



**UNIVERSITY OF SOUTH ALABAMA**

Basic Financial Statements and Supplementary Information  
on Federal Awards Programs

Year ended September 30, 2005



**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Management's Discussion and Analysis (Unaudited)

September 30, 2005 and 2004

**Introduction**

The following discussion presents an overview of the financial position and financial activities of the University of South Alabama (the University), including the University of South Alabama Hospitals (the Hospitals), a division of the University, at September 30, 2005 and 2004 and for the years then ended. This discussion was prepared by University management and should be read in conjunction with the financial statements and notes thereto, which follow.

The basic financial statements of the University consist of the University and its component units. The financial position and results of operations of the component units are either blended with the University's financial position and results of operations or are discretely presented. The treatment of each component unit is governed by pronouncements issued by the Governmental Accounting Standards Board. As more fully described in footnote number one to the basic financial statements, the University of South Alabama Professional Liability Trust Fund and the University of South Alabama General Liability Trust Fund are reported as blended component units. The University of South Alabama Foundation and the University of South Alabama Health Services Foundation are discretely presented.

**Financial Highlights**

At September 30, 2005, 2004 and 2003, the University has total assets of \$485,986,000, \$460,180,000, and \$391,929,000, respectively; total liabilities of \$230,030,000, \$226,070,000 and \$173,737,000, respectively; and net assets of \$255,956,000, \$234,110,000 and \$218,192,000, respectively. University net assets increased \$21,846,000 during the year ended September 30, 2005 compared to increases of \$15,918,000 and \$8,871,000 in the years ended September 30, 2004 and 2003, respectively.

An overview of each statement is presented herein along with a financial analysis of the transactions impacting each statement. Where appropriate, comparative financial information is presented to assist in the understanding of this analysis.

**Analysis of Financial Position and Results of Operations**

*S a e e f N e A e*

The statement of net assets presents the assets, liabilities, and net assets of the University at September 30, 2005 and 2004. The net assets are displayed in three parts: invested in capital assets, net of related debt, restricted and unrestricted. Restricted net assets may either be expendable or nonexpendable and are those assets that are restricted by law or external donor. Unrestricted net assets, while they are generally designated for specific purposes, are available for use by the University to meet current expenses for any purpose. The statement of net assets, along with all of the University's basic financial statements, are prepared under the economic resources measurement focus and the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recognized when incurred by the University, regardless of when cash is exchanged.

Assets included in the statement of net assets are classified as current or noncurrent. Current assets consist primarily of cash and cash equivalents, investments, and hospital patient accounts receivable. Of these amounts, cash and cash equivalents, investments, and patient accounts receivable comprise approximately 20%, 44%, and 19%, respectively, of current assets at September 30, 2005. Noncurrent assets at September 30, 2005 consist primarily of capital assets.



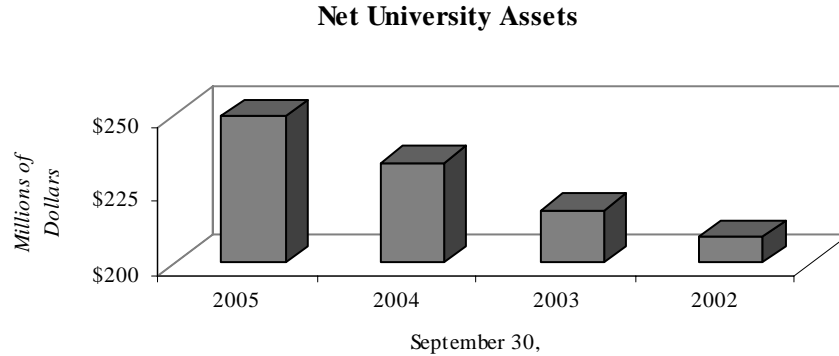


**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Management's Discussion and Analysis (Unaudited)

September 30, 2005 and 2004

Net assets of the University for the last four years are as follows:



Net assets invested in capital assets, net of related debt, increased approximately \$11,768,000 from September 30, 2004 to 2005. This increase was due primarily to increase in construction activity and the repayment of principal on notes and bonds payable. Restricted expendable net assets decreased from \$25,722,000 at September 30, 2003 to \$7,150,000 at September 30, 2004 primarily due to the release of restrictions on certain funds related to the refunding of the Series 1993 bonds. Other net assets balances were relatively constant among the 2003 to 2005 fiscal years.

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

Changes in total University net assets as reported in the statement of net assets are based on the activity presented in the statement of revenues, expenses, and changes in net assets. The purpose of this statement is to present the change in net assets resulting from revenues earned by the University, both operating and nonoperating, and the expenses incurred by the University, both operating and nonoperating, as well as any other revenues, expenses, gains, and losses earned or incurred by the University.

Generally, operating revenues have the characteristics of exchange transactions and are received or accrued for providing goods and services to the various customers and constituencies of the University. These include hospital patient care services, tuition and fees (net of scholarship discounts and allowances), most non-capital grants and contracts and revenues from auxiliary activities and sales and services of education activities (primarily athletic activities.) Operating expenses are those expenses paid or accrued to acquire or produce the goods and services provided in return for the operating revenues, and to carry out the mission of the University.

Nonoperating revenues have the characteristics of nonexchange transactions and are revenues generally earned for which goods and services are not provided, such as investment income, capital appropriations, gifts and other contributions. State appropriations are required by the Governmental Accounting Standards Board to be classified as nonoperating revenues. Nonoperating expenses are those expenses required in the operation and administration of the University, but not directly incurred to acquire or produce the goods and services provided in the return for operating revenues. Such nonoperating expenses include interest on the University's indebtedness and losses related to the disposition of capital assets.

**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Management's Discussion and Analysis (Unaudited)

September 30, 2005 and 2004

The Condensed Schedule of Revenues, Expenses, and Changes in Net Assets for the years ended September 30, 2005, 2004 and 2003 follows (in thousands):

|  | 2005       | 2004     | 2003     |
|--|------------|----------|----------|
| <b>Condensed Schedule of Revenues, Expenses,<br/>and Changes in Net Assets</b> |            |          |          |
| Operating revenues:  |            |          |          |
| Tuition and fees   | \$ 43,737  | 38,832   | 32,592   |
| Net patient service revenue  | 219,006    | 211,124  | 208,698  |
| Federal, state and private grants and contracts                                | 73,385     | 72,228   | 64,201   |
| Other  | 28,322     | 25,067   | 23,684   |
|  | 364,450    | 347,251  | 329,175  |
| Operating expenses:  |            |          |          |
| Salaries and benefits  | 307,039    | 292,089  | 276,808  |
| Supplies and other services  | 105,116    | 106,564  | 103,714  |
| Other  | 32,432     | 31,913   | 30,465   |
|  | 444,587    | 430,566  | 410,987  |
| Operating loss   | (80,137)   | (83,315) | (81,812) |
| Nonoperating revenues (expenses):  |            |          |          |
| State appropriations   | 86,622     | 84,233   | 83,846   |
| Other, net   | 5,664      | 1,807    | (828)    |
| Net nonoperating revenues  | 92,286     | 86,040   | 83,018   |
| Income before capital contributions<br>and additions to endowment              | 12,149     | 2,725    | 1,206    |
| Capital contributions and additions to endowment                               | 9,697      | 13,193   | 7,665    |
| Increase in net assets   | 21,846     | 15,918   | 8,871    |
| Beginning net assets   | 234,110    | 218,192  | 209,321  |
| Ending net assets  | \$ 255,956 | 234,110  | 218,192  |

In 2005, 2004 and 2003, approximately 60%, 61% and 63%, respectively, of operating revenues of the University were net patient service revenue. Excluding net patient service revenue, state appropriations represent the largest component of total university revenues, approximately 18% of total revenues in fiscal 2005. Also in 2005 tuition and fees charged to students and grants and contracts (federal, state and private) represented approximately 9% and 16% of total revenues, respectively.

