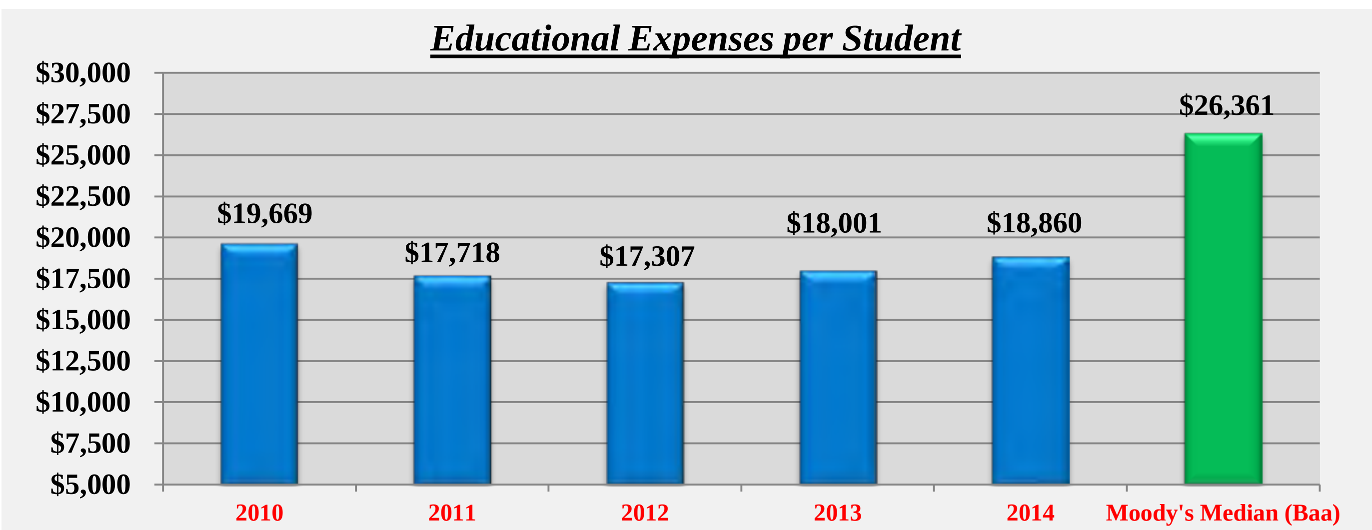
<u>Net Tuition per Student</u> (Continued)

Our Analysis & Comments on Your Net Tuition per Student

Contrary to the industry as a whole, prior to 2014 the College has successfully increased enrollment and net tuition dramatically in recent years. The College has elected to keep net tuition very affordable and accordingly is well below the Moody's median but very close to the Brown Edwards median. Most institutions are struggling just to maintain enrollments. The College has accomplished this while holding the level of financial aid granted to below average levels, causing a steady increase to net tuition per student. Net tuition amounts to a substantial portion of operating revenue, so this is a critical focus area. It is important to note that tuition discounts are based on tuition only and do not include other student fee factors such as room and board charges.

<u>Educational Expenses per Student</u>

The **Educational Expenses per Student Ratio** compares operating expenses less auxiliary service expenses to student enrollment (FTEs) and indicates the average educational expenses per student.



The Brown Edwards' educational expense per FTE group median was $23,729 in 2014 and $22,519 in 2013; the educational expense per FTE median for the top 10 was $24,982 in 2014.

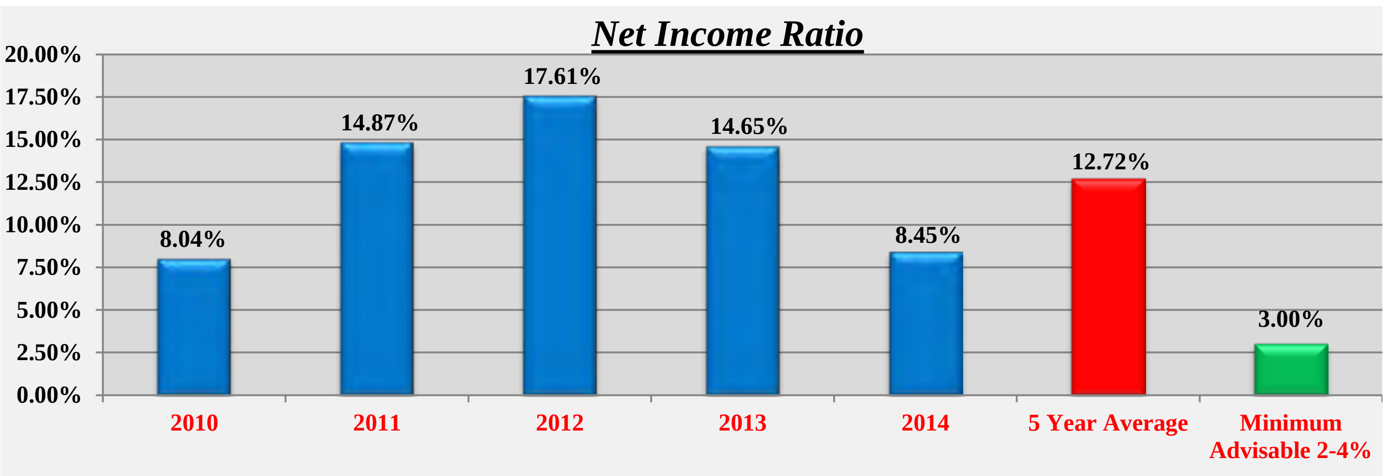
Our Analysis & Comments on Your Educational Expenses per Student

The College has held educational expenses to a reasonable level over the trend period, and this is during a time when enrollment was increasing dramatically. Also, as mentioned elsewhere there are significant pressures on rising costs in higher education.

The education expenses per student came down dramatically over this period due partially to being spread over significantly more students. Undergraduate student enrollment has grown from 1,155 to as high as 1,520 during this period. Just as net tuition per student is well below the Moody's median (Baa) so are educational expenses per student.

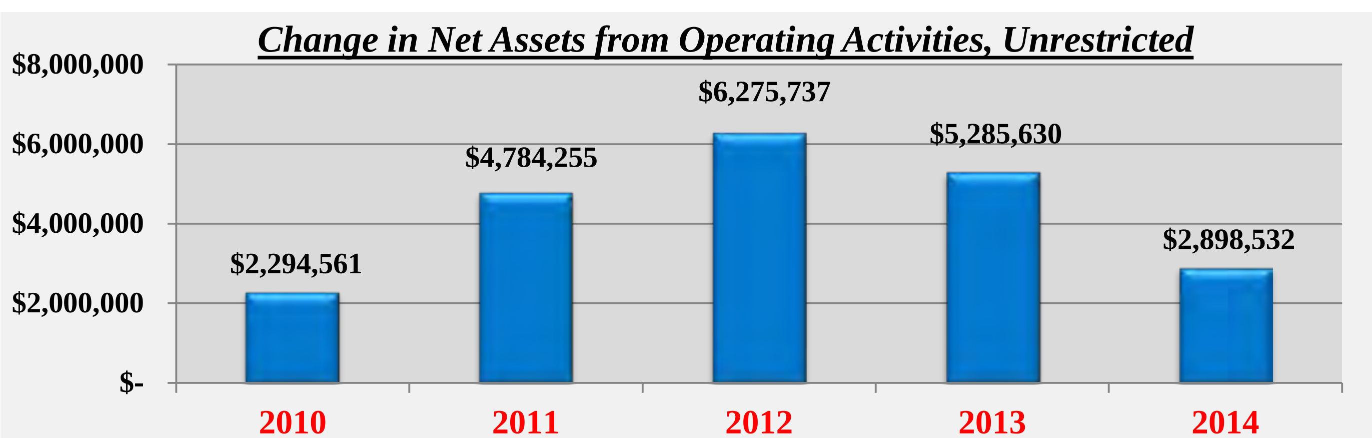
<u>Net Income Ratio, Change in Net Assets from Operating Activities, Unrestricted and Net Cash Provided by (Used in) Operating Activities</u>

The **Net Income Ratio**, also included in the CFI calculation, was **developed to measure whether operating results indicate an institution is functioning within its available resources**. It is calculated as the **unrestricted operating indicator** or change in unrestricted net assets divided by total **unrestricted operating revenue**. It indicates whether unrestricted activities resulted in a surplus or deficit. A positive ratio indicates a surplus and the larger the surplus, the stronger the financial performance for the year. A negative ratio indicates a loss for the year. A small deficit can be manageable particularly by a financially strong institution. However, large, recurring deficits are almost always not a good sign. A target rate of 2 to 4 percent is a reasonable goal, but could be modified based on strategic initiatives in play.



