



**FRANKLIN W. OLIN COLLEGE OF ENGINEERING, INC.**

Financial Statements

June 30, 2003 and 2002

(With Independent Auditors' Report Thereon)



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## Independent Auditors' Report

The Board of Trustees  
Franklin W. Olin College of Engineering, Inc.:

We have audited the accompanying statements of financial position of the Franklin W. Olin College of Engineering, Inc. (the College) as of June 30, 2003 and 2002, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the College's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the College at June 30, 2003 and 2002, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

September 30, 2003



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**FRANKLIN W. OLIN COLLEGE OF ENGINEERING, INC.**

Statements of Financial Position

June 30, 2003 and 2002

<b>Assets</b>	<b>2003</b>	<b>2002</b>
Cash	\$ 903,625	1,294,617
Short-term investments	3,496,993	3,196,757
Interest and dividends receivable	52,428	—
Other current assets	461,719	309,637
Loan receivable	200,000	—
Contributions receivable from F.W. Olin Foundation (notes 8 and 9)	216,059,863	—
Long-term investments (note 3)	29,848,645	—
Property and equipment, net (note 4)	122,350,295	102,636,231
Total assets	<u>\$ 373,373,568</u>	<u>107,437,242</u>
<b>Liabilities and Net Assets</b>		
Liabilities:		
Accounts payable and accrued expenses	\$ 5,231,585	4,276,610
Deferred revenue and deposits	470,497	418,254
Total liabilities	<u>5,702,082</u>	<u>4,694,864</u>
Net assets (deficit):		
Unrestricted	(511,391)	1,070,003
Temporarily restricted (note 9)	351,859,031	85,378,137
Permanently restricted (note 9)	16,323,846	16,294,238
Total net assets	<u>367,671,486</u>	<u>102,742,378</u>
Total liabilities and net assets	<u>\$ 373,373,568</u>	<u>107,437,242</u>

See accompanying notes to financial statements.

**FRANKLIN W. OLIN COLLEGE OF ENGINEERING, INC.**

Statements of Activities

Years ended June 30, 2003 and 2002

	2003				2002			
	Unrestricted	Temporarily restricted	Permanently restricted	Total	Unrestricted	Temporarily restricted	Permanently restricted	Total
Revenues and other support:								
Contributions from								
Foundation (note 8)	\$ 5,803,912	257,827,426	—	263,631,338	9,742,653	48,150,524	5,000	57,898,177
Change in fair value of contributions receivable from Foundation (note 8)	—	15,429,505	—	15,429,505	—	—	—	—
Contributions from others	127,985	81,857	29,608	239,450	2,900	55,425	26,600	84,925
Grants	1,465,148	—	—	1,465,148	1,016,451	—	—	1,016,451
Fees, net	484,227	—	—	484,227	30,540	—	—	30,540
Interest and dividend income	19,669	201,818	—	221,487	40,905	50,822	—	91,727
Net unrealized gains on long-term investments	—	2,986,505	—	2,986,505	—	—	—	—
Other	91,366	—	—	91,366	23,515	—	—	23,515
Net assets released from restrictions (note 9)	10,046,217	(10,046,217)	—	—	171,404	(171,404)	—	—
Total revenues and other support	18,038,524	266,480,894	29,608	284,549,026	11,028,368	48,085,367	31,600	59,145,335
Expenses (note 6):								
Instruction	3,873,317	—	—	3,873,317	2,817,028	—	—	2,817,028
Academic support	2,711,656	—	—	2,711,656	1,448,626	—	—	1,448,626
Student services	3,991,290	—	—	3,991,290	1,364,102	—	—	1,364,102
Research	784,190	—	—	784,190	557,788	—	—	557,788
Sponsored programs	1,444,197	—	—	1,444,197	1,150,366	—	—	1,150,366
Institutional support	6,815,268	—	—	6,815,268	4,363,758	—	—	4,363,758
Total expenses	19,619,918	—	—	19,619,918	11,701,668	—	—	11,701,668
Net assets reclassified (note 8)	—	—	—	—	(51,850,901)	37,246,388	14,604,513	—
(Decrease) increase in net assets	(1,581,394)	266,480,894	29,608	264,929,108	(52,524,201)	85,331,755	14,636,113	47,443,667
Net assets at beginning of year	1,070,003	85,378,137	16,294,238	102,742,378	53,594,204	46,382	1,658,125	55,298,711
Net assets (deficit) at end of year	\$ (511,391)	351,859,031	16,323,846	367,671,486	1,070,003	85,378,137	16,294,238	102,742,378

See accompanying notes to financial statements.