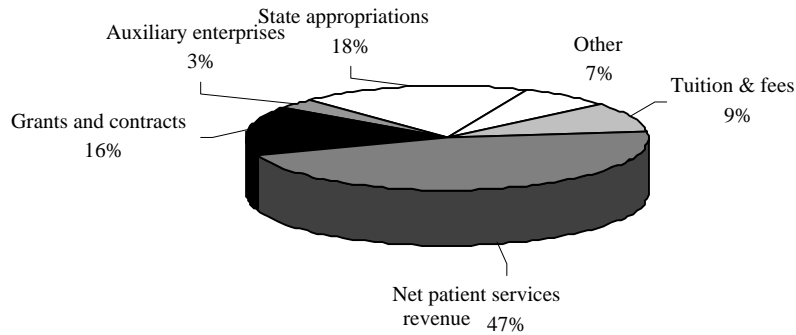
**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Management's Discussion and Analysis (Unaudited)

September 30, 2005 and 2004

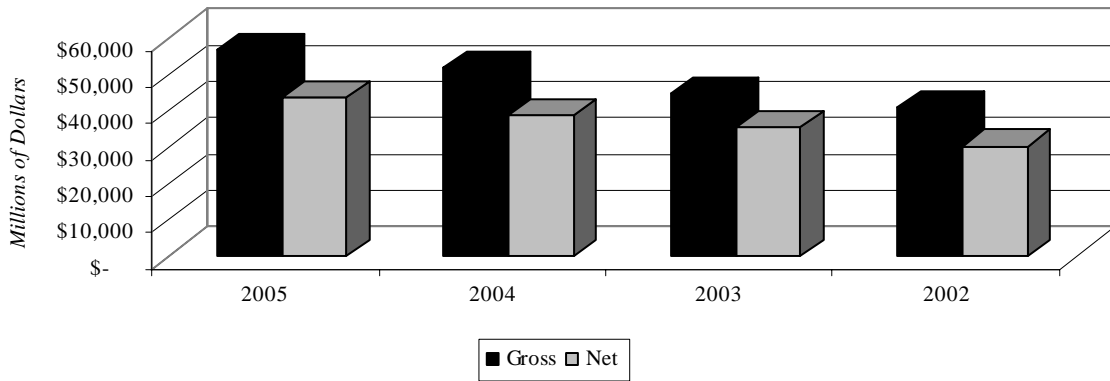
A summary of University revenues for the year ended September 30, 2005 is presented below:

**Total Revenues**



Tuition and fees have increased significantly in each of the last three years. These increases are due to increases in tuition and fee rates charged to students as well as to an increase in the number of student enrolled. Additionally, tuition and fees as a percent of total operating revenue (excluding state appropriations) continue to increase, from 9.5% of operating revenues in 2002 to 12.0% in 2005. Tuition and fees, gross and net of scholarship allowances, for the past four fiscal years are as follows:

**Tuition and Fees**





**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

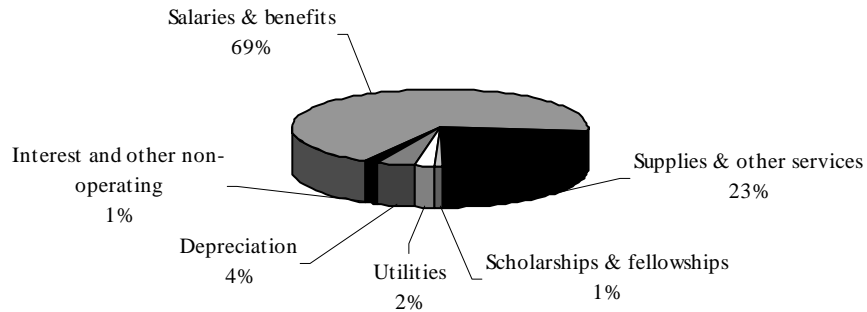
Management's Discussion and Analysis (Unaudited)

September 30, 2005 and 2004

In addition to tuition and fees, other operating revenues increased from approximately \$10,495,000 in 2004 to \$13,431,000 in 2005 primarily due to increases in patient care revenue from the USA Cancer Research Institute. Financial market conditions have resulted in a consistent increase in investment income from \$1,650,000 in 2003 to \$3,789,000 in 2004 and \$7,545,000 in 2005.

University expenses are presented using their natural expense classifications. A summary of University expenses for the year ended September 30, 2005 is presented below

**Total Expenses**



While the University reports its expenses on a natural expense classification basis, functional classifications represent expenses categorized based on the function within the University. Such University functions include instruction, research, public service, academic support, student services, institutional support, scholarships, and operation and maintenance of plant. Expenses related to auxiliary enterprise activities and the hospitals are presented separately.

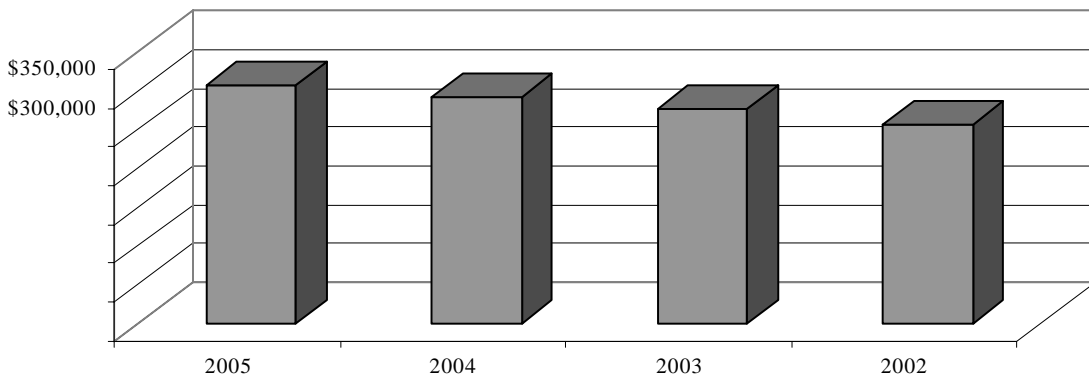
**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Management's Discussion and Analysis (Unaudited)

September 30, 2005 and 2004

In 2005, 2004 and 2003, approximately 69%, 68% and 67%, respectively, of the University's total operating expenses were salaries and benefits. Salaries and benefits have steadily increased over the last four years, resulting primarily from increases in salary rates to faculty and staff, as shown below:

**Total Salaries and Benefits Expense**

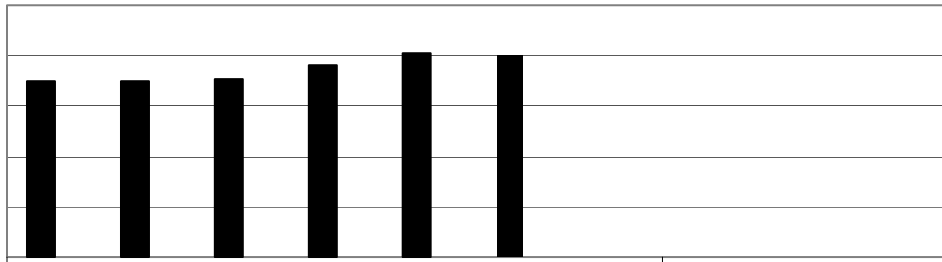


For the years ended September 30, 2005, 2004 and 2003, the University reported an operating loss of approximately \$80,137,000, \$83,315,000 and \$81,812,000, respectively. Net operating losses are offset by state appropriations which are included as nonoperating revenue. After adding state appropriations and other nonoperating revenues and expenses, (primarily capital contributions and additions to endowment) the total increase in net assets was approximately \$21,846,000, \$15,918,000 and \$8,871,000 for the years ended September 30, 2005, 2004 and 2003, respectively.

The Hospitals represent approximately half of total University revenues and expenses, which have remained relatively constant over the past four years. Operating hospital revenues and expenses for the last four fiscal years have not changed significantly and are presented below:











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**UNIVERSITY OF SOUTH ALABAMA FOUNDATION**  
(Discretely Presented Component Unit)

Consolidated Statements of Financial Position

June 30, 2005 and 2004

(In thousands)

| <b>Assets</b>                 | <b>2005</b>       | <b>2004</b>    |
|-------------------------------|-------------------|----------------|
| Cash and cash equivalents     | \$ 1,920          | 2,235          |
| Investments:                  |                   |                |
| Securities, at fair value     | 118,405           | 125,548        |
| Timber and mineral properties | 141,954           | 138,906        |
| Real estate                   | 17,256            | 16,475         |
| Accounts receivable           | 420               | 447            |
| Other assets                  | 282               | 375            |
| Total assets                  | \$ <u>280,237</u> | <u>283,986</u> |



**UNIVERSITY OF SOUTH ALABAMA  
HEALTH SERVICES FOUNDATION**  
(Discretely Presented Component Unit)

Statements of Financial Position

September 30, 2005 and 2004

(In thousands)

| <b>Assets</b>   | <b>2005</b> | <b>2004</b> |
|---|-------------|-------------|
| Current assets:   |             |             |
| Cash and cash equivalents   | \$ 243      | 513         |
| Investments   | 1,099       | 1,089       |
| Patient accounts receivable (net of allowance for uncollectible<br>accounts of approximately \$5,038 and \$4,549) | 10,115      | 6,598       |
| Other current assets  | 1,196       | 1,033       |
| Total current assets  | 12,653      | 9,233       |
| Assets limited as to use, held by trustee   | 12,165      | 9,031       |
| Property and equipment, net   | 1,287       | 1,405       |
| Total assets  | \$ 26,105   | 19,669      |
| <b>Liabilities and Deficit</b>  |             |             |
| Current liabilities:  |             |             |
| Accounts payable  | \$ 948      | 813         |
| Accrued payroll   | 178         | 240         |
| Current portion of notes payable  | 838         | 855         |
| Current portion of obligation under capital lease   | 52          | 47          |
| Due to affiliates   | 9,223       | 6,221       |
| Total current liabilities   | 11,239      | 8,176       |
| Notes payable, less current portion   | 2,370       | 3,209       |
| Obligation under capital lease, less current portion  | 47          | 103         |
| Estimated professional liability costs  | 12,165      | 9,031       |
| Total liabilities   | 25,821      | 20,519      |
| Unrestricted net assets (deficit)   | 284         | (850)       |
| Total liabilities and net assets (deficit)  | \$ 26,105   | 19,669      |

See accompanying notes to financial statements.

