FRANKLIN UNIVERSITY AND SUBSIDIARY
Columbus, Ohio

CONSOLIDATED ANNUAL REPORT
July 31, 2017 and 2016

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Independent Auditor's Report

To the Board of Directors
Franklin University and Subsidiary

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Franklin University and Subsidiary, which comprise the consolidated statement of financial position as of July 31, 2017 and the related consolidated statements of activities and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Franklin University and Subsidiary as of July 31, 2017, and the changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

To the Board of Directors
Franklin University and Subsidiary

Report on Prior Year Consolidated Financial Statements

The consolidated financial statements of Franklin University and Subsidiary as of July 31, 2016 were audited by other auditors, whose report dated January 6, 2017 expressed an unmodified opinion on those statements.

Other Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The schedule of expenditures of federal awards, as required by Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, is presented for the purpose of additional analysis and is not a required part of the consolidated financial statements.

The schedule of expenditures of federal awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 29, 2017 on our consideration of Franklin University and Subsidiary's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Franklin University and Subsidiary's internal control over financial reporting and compliance.

Plante & Moran, PLLC

September 29, 2017

FRANKLIN UNIVERSITY AND SUBSIDIARY
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
July 31, 2017 and 2016
(In thousands)

	2017	2016
ASSETS		
Cash	$ 7,823	$ 3,712
Accounts receivable, tuition and fees		
Students (less allowance of $6,099 and $5,632, respectively)	1,627	2,236
Department of Education	276	332
Grants and other	686	1,039
Accounts receivable, other income (less allowance of $137 and $1,096, respectively)	2	577
Prepaid expenses	1,007	1,118
Pledged contributions receivable (less allowance of $60 and $61, respectively)	83	118
Student notes receivable (less allowance of $790 and $790, respectively)	1,048	1,035
Other assets	461	448
Investments	85,476	79,285
Bond proceeds restricted for buildings and equipment	7,925	10,341
Educational property		
Land and improvements	9,934	10,098
Buildings	47,160	46,727
Equipment, furniture, and software	23,267	22,068
Construction in progress	723	34
Total educational property at cost	81,084	78,927
Less accumulated depreciation	43,844	40,234
Educational property, net	37,240	38,693
Total assets	$ 143,654	$ 138,934
LIABILITIES AND NET ASSETS		
Liabilities		
Accounts payable and accrued liabilities	$ 3,546	$ 3,871
Accrued payroll	5,002	4,834
Deferred revenue	901	712
Accounts held on behalf of others	584	553
Federal government advances for student notes receivable	940	941
Other liabilities	476	509
Capital lease obligations payable	18,464	19,749
Total liabilities	29,913	31,169
Net assets		
Unrestricted	107,769	102,370
Temporarily restricted	2,600	2,140
Permanently restricted	3,372	3,255
Total net assets	113,741	107,765
Total liabilities and net assets	$ 143,654	$ 138,934

See accompanying notes to consolidated financial statements.

FRANKLIN UNIVERSITY AND SUBSIDIARY
CONSOLIDATED STATEMENT OF ACTIVITIES
Year ended July 31, 2017 with comparative 2016 totals
(In thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total 2017	Total 2016
Operating revenues					
Student tuition and fees	$ 65,016	$ -	$ -	$ 65,016	$ 67,864
Scholarship allowances	6,009	-	-	6,009	6,536
Net student tuition and fees	59,007	-	-	59,007	61,328
Private gifts and grants	343	251	-	594	1,114
Federal grants	692	-	-	692	559
Investment income	123	494	-	617	368
Other income	1,326	-	-	1,326	6,438
Auxiliary services	2,245	-	-	2,245	2,379
Total	63,736	745	-	64,481	72,186
Net assets released from restrictions	285	(285)	-	-	-
Total operating revenues	64,021	460	-	64,481	72,186
Operating expenses					
Instruction	16,683	-	-	16,683	19,344
Academic support	8,438	-	-	8,438	9,713
Student services	10,572	-	-	10,572	10,812
Institutional support	29,108	-	-	29,108	35,893
Development	1,016	-	-	1,016	1,155
Auxiliary services	857	-	-	857	918
Total operating expenses	66,674	-	-	66,674	77,835
Change in net assets from operations	(2,653)	460	-	(2,193)	(5,649)
Nonoperating items					
Private gifts and grants	-	-	109	109	4
Investment income, net of fees	7,932	-	8	7,940	3,325
Gain on disposition of assets	120	-	-	120	-
Total nonoperating items	8,052	-	117	8,169	3,329
Change in net assets	5,399	460	117	5,976	(2,320)
Net assets at beginning of year	102,370	2,140	3,255	107,765	110,085
Net assets at end of year	**$ 107,769**	**$ 2,600**	**$ 3,372**	**$ 113,741**	**$ 107,765**

See accompanying notes to consolidated financial statements.