**FRANKLIN W. OLIN COLLEGE OF ENGINEERING, INC.**

Statements of Cash Flows

Years ended June 30, 2003 and 2002

	<b>2003</b>	<b>2002</b>
Cash flows from operating activities:		
Increase in net assets	\$ 264,929,108	47,443,667
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation	3,781,960	171,404
Net unrealized gains on long-term investments	(2,986,505)	—
Securities received under contributions receivable from Foundation	(26,745,260)	—
Contributions from Foundation restricted for acquisition and construction of property and equipment	(22,235,000)	(48,155,524)
Contributions from others restricted for long-term investment	—	(26,600)
Increase in interest and dividends receivable	(52,428)	—
Increase in other assets	(152,082)	(147,972)
Increase in contributions receivable from Foundation	(216,059,863)	—
Increase in operating accounts payable and accrued expenses	241,456	936,059
Increase in deferred revenue and deposits	52,243	198,559
Net cash provided by operating activities	773,629	419,593
Cash flows from investing activities:		
Increase in loan receivable	(200,000)	—
Purchases of short-term investments	(417,116)	(387,883)
Cash paid for acquisition and construction of property and equipment	(22,782,505)	(48,155,524)
Net cash used by investing activities	(23,399,621)	(48,543,407)
Cash flows from financing activities:		
Contributions from others restricted for long-term investment	—	26,600
Contributions from Foundation restricted for acquisition and construction of property and equipment	22,235,000	48,155,524
Net cash provided by financing activities	22,235,000	48,182,124
Net (decrease) increase in cash	(390,992)	58,310
Cash at beginning of year	1,294,617	1,236,307
Cash at end of year	\$ 903,625	1,294,617

See accompanying notes to financial statements.

# FRANKLIN W. OLIN COLLEGE OF ENGINEERING, INC.

## Notes to Financial Statements

June 30, 2003 and 2002

### (1) Organization

The Franklin W. Olin College of Engineering, Inc. (the College) was founded by the F. W. Olin Foundation, Inc. (the Foundation) in 1997 in response to a national agenda for the advancement of engineering education in the 21<sup>st</sup> century. The College ran a "Partners Program" for the academic year starting in Fall 2001 with a team of 30 students who assisted in developing and testing the curriculum and certain aspects of campus culture. The College officially opened its new campus in Fall 2002 and welcomed the inaugural freshman class of 75 students. In Fall 2003, there will be approximately 150 students, with the ultimate total enrollment expected to be 600 to 650 students. The College offers undergraduate programs in engineering, electrical and computer engineering and mechanical engineering.

Operations to date include the planning, design, and construction of the physical campus, hiring faculty and other administrators, designing the academic and operational aspects of the College, and delivering the first-year curriculum.

While the College maintains its own independent financial resources, governance, identity, and style, a collaborative relationship exists between the College and the adjacent Babson College. The two colleges cooperate in academic programming and share certain facilities and services. The College pays Babson College a fee for certain administrative and programmatic services and other associated expenses. Such fees were \$1,937,340 and \$1,273,243 in 2003 and 2002, respectively, and have been included in institutional support in the accompanying statements of activities.

### (2) Summary of Significant Accounting Policies

#### (a) Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting. Net assets and revenues, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified as follows:

#### *Permanently Restricted Net Assets*

Net assets subject to donor-imposed stipulations that they be maintained in perpetuity by the College. The donors of these assets permit the College to use all or part of the related investment income and appreciation earned, as applicable, for general or specific purposes.

#### *Temporarily Restricted Net Assets*

Net assets subject to donor-imposed stipulations, or law, that may or will be met by actions of the College and/or the passage of time.

#### *Unrestricted Net Assets*

Net assets not subject to donor-imposed stipulations which the College may use at its discretion.