The Brown Edwards' net income ratio group median was 3.06% in 2014 and 3.29% in 2013; the net income ratio median for the top 10 was 3.06% in 2014.

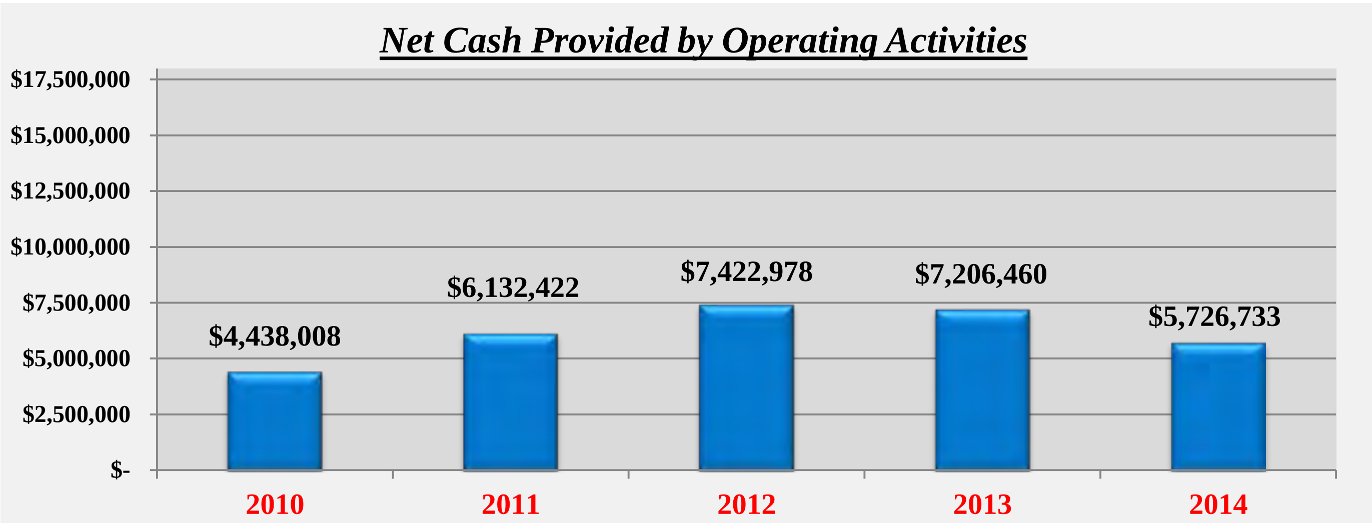
The sister to the net income ratio is the **Change in Net Assets from Operating Activities, Unrestricted**. This operating measure is the closest measure on the financial report to the institution's operating budget. It does include depreciation and interest costs whereas as many institution operating budgets do not.



The Brown Edwards' change in net assets from operating activities, unrestricted group median was $1.28 million in 2014 and $1.28 million in 2013; the change in net assets from operating activities, unrestricted median for the top 10 was $1.28 million in 2014.

<u>Net Income Ratio, Change in Net Assets from Operating Activities, Unrestricted and Net Cash Provided by (Used in) Operating Activities</u>

Net cash provided by operating activities is another operational measure focused on cash. Most institutions have historically struggled to achieve positive cash flow from operating activities. However, in more recent years as a result of significant reengineering of operations necessary due to the many pressures on small private colleges and universities, many have improved significantly.



The Brown Edwards' net cash provided by operations group median was $2.68 million in 2014 and $3.02 million in 2013; the net cash provided by operations median for the top 10 was $2.68 million in 2014.

Our Analysis and Comments on Your Change in Net Assets from Operating Activities, Unrestricted and Net Cash Provided by Operating Activities

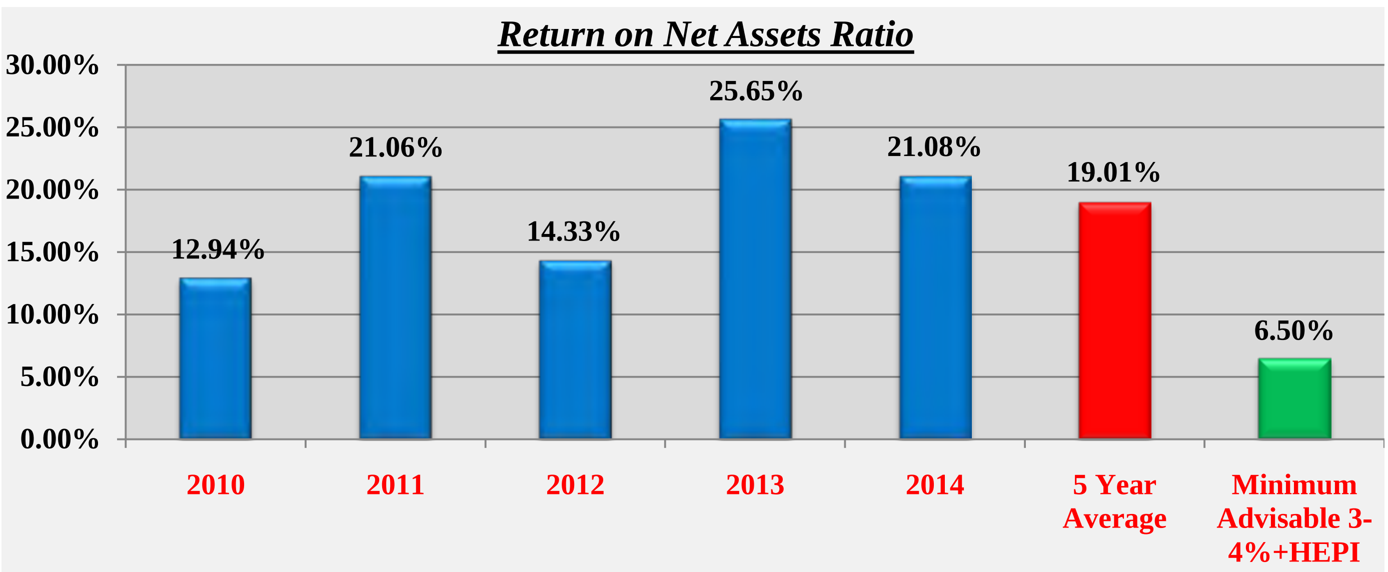
The College has had strong operating results during this period averaging a net income ratio of 12.72%, and it has been a financial strength. In the current year, operating revenue was down significantly, while operating expenses were up modestly resulting in a strong positive, but significantly reduced operating result from the prior year.

Net cash provided by operations also remains strong, and as the old accountant saying goes, "cash is king". Generating a healthy stream of cash flows from operations is always a good thing.

Return on Net Assets Ratio

The **Return on Net Assets Ratio** compares the change in net assets to average net assets during the year. **The ratio determines whether the institution is financially better off by measuring total economic return versus only operating return. It measures the institution's performance in generating net assets compared to the capital base used to produce those net assets.** A decline in this ratio may be appropriate and even warranted if it reflects a strategy to better fulfill the institution's mission. On the other hand, an improving trend in this ratio indicates that the institution is increasing its net assets and able to set aside financial resources to strengthen its future financial flexibility.

An increasing trend indicates that more funds are being made available for the future. A target rate of return should be approximately 3 to 4 percent plus the actual inflation index (CPI or HEPI). Brown Edwards typically uses HEPI, which was 3 percent in 2014.