**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Statements of Revenues, Expenses, and Changes in Net Assets

Years ended September 30, 2005 and 2004

(In thousands)

|   |       |       |
|---|-------|-------|
| Operating revenues:   | _____ | _____ |
| Tuition and fees (net of scholarship allowances of \$12,971 and \$13,026)             |       |       |
| Net patient service revenue (net of provision for bad debts of \$74,529 and \$71,779) |       |       |
| Federal grants and contracts  |       |       |
| State grants and contracts  |       |       |
| Private grants and contracts  |       |       |
| Auxiliary enterprises (net of scholarship allowances of \$363 and \$364)              |       |       |
| Other operating revenues  | _____ | _____ |
| Total operating revenues  | _____ | _____ |
| Operating expenses:   |       |       |
| Salaries and benefits   |       |       |
| Supplies and other services   |       |       |
| Scholarships and fellowships  |       |       |
| Utilities   |       |       |
| Depreciation  | _____ | _____ |
| Total operating expenses  | _____ | _____ |
| Operating loss  | _____ | _____ |
| Nonoperating revenues (expenses):   |       |       |
| State appropriations  |       |       |
| Investment incom  |       |       |
|   | _____ | _____ |
|   | _____ | _____ |
|   | _____ | _____ |
|   | ===== | ===== |

**UNIVERSITY OF SOUTH ALABAMA FOUNDATION**  
(Discretely Presented Component Unit)

Consolidated Statement of Activities and Changes in Net Assets

Year ended June 30, 2005

(In thousands)

|  | <u>Unrestricted</u> | <u>Temporarily<br/>restricted</u> | <u>Permanently<br/>restricted</u> | <u>Total</u>   |
|--|---------------------|-----------------------------------|-----------------------------------|----------------|
| Revenues, gains, and other support:                          |                     |                                   |                                   |                |
| Net realized and unrealized gains<br>(losses) on investments | \$ 9,292            | (1,266)                           | 40                                | 8,066          |
| Rents, royalties and timber sales                            | 5,109               | —                                 | 97                                | 5,206          |
| Interest and dividends                                       | 1,724               | 984                               | 9                                 | 2,717          |
| Gifts  | 2                   | 149                               | 55                                | 206            |
| Required match of donor contributions                        | (54)                | —                                 | 54                                | —              |
| Interfund interest   | (3,645)             | 3,645                             | —                                 | —              |
| Net assets released from program<br>restrictions             | 5,055               | (5,055)                           | —                                 | —              |
| Total revenues, gains, and<br>other support                  | <u>17,483</u>       | <u>(1,543)</u>                    | <u>255</u>                        | <u>16,195</u>  |
| Expenditures:  |                     |                                   |                                   |                |
| Program services:  |                     |                                   |                                   |                |
| Faculty support  | 2,631               | —                                 | —                                 | 2,631          |
| Scholarships   | 1,019               | —                                 | —                                 | 1,019          |
| Other  | 2,563               | —                                 | —                                 | 2,563          |
| Total program service<br>expenditures                        | <u>6,213</u>        | <u>—</u>                          | <u>—</u>                          | <u>6,213</u>   |
| Management and general                                       | 2,148               | —                                 | —                                 | 2,148          |
| Other investment expense                                     | 1,300               | —                                 | —                                 | 1,300          |
| Interest expense   | 907                 | —                                 | —                                 | 907            |
| Depreciation and depletion expense                           | 5,529               | —                                 | —                                 | 5,529          |
| Total expenditures   | <u>16,097</u>       | <u>—</u>                          | <u>—</u>                          | <u>16,097</u>  |
| Increase (decrease) in<br>net assets                         | 1,386               | (1,543)                           | 255                               | 98             |
| Net assets – beginning of year                               | <u>56,880</u>       | <u>44,632</u>                     | <u>164,091</u>                    | <u>265,603</u> |
| Net assets – end of year                                     | <u>\$ 58,266</u>    | <u>43,089</u>                     | <u>164,346</u>                    | <u>265,701</u> |

See accompanying notes to financial statements.

**UNIVERSITY OF SOUTH ALABAMA FOUNDATION**  
(Discretely Presented Component Unit)

Consolidated Statement of Activities and Changes in Net Assets

Year ended June 30, 2004

(In thousands)

|   | <u>Unrestricted</u>         | <u>Temporarily<br/>restricted</u> | <u>Permanently<br/>restricted</u> | <u>Total</u>                |
|---|-----------------------------|-----------------------------------|-----------------------------------|-----------------------------|
| Revenues, gains, and other support:                 |                             |                                   |                                   |                             |
| Net realized and unrealized gains on<br>investments | \$ 24,741                   | 10,347                            | 325                               | 35,413                      |
| Rents, royalties and timber sales                   | 12,292                      | 23                                | 75                                | 12,390                      |
| Interest and dividends                              | 1,159                       | 854                               | 7                                 | 2,020                       |
| Gifts   | 3                           | 1                                 | 1                                 | 5                           |
| Required match of donor contributions               | (16)                        | —                                 | 16                                | —                           |
| Interfund interest                                  | (2,382)                     | 2,382                             | —                                 | —                           |
| Net assets released from program<br>restrictions    | 5,825                       | (5,825)                           | —                                 | —                           |
| Total revenues, gains, and<br>other support         | <u>41,622</u>               | <u>7,782</u>                      | <u>424</u>                        | <u>49,828</u>               |
| Expenditures:                                       |                             |                                   |                                   |                             |
| Program services:                                   |                             |                                   |                                   |                             |
| Faculty support                                     | 2,344                       | —                                 | —                                 | 2,344                       |
| Scholarships  | 1,009                       | —                                 | —                                 | 1,009                       |
| Other   | 3,539                       | —                                 | —                                 | 3,539                       |
| Total program service<br>expenditures               | <u>6,892</u>                | <u>—</u>                          | <u>—</u>                          | <u>6,892</u>                |
| Management and general<br>Other investment expens   | 2,289                       | —                                 | —                                 | 2,289                       |
|   | <u>                    </u> | <u>                    </u>       | <u>                    </u>       | <u>                    </u> |
|   | <u>                    </u> | <u>                    </u>       | <u>                    </u>       | <u>                    </u> |
|   | <u>                    </u> | <u>                    </u>       | <u>                    </u>       | <u>                    </u> |
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**UNIVERSITY OF SOUTH ALABAMA  
HEALTH SERVICES FOUNDATION**  
(Discretely Presented Component Unit)

Statements of Operations and Changes in Net Assets (Deficit)

Years ended September 30, 2005 and 2004

(In thousands)

|  | <b>2005</b> | <b>2004</b> |
|--|-------------|-------------|
| Unrestricted revenues, gains and other support:  |             |             |
| Net patient service revenue  | \$ 51,680   | 46,151      |
| Other revenue  | 6,688       | 6,163       |
| Total unrestricted revenues, gains and other support                                     | 58,368      | 52,314      |
| Expenses:  |             |             |
| Salaries and benefits  | 33,918      | 31,125      |
| General and administrative   | 13,418      | 13,176      |
| Provision for uncollectible accounts   | 10,377      | 9,289       |
| Depreciation and amortization  | 621         | 578         |
| Interest   | 157         | 144         |
| Total expenses   | 58,491      | 54,312      |
| Operating loss   | (123)       | (1,998)     |
| Nonoperating revenue   | 276         | 253         |
| Revenues over (under) expenses   | 153         | (1,745)     |
| Contributions restricted for debt service, received and<br>expended within the same year | 1,000       | 1,000       |
| Unrealized loss on other than trading securities   | (19)        | (22)        |
| Change in unrestricted net assets (deficit)  | 1,134       | (767)       |
| Deficit at beginning of year   | (850)       | (83)        |
| Unrestricted net assets (deficit) at end of year   | \$ 284      | (850)       |

See accompanying notes to financial statements.



**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Statements of Cash Flows

Years ended September 30, 2005 and 2004

(In thousands)

|  | <b>2005</b> | <b>2004</b> |
|--|-------------|-------------|
| Reconciliation of operating loss to net cash used in operating activities:               |             |             |
| Operating loss   | \$ (80,137) | (83,315)    |
| Adjustments to reconcile operating loss to net cash used in operating activities:        |             |             |
| Depreciation expense   | 18,661      | 17,934      |
| Changes in assets and liabilities, net:  |             |             |
| Student receivables  | (459)       | (538)       |
| Net patient accounts receivable  | (2,095)     | 1,574       |
| Grants and contracts receivables   | (1,329)     | (1,340)     |
| Student loan program receivables   | 559         | 139         |
| Other receivables  | (2,983)     | (1,961)     |
| Prepaid expenses, inventories, and other   | (597)       | 132         |
| Accounts payable and accrued liabilities   | 9,762       | (4,104)     |
| Deferred revenue   | 1,031       | 2,020       |
| Net cash used in operating activities  | \$ (57,587) | (69,459)    |
| Noncash investing, noncapital financing, and capital and related financing transactions: |             |             |
| Increase in fair value of investments recognized as a component of investment income     | \$ 1,430    | 233         |
| Additional maturity on capital appreciation bonds payable recorded as interest expense   | 1,330       | 1,265       |
| Gift of capital assets   | —           | 1,698       |
| Gift of remainder interest in real estate  | —           | 1,649       |
| Pledges of capital gifts   | —           | 480         |
| Capitalization of construction per C-1.31.1 state 200                                    |             |             |

**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

**(1) Summary of Significant Accounting Policies**

**(a) Reporting Entity**

The accompanying basic financial statements present the financial position and activities of the University of South Alabama (the University), which is a component unit of the State of Alabama.