Revenues are reported as increases in unrestricted net assets unless use of the related net assets is limited by donor-imposed restrictions, including time restrictions. Expenses are reported as decreases in unrestricted net assets. The College reports all temporarily restricted contributions as increases to that net asset class and reclassifies them to unrestricted net assets when the restrictions are met,

**FRANKLIN W. OLIN COLLEGE OF ENGINEERING, INC.**

Notes to Financial Statements

June 30, 2003 and 2002

regardless of when the contribution is received. Expirations of temporary restrictions on net assets are reported as reclassifications between the applicable classes of net assets. Expirations of temporary restrictions occur when donor-imposed stipulated purposes have been accomplished and/or the stipulated time period has elapsed. Contributions restricted for the purchase of land are reported as permanently or temporarily restricted net assets, depending on the donor's intent. To the extent such contributions are temporarily restricted, the restrictions are released when the amounts are expended for land. Contributions restricted for the acquisition or construction of buildings and equipment are reported as increases in temporarily restricted net assets and are reclassified to unrestricted net assets over the useful lives of the related assets. If an expense is incurred for a purpose for which both unrestricted and temporarily restricted net assets are available, a donor-imposed restriction is fulfilled to the extent of the expense incurred unless the expense is for a purpose that is directly attributable to another specific external source of revenue. Changes in donor-imposed restrictions subsequent to the period of contribution are reported as reclassifications within the appropriate net asset classes.

Dividends, interest, and net gains (losses) on investments are reported as follows:

- as increases in permanently restricted net assets if the terms of the gift require that they be added to the principal of a permanent endowment fund;
- as increases (decreases) in temporarily restricted net assets if the terms of the gift impose restrictions on the current use of the income or net gains; and
- as increases (decreases) in unrestricted net assets in all other cases.

Contributions, including unconditional promises to give, are recognized as revenues in the period received and generally increase temporarily restricted net assets. Promises to give subject to donor-imposed stipulations that the corpus be maintained in perpetuity are recognized as increases in permanently restricted net assets. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash are reported at their estimated fair value at the date of gift.

**(b) Property and Equipment**

Land, buildings, and equipment are reported at cost at date of acquisition or at fair value at date of donation in the case of gifts. For assets placed in service, depreciation is provided using the straight-line method over the estimated useful lives of the assets. The cost of normal maintenance and repairs that does not add to the value of the asset or materially extend asset lives is not capitalized.

Depreciation is provided on a straight-line basis over the following estimated useful lives:

	<u>Years</u>
Buildings and improvements	15 to 40
Land improvements	10 to 35
Equipment	3 to 20

**FRANKLIN W. OLIN COLLEGE OF ENGINEERING, INC.**

Notes to Financial Statements

June 30, 2003 and 2002

**(c) Short-Term Investments**

Short-term investments are stated at fair value and consist solely of holdings in the Common Fund Short-Term Fund.

**(d) Long-Term Investments**

Long-term investments are carried at fair value based on quoted market prices.

**(e) Functional Reporting of Expenses**

The costs of providing the College's activities have been summarized on a functional basis in the accompanying statements of activities. For the year ended June 30, 2003, expenses associated with the College's property and equipment, including depreciation and operations and maintenance expenses, were functionally allocated based on estimated space utilized. For the year ended June 30, 2002, the allocation was based on the pro-rata portion of each function.

**(f) Deferred Revenue and Deposits**

The College recognizes revenue on grants and contracts for research as related costs are incurred. Payments received in advance of expenditures are recorded as deferred revenue. Advance payments received for student-related activities are recorded as deposits.

**(g) Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

**(h) Income Tax Status**

The College is an organization described under Internal Revenue Code (IRC) Section 501(c)(3) and is generally exempt from income taxes under the provisions of IRC Section 501(a).

**(i) Reclassifications**

Certain 2002 information has been reclassified to conform to the 2003 presentation.

**(3) Long-Term Investments**

Long-term investments consisted of the following at June 30, 2003:

Common stock securities	\$	29,461,463
Preferred stock securities		269,390
Money market mutual funds		117,792
	\$	<u>29,848,645</u>

**FRANKLIN W. OLIN COLLEGE OF ENGINEERING, INC.**

Notes to Financial Statements

June 30, 2003 and 2002

Interest and dividends receivable on long-term investments was \$52,428 at June 30, 2003.