FRANKLIN UNIVERSITY AND SUBSIDIARY
CONSOLIDATED STATEMENT OF ACTIVITIES
Year ended July 31, 2016
(In thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Operating revenues				
Student tuition and fees	$ 67,864	$ -	$ -	$ 67,864
Scholarship allowances	6,536	-	-	6,536
Net student tuition and fees	61,328	-	-	61,328
Private gifts and grants	729	385	-	1,114
Federal grants	559	-	-	559
Investment income	180	188	-	368
Other income	6,438	-	-	6,438
Auxiliary services	2,379	-	-	2,379
Total	71,613	573	-	72,186
Net assets released from restrictions	444	(429)	(15)	-
Total operating revenues	72,057	144	(15)	72,186
Operating expenses				
Instruction	19,344	-	-	19,344
Academic support	9,713	-	-	9,713
Student services	10,812	-	-	10,812
Institutional support	35,893	-	-	35,893
Development	1,155	-	-	1,155
Auxiliary services	918	-	-	918
Total operating expenses	77,835	-	-	77,835
Change in net assets from operations	(5,778)	144	(15)	(5,649)
Nonoperating items				
Private gifts and grants	-	-	4	4
Investment income, net of fees	3,321	-	4	3,325
Total nonoperating items	3,321	-	8	3,329
Change in net assets	(2,457)	144	(7)	(2,320)
Net assets at beginning of year	104,827	1,996	3,262	110,085
Net assets at end of year	**$ 102,370**	**$ 2,140**	**$ 3,255**	**$ 107,765**

See accompanying notes to consolidated financial statements.

FRANKLIN UNIVERSITY AND SUBSIDIARY
CONSOLIDATED STATEMENT OF CASH FLOWS
Years ended July 31, 2017 and 2016
(In thousands)

	2017	2016
Cash flows from operating activities		
Change in net assets	$ 5,976	$ (2,320)
Adjustments to reconcile change in net assets to net cash and cash equivalents from operating activities:		
Depreciation and amortization	3,620	3,420
Provision for uncollectible accounts receivable	71	1,820
Noncash in-kind contributions	-	(315)
Realized and unrealized gains on investments	(7,316)	(1,879)
Gain on sale/disposition of educational property	(120)	-
Gifts for permanently restricted purposes	(109)	(4)
Changes in operating assets and liabilities:		
Accounts receivable, tuition and fees	226	(1,877)
Accounts receivable, other income	1,296	266
Prepaid expenses	111	(157)
Pledged contributions receivable	35	37
Student notes receivable	(13)	38
Other assets	(13)	5
Accounts payable and accrued liabilities	(325)	1,049
Accrued payroll	168	697
Deferred revenue	189	(1,905)
Accounts held on behalf of others	31	21
Federal government advances for student notes receivable	(1)	(169)
Other liabilities	(33)	-
Net cash and cash equivalents provided by (used in) operating activities	3,793	(1,273)
Cash flows from investing activities		
Purchases of investments	(107,422)	(69,533)
Proceeds from sales of investments	108,547	73,839
Purchases of educational property	(2,720)	(2,357)
Proceeds from sales of educational property	673	-
Net cash and cash equivalents (used in) provided by investing activities	(922)	1,949
Cash flows from financing activities		
Payments on long-term borrowings	(1,285)	(1,005)
Proceeds from long-term borrowings	2,416	167
Gifts for permanently restricted purposes	109	4
Net cash and cash equivalents provided by (used in) financing activities	1,240	(834)
Net change in cash	4,111	(158)
Cash, beginning of year	3,712	3,870
Cash, end of year	**$ 7,823**	**$ 3,712**
Supplemental disclosures of cash flow information		
Cash paid during the year for interest	$ 423	$ 340

During the fiscal year ended July 31, 2016, $18,000 of new capital lease obligations were issued in a non-cash transaction, resulting in $10,341 of restricted bond proceeds held in escrow, the refinance of $7,496 of previously issued and outstanding capital lease obligations, and deferred issuance costs of $163.