The financial reporting entity, as defined by Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity* and amended by GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units*, consists of the primary government and all of its component units. Component units are legally separate organizations for which the primary government is financially accountable and other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the financial statements to be misleading or incomplete. Accordingly, the basic financial statements include the accounts of the University, as the primary government, and the accounts of the following entities as component units.

As of October 1, 2003, the University adopted GASB Statement No. 39 which provides criteria for determining whether certain organizations should be reported as component units based on the nature and significance of their relationship with the primary government. The statement also clarifies reporting requirements for those organizations. Based on these criteria, the University reports the University of South Alabama Foundation (USA Foundation) and the University of South Alabama Health Services Foundation (USAHSF) as discretely presented component units.

The University is also affiliated with the South Alabama Medical Science Foundation and USA Research and Technology Corporation. These entities are not considered component units of the University under the provisions of GASB Statement Nos. 14 and 39 (see note 12 for further discussion of these entities).

**(b) Professional Liability Trust Fund**

GASB Statement No. 14 requires the University, as the primary government, to include in its financial statements, as a component unit, organizations that, even though they are legally separate entities, meet certain requirements as defined by GASB Statement No. 14. The medical malpractice liability of the University is maintained and managed in a separate professional liability trust fund (the PLTF) in which the University and USAHSF are the only participants. In accordance with the bylaws of the trust fund, the president of the University is responsible for appointing members of the trust fund policy committee. Additionally, the general liability of the University is maintained and managed in a general liability trust fund (the GLTF) for which the University, as defined by GASB Statement No. 14, is responsible. The PLTF and GLTF are separate legal entities which are governed by the University Board of Trustees through the University president. As such, PLTF and GLTF are reported as blended component units.



**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

*(c) U e f S A a b a a F d a*

The USA Foundation is a not-for-profit foundation that was organized for the purpose of promoting education, scientific research and charitable purposes, and to assist in developing and advancing the University in furthering, improving and expanding its properties, services, facilities, and activities. Because of the significance of the relationship between the University and the USA Foundation, the USA Foundation is considered a component unit of the University. The Board of Directors of the USA Foundation is not appointed or controlled by the University. The University receives distributions from the USA Foundation primarily for scholarship, faculty and other support. Total distributions received or accrued by the University for the years ended September 30, 2005 and 2004 were \$6,143,000 and \$6,826,000, respectively, and are primarily included in other nonoperating revenues and capital contributions and grants in the University's statements of revenues, expenses, and changes in net assets. The USA Foundation presents its financial statements in accordance with standards issued by the Financial Accounting Standards Board (FASB). The USA Foundation is reported in separate financial statements because of the difference in the financial reporting format for the USA Foundation. The USA Foundation has a June 30 fiscal year end which differs from the University's September 30 fiscal year end. In accordance with GASB Statement No. 14, this discretely presented unit has been included with the most recent fiscal year. The consolidated statements of financial position and the consolidated statements of activities and changes in net assets for the USA Foundation as of and for the years ended June 30, 2005 and 2004 are discretely presented following the statements of net assets and statements of revenues, expenses, and changes in net assets of the University.

*(d) U e f S A a b a a H e a S e c e F d a*

The USAHSF is a not-for-profit corporation that exists to provide a group medical practice for physicians who are faculty members of the University and to further medical education and research at the University. Because of the significance of the relationship between the University and USAHSF, USAHSF is considered a component unit of the University. The USAHSF reimburses the University for salaries, certain administrative expenses and other support services. Total amounts received and accrued for such expenses were approximately \$28,959,000 and \$27,280,000 for the years ended September 30, 2005 and 2004, respectively, and are reflected as private grants and contracts in the accompanying statements of revenues, expenses, and changes in net assets of the University. The USAHSF presents its financial statements in accordance with standards issued by the FASB. The statements of financial position and the statements of operations and changes in unrestricted net assets (deficit) for the USAHSF for the years ended September 30, 2005 and 2004 are discretely presented following the statements of net assets and statements of revenues, expenses, and changes in net assets of the University.

*(e) M e e F c a d B a f A c c* **g**

**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

The University prepares its basic financial statements in accordance with accounting principles generally accepted in the United States of America, as prescribed by GASB, including all applicable effective statements of the GASB and all statements of the FASB issued through November 30, 1989

**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

incurred. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and the gain or loss, if any, is included in nonoperating revenues (expenses) in the statements of revenues, expenses, and changes in net assets.

All capital assets other than land are depreciated using the following asset lives:

|                              |                |
|------------------------------|----------------|
| Buildings and infrastructure | 40 to 50 years |
| Fixed equipment              | 10 to 20 years |
| Land improvements            | 8 to 20 years  |
| Library materials            | 10 years       |
| Other equipment              | 4 to 15 years  |

Interest costs, net of any related investment earnings, for certain assets constructed are capitalized as a component of the cost of acquiring those assets.

( ) *Deferred Revenue*

Student tuition, fees, and dormitory rentals are deferred and recognized over the applicable portion of each school term.

( ) *Capital Net Assets*

The University's net assets are classified as follows:

*Invested in capital assets, net of related debt* represents the University's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such debt is excluded from the calculation of *invested in capital assets, net of related debt*.

*Restricted, nonexpendable* net assets consist of endowment and similar type funds which donors or other outside sources have stipulated, as a condition of the gift instrument, the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to principal.

*Restricted, expendable* net assets include resources that the University is legally or contractually obligated to spend in accordance with restrictions imposed by external parties.

*Unrestricted* net assets represent resources derived from student tuition and fees, state appropriations, net patient service revenue, sales and services of educational activities and auxiliary enterprises. Auxiliary enterprises are substantially self-supporting activities that provide services for students, faculty, and staff. While unrestricted net assets may be designated for specific purposes by action of management or the Board of Trustees, they are available for use at the discretion of the governing board, to meet current expenses for any purpose. Substantially all unrestricted net assets are designated for academic and research programs and initiatives, and capital programs.

**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

When an expense is incurred that can be paid using either restricted or unrestricted resources, the University addresses each situation on a case-by-case basis prior to determining the resources to be used to satisfy the obligation.

*( ) S c a A a c e a d S d e F a c a A d*

Student tuition and fees, and certain other revenues from students, are reported net of scholarship discounts and allowances in the statements of revenues, expenses, and changes in net assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the University and the amount that is paid by students and/or third parties making payments on the students' behalf. Certain governmental grants, such as Pell grants and other federal, state, or nongovernmental programs are recorded as either operating or nonoperating revenues in the University's basic financial statements based on their classification as either an exchange or nonexchange transaction. To the extent that revenues from such programs are used to satisfy tuition and fees and certain other student charges, the University has recorded a scholarship discount and allowance.

*( ) D R e c e d E d e*

The University is subject to the "Uniform Management of Institutional Funds Act (UMIFA)" of the Code of Alabama. This law allows the University, unless otherwise restricted by the donor, to spend net appreciation, realized and unrealized, on the endowment. The University's endowment spending policy provides that 5% of the three-year invested net asset moving average value (inclusive of net realized and unrealized gains and losses), as measured at September 30, is available annually for spending. The University's policy is to retain the endowment net interest and dividend income and net realized and unrealized appreciation with the endowment after distributions allowed by the spending policy have been made. These amounts, unless otherwise directed by the donor, are included in restricted, expendable net assets.

*( ) C a f c a f R e e e*

The University has classified its revenues as either operating or nonoperating revenues.

Operating revenues include activities that have the characteristics of exchange transactions such as student tuition and fees, net of scholarship discounts and allowances; sales and services of auxiliary enterprises, net of scholarship allowances; most federal, state, and local grants and contracts; and, net patient service revenue.

Nonoperating revenues include activities that have the characteristics of nonexchange transactions,



**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

**(2) Income Taxes**

The University is classified as both a governmental entity under the laws of the State of Alabama and as a

**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

Investments of the University, by type, at fair value, are as follows at September 30, 2005 and 2004 (in thousands).

|  | <b>2005</b> | <b>2004</b> |
|--|-------------|-------------|
| U. S. Treasury notes                   | \$ 10,686   | —           |
| U. S. federal agency notes             | 78,708      | 106,974     |
| Commercial paper                       | 23,654      | —           |
| Pooled equity mutual funds             | 20,038      | 16,606      |
| Pooled debt mutual funds               | 2,143       | 3,818       |
| Managed income alternative investments | 5,744       | 1,000       |
| Collateralized mortgage obligations    | 701         | —           |
| Other                                  | 391         | 80          |
|  | \$ 142,065  | 128,478     |

At September 30, 2005 and 2004, \$1,828,000 and \$822,000, respectively, of appreciation in fair value of investments of donor-restricted endowments was recognized and are included in restricted expendable net assets in the accompanying statements of net assets.

*Credit Risk*

The University Investment Policies limit investment in corporate bonds to securities with a minimum “A” rating, at the time of purchase, by both Moody’s and Standard and Poor’s. Investments in corporate paper are limited to issuers with a minimum quality rating of P-1 by Moody’s, A-1 by Standard and Poor’s or F-1 by Fitch.