**(4) Property and Equipment**

Property and equipment consisted of the following at June 30:

	<u>2003</u>	<u>2002</u>
Land	\$ 14,609,513	14,609,513
Buildings and improvements	104,288,450	2,720,311
Equipment	6,396,921	384,317
Construction in progress	1,207,132	85,291,851
	<u>126,502,016</u>	<u>103,005,992</u>
Less accumulated depreciation	<u>(4,151,721)</u>	<u>(369,761)</u>
	<u>\$ 122,350,295</u>	<u>102,636,231</u>

**(5) Retirement Plan**

The College has established a defined contribution retirement plan for eligible personnel. The Plan is designed in accordance with the provisions of Section 403(b) of the Internal Revenue Code. The College's expense under the Plan in 2003 and 2002 was \$564,263 and \$414,269, respectively.

**(6) Natural Classification of Expenses**

Expenses by their natural classification were as follows for the years ended June 30:

	<u>2003</u>	<u>2002</u>
Salaries	\$ 5,885,408	4,773,194
Benefits	1,276,921	909,618
Depreciation	3,781,960	171,404
Information and communications	2,033,951	1,069,813
Facility services	2,021,014	1,660,130
Babson College services and expenses (note 1)	1,937,340	1,273,243
Professional services	1,003,117	636,841
Training, travel, and entertainment	567,582	414,062
Dining service fees	534,488	88,326
Materials and supplies	249,693	147,011
Insurance	145,115	36,493
Consumable equipment	111,710	396,712
Other	71,619	124,821
	<u>\$ 19,619,918</u>	<u>11,701,668</u>

**FRANKLIN W. OLIN COLLEGE OF ENGINEERING, INC.**

Notes to Financial Statements

June 30, 2003 and 2002

**(7) Rental Expense and Lease Obligations**

The College leases office equipment and construction trailers under noncancelable agreements which expire on various dates through 2006. Rental expense under these agreements aggregated \$506,603 in 2003 and \$709,580 in 2002, respectively.

Future minimum annual lease payments required under noncancelable leases were as follows at June 30, 2003:

<u>Year ending June 30</u>	<u>Amount</u>
2004	\$ 70,611
2005	64,386
2006	13,278
	<u>\$ 148,275</u>

**(8) Contributions from F.W. Olin Foundation**

**(a) Gift Agreement**

On December 26, 2002, the Foundation entered into an Endowment Grant Agreement (the Agreement) with the College. The Agreement provides that, except for \$55,000,000 reserved by the Foundation for other purposes, the Foundation will transfer its remaining net assets to the College to establish the Olin Endowment, as discussed further below, and to subsidize as necessary the College's operating and capital requirements from the date of the Agreement through December 31, 2005. The Agreement stipulates that the College will receive at least one-third of the Olin Endowment by the end of calendar 2003, two-thirds by the end of calendar 2004, and the entire amount by the end of calendar 2005. The calculation of the transfers to be made in each of those years is to be based on the fair value of the Foundation's assets at the date of each annual calculation less the outstanding balance of the \$55,000,000 reserve and the remaining estimated operating and capital subsidies to the College through 2005. The Agreement states that the Foundation may elect to exceed the transfers required under these calculations in any given year.

The Agreement also defines the terms of the Olin Endowment, which includes the original principal transferred pursuant to the Agreement, plus any additions to the Olin Endowment from any other source, plus or minus any changes in fair value, plus any income earned with respect to such principal, less properly chargeable expenses (whether principal or income), and less any withdrawals (whether principal or income) permitted under the Agreement. All such amounts constituting the Olin Endowment are available for the College's use in certain specified circumstances. However, the Agreement also stipulates that the Endowment Take, that is, the annual amount appropriated by the College to fund its operating needs, may not exceed 6% of the Olin Endowment; Endowment Take beyond this 6% limit requires Board action. There are also certain restrictions regarding permissible uses of the Endowment Take and any operating surpluses generated by the College. Because of these various use and time restrictions, the Olin Endowment, including interest, dividends and net gains (losses) thereon, increases (decreases) temporarily restricted net assets.

**FRANKLIN W. OLIN COLLEGE OF ENGINEERING, INC.**

Notes to Financial Statements

June 30, 2003 and 2002

The Agreement requires the College to adhere to the Founding Precepts of the College, as defined in the Agreement, in perpetuity. These Founding Precepts include concepts about the College's name, culture, and commitment to providing an education at significantly reduced costs to students and their families.