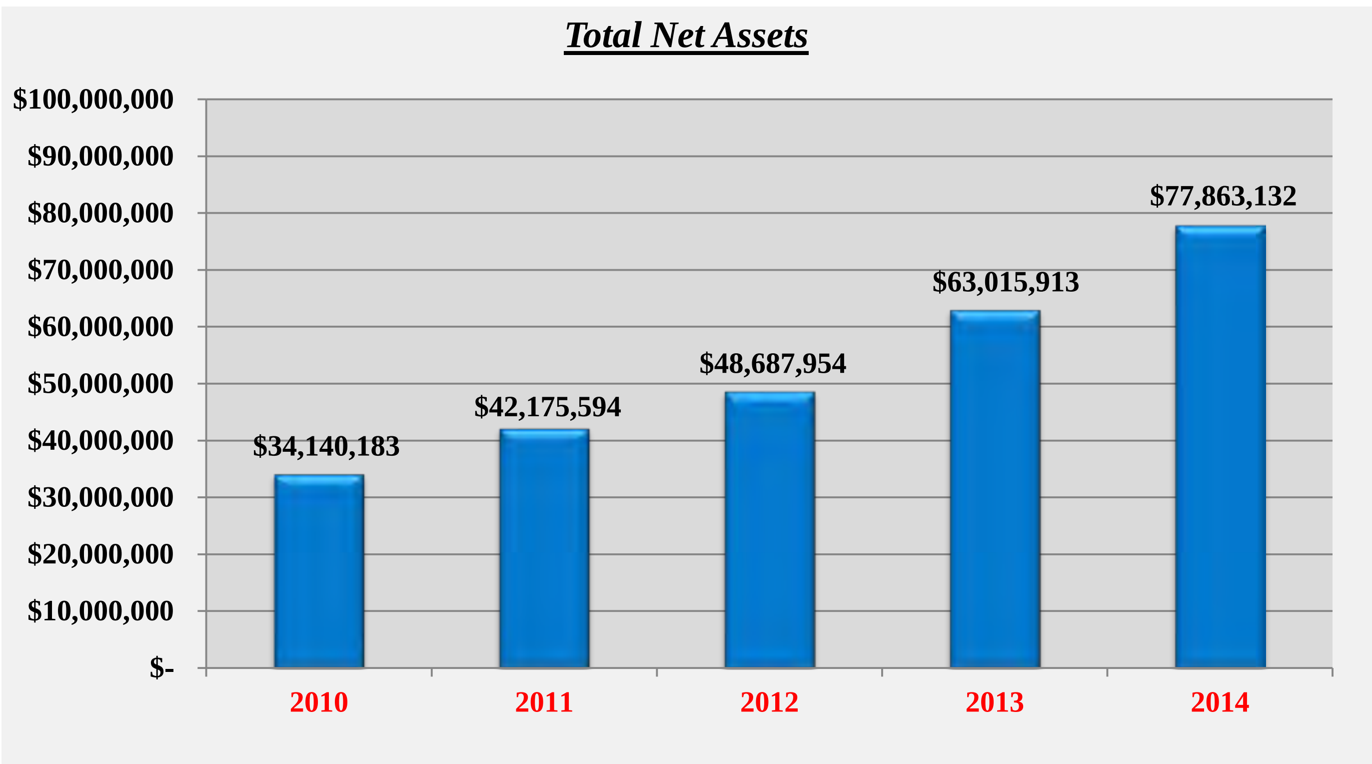
The Brown Edwards' return on net assets ratio group median was 11.24% in 2014 and 9.13% in 2013; the return on net assets ratio median for the top 10 was 12.76% in 2014.

Return on Net Assets Ratio (Continued)

Our Analysis and Comments on Your Return on Net Assets Ratio

This indicator has fluctuated from year to year, primarily due to economic and financial market conditions, but has averaged 19.01% during the five years.

Long-term sustainability of this ratio is necessary to build expendable net assets and improve short-term strength and liquidity. A strong measure over an extended time period is a desired goal. As a result of the College's consistent and significant positive Return on Net Assets Ratio, total net assets have incredible growth over this period**.**



The Brown Edwards' total net assets group median was $114.9 million in 2014 and $104.9 million in 2013; the total net assets median for the top 10 was $140.4 million for 2014.

TRINITY COLLEGE

RATIO ANALYSIS IN HIGHER EDUCATION

The "**Ratio Analysis in Higher Education**" developed by BearingPoint, Inc., KPMG, and Prager, Sealy & Co. focuses on the evaluation of an institution's use of financial resources to achieve its unique mission. These ratios quantify the status, sources, and uses of these resources and the debt paying ability of an institution. They are categorized into four areas of measurement and are designed to answer the following basic questions:

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

A unique concept with this analysis is the integration of a key ratio from each of the four categories into a combined, single measurement of the overall level of financial health of an institution. This measure is called the Composite Financial Index (**CFI**). **CFI** can be useful to an institution in helping to understand its financial position in the marketplace and in assessing its financial viability. It is best used as a component of financial goals in an institution's strategic plan.

CFI is based on four core ratios, further described below, that represent measurement of key components in relation to institutional risk that must be consistently addressed:

- Balance sheet measurements reflecting wealth accumulation and financial flexibility, each with 35% weighting
  - **Primary Reserve** – compares operating commitments to expendable accumulated wealth or financial cushion; expendable net assets/expenses; a ratio of .40 or better is the minimum advisable reserve (resources to cover operating expenses for about 5 months (.40 of 12 months).
  - **Viability** – measures debt capacity; compares outstanding long-term obligations to expendable wealth; expendable net assets/debt; a ratio of 1.25 to 2 is considered a minimum advisable range. A ratio of 1 indicates an institution has the expendable resources to pay off its debt.
- Operating measurements indicating annual operating performance
  - **Net Income** – measures, on a short-term basis, the ability to live within your means; change in unrestricted operating net assets/unrestricted operating revenues; an institution should target two to four percent as a goal and that target may vary from year to year depending on institutional strategic initiatives. Metric most within the control of management. 10% weighting.
  - **Return on Net Assets** – measures the ability to generate overall return against all net resources; a real return of three to four percent plus the higher education price index (HEPI) might be considered a reasonable target, depending on the institution's specific strategic plan. 20% weighting.

These four ratios are properly weighed and scored on a common scale to arrive at **CFI**. Using a single score is superior to the individual measurement of each ratio because it allows a weakness in a particular ratio to be offset by strength in another ratio, similar to the use of GPA (grade point average) for students. Note that **CFI** and all these ratios deal only with the financial aspects of an institution and must be blended with key performance indicators in areas such as academics, infrastructure, and student and faculty satisfaction to understand a complete measure of institutional strength.

CFI is quantified on a progressive scale of one to ten, with one indicating the need to assess the viability to survive and ten indicating strong financial conditions and flexibility. Once **CFI** is determined, it can be compared to the following scale for an indicator of the range of overall institutional well-being, appropriately considering nonfinancial indicators. The scores overlap because the index is not intended to represent financial health as a precise point on the chart, but rather as a range for a particular level of health.

Given the **CFI** score, there are also suggested actions that an institution should consider which are summarized in the table below.

Ratio Analysis in Higher Education – CFI: Scoring Scale

Scale Level	CFI Scoring Range	Action
One	-1 to 1	Severe financial stress – assess viability; Can the college survive?
Two Three	0 to 2 1 to 3	Moderate financial stress – reengineer the institution.
Four Five	2 to 4 3 to 5	Direct resources toward becoming a stronger institution and moving to the next level.
Six Seven	4 to 6 5 to 7	Focus resources to compete in the future.
Eight	6 to 8	*Experiment with new initiatives.*
Nine	7 to 9	New initiatives. Design a robust mission.
Ten	> 9	Deploy resources to achieve a robust mission.

It is most appropriate to review **CFI** over a period of three to five years and to evaluate the trend (see page 8) as opposed to focusing on one year. This allows the ratio to normalize for an atypical bad year or as key institutional strategic initiatives are implemented and take hold. To improve **CFI**, the components of the individual ratios suggest where to focus attention.

If you calculate **CFI** (for an institution with long-term debt) by using the advisable indicators for the four core ratios and assuming a consumer price index of 3.0%, **a minimum advisable or target CFI would be 3-4.**