The University’s exposure to credit risk at September 30, 2005 is as follows:

|   | Credit<br>rating | % of total<br>investments |
|---|------------------|---------------------------|
| Federal National Mortgage Association         | AAA              | 24.70%                    |
| Federal Home Loan Mortgage Corporation        | AAA              | 22.80%                    |
| G. E. Capital Corporation                     | A-1              | 9.00%                     |
| Federal Home Loan Bank Corporation            | AAA              | 4.80%                     |
| Citigroup Funding, Inc.                       | A1+              | 4.20%                     |
| Toyota Motor Credit Corporation               | A1+              | 3.50%                     |
| Federal Farm Credit Banks Funding Corporation | AAA              | 3.30%                     |
| Common Fund pooled debt fund                  | AA               | 1.50%                     |
| Government National Mortgage Association      | AAA              | 0.30%                     |

**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

Concentration of Credit Risk

At September 30, 2005, more than five percent of the University's investments were invested in the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation and G. E. Capital Corporation. These investments represent approximately 25%, 23%, and 9% of the University's investments, respectively, and 23%, 21%, and 8% of the University's cash, cash equivalents and investments. The University Investment Policies require that not more than 10% of the cash, cash equivalents and investments of the University be invested in the obligations of a single private corporation and not more than 35% of the cash, cash equivalents and investments of the University be invested in the obligations of a single government agency.

Interest Rate Risk

At September 30, 2005, the maturity dates of the University's debt investments were as follows (in thousands):

|                                     | Fair<br>Value     | Years to Maturity |               |            |              |
|-------------------------------------|-------------------|-------------------|---------------|------------|--------------|
|                                     |                   | Less than 1       | 1-5           | 6-10       | More than 10 |
| U. S. Treasury notes                | \$ 10,686         | 4,606             | 6,080         | —          | —            |
| U. S. Federal agency notes          | 78,708            | 67,567            | 10,800        | 244        | 97           |
| Collateralized mortgage obligations | 701               | —                 | 9             | —          | 692          |
| Commercial paper                    | 23,654            | 23,654            | —             | —          | —            |
| Pooled debt mutual funds            | 2,143             | —                 | 2,143         | —          | —            |
|                                     | <u>\$ 115,892</u> | <u>95,827</u>     | <u>19,032</u> | <u>244</u> | <u>789</u>   |

Because the debt mutual funds had a weighted average maturity of 4.4 years at September 30, 2005, the investment was presented in the 1-5 year maturity category.

The University's Investment Policies do not specifically address the length to maturity on investments which the University must follow, however, it does require that the maturity range of investments be consistent with the liquidity requirements of the University.

Mortgage-Backed Securities

The University invests in mortgage-backed securities issued by the Government National Mortgage Association (GNMA) and the Federal National Mortgage Association (FNMA), agencies of the United States government. The University invests in these securities to increase the yield and return on its investment portfolio given the available alternative investment opportunities.

The fair value of mortgage-backed securities is generally based on the cash flows from principal and interest receipts on the underlying mortgage pools. These securities include collateralized mortgage obligations (CMOs). In CMOs, the cash flow from principal and interest payments from one or more mortgage pass-through securities or a pool of mortgages may be reallocated to multiple security classes with different priority claims and payment streams (commonly referred to as tranches). A holder of the CMO security thus chooses the class of security that best meets its risk and return objectives. CMOs are subject to significant market risk due to fluctuations in interest rates, prepayment rates and various liquidity factors related to their specific markets.



**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

**(b) U e f S A a b a a F d a**

Investments in securities consist primarily of marketable equity securities totaling \$118,405,000 and \$125,548,000, at June 30, 2005 and 2004, respectively.

Investment income was comprised of the following for the years ended June 30, 2005 and 2004 (in thousands):

|                        | <b>2005</b> | <b>2004</b> |
|------------------------|-------------|-------------|
| Unrealized gains       | \$ 853      | 30,563      |
| Realized gains         | 7,213       | 4,850       |
| Timber sales           | 4,533       | 11,857      |
| Interest and dividends | 2,717       | 2,020       |
| Rents                  | 494         | 380         |
| Royalties              | 179         | 153         |
|                        | \$ 15,989   | 49,823      |

Investment related expenses in the amount of \$358,000 and \$359,000, respectively, are included in the USA Foundation's management and general expenses in the accompanying 2005 and 2004 consolidated statements of activities and changes in net assets.

Real estate at June 30, 2005 and 2004 consisted of the following property held (in thousands):

|  | <b>2005</b> | <b>2004</b> |
|--|-------------|-------------|
| Land and land improvements – held for investment         | \$ 15,035   | 14,018      |
| Building and building improvements – held for investment | 5,072       | 5,064       |
|  | 20,107      | 19,082      |
| Less accumulated depreciation                            | 2,851       | 2,607       |
|  | \$ 17,256   | 16,475      |

Depreciation expense on real estate available for rent and occupied was \$245,000 and \$221,000 in 2005 and 2004, respectively.

Timber and mineral properties are stated at fair market value. Depletion of mineral properties is recognized over the remaining producing lives of the properties based on total estimated production and current period production. Depletion of timber properties is recognized on a specific identification basis as timber rights are sold or on a unit basis for sales made on that basis. Reforestation costs consisting of site preparation and planting of seedlings are capitalized.

**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

**(5) Capital Assets**

A summary of the University's capital asset activity for the year ended September 30, 2005 follows (in thousands):

|  | <u>Beginning<br/>balance</u> | <u>Additions</u> | <u>Transfers</u> | <u>Reductions</u> | <u>Ending<br/>Balance</u> |
|--|------------------------------|------------------|------------------|-------------------|---------------------------|
| Capital assets not being depreciated:          |                              |                  |                  |                   |                           |
| Land   | \$ 23,774                    | 112              | —                | —                 | 23,886                    |
| Construction-in-progress                       | 11,919                       | 22,865           | (6,706)          | —                 | 28,078                    |
|  | <u>35,693</u>                | <u>22,977</u>    | <u>(6,706)</u>   | <u>—</u>          | <u>51,964</u>             |
| Capital assets being depreciated:              |                              |                  |                  |                   |                           |
| Land improvements                              | 13,163                       | —                | 4,271            | —                 | 17,434                    |
| Buildings, fixed equipment, and infrastructure | 284,924                      | 125              | 672              | (117)             | 285,604                   |
| Other equipment                                | 90,649                       | 7,800            | 1,763            | (4,146)           | 96,066                    |
| Library materials                              | 33,346                       | 2,181            | —                | —                 | 35,527                    |
|  | <u>422,082</u>               | <u>10,106</u>    | <u>6,706</u>     | <u>(4,263)</u>    | <u>434,631</u>            |
| Less accumulated depreciation for:             |                              |                  |                  |                   |                           |
| Land improvements                              | (8,069)                      | (904)            | —                | —                 | (8,973)                   |
| Buildings, fixed equipment, and infrastructure | (147,211)                    | (7,424)          | —                | 111               | (154,524)                 |
| Other equipment                                | (61,429)                     | (8,636)          | —                | 3,990             | (66,075)                  |
| Library materials                              | (24,299)                     | (1,697)          | —                | —                 | (25,996)                  |
|  | <u>(241,008)</u>             | <u>(18,661)</u>  | <u>—</u>         | <u>4,101</u>      | <u>(255,568)</u>          |
| Capital assets being depreciated, net          | <u>181,074</u>               | <u>(8,555)</u>   | <u>6,706</u>     | <u>(162)</u>      | <u>179,063</u>            |
| Capital assets, net                            | <u>\$ 216,767</u>            | <u>14,422</u>    | <u>—</u>         | <u>(162)</u>      | <u>231,027</u>            |

At September 30, 2005, the University had commitments of approximately \$14,364,000 related to various construction projects.



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**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

Substantially all student tuition and fee revenues secure University bonds. Series 1996 Bonds began maturing November 2000, and are redeemable beginning May 2006, at varying premiums. Series 1999 Current Interest Bonds began maturing November 2002, and Capital Appreciation Bonds mature beginning November 2011. Series 1999 Bonds are not redeemable prior to maturity. Series 2004 Bonds began maturing in March 2005 and are redeemable beginning in March 2014.

During the years ended September 30, 2005 and 2004, the maturity value of the Capital Appreciation Bonds increased \$1,330,000 and \$1,265,000, respectively, over the original principal amount of \$19,810,000, reflecting accretion of interest.

During the year ended September 30, 2004, the University refunded the Series 1993 bonds with the proceeds from the issuance of the Series 2004 bonds. The 2004 refunding transaction resulted in an accounting loss totaling \$859,000, which has been deferred and is being amortized using the straight-line method through 2010. Aggregate cash flows from the refunding date through contractual maturity of the Series 1993 bonds totaled approximately \$25,669,000, while aggregate cash flows from refunding the Series 2004 bonds totaled approximately \$21,831,000, resulting in a positive net cash flow differential for the refunding of approximately \$3,838,000. The economic gain (generally defined as the present value of the net cash flow differential discounted at the effective interest rate of the new debt) on the 2004 refunding transaction totaled approximately \$3,427,000.