**(b) Contributions Receivable**

The College determined that the Agreement constitutes an unconditional promise to give and, accordingly, recognized contributions receivable of \$238,898,478 at the date of the Agreement. The amount recognized represents the fair value of the Foundation's underlying net assets, consisting principally of marketable securities, which were transferable to the College at that date. Since all contributions receivable under the Agreement are time and/or purpose restricted, revenue increased temporarily restricted net assets. The College will adjust such contributions receivable to reflect the fair value of the Foundation's underlying net assets transferable to the College as of each June 30.

Transfers received under contributions receivable from the date of the Agreement through June 30, 2003 included \$26,745,260 for the Olin Endowment, operating subsidies of \$6,252,860 (which are reported as net assets released from restrictions), and capital subsidies of \$5,270,000. The increase in the fair value of contributions receivable of \$15,429,505 represents additional contribution revenue from the date of Agreement through June 30, 2003 and resulted in a year-end balance of \$216,059,863.

**(c) Fiscal 2002 and Prior Contributions from the Foundation**

In fiscal 2002, in anticipation of the Agreement, the Foundation clarified its intentions with respect to its current and previous contributions for the College's acquisition and construction of property and equipment. Accordingly, restrictions on such contributions to purchase land shall remain in perpetuity, and restrictions on all other such contributions will be released over the useful lives of the related depreciable assets. Given the Foundation's intent, in fiscal 2002 the College reported temporarily restricted and permanently restricted contributions from the Foundation of \$48,150,524 and \$5,000, respectively, and reclassified prior-year unrestricted net assets of \$37,246,388 to temporarily restricted net assets and \$14,604,513 to permanently restricted net assets.

**(9) Restricted Net Assets**

**(a) Temporarily Restricted Net Assets**

Temporarily restricted net assets consisted of the following at June 30:

	<b>2003</b>	<b>2002</b>
Contributions receivable from the Foundation	\$ 216,059,863	—
Olin Endowment	29,901,073	—
Purpose restrictions	255,599	152,629
Investments in fixed assets (to be released over time)	105,642,496	85,225,508
	\$ 351,859,031	85,378,137

**FRANKLIN W. OLIN COLLEGE OF ENGINEERING, INC.**

Notes to Financial Statements

June 30, 2003 and 2002

**(b) Permanently Restricted Net Assets**

Permanently restricted net assets consisted of the following at June 30:

	<u>2003</u>	<u>2002</u>
Land purchased with Foundation contributions	\$ 14,609,513	14,609,513
Bioengineering chair	1,633,125	1,633,125
Milas Library fund	76,000	50,000
Other endowment	5,208	1,600
	<u>\$ 16,323,846</u>	<u>16,294,238</u>

**(c) Net Assets Released From Restrictions**

Net assets released from restrictions consisted of the following at June 30:

	<u>2003</u>	<u>2002</u>
Depreciation	\$ 3,781,960	171,404
Collections on Foundation contributions receivable utilized for operations	6,252,860	—
Nordex scholarship	11,397	—
	<u>\$ 10,046,217</u>	<u>171,404</u>

**(10) Subsequent Events**

**(a) Issuance of Long-Term Debt**

On August 11, 2003, the College issued Taxable Revenue Bonds, Series A-1 and A-2 Select Auction Variable Rate Securities, in the amount of \$93,200,000, and Tax-Exempt Revenue Bonds, Series B, in the amount of \$65,910,000. A portion of the proceeds will be used to reimburse the College for construction of Phase I of the main campus, and the balance will be used to fund construction of a second residence hall. The taxable bonds mature from 2030-2033. The tax-exempt bonds mature from 2028-2033 and have a coupon rate of 5.25%.

**(b) Olin Endowment Receipt**

On August 5, 2003, the Foundation transferred securities with a fair value of \$62,915,924 to the College to be added to the Olin Endowment. This transfer, in combination with the transfer of \$26,745,260 received by the College in April 2003, represented the Foundation's calendar year 2003 transfer commitment under the Agreement and the first one-third of the calculated amount distributable from the Foundation as the Olin Endowment.