Ratio Analysis in Higher Education**

	Advisable Indicator	Trinity College Current Year	Prior Year	2nd Prior Year
MEASURING OVERALL FINANCIAL HEALTH				
1) **Composite Financial Index** - measures the financial component of an institution's well-being using four core ratios: **primary reserve, net income, return on net assets and viability**	At least 3.00 - 4.00 (Also, see CFI Scoring Scale)	8.17	7.76	6.44
MEASURING RESOURCE SUFFICIENCY AND FLEXIBILITY				
2) **Primary reserve** - measures how long the institution could operate without relying on additional net assets generated by operations	0.40 or better	1.25	1.13	0.98
3) **Secondary reserve** - an assessment of the significance of permanently restricted net assets in relation to operating size	Increasing trend	0.65	0.63	0.63
MEASURING OPERATING RESULTS				
4) **Net income** - indicates whether total unrestricted activities resulted in a surplus or a deficit (using an operating indicator)	2.00 - 4.00% and higher	8.45%	14.65%	17.61%
5) **Cash income** - indicates whether unrestricted activities, excluding gains, resulted in a net cash inflow or outflow	Increasing trend	36.71%	19.40%	20.78%
6) **Operating income** - measures institutional self-sufficiency	"	102.42%	112.38%	118.03%
7) **Contributed income** - measure of the institution's dependency on externally generated resources, other than debt, to finance operations	Increasing trend	10.69%	7.44%	7.86%
8) **Educational core services** - measures whether core services are using a growing or dwindling share of institutional resources	Stable or increasing trend	33.45%	31.00%	30.13%
9) **Educational support** - measures whether educational support services are using a growing or dwindling share of institutional resources	Stable or increasing trend	26.94%	24.86%	23.94%
10) **General support** - measures whether general support expenses are using a growing or dwindling share of institutional resources	Stable trend	27.59%	25.35%	25.14%
11) **Facilities maintenance** - measures the percentage of educational and general income allocated to plant maintenance	Stable or increasing trend	12.68%	11.31%	11.63%
MEASURING FINANCIAL ASSET PERFORMANCE				
12) **Return on average net assets** - measures the institution's performance in generating net assets compared to the capital base used to produce those net assets	3.00 - 4.00% plus CPI and higher	21.08%	25.65%	14.33%
13) **Capitalization** - measures total financial flexibility to respond to additional capital or programmatic needs over a specified period of time; **total net assets/total assets**	50%-85%	76.73%	73.13%	66.73%
14) **Financial net assets ratio** - measures the % of financial net assets to total net assets; ***equity resources available for new initiatives***	These 2 ratios must be in equilibrium	76.66%	85.89%	97.03%
Physical net assets ratio - measures the investment in physical plant to total net assets; ***too high % reduces financial flexibility***	for best financial flexibility	23.34%	14.11%	2.97%
MEASURING STRATEGIC MANAGEMENT OF DEBT				
15) **Viability** - measures availability of net assets to cover debt should the institution need to settle its obligations as of the balance sheet date	1.25 - 2.00 and higher	2.24	2.14	1.70
16) **Debt burden** - measures the institution's dependence on borrowed funds as a source of financing its mission and the relative cost of borrowing to overall expenditures	7% or less	4.17%	4.50%	4.81%
17) **Debt coverage** - measures the excess of income over adjusted expenses available to cover annual debt service payments	High ratio	4.24	5.89	6.15
18) **Leverage** - measure of debt in relation to unrestricted and temporarily restricted assets in the institution's capital structure	2.00 and higher	3.28	2.69	1.79
19) **Age of plant** - measures the relative age of plant assets and equipment	Low ratio; 14 or less	24.07	24.49	23.02
20) **Debt capitalization** - measure of what percent of capital comes from debt; debt/ total net assets plus debt	< 20%	18.4%	20.5%	25.7%

**** Taken from the book, *Strategic Financial Analysis for Higher Education* jointly published by BearingPoint, Inc., KPMG, LLP and Prager, Sealy & Co.**

Trinity College
Composite Financial Index
"Measuring The Overall Level of Financial Health"

Current Year

RATIO	RATIO VALUE	STRENGTH FACTOR**	WEIGHTING FACTOR*	SCORE	MAXIMUM POSSIBLE SCORE
Primary Reserve	1.25	9.41	35%	3.29	3.50
Net Income**	8.45%	10.00	10%	1.00	1.00
Return on Net Assets	21.08%	10.00	20%	2.00	2.00
Viability	2.24	5.37	35%	1.88	3.50
	Composite Financial Index			8.17	10.00

Prior Year

RATIO	RATIO VALUE	STRENGTH FACTOR**	WEIGHTING FACTOR*	SCORE
Primary Reserve	1.13	8.47	35%	2.96
Net Income**	14.65%	10.00	10%	1.00
Return on Net Assets	25.65%	10.00	20%	2.00
Viability	2.14	5.13	35%	1.80
	Composite Financial Index			7.76

Second Prior Year

RATIO	RATIO VALUE	STRENGTH FACTOR**	WEIGHTING FACTOR*	SCORE
Primary Reserve	0.98	7.36	35%	2.58
Net Income**	17.61%	10.00	10%	1.00
Return on Net Assets	14.33%	7.17	20%	1.43
Viability	1.70	4.09	35%	1.43
	Composite Financial Index			6.44

* Institution with long-term debt
** Net income ratio calculated using an operating indicator
Note: Taken from the book, *Strategic Financial Analysis for Higher Education* jointly published by BearingPoint, Inc., KPMG, LLP and Prager, Sealy & Co.

TRINITY COLLEGE

MOODY'S AND STANDARD & POORS' RATIOS

Moody's and Standard & Poors view higher education as a business enterprise that must be concerned with the demand and pricing for its service and its market niche. These rating agencies look at five key areas in assessing the financial viability of an organization.

- Market position. Student demand translates into revenue streams.
- Financial performance. Is the institution financially sound?
- Debt position. An examination of the role of debt in the capital structure of the organization as well as issues surrounding deferred maintenance.
- Legal structure. How is the debt of the organization secured?
- Management. Does the management team have a credible financial and market strategy, and has it shown it can execute that strategy?

To complete their assessments, Moody's and Standard & Poors also considers environmental factors that influence financial health, such as government, the economy, and demographics.

*Moody's Ratios****

MARKET DATA AND RATIOS	Baa Benchmark*	Trinity College Current Year	Prior Year
Total Enrollment FTE, undergraduate	1844	1474	1520
Net tuition per student, undergraduate	$ 19,192	$ 13,297	$ 13,664
Educational expenses per student, all	$ 26,361	$ 18,860	$ 18,001
Institutional tuition discount, undergraduate	N/A	29.60%	27.36%
Total tuition discount, undergraduate	40.30%	31.11%	28.69%
Tuition rate, undergraduate	N/A	$ 20,970	$ 20,550
Tuition increase over prior year, undergraduate	2.7%	2.0%	2.0%
FINANCIAL DATA			
Total Financial Resources **	$ 94,006	$ 59,693	$ 54,033
Total Debt **	$ 41,510	$ 17,544	$ 16,200
Total Revenues **	$ 61,672	$ 46,232	$ 45,116
Total Cash and Investments**	$ 96,365	$ 68,824	$ 55,355
Total Expenses**	$ 57,182	$ 31,385	$ 30,788
Total Gift Revenue**	$ 5,060	$ 11,180	$ 8,484
CAPITAL RATIOS			
Unrestricted financial resources to debt (x)	0.48	1.86	1.79
Expendable financial resources to debt (x)	1.17	2.24	2.13
Total financial resources to debt (x)	2.30	3.40	3.34
Total cash and investments to debt (x)	2.34	3.92	3.42
Debt service to operations	5.60%	4.12%	4.45%
Capital Spending Ratio (x)	1.09	1.96	1.03
Age of plant (number of years)	13.79	24.07	24.49
BALANCE SHEET RATIOS			
Unrestricted financial resources to operations (x)	0.39	1.04	0.94
Expendable financial resources to operations (x)	0.81	1.25	1.12
Free expendable financial resources to operations (x)	0.12	0.69	0.60
Expendable financial resources to total net assets	N/A	50.46%	54.87%
Debt capitalization	24.60%	18.39%	20.45%
Total financial resources per student	$ 50,054	$ 40,498	$ 35,548
Debt per student	$ 23,239	$ 11,903	$ 10,658
OPERATING RATIOS			
Operating margin	2.90%	8.45%	14.65%
Operating margin, excluding gifts	-3.60%	6.55%	12.50%
Operating cash flow margin	14.40%	13.42%	19.46%
Actual debt service coverage (x)	2.59	3.56	5.13
Return on average net assets	7.10%	21.08%	25.65%
Return on financial resources	11.00%	9.95%	13.41%
NONOPERATING RATIOS			
Market value of investments and FHIT by others**	N/A	$ 54,812	$ 48,579
Total return on investments and FHIT by others	N/A	6.1%	4.0%
Investments and FHIT by others per student	N/A	$ 37,186	$ 31,960
CONTRIBUTION RATIOS (% of total unrestricted operating revenue)			
Net tuition and auxiliaries	83.40%	92.02%	93.04%
Grants and contracts	1.80%	0.84%	0.91%
Investment income (including gains)	7.40%	0.37%	0.36%
Gifts and pledges	5.80%	2.04%	2.46%
Other	1.80%	0.65%	0.78%
	100.20%	95.92%	97.56%
Net assets released from restriction	-0.20%	4.08%	2.44%
	100.00%	100.00%	100.00%

* Moody's - Medians for small, private colleges and universities rated "Baa"; fiscal 2013 data (dated July 11, 2014).