Approximately \$21,764,000 and \$29,982,000 of proceeds from the issuance of the Series 2004 Bonds remained unspent at September 30, 2005 and 2004, respectively. These amounts are included in restricted cash and cash equivalents (\$4,003,000 in 2005 and \$5,001,000 in 2004) and restricted investments (\$17,761,000 in 2005 and \$24,981,000 in 2004) on the statements of net assets and are restricted for capital purposes as outlined in the indenture.

The University defeased certain indebtedness during 1978 and 1984 by depositing funds in escrow trust accounts sufficient to provide for the subsequent payment of principal and interest on the defeased indebtedness. Neither the assets of the escrow trust accounts nor the defeased indebtedness is included in the accompanying statements of net assets. The principal outstanding on all defeased issues was \$9,040,000 at September 30, 2005.

The University is subject to restrictive covenants related to certain notes and bonds payable. At September 30, 2005, management believes the University was in compliance with such financial covenants.

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**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

On October 16, 2001, the USA Foundation entered



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**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

**(10) Employee Benefits**

*(a) Re e e a d P e P a*

Employees of the University are covered by two pension plans: a cost sharing multiple-employer defined benefit pension plan administered by the Teachers' Retirement System of the State of Alabama (TRS), and a defined contribution pension plan.

Permanent employees of the University participate in TRS, a public retirement system created by an act of the State Legislature, with benefit provisions established by the Code of Alabama. Responsibility for general administration and operation of the TRS is vested in the Board of Control (currently 14 members). Benefits fully vest after 10 years of full-time, permanent employment. Vested employees may retire with full benefits at age 60 or after 25 years of service. Participating retirees may elect the maximum benefit, or may choose among four other monthly benefit options. Under the maximum benefit, participants are allowed 2.0125% of their average final salary (average of three highest years of annual compensation during the last ten years of service) for each year of service. The TRS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the Retirement Systems of Alabama, P.O. Box 302150, Montgomery, Alabama 36130-2150, or by calling (334) 832-4140.

All employees covered by this retirement plan must contribute 5% of their eligible earnings to TRS. An actuary employed by the TRS Board of Control establishes the employer-matching amount annually. During 2005, 2004 and 2003, the University made total contributions of \$15,758,000, \$14,169,000, and \$10,467,000 (100% of the required contributions), respectively, to TRS on behalf of participants, which represents 7.03%, 6.56%, and 5.02%, respectively, of each participant's gross earnings. The University's payroll for all employees was approximately \$256,954,000 and \$241,357,000 in 2005 and 2004, respectively. Total payroll for University employees participating in the Teachers' Retirement System of Alabama was approximately \$224,158,000 and \$216,142,000 in 2005 and 2004, respectively.

The defined contribution pension plan covers certain academic and administrative employees, and participation by eligible employees is optional. Under this plan, administered by Teachers Insurance and Annuity Association – College Retirement Equities Fund (TIAA-CREF), contributions by eligible employees are matched equally by the University up to a maximum of 3% of current annual pay. The University and the employees each contributed \$789,000 and \$747,000 in 2005 and 2004, respectively, representing 428 and 412 employees participating in this Plan.



**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

The changes in the total self-insurance liabilities for the years ended September 30, 2005 and 2004 for the PLTF, GLTF and health plan are summarized as follows (in thousands):

|   | <b>2005</b> | <b>2004</b> |
|---|-------------|-------------|
| Balance, beginning of year                            | \$ 31,623   | 9,917       |
| Liabilities incurred and other additions              | 26,949      | 53,295      |
| Claims, administrative fees paid and other reductions | (24,087)    | (31,589)    |
| Balance, end of year                                  | \$ 34,485   | 31,623      |

**(12) Other Related Parties**

The South Alabama Medical Science Foundation (SAMSF) is a not-for-profit corporation that exists for the purpose of promoting education and research at the University. SAMSF reimburses the University for certain administrative expenses and other related support services. Total amounts received for such expenses were approximately \$770,000 and \$1,225,000 in 2005 and 2004, respectively, and are reflected as private grants and contracts in the accompanying statements of revenues, expenses, and changes in net assets.

The USA Research and Technology Corporation (the Corporation) is a not-for-profit corporation that exists for the purpose of furthering the educational and scientific mission of the University by developing, attracting, and retaining technology and research industries in Alabama that will provide professional and career opportunities to the University's students and faculty. During the year ended September 30, 2004, the University sold a building to the Corporation. The total amount received by the University for the building was \$10,513,000, resulting in no profit or loss to the University. Included in liabilities of the Corporation is a commercial mortgage note payable to Whitney National Bank, with annual interest of 6.00% payable monthly through January 2014. This note is not reflected in the University's statement of net assets nor is the note guaranteed by the University. The note payable is secured by a security interest in the ground lease with respect to the parcel of land on which the Corporation's building stands, a security interest in the Corporation's building, a security interest in tenant leases and a security interest in income received by the Corporation for rental of the building.

**(13) Commitments and Contingencies**

**(a) Grants and Contracts**

At September 30, 2005 and 2004, the University had been awarded approximately \$32,400,000 and \$32,542,000, respectively, in grants and contracts for which resources had not been received and for which reimbursable expenditures had not been made for the purposes specified. These awards, which represent commitments of sponsors to provide funds for research or training projects, have not been reflected in the accompanying basic financial statements as the eligibility requirements of the award have not been met. Advances include amounts received from grant and contract sponsors which have not been earned under the terms of the agreements and, therefore, have not yet been included in revenues in the accompanying basic financial statements. Federal awards are subject to audit by





**UNIVERSITY OF SOUTH ALABAMA**  
(A Component Unit of the State of Alabama)

Notes to Basic Financial Statements

September 30, 2005 and 2004

**(16) In August 2005, the University and Infirmity Health System, Inc. (IHS) entered into a memorandum of Subsequent Event**

understanding regarding the development of a formal relationship between the University and IHS. The provisions of the memorandum were to execute a long-term lease of USA Knollwood Hospital to IHS, to relocate the USA Cancer Research Institute to property procured by the University from IHS near the Mobile Infirmity and USA Children's and Women's Hospital, and to expand the role of IHS in medical education. While certain costs may be required by the University related to the potential relocation of the USA Cancer Research Institute to the new location, such costs have not been recognized in the University's 2005 basic financial statements and will be recognized when a formal agreement between the parties is executed.

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
AND OMB CIRCULAR A-133 REPORTS**



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**UNIVERSITY OF SOUTH ALABAMA**  
Schedule of Expenditures of Federal Awards  
Year ended September 30, 2005

| <b>Federal Grantor/ Pass-Through Grantor/<br/>Program or Cluster Title</b>                           | <b>Federal<br/>CFDA<br/>Number</b> | <b>Federal<br/>Expenditures</b> |
|--|------------------------------------|---------------------------------|
| Environmental Protection Agency:<br>Environmental Protection Comprehensive Research Grants           | 66.500                             | \$ 666,829                      |
| U.S. Department of Commerce:<br>Habitat Conservation   | 11.463                             | 690,018                         |
| Centers for Disease Control:<br>Squirrel Monkey  | 93.200-203-<br>01848               | 72,618                          |
| U.S. Department of Defense:<br>Basic and Applied Scientific Research                                 | 12.300                             | 34,261                          |
| Basic Scientific Research  | 12.431                             | 71,015                          |
| Military Medical Research and Development  | 12.420                             | 23,680                          |
| U.S. Department of Energy:<br>Office of Science Financial Assistance Program                         | 81.049                             | 30,923                          |
| Renewal Energy Research and Development  | 81.087                             | 529,496                         |
| U.S. Department of Transportation:<br>University Transportation Centers Program                      | 20.701                             | 508,219                         |
| State and Community Highway Safety   | 20.600                             | (61)                            |
| U.S. Department of Interior:<br>National Cooperative Geologic Mapping Program                        | 15.810                             | 1,530                           |
| U.S. Department of Agriculture:<br>Competitive Research Grants                                       | 10.206                             | 12,446                          |
| U.S. Department of Justice:<br>National Institute for Juvenile Justice and Delinquency<br>Prevention | 16.542                             | 920,566                         |
| Total direct programs  |                                    | <u>16,225,860</u>               |