See accompanying notes to consolidated financial statements.

NOTE 1 – NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES

Organization: Franklin University ("Franklin"), founded in 1902, is a nonprofit 501(c)(3) educational corporation and, accordingly, is exempt from Federal income and state taxes. All funds and property received by the University are irrevocably dedicated to and used exclusively for educational purposes.

On May 30, 2014, Franklin incorporated Franklin University – Urbana, LLC ("Franklin LLC"). As a single-member LLC, Franklin LLC is a disregarded entity for tax purposes and operating as a division of Franklin under the name Urbana University ("Urbana").

Urbana is a four-year, nonprofit co-educational liberal arts institution with its primary campus located in Urbana, Ohio.

Financial Statement Presentation: The accompanying consolidated statement of financial position includes the consolidated accounts of Franklin and its wholly owned subsidiary, Franklin LLC, dba Urbana University, collectively referred to as "the University". Intercompany transactions and balances have been eliminated in consolidation.

Resources are reported for accounting purposes into separate classes of net assets based on the existence or absence of donor-imposed restrictions.

Gifts of cash and other assets received with donor stipulations that limit the use of the donated assets are reported as restricted revenue. When a donor restriction expires, a stipulated time restriction ends, or the purpose for the restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of activities as net assets released from restrictions.

The University reports gifts of property, plant and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted revenues. Absent explicit donor stipulations about how long-lived assets must be maintained, the University reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

Permanently restricted funds include endowment funds for scholarships and operations of the Leadership Center that are subject to the restrictions of gift instruments requiring that the principal be invested in perpetuity and only the income be utilized.

Accounts Receivable: The University carries the following categories of accounts receivable:

Tuition and fees: Accounts receivable, tuition and fees consist of charges to students accounts for tuition and fees. The outstanding balances are due from students or their sponsors, the federal Department of Education for financial assistance granted to students, and from grants and other assistance provided to students by state and local government agencies. Interest is not charged by the University on student accounts receivable.

Other income: Accounts receivable, other income primarily consists of amounts due from other colleges and universities for educational services.

Pledged contributions receivable: Pledged contributions receivable are due from donors for unconditional promises to give. Contributions to be received beyond the fiscal year are discounted at an appropriate discount rate.

(Continued)

NOTE 1 – NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

Allowance for uncollectible accounts receivable: The University uses the allowance method to estimate uncollectible receivables, from tuition and fees, other income, and pledged contributions receivable. The allowances are based upon prior experience and management's analysis of specific receivables and promises to give.

Student notes receivable: Student notes receivable are carried at unpaid principal balances less an allowance for uncollectible notes.

Allowance for uncollectible student notes receivable: The University uses the allowance method to estimate uncollectible notes receivable. The allowance for uncollectible notes is increased by charges to Federal government advances for student notes receivable, and decreased by charge-offs which reduce the corresponding liability. Management's periodic evaluation of the adequacy of the allowance is based on Perkins Loan Program requirements, the University's past note loss experience, specific impaired notes, adverse situations that may affect the borrower's ability to repay, and current economic conditions. Notes are considered impaired if full principal or interest payments are not anticipated in accordance with the contractual terms. The University's practice is to charge off any note or portion of a note when the note is determined by management to be uncollectible due to the borrower's failure to meet repayment terms, the borrower's deteriorating or deteriorated financial condition, or for other reasons. Notes are placed on nonaccrual status when management believes, after considering economic conditions, business conditions, and collection efforts, that the notes are impaired or collection of interest is doubtful. Uncollected interest previously accrued is charged off or an allowance is established by a charge to interest income. Interest income on nonaccrual notes is recognized only to the extent cash payments are received.

Interest on notes is recognized over the term of the note and is calculated using the simple interest method on principal amounts outstanding.