** In thousands (x) Indicates times or a multiple

*** Moody's adjusts total unrestricted operating revenue to limit investment income to 5% of average of previous three year's ending value of cash and investments. This has not been done on the college's ratios above and will cause variances from those calculated by Moody's.

Standard and Poor's Ratios

	*Benchmark	Trinity College Current Year	Trinity College Prior Year
DEMAND AND OTHER DATA			
FTE Enrollment, undergraduate	3,274	1,474	1,520
Endowment Market Value**	$ 54,901	$ 26,061	$ 24,011
Endowment Market Value per FTE, UG	$ 16,582	$ 17,680	$ 15,797
STATEMENT OF ACTIVITIES RATIOS			
REVENUE DIVERSITY - a diversified revenue base is advisable			
Tuition	76.40%	85.54%	86.72%
Grants and Contracts	1.10%	0.66%	0.74%
Gifts and Pledges	1.10%	1.61%	1.98%
Investment and endowment income	1.20%	0.29%	0.29%
Auxiliary operations	12.70%	8.18%	7.66%
EXPENSE AND FINANCIAL AID - ability to reduce costs if revenues decline; a low ratio of fixed to variable cost is advisable			
Instruction	28.30%	26.48%	26.87%
Tuition discount, total, undergraduate	32.30%	31.11%	28.69%
Financial aid burden	25.60%	21.15%	20.56%
STATEMENT OF FINANCIAL POSITION RATIOS			
LIQUIDITY RATIOS - ability to continue to operate without taking on additional revenue			
Cash and investments to operations	67.70%	172.90%	142.83%
Unrestricted resources to operations	N/A	82.08%	74.96%
Expendable resources to operations	42.90%	98.71%	89.22%
Cash and investments to debt	134.60%	392.28%	341.70%
Unrestricted resources to debt	N/A	186.22%	179.34%
Expendable resources to debt	75.50%	223.95%	156.73%
DEBT RATIOS			
Total debt, including any current financing**	$53,642	$17,544	$16,200
Current debt service burden (advisable = less than 10%)	3.98%	3.28%	1.84%
Average age of plant	12.30	24.07	24.49
FULL-TIME EQUIVALENT MEASURES (Undergraduate only)			
Net tuition per FTE	$ 17,460	$ 13,297	$ 13,664
Total operating revenue per FTE	$ 35,384	$ 23,725	$ 23,377
Total operating expenses per FTE (all operating expenses)	$ 26,007	$ 27,005	$ 25,498
Total outstanding debt per FTE	$ 18,913	$ 11,903	$ 10,658
Unrestricted resources per FTE	N/A	$ 22,165	$ 19,114
Expendable resources per FTE	$ 15,183	$ 26,656	$ 16,704

* Median averages of private colleges and universities with a debt rating of "BBB" by Standard & Poor's: fiscal 2013 data (dated July 8, 2014)

** In thousands

Note: Generally, Standard & Poor's treats financial aid/scholarships as an expense (versus the FASB approach of netting against tuition and fees).

TRINITY COLLEGE

OTHER ANALYSIS, INCLUDING THE U.S. DEPARTMENT OF EDUCATION COMPOSITE SCORE

Included on the following page is some other key financial analysis such as **sources of revenue, expenses by function and percent change from the prior year, some key fundraising ratios, inflationary indexes, auxiliary services net margin and the U.S. Department of Education Composite Score.**

The **U.S. Department of Education** has also adopted Financial Responsibility Standards for institutions participating in student financial-assistance programs under Title IV. Failure to meet these minimums will result in being monitored by the Department. Their ratios provide a measure of an institution's financial health by focusing on the ability to meet debt obligations, the level of reserves available to support current operations, as well as the ability to function within its means in a given operating cycle.

The U.S. Department of Education's Financial Responsibility test ***should not be confused with the Composite Financial Index***. The Financial Responsibility test uses a composite score based upon three ratios, two of which are ratios also used in the **CFI**, the primary reserve ratio and the net income ratio. The third ratio in the Department of Education's methodology is the equity ratio, which is a measure of financial strength indicating an institution's ability to borrow. This financial responsibility index was developed for the Department of Education by KPMG to determine eligibility for Title IV funds. Its purpose is primarily to identify institutions that are at increased financial risk (using a scale of -1 to 3) to the student financial aid program in a short time horizon.

The CFI methodology presents a more complete picture of an institution's financial strengths and weaknesses (using a scale of –X to 10). Moreover, CFI assists institutions in understanding the affordability of their strategic plans and to monitor and evaluate the financial results of implementing those strategic initiatives over a longer time horizon.

The Brown Edwards' group median for the ED Composite Score was 3.00 in 2014 and 2013, and this was also the median score of the Top 10.

Other Analysis

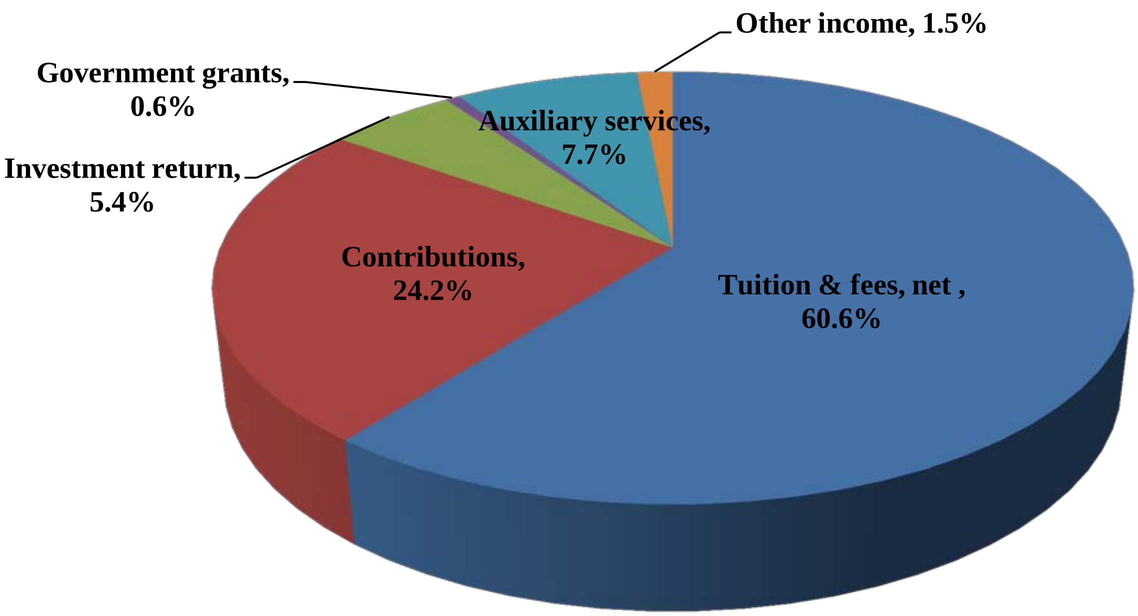
	Trinity College Current Year	Trinity College Prior Year
Revenue Sources as a Percent of Total Revenues, Gains and Other Support		
Tuition & fees, net	60.6%	66.8%
Contributions	24.2%	18.8%
Investment income spent	1.6%	1.6%
Government grants	0.6%	0.7%
Auxiliary services	7.7%	7.6%
Other income	-0.2%	1.8%
Investment total return retained	3.8%	1.0%
Change in funds held in trust	1.7%	1.7%
Total revenues, gains and other support	100.0%	100.0%
Fundraising ratio (cost of fundraising as a percent of total contributions)	6.2%	7.1%
Fundraising expense ratio (cost of fundraising as a percent of total expenses)	2.2%	2.0%
Functional Expenses as a Percent of Total Expenses		
Instruction	33.5%	33.9%
Public service	0.1%	0.1%
Academic support	12.6%	11.9%
Student services	14.6%	15.3%
Institutional support	27.8%	27.7%
Auxiliary services	11.4%	11.1%
Total operating expenses	100.0%	100.0%
Percent increase in operating expenses/FTE	5.1%	2.3%
Percent increase in operating expenses	1.9%	4.9%
CPI (June to June)	2.1%	1.8%
Higher Education PI (by Commonfund) *(CY Preliminary Forecast)*	3.0%	1.6%
Auxiliary Services Net Margin	-0.5%	-0.1%
Department of Education Title IV Financial Responsibility Standards (A composite score of 1.5 or higher is considered financially responsible)		
Primary Reserve Ratio		
Ratio (Expendable Net Assets / Total Expenses)	1.704	1.275
Strength Factor (Primary Reserve ratio x 10)	3.000	3.000
Score (Strength Factor x 40%)	1.200	1.200
Equity Ratio		
Ratio (Modified Net Assets/Modified Assets)	0.767	0.731
Strength Factor (Equity ratio x 6)	3.000	3.000
Score (Strength Factor x 40%)	1.200	1.200
Net Income Ratio		
Ratio (Change in Unrestricted Net Assets / Total Unrestricted Income)	0.108	0.170
Strength Factor (Factor when Net Income ratio is positive)	3.000	3.000
Score (Strength Factor x 20%)	0.600	0.600
Composite Score (Sum of above ratios)	3.00	3.00