**UNIVERSITY OF SOUTH ALABAMA**  
Schedule of Expenditures of Federal Awards  
Year ended September 30, 2005

| <b>Federal Grantor/ Pass-Through Grantor/<br/>Program or Cluster Title</b> | <b>Federal<br/>CFDA<br/>Number</b> | <b>Federal<br/>Expenditures</b> |
|--|------------------------------------|---------------------------------|
| Pass-through programs:   |                                    |                                 |
| Pass-through from National Institutes of Health:                           |                                    |                                 |
| Educational Development Center, Inc.                                       | 93.273                             | \$ 170                          |
| University of Pennsylvania   | 93.213                             | 145,125                         |
| Sequella, Inc.   | 93.371                             | 75,277                          |
| Mallard Medical, Inc.  | 93.838                             | 1,276                           |
| Rockefeller University   | 93.839                             | 14,184                          |
| Emory University   | 93.839                             | 17,820                          |
| University of Miami  | 93.846                             | 16,292                          |
| National Childhood Cancer Foundation                                       | 93.395                             | 19,909                          |
| University of Texas  | 93.853                             | 57,984                          |
| University of Alabama at Birmingham  | 93.865                             | (1,297)                         |
| University of Maryland   | 93.879                             | 1,713                           |
| Pass-through from National Science Foundation:                             |                                    |                                 |
| Florida State University   | 47.049                             | 8,954                           |
| University of Georgia  | 47.074                             | 2,923                           |
| University of Alabama  | 47.076                             | 22,003                          |
| University of Alabama in Huntsville  | 47.076                             | 16,447                          |
| Tuskegee University  | 47.076                             | 41,459                          |
| Bigelow Laboratory for Ocean Sciences                                      | 47.078                             | 52,169                          |
| University of Alabama  | 43.002                             | 98,509                          |
| University of Alabama in Huntsville  | 43.002                             | (900)                           |
| Pass-through from U.S. Department of Commerce:                             |                                    |                                 |
| University of Southern Mississippi   | 11.417                             | 62,747                          |
| Alabama Department of Conservation and Natural Resources                   | 11.419                             | 204,299                         |
| Alabama Department of Emergency Management                                 | 11.419                             | 13,136                          |
| Pass-through from U.S. Department of Interior:                             |                                    |                                 |
| Alabama Department of Conservation and Natural Resources                   | 15.605                             | 57,243                          |
| Friends of Old Mobile  | 15.923                             | 33,400                          |
| Louisiana State University   | 15.000                             | 2,334                           |
| Pass-through from U.S. Department of Health and Human<br>Services:         |                                    |                                 |
| Sickle Cell Foundation of Greater Montgomery                               | 93.110                             | 1,356                           |
| Sickle Cell Disease Association  | 93.110A                            | (26)                            |
| Northrop Grumman   | 93.243                             | 134,735                         |
| Florida State University   | 93.969                             | 12,357                          |
| Pass-through from U.S. Department of Transportation:                       |                                    |                                 |
| Volkert and Associates, Inc.   | 20.205                             | 3,800                           |
| University of Alabama at Birmingham  | 20.OGCA-<br>180122                 | 46,725                          |

UNIVERSITY OF SOUTH ALABAMA

Schedule of Expenditures of Federal Awards

Year ended September 30, 2005

|   | Federal<br>CFDA<br>Number | Federal |
|---|---------------------------|---------|
|   |                           |         |
|   | 81.2328                   | \$      |
|   | 81.B529446                |         |
|   | 81.40000                  |         |
|   | 313330                    |         |
| Pass-through from U.S. Department of Housing and<br>Development:  |                           |         |
| The Mitchell Company  |                           |         |
| Mobile County Commission  |                           |         |
| Mobile Fair Housing Center  |                           |         |
| Pass-through from Environmental Protection Agency:<br>Mobile Water and Sewer Service  |                           |         |
| Pass-through from Environmental Improvement Restoration Fund<br>Prince William Sound Science Center   |                           |         |
| Pass-through from Exxon Valdez Oil Spill Trustee Council:<br>Prince William Sound Science Center<br>Prince William Sound Science Center             |                           |         |
| Pass-through from U.S. Department of Defense:<br>University of Colorado<br>University of Washington<br>Naval Research Laboratory<br>Yale University |                           |         |
| Radiance Technologies, Inc.<br>Clemson University   |                           |         |
| Pass-through from NASA:   |                           |         |
| Department of Education.<br>Student Support Services<br>Talent Search<br>Trio Upward Bound  |                           |         |

**UNIVERSITY OF SOUTH ALABAMA**

Schedule of Expenditures of Federal Awards

Year ended September 30, 2005

| <b>Federal Grantor/ Pass-Through Grantor/<br/>Program or Cluster Title</b>                 | <b>Federal<br/>CFDA<br/>Number</b> | <b>Federal<br/>Expenditures</b> |
|--|------------------------------------|---------------------------------|
| U.S. Department of Health and Human Services:  |                                    |                                 |
| Maternal and Child Health Federal Consolidated Programs                                    | 93.110                             | \$ 663,479                      |
| Rural Telemedicine Grants  | 93.211                             | 32,727                          |
| Advanced Education Nursing Grant Programs  | 93.247                             | 371,625                         |
| Advanced Education Nursing Traineeships  | 93.358                             | 210,022                         |
| Basic Nurse Education and Practice Grants  | 93.359                             | 328,099                         |
| U.S. Department of Energy:   |                                    |                                 |
| Office of Science Financial Assistance Program   | 81.049                             | 2,245,856                       |
| Health Resources and Services Administration:  |                                    |                                 |
| Community Based Abstinence Education   | 93.010                             | 116,887                         |
| Grants for Residency Training for General Pediatrics                                       | 93.884                             | 56,482                          |
| Specially Selected Health Projects   | 93.888                             | 536,463                         |
| Coordinated HIV Services and Access to Research for<br>Children, Youth, Women and Families | 93.153                             | 315,677                         |
| National Institutes of Health:   |                                    |                                 |
| Medical Library Assistance   | 93.879                             | 99                              |
| National Science Foundation:   |                                    |                                 |
| Education and Human Resources  | 47.076                             | 89,593                          |
| Biological Sciences  | 47.074                             | 95,103                          |
| U. S. Department of Housing and Urban Development  |                                    |                                 |
| Community Development Block Grants - Economic<br>Development Initiative                    | 14.246                             | 462,261                         |
| Centers for Disease Control:   |                                    |                                 |
| Investigation and Technical Assistance   | 93.283                             | 263,707                         |
| U.S. Department of Justice:  |                                    |                                 |
| Community Prosecution and Project Safe Neighborhoods                                       | 16.609                             | 45,137                          |
| Byrne Formula Grant Program  | 16.579                             | 10,110                          |
| U.S. Agency for International Development:   |                                    |                                 |
| USAID Foreign Assistance for Programs Overseas   | 98.001                             | 286,065                         |
| U.S. Department of Transportation:   |                                    |                                 |
| National Motor Carrier Safety  | 20.218                             | 352,937                         |
| Federal Transit – Capital Investment Grants  | 20.500                             | 3,049,956                       |
| Americorp:   |                                    |                                 |
| Corporation of National and Community Service  | 94.006                             | 20,131                          |
| Total direct programs  |                                    | <u>10,198,791</u>               |

**UNIVERSITY OF SOUTH ALABAMA**

Schedule of Expenditures of Federal Awards

Year ended September 30, 2005

| <b>Federal Grantor/ Pass-Through Grantor/<br/>Program or Cluster Title</b> | <b>Federal<br/>CFDA<br/>Number</b> | <b>Federal<br/>Expenditures</b> |
|--|------------------------------------|---------------------------------|
| Pass-through programs:   |                                    |                                 |
| Pass-through from U.S. Department of Education:                            |                                    |                                 |
| Alabama Department of Education  |                                    |                                 |
| Lamar County Board of Education  |                                    |                                 |
| Alabama Department of Education  |                                    |                                 |
| Alabama Department of Education  |                                    |                                 |
| Alabama Department of Rehabilitation Services                              |                                    |                                 |
| Alabama Commission on Higher Education                                     |                                    |                                 |
| Alabama Department of Education  |                                    |                                 |
| National Writing Project   |                                    |                                 |
| Alabama Department of Education  |                                    |                                 |
| Alabama Department of Education  |                                    |                                 |
| Mobile County Public Schools   |                                    |                                 |

**UNIVERSITY OF SOUTH ALABAMA**  
Schedule of Expenditures of Federal Awards  
Year ended September 30, 2005

| <b>Federal Grantor/ Pass-Through Grantor/<br/>Program or Cluster Title</b> | <b>Federal<br/>CFDA<br/>Number</b> | <b>Federal<br/>Expenditures</b> |
|--|------------------------------------|---------------------------------|
| Pass-through from U.S. Department of Health and Human Services:            |                                    |                                 |
| Alabama Department of Rehabilitative Services                              | 93.110                             | \$ 6,838                        |
| Sickle Cell Foundation of Greater Montgomery                               | 93.110A                            | 1,870                           |
| Administration on Aging  | 93.048                             | 9,950                           |
| University of Alabama  | 93.648                             | 11,572                          |
| Alabama Department of Public Health  | 93.153                             | 258,358                         |
| Alabama Department of Public Health  | 93.003                             | 642,170                         |
| Alabama Department of Public Health  | 93.283                             | 108,174                         |
| Total pass-through programs  |                                    | <u>3,482,878</u>                |
| Total other federal assistance   |                                    | <u>13,681,669</u>               |
| Total federal expenditures   |                                    | <u>\$ 102,366,633</u>           |

\* Denotes major program.

See accompanying notes to schedule of expenditures of federal awards.

See accompanying independent auditors' report on supplementary information.

**UNIVERSITY OF SOUTH ALABAMA**

Notes to Schedule of Expenditures of Federal Awards

September 30, 2005

**(1) Basis of Presentation**

The accompanying schedule of expenditures of federal awards includes the federal grant activity of University of South Alabama (the University) and is presented in accordance with accounting principles generally accepted in the United States of America. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

Expenditures listed on the accompanying schedule of expenditures of federal awards, except for Perkins Loans, Federal Family Educational Loan (FFEL) Programs, Parent Loans-PLUS loans, Loans to Disadvantaged Students and Health Education Assistance Loans (HEAL), represent actual expenditures incurred under the accrual basis of accounting for the year ended September 30, 2005. The loan programs representing loans made by the University are included in notes receivable in the accompanying 2005 statement of net assets and consist of the following:

|   |                            |
|---|----------------------------|
| Perkins loan program  | \$ 4,025,610               |
| Loans to disadvantaged students                             | 9,661                      |
| Health professional loans                                   | <u>230,643</u>             |
|   | 4,265,914                  |
| Less outstanding balance of loans granted in previous years | <u>(3,108,111)</u>         |
| New loans granted to eligible students of the University    | <u><u>\$ 1,157,803</u></u> |

The FFEL and HEAL federal awards represent loans received by students of the University during fiscal year 2005 which were not made by the University. Accordingly, FFEL and HEAL amounts are not reflected in the University's basic financial statements.