Interpretation of Composite Score Range	Composite Score	Regulatory Result
School is financially healthy enough to participate without additional monitoring	1.5 to 3.0	Financially Responsible
"In the zone," additional monitoring needed to participate	1.0 to 1.4	Financially Responsible
School is not financially healthy enough to be considered financially responsible	-1.0 to .9	Not Financially Responsible

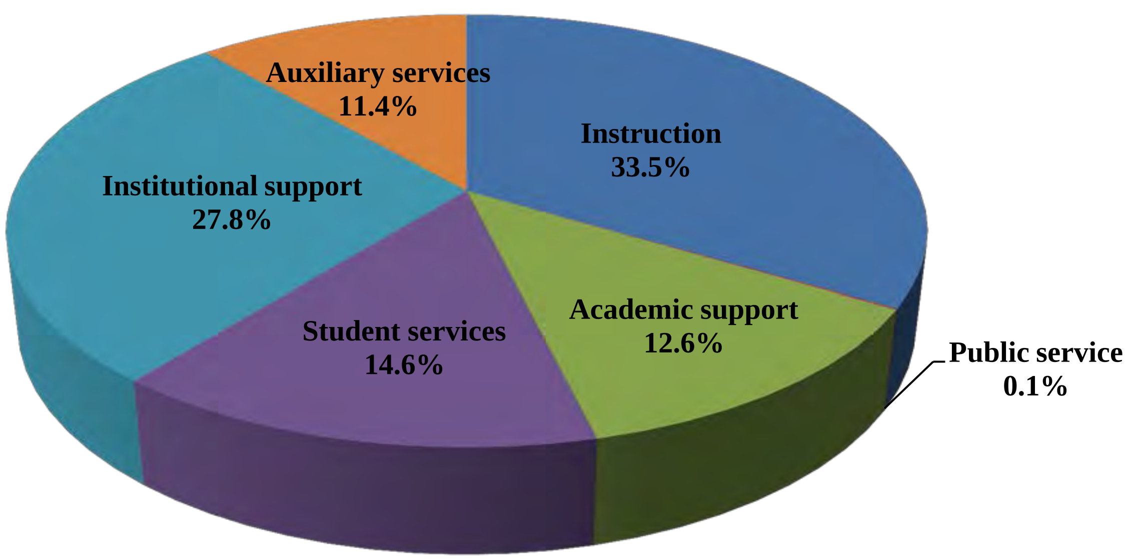
TRINITY COLLEGE

OTHER ANALYSIS, INCLUDING THE U.S. DEPARTMENT OF EDUCATION COMPOSITE SCORE
(Continued)

Current Year Revenue by Source



Current Year Expenses by Function



AN UPDATE FOR PRIVATE HIGHER EDUCATION AND OTHER NOT-FOR-PROFIT ORGANIZATIONS

The Battle for Sustainability Rages On – Only the Strong Will Survive

Small, private colleges and universities and not-for-profits have adjusted well to the lingering impact of the Great Recession with management teams' stellar fiscal stewardship and difficult decision-making concerning the allocation of constrained resources. These **organizations are being asked to do more with less – and do it better.** So far with the aid of healthy investment returns and gift flow, they are doing just that. Operating results have improved even with declining net student fees and rising operating costs.

Yet, even with this stability the industry continues to face strong headwinds from a variety of issues. **Moody's Investor Services (Moody's) 2014 outlook for the higher education and not-for-profits sectors remains negative.** Moody's indicates "*fundamental business conditions in the US higher education and not-for-profit sectors will remain stressed in 2014, with continued price resistance and a challenged federal budget leading to weak revenue growth. Heightened competition for students, donors and government funds combined with pressure to increase compensation and invest in programs and facilities will result in continued deterioration of financial performance. Quickly evolving delivery models are also intensifying competition. Evolving federal and state higher education policies and erratic public funding exacerbate uncertainty. Colleges, universities and not-for-profits have exhibited willingness and ability to adapt to weak economic conditions. However, the uncertainty in the funding and regulatory environment overshadows the strengths of these sectors in the near term and the need for strong governance remains paramount. Historically reliable revenues streams for the diverse not-for-profit sector are now strained by a variety of factors.*"

Additional discussion on the pressures currently bearing down on the industry are summarized below:

- **Economic malaise – reduced family net worth and personal income, rapidly increasing student debt loads and stubborn unemployment.** The impact of these pressures is that families are looking for a less expensive alternative for higher education. Institutions will have to ask and find answers to tough questions such as – are sticker prices more than a family can afford, what pricing strategy is best for our institution, and is a pricing reset a viable option? The current model of holding down net tuition while the upward pressure on costs continues is not sustainable long-term. In addition, **demographics continue to shift** to reflect more "nontraditional," nonwhite, female students and fewer high school graduates. To increase enrollment today and in the future will require a more focused effort on new centers of enrollment growth. With a smaller pool of potential students that have less financial resources, the competition for them is heightened which in turn is resulting in significantly more financial aid and net tuition revenues growing very slowly at best.

- **Cautious outlook – the financial metrics don't look good.** Institutions have been building and spending over the past several years to strategically position themselves for the future. However, in some cases the result has been increased debt and overleveraging. Operating expenses are up as a percent of revenue due to federal mandates and regulations, the additional costs associated with new infrastructure, increased information technology costs for security and shifting business models, and a variety of other reasons. In the past these problems were addressed by passing the costs on to students or by obtaining more government support. Today, neither have the ability to bridge the gap. In fact, with very challenged budgets government funding is flat to declining and unpredictable. A large endowment can provide a competitive edge by making more financial aid available. Yet, experts indicate that the year-over-year growth of endowments is not likely to be what we were all accustomed to before the recession. Institutions must go beyond cost control as it will only go so far. And, some costs such as deferred maintenance and shoring up IT environments and security, simply must be addressed. *More than ever institutions will need to continue to adapt and carefully reallocate their precious resources and strategically manage their budgets.*

The Battle for Sustainability Rages On – Only the Strong Will Survive
(Continued)

- **Heightened political scrutiny with regulatory oversight to improve** – the role and effectiveness of the federal government in improving higher education has long been debated. Nonetheless, a proposal for performance based funding to improve and help control cost has been floated that would reward institutions with higher scores for making their institution more affordable, more accessible to disadvantaged students, and provides better outcomes such as graduation rates, earning potential of graduates, and the number of advanced degrees pursued by graduates. In addition, with human resources as one of its components, anything that impacts this area, such as health care costs, has a tremendous effect on the institution. Potential tax reform with restrictions on tax deductions could also have an impact.

- **Working on sustainable strategies –** with all these other pressures institutions must also look carefully at the current business model and consider alternatives for the future. Change is always difficult, but technology will continue to push forward. Institutions will have to consider whether their future model includes different delivery models, courses with blended online and land-based, or maybe online only, courses with much larger enrollments and leveraged technology, more flexible hiring with different reward structures, and expanding alliances with other institutions.

Moving Forward Strategically

These challenges are a strong indication that the status quo is no longer an option. It is more important than ever for an organization to develop a robust strategic plan to address current issues, and to survive and prosper for years to come. Organizations will need to operate more efficiently and effectively. They will have to meet the core issue, examining cost structures and rationales for programs and support structure, head on. More difficult decisions will have to be made. The most successful will adjust and focus their efforts on their core mission and their interrelated strategic plans.

However, an institution may have a superb strategic plan, wide-ranging and well-developed, but that does not guarantee success. Success is a function of leadership, finances, the economic environment, among other things. Although finances can't drive the strategic plan, the financial component is critical for programs, buildings, and infrastructure. While implementing its plan, an institution and its stakeholders must constantly be asking themselves many important questions. The questions that keep you up at night, such as:

- **What is our overall financial health?** How do we really know what our financial health is? How can we reasonably assess financial health?
- **Are our resources sufficient and flexible to support our mission**…today, 3-5 years from now, in perpetuity?
- **Do our operating results indicate we're living within our means?**
- Given a reasonable time for implementation of strategies, **does financial performance support the strategic direction**, or is it time to change direction?
- Are increasingly limited financial resources being allocated appropriately to support prioritized strategies?
- Is debt being used and managed strategically? How do we know when enough debt is enough, before it's too late?

As you guide your organization to the "new normal," it is imperative that you know the answers to these questions.

The Battle for Sustainability Rages On – Only the Strong Will Survive
(Continued)

<u>Other Tactics to Consider in Addressing These Challenges</u>?

What else can small, private colleges and universities and not-for-profits, especially those that are most vulnerable, do to deal with the significant issues affecting the industry? As previously noted, institutions must be strategic in addressing these issues, and involvement of all constituents will be important to the efforts required. Below are other tactics to consider in meeting these challenges.

- **Reevaluate the traditional higher education cost structure**, considering all areas, including faculty salaries, shared governance, classroom instruction, and student services. Is guaranteed employment (tenure) still relevant? Can both faculty and administrative leadership guide institutions toward cost efficiency? Can more efficient models of instruction, besides traditional in-classroom instruction, be developed? How can student services be provided more cost-effectively? Institutions have relied on nonrecurring savings strategies in the past (e.g., leaving positions vacant, furloughs, early retirement plans, delayed capital expansion); however, now long-term changes in the core cost structure are necessary, likely resulting in the elimination of programs that are small and under-enrolled. Also, consolidating or integrating general education courses across curricula can free resources that might better be directed toward niche programs that can fuel enrollment growth.
- **Increase on-line offerings**—which might mean actually reducing investments in student services and capital facilities and reducing the cost of course delivery. An on-line presence also minimizes geographic campus constraints—in recruiting both students and faculty. On-line market opportunities include specific distance learning programs, degree completion offerings, hybrid classes, fully on-line degrees, and Massive Online Open Course (MOOC). Several efficiencies exist in online education, including distribution of faculty (do not need office space on campus); lower faculty costs (more part-time/adjunct faculty, who do not require benefits and can be paid less); fewer tenured faculty (allowing hiring flexibility and avoiding long-term locked-in personnel costs); e-texts (the use of electronic textbooks, allowing traditional campus "book" stores to carry more retail items with higher profit margins and to avoid losing book sales to online competitors such as Amazon); and pedagogical flexibility (incorporation of various learning mechanisms, such as simulations, video, and other electronic learning tools – more easily than in the classroom).
- **Diversify program "products**," by offering career program certificates, individual course completion certificates, job-market degrees, licenses, developmental/remedial "boot camps." Institutions also should be mindful of program needs from students outside of the U.S.; many international students see the U.S. degree as "the most prestigious."
- **Continue to stress the long-term value of postsecondary degrees** – especially higher income earning potential and lower unemployment rates:

Bureau of Labor Statistics, Current Population Survey (rounded)				
	Earnings		Unemployment Rate	
	2007	2011	2007	2011
High School	**$31,000**	**$32,000**	**4.5%**	**9.0%**
Bachelor's	**$51,000**	**$55,000**	**1.8%**	**4.6%**
Master's	**$55,000**	**$65,000**	**1.5%**	**3.8%**
Doctoral	**$60,000**	**$80,000**	**1.0%**	**2.8%**

***The Battle for Sustainability Rages On – Only the Strong Will Survive* (Continued)**

<u>Other Tactics to Consider in Addressing These Challenges</u>? (Continued)

- **Ensure that students graduate in four years (or less!)**. In this regard, helping the institution's staff and faculty understand the role of debt in students' lives and encouraging faculty and staff to develop and participate in initiatives to ensure timely or expedited graduation is critical.
- **Consider "anywhere" education**. For example, more and more high school students desire to earn college credit before they complete high school. In addition to bringing local high school students to their own campuses (not to be discouraged because of its marketing angle), private institutions might take the professor to the high school class – either in person or in an online format. Colleges and universities also are taking their educational opportunities to venues where the adult learner can be reached easily and conveniently. Venues such as company conference rooms, shopping malls (vacant stores and even movie theaters), military installations, and even prisons offer excellent facilities for classes to be taught. (Regarding prisons, do not focus only on the employees – those that are incarcerated can be ambitious students, particularly through "incarcerated re-entry programs.")
- **Evaluate tuition levels**, perhaps minimizing tuition increases and even lowering tuition. Other mechanisms for enhancing affordability include freezing tuition for students' entire undergraduate college careers (up to four years, perhaps) or allowing students to pay for up to four years up front at a discounted rate. These options provide greater transparency, allowing for easier student/family budget planning.
- **Teach financial literacy skills** to students (and their families), to help them understand basic money management skills, such as budgeting/saving, completing financial aid documents, handling credit and debt, and planning financially for a career/graduate school. With this information, they can not only complete their education without getting into financial difficulty, they can carry this solid foundation into a lifetime of financial success, becoming supportive alumni to their alma mater.
- **Partner with other colleges and universities**, creating consortia offering greater programing diversity, while allowing more niche specialization within individual institutions, reducing costs while enhancing specific program reputation at these colleges. As several states consider consolidating campuses within public systems (Georgia, Louisiana, West Virginia, and New Jersey), private institutions just as well benefit from similar operating efficiencies and reduced overhead. Shared services models can reduce duplication of administrative functions and generate efficiencies in areas such as human resources, fundraising, financial services, information technology, internal audit, and purchasing. Academic synergies may be developed jointly through dual enrollment programs and joint bachelor/master programs.
- **Manage cash flow tightly**, including maintenance of cash reserves. Consider having a line of credit available, even if it is never used – especially in light of potential delays in release of federal (and state) funds, not to mention slower payment by individuals.
- **Manage debt structure carefully**, including awareness that debt capacity levels are tighter than previously, because of the general volatility in the higher education marketplace. That is, institutions (especially small, less well-known ones) cannot assume that the flow of students will remain steady to support increased debt service. Consideration should be given to incurring more fixed-rate than variable-rate debt, again because of the volatility in the higher education marketplace and general economic concerns.

The Battle for Sustainability Rages On – Only the Strong Will Survive (Continued)

<u>Other Tactics to Consider in Addressing These Challenges</u>? (Continued)

- **Commercialize intellectual property**, encouraging and supporting faculty to be innovative in their research pursuits, even at the smaller colleges and universities.

- **Continue to automate**, including: online distribution of materials, reports, documents, etc.; electronic timekeeping for employees; digitized document storage; e-procurement/payment; consolidation of technology (e.g., desktop printers); and cloud computing. Additional technology transitions include outsourcing technology infrastructure (e.g., servers) and system hosting services (email service) – going to "the cloud." Internal virtualization also is proving cost effective, where desktop personal computers in offices and technology laboratories are replaced with "thin clients" (like monitors) that link to central servers for necessary software.

- **Identify alternative revenue streams**, such as continuing education seminars, adult-learning short courses, enrichment certifications, and corporate-sponsored achievement milestones. Institutions might also consider winter terms or summer programs – not only for their own current students, but also for those students returning home for their breaks from other institutions and for students from other localities (even international) who desire special program and travel opportunities. Other revenue diversity opportunities include revenue-generating partnerships (space-sharing), auxiliary programming (economic analysis centers, tourism coordination hubs, local or regional history/heritage resource archives, cultural symposia festivals, and after school programming sites), and entrepreneurial activities (life-long learning initiatives, intellectual property development, and alumni branding opportunities).

- **Evaluate and tweak fundraising strategies**, perhaps considering longer-term pledge periods, mini-campaigns that are focused, elimination of "distracting campaigns" to focus on annual fund and scholarship giving, and evaluation of existing restricted fund balances as an occasion to reconnect with donors.

- **Evaluate endowment policies**. As the investment markets appear to be improving, now is a great time especially to consider adjustments to the payout formula – perhaps calculating spending based on a blend of market value percentage and inflationary increases in payout amounts – to better preserve the endowment for the future, while also achieving strong support from the endowment on a current basis.

The fight for sustainability will rage on, and there's no silver bullet in this battle. Each organization must customize the strategies that best fit their unique strengths and challenges. ***The only certainty is that those with financial flexibility will be better equipped to survive*** while those that are highly leveraged and have little financial flexibility will struggle.

Outlook in Key Economic Areas Affecting the Industry

Various indicators specifically relevant to the economy are helpful to review as organizations attempt to remain nimble while addressing various key issues.