**(2) Contingencies**

These federal programs are subject to financial and compliance audits by grantor agencies which, if instances of material noncompliance are found, may result in disallowed expenditures and affect the University's continued participation in specific programs.



**UNIVERSITY OF SOUTH ALABAMA**

Notes to Schedule of Expenditures of Federal Awards

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**UNIVERSITY OF SOUTH ALABAMA**

Notes to Schedule of Expenditures of Federal Awards

September 30, 2005

**(5) Subrecipients**

Of the federal expenditures presented in the schedule of expenditures of federal awards, the University provided federal awards to subrecipients under the following programs:

|  | <u>Federal<br/>CFDA #</u> |    | <u>Amounts<br/>expended</u> |
|--|---------------------------|----|-----------------------------|
| Direct programs:   |                           |    |                             |
| Competitive Research Grants  | 10.206                    | \$ | 10,423                      |
| Habitat Conservation   | 11.463                    |    | 145,818                     |
| University Transportation Center   | 20.701                    |    | 2,450                       |
| Environmental Protection Comprehensive<br>Research Grants                                | 66.500                    |    | 234,459                     |
| Community Based Abstience Education  | 93.010                    |    | 82,829                      |
| Adolecesent Family Life Research Grants  | 93.110                    |    | 513,949                     |
| Biological Response to Environmental Health Hazard                                       | 93.113                    |    | 83,443                      |
| Coordinated Services for Access to Research for Women,<br>Infants, Children and Youth    | 93.153                    |    | 2,923                       |
| Heart and Vascular Disease Research  | 93.837                    |    | 23,995                      |
| Lung Disease Research  | 93.838                    |    | 82,683                      |
| Aging Research   | 93.866                    |    | 43,490                      |
| Pass-through programs:   |                           |    |                             |
| U.S. Department of Health and Human Services/<br>Northrop Grumman                        | 93.243                    |    | 22,855                      |
| U. S. Department of Commerce/Alabama Department<br>of Conservation and Natural Resources | 11.419                    |    | 37,617                      |
| U.S. Department of Interior/Friends of Old Mobile  | 15.923                    |    | 9,290                       |
| U.S. Department of Health and Human Services/<br>Alabama Department of Public Health     | 81.087                    |    | 179,222                     |
| U.S. Department of Health and Human Services/<br>Alabama Department of Public Health     | 93.003                    |    | 42,762                      |
| U.S. Department of Health and Human Services/<br>Alabama Department of Public Health     | 93.283                    |    | 6,094                       |
| U. S. Department of Education/Alabama<br>Department of Education                         | 84.366B                   |    | 401,316                     |
| U. S. Department of Education/Alabama<br>Commission on Higher Educations                 | 84.367B                   |    | 43,031                      |
|  |                           | \$ | <u><u>1,968,649</u></u>     |



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**Independent Auditors' Report on Internal Control Over Financial Reporting and on  
Compliance and Other Matters Based on an Audit of Financial Statements Performed in  
Accordance *W G e e A d g S a d a d***

The Board of Trustees



This report is intended solely for the information and use of the board of trustees, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

November 11, 2005



**KPMG LLP**  
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## **Independent Auditors' Report on Compliance With Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance With OMB Circular A-133**

The Board of Trustees  
University of South Alabama:

### *C a c e*

We have audited the compliance of the University of South Alabama (the University) with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement (Compliance Supplement)* that are applicable to each of its major federal programs for the year ended September 30, 2005, except those requirements discussed in the third following paragraph. The University's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the University's management. Our responsibility is to express an opinion on the University's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the University's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the University's compliance with those requirements.

In our opinion, the University complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 2005, other than those requirements discussed in the following paragraph. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as item 2005-1, 2005-2 and 2005-3.

We did not audit the University's compliance with requirements governing maintaining contact with and billing borrowers and processing deferment and cancellation requests and payments for the Federal Perkins Loan Program. Those requirements govern functions that are performed by Affiliated Computer Services, Inc. (ACS). Since we did not apply auditing procedures to satisfy ourselves as to compliance with those requirements, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on compliance with those requirements.



ACS's compliance with the requirements governing the functions that it performs for the University was examined by accountants for the servicer whose report has been furnished to us. The report of the accountants for the servicer indicates that compliance with those requirements was examined in accordance with the Department of Education's Audit Guide, *Compliance Audits (Attestation Engagements) of Federal Student Financial Assistance Programs at Participating Institutions and Institution Servicers*. Based on our review of the service organization accountants' report, we have determined that all of the compliance requirements included in the *Compliance Supplement* that are applicable to each of the major programs in which the University participates are addressed in either our report or the report of the service organization accountants. Further, based on our review of the service organization accountants' report, we have determined that it does not contain any findings of noncompliance that would have a direct and material effect on the University's major programs.

*I e a C      O e C      a c e*

The management of the University is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the University's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Requirements governing maintaining contact with and billing borrowers and processing deferment and cancellation requests and payments for the Federal Perkins Loan Program are performed by ACS. Internal control over compliance relating to such functions was reported on by accountants for the servicer in accordance with the Department of Education's Audit Guide, *Compliance Audits (Attestation Engagements) of Federal Student Financial Assistance Programs at Participating Institutions and Institution Servicers*. A copy of the service organization accountants' report has been furnished to us. However, the scope of our work did not extend to internal control maintained at ACS.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the board of trustees, management and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

*KPMG LLP*

November 11, 2005

**UNIVERSITY OF SOUTH ALABAMA**

Schedule of Findings and Questioned Costs

Year ended September 30, 2005

I – Summary of Auditors’ Results

*Financial Statements*

Type of auditors’ report issued: Unqualified

Internal control over financial reporting:

Material weakness(es) identified? \_\_\_\_\_yes  X no

Reportable condition(s) identified that are not considered to be material weaknesses? \_\_\_\_\_yes  X none reported

Noncompliance material to financial statements noted? \_\_\_\_\_yes  X no

*Federal Awards*

Internal control over major programs:

Material weakness(es) identified? \_\_\_\_\_yes  X no

Reportable condition(s) identified that are not considered to be material weaknesses? \_\_\_\_\_yes  X none reported

Type of auditors’ report issued on compliance for major program: Unqualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133?  X yes \_\_\_\_\_no

Identification of major programs:

| <i>CFDA Numbers</i>                    | <i>Name of Federal Program or Cluster</i> |
|--|---|
| 84.063, 84.007, 84.032, 84.033, 84.038 | Student Financial Aid Cluster             |
| Various                                | Research and Development Cluster          |

Dollar threshold used to distinguish between type A and type B programs: \_\_\_\_\_\$3,000,000\_\_\_\_\_

Auditee qualified as low-risk auditee?  X yes \_\_\_\_\_no





**UNIVERSITY OF SOUTH ALABAMA**

Schedule of Findings and Questioned Costs

Year ended September 30, 2005

Section III – Federal Award Findings and Questioned Costs relating to Federal Awards

**Finding No. 2005-01**

**Equipment and Real Property Management**

**Research and Development Cluster**

*Criteria*

OMB Circular A-110 requires that property records contain the following information about equipment purchased with federal funds: description, source, title holders, acquisition date and cost, percentage of federal participation in the cost, location, condition and any ultimate disposal costs.

*Condition*

The University did not tag three federal equipment purchases.

*Questioned Costs*

None

*Context*

The University should strengthen its internal control procedures related to cash management to ensure that federal funds are properly approved before being recorded in the general ledger.

*Condition*

The University did not properly document approval of the journal entries to record the federal drawdown before the journal entries were sent to the Business Office.

*Questioned Costs*

None

*Context*

During our review of the internal controls over cash management, thirty journal entries were reviewed to test proper approval and we noted sixteen exceptions, all of which were related to research and development expenditures.

*Effect*

The University is not in compliance with its internal control policies regarding documentation of approval of journal entries.

*Recommendation*

The University should ensure that appropriate personnel in Grants and Contracts Accounting review and document approval of journal entries before being sent to the Business Office for input into the general ledger.

*Management Views*

All journal entries noted above were approved prior to being input into the general ledger. The review on the sixteen items noted, however, was performed only by Business Office personnel. Management will implement procedures to ensure that journal entries are approved in Grants and Contracts Accounting and that these approvals are adequately documented prior to submitting the entries to the Business Office.

**Finding No. 2005-03**

**Cash Management**

**Research and Development Cluster**

*Criteria*

The University should strengthen its internal control procedures regarding documentation of approval of federal expenditure drawdown requests.

*Condition*

The University did not document approval of federal drawdowns before the drawdowns were requested.

*Questioned Costs*

None

*Context*