Kiplinger's Economic Outlooks

GDP **2.1% in 2014; 3% or better in second half of the year**	**Unemployment** **Bouncing around; about 6.1% by end 2014**
Interest rates **Short-term rates to stay low through 2014**	**Inflation** **Ticking up slowly to 2.4% in 2014**
Business spending **Spending up 4.5%-5% in 20114 as U.S. growth strengthens**	**Energy** **Oil trading from $90 to $95/bbl. by December**
Housing sales **Continuing to pick up after a poor first quarter**	**Retail sales** **About 4% growth in 2014**
Trade deficit **Unchanged from 2013; U.S. growth pulling in more imports**	

- **General Economic Outlook** – The U.S. economic recovery from the Great Recession remains slower paced than after past recessions, at about half the rate. This has made consumers and businesses cautious about spending. However, consumer spending, business investment and housing increases are all expected to support good economic growth during the latter part of 2014 and for 2015. Accommodative interest rate policy has obviously helped. Although there is no "simple recipe" for unwinding this policy, the expected increase in interest rates by the Federal Reserve over the next 12-18 months is not expected to have more than a mild depressive effect.
- **Gross Domestic Product (GDP)** – GDP measures the output of goods and services produced by labor and property located in the United States and is considered the best barometer of the country's economy. The GDP was 2.2% for calendar year 2013; the first quarter of 2014 started off very slow due to severe winter weather but picked up quickly in the second quarter. Through the end of 2014 and into 2015, GDP is expected to grow at up to 3%, indicating underlying strength to the economy.
- **Employment** – Employment actually is gauged based on the unemployment rate – the percentage of working-age men and women who want jobs but are unable to find them. During 2014, employment has improved even faster than anticipated. The 12-month unemployment rate for 2013 was 7.4 percent and is expected to fall to below 6.0% by the end of 2014 and into 2015.
- **Interest Rates** – The Prime Interest Rate is the interest rate charged by banks to their most creditworthy customers; the rate is almost always the same among major banks and usually is adjusted in correlation to the adjustments of the Federal Funds Rate. Currently the prime rate is 3.25% and is expected to remain at that level through 2014. It is anticipated that the Fed will begin increasing it at some point in mid-2015 as employment continues to improve and inflation picks up.
- **Inflation** – Economists note that inflation will moderate some in the second half of 2014 from 2.6% in the first half. Overall inflation for 2013 (the 12-month period), (as measured by the Consumer Price Index for All Urban Consumers – CPI-U) was 1.5 percent. It is expected to be 2.0 to 2.5 percent for all of 2014 and for 2015 as well.
- **Consumer Income/Spending Growth** – Personal income is expected to increase by 4% over the next half of 2014 and will feed consumer spending, a significant component of a strong economy. In addition, retail sales should grow as the economy, job growth, and consumer confidence continue to improve. The housing market, another big component of a vibrant economy, should improve in the second half of 2014 even with headwinds from rising home values, slim wage gains, and tight mortgage lending.

Outlook in Key Economic Areas Affecting the Industry (Continued)

- **Consumer Confidence** – The Conference Board Consumer Confidence Index is a barometer of the health of the U.S. economy from the perspective of the consumer. In August 2014, index was 92.4 (an index of 90 indicates a healthy economy).
- **Equity and Fixed Income Markets** – Despite the age of the bull market, equities continued to move forward in fiscal 2013-14 while fixed income instruments advanced at a modest pace. Looking forward, some key themes to watch; (1) the U.S. expansion is expected to remain intact however keep a close eye on good fundamentals, demonstrated earnings growth, and reasonable valuations; (2) even with an increase to interest rates on the horizon the current bull market appears to have more life in it, nevertheless it is getting old and a significant correction is due; (3) large caps tend to lead the market later in business recoveries; (4) some international equities may offer slightly compelling valuations and earnings growth potential; and (5) fixed income opportunities will continue to be a challenge and require agile portfolio management. Obviously geopolitical tensions around the world – in Ukraine and the Middle East – can rock the financial markets at any time.

Below are some well-known market indices for the past fiscal year:

Annualized Returns as of June 30, 2014	One-Year	Three-Year
Domestic Equities		
S&P 500	**24.6%**	**16.6%**
Russell 1000 *(Large Cap)*	**25.4%**	**16.6%**
Russell Midcap	**26.9%**	**16.1%**
Russell 2000 *(Small Cap)*	**23.6%**	**14.6%**
Russell 3000 *(All Cap)*	**25.2%**	**16.5%**
Dow Jones Industrials	**15.6%**	**13.6%**
NASDAQ Composite	**31.2%**	**18.2%**
International & Emerging Markets Equities		
MSCI EAFE International Index	**23.6%**	**8.1%**
MSCI Emerging Markets Index	**14.7%**	**-0.1%**
Fixed Income		
Barclays U.S. Aggregate Bond Index	**4.4%**	**3.7%**
Citigroup World Govt Bond Index	**6.8%**	**1.6%**
Barclays Capital U.S. TIPS Index	**4.4%**	**3.6%**
BOA ML 91 Day T-Bills	**0.1%**	**0.1%**
Alternatives		
HFRI Fund of Funds Composite Index	**7.7%**	**3.3%**
FTSE NAREIT Equity REIT	**13.0%**	**11.9%**
Traditional Benchmarks		
60% S&P 500/40% Barclays Aggregate Bond Index	**16.2%**	**11.5%**
70% S&P 500/30% Barclays Aggregate Bond Index	**18.3%**	**12.8%**

Outlook in Key Economic Areas Affecting the Industry (Continued)

- **HEPI (Higher Education Price Index)** – HEPI, issued annually by Commonfund Institute, is an inflation index that tracks the main cost drivers in higher education. This index is a more accurate indicator of the fluctuations in costs for colleges and universities than the Consumer Price Index (CPI) because it measures the average relative level of prices in a fixed basket of goods and services purchased by colleges and universities each year through educational and general expenditures (exclusive of research). HEPI is also calculated by U.S. region. The regional HEPI numbers are calculated using the appropriate faculty salary and fringe benefit information for each region, while holding the other six HEPI cost factors constant. The chart below shows HEPI (and CPI) and the categories of operational costs included in calculating it; the South Atlantic region includes Delaware, District of Columbia, Florida, Georgia, Maryland, North Carolina, Puerto Rico, South Carolina, Virginia, and West Virginia:

Cost Factor	Weighting	Preliminary FY 2014 (7/24/2014)	Official FY2013	Official FY2012	Official FY2011	Official FY2010
Faculty salaries	35.0%	2.2%	1.7%	1.8%	1.4%	1.2%
Administrative salaries	11.0	1.1%	2.9%	2.7%	1.7%	2.0%
Clerical salaries	18.0	1.9%	1.9%	1.7%	2.0%	1.4%
Service employee salaries	8.0	1.1%	1.6%	1.1%	1.4%	1.4%
Fringe benefits	13.0	4.8%	2.9%	1.8%	3.7%	2.1%
Miscellaneous services	2.0	1.8%	1.8%	1.7%	1.8%	1.1%
Supplies and materials	6.0	11.2%	-11.7%	5.2%	8.2%	-1.3%
Utilities	7.0	8.0%	2.0%	-4.9%	4.1%	-9.5%
	100.0%					
HEPI (all institutions)		3.0%	1.6%	1.7%	2.3%	0.9%
HEPI (private baccalaureate)		Not available yet	2.2%	1.6%	1.9%	0.2%
HEPI (private master's)		Not available yet	2.3%	1.4%	1.8%	0.1%
HEPI (South Atlantic)		Not available yet	0.2%	1.2%	1.5%	0.9%
CPI (Consumer Price Index)		2.1%	1.7%	2.9%	2.0%	1.0%

Note:
We also recommend the following for the higher education and not-for-profit industry in such areas as trends and emerging issues, accounting, tax, risk management, etc. We would be happy to provide you with an electronic copy if requested:

1) ***The State of Higher Education in 2014*, Grant Thornton**
2) ***The State of the Not-for-Profit Industry in 2014*, Grant Thornton**
3) ***2014 Higher Education Update, Trends and Accounting Changes*, CapinCrouse**

Resources:

- **Various periodicals (particularly those related to higher education) including, in some cases, Internet links to articles and related research reports.**
- **Various reports from Moody's Investors Services.**
- **Various investment market, economic, and news websites, including those of Bureau of Labor Statistics, Bureau of Economic Analysis, The Conference Board, Commonfund, and various investment managers (with benchmark index returns).**