The following tables set forth the aging of gross student notes receivable as of July 31, 2017 and 2016:

(In thousands)

	Delinquency Period					
	30-59 Days	60-89 Days	Greater than 90 Days	Total Delinquent	Current	Total Balance at Year End
2017	$ 15	$ 6	$ 770	$ 791	$ 1,047	$ 1,838
2016	47	6	781	834	991	1,825

The following is an analysis of the balance and annual activity in the allowance for loan losses for student notes receivable as of and for the years ending July 31, 2017 and 2016:

	2017	2016
	(In thousands)	
Allowance for loan losses:		
Allowance at beginning of year	$ 790	$ 776
Loans charged-off	-	-
Recovery of loans previously charged-off	-	-
Current year provision for uncollectible loans	-	14
Allowance at end of year	$ 790	$ 790
Student notes receivable balances at year-end collectively evaluated for impairment	$ 1,838	$ 1,825

(Continued)

NOTE 1 – NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

Agency Transactions: The University receives resources in certain transactions where it is acting as an intermediary for the resource providers. The resources are then promptly delivered to third-party recipients. These transactions are recognized as changes in assets and liabilities and do not affect the consolidated statement of activities. Most federal grants and certain Ohio grants are considered agency relationships.

Accounts Held on Behalf of Others: The University has received funds that are held in accounts on behalf of others. The amount presented as a liability on the consolidated statement of financial position primarily consists of a charitable remainder Unitrust, student housing deposits, and funds held on behalf of student organizations.

Investments: Investments are stated at fair value based on market values or dealer quotes, with changes in fair value being recognized as gains and losses during the period in which they occur.

Limited partnerships, for which there is no ready market, are valued at fair value as estimated by management. To estimate fair value, management may rely on valuations reported by the general partners of such investments and/or the University's independent investment advisor. Because of the inherent uncertainty of valuation in the absence of readily ascertainable market values, the estimated values of those investments may differ from the values that would have been used had a ready market existed for such investments or if the investments were realized, and the differences could be material. Such investments are, by their nature, generally considered to be long-term investments and are not intended to be liquidated on a short-term basis.

Federal Government Advances for Student Notes Receivable: Funds provided by the United States government pursuant to the Perkins Loan Program are loaned to qualified students and may be re-loaned upon collection. Since these funds are ultimately distributable to the federal government upon liquidation of the program, should it occur, the advances are reflected as a liability on the accompanying consolidated statement of financial position.

The Federal Perkins Loan Program is scheduled to expire on September 30, 2017. As of July 31, 2017, the University has made $482,000 in institutional capital contributions that are reflected as part of the University's net assets. Under current guidance issued by the Department of Education, at the time the University liquidates the loan portfolio and assigns the student loans to the Department of Education, the University will be forgoing its institutional capital contribution and short-term loans not yet received back through loan collections.

Educational Properties and Depreciation: Educational properties represented by buildings, improvements and equipment, are carried at cost, or fair value at the date of the gift, less accumulated depreciation. Depreciation is provided on the straight-line basis over the estimated useful lives of the assets. Expenditures for additions, renewals or betterments with a cost in excess of $10,000 are capitalized. Expenditures for maintenance and repairs are charged to expense. Expenses related to educational properties have been allocated to the following expenses based on square footage: instruction, academic support, student services, institutional support and development. Interest cost during construction is capitalized as part of the cost of capital projects. There was no capitalized interest for the years ended July 31, 2017 and 2016. There are no contractual commitments remaining under ongoing construction projects at July 31, 2017 and 2016.

Evaluation of Impairment of Long-lived Assets: The University reviews its long-lived assets for impairment in accordance with guidance issued by the Financial Accounting Standards Board (FASB), which requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. Management determined there was no impairment of long-lived assets as of July 31, 2017 and 2016.

(Continued)

NOTE 1 – NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

Fair Value of Financial Instruments: The University's carrying value for its financial instruments, which include cash and cash equivalents, accounts receivable, contributions receivable, investments, accounts payable, and fixed rate capital lease obligations at July 31, 2017 and 2016, approximate their estimated fair values for all but the capital lease obligations (see Note 5). The estimated fair value amounts have been determined by the University using available market information and appropriate valuation methodologies. Considerable judgment is required in interpreting market data and developing these estimates.

Nonoperating Activities: The University has defined nonoperating activity to include the following:

> Private gifts and grants: Contributions to the permanent endowment of the University not available to be spent, contributions restricted for capital purchases not available to be spent for operations, and bequests not a part of the University's routine revenue generation processes.
>
> Investment income: Endowment income and realized gains (losses) in excess of the spending policy and unrealized gains (losses) on endowments and other investments not available for current operations.
>
> Gains (losses) on sale/disposition of assets: Gains or losses associated with sales of educational properties and certain other asset dispositions or impairments.

Revenue Recognition: The University utilizes the following policies for revenue recognition:

> Student tuition and fees: Student tuition and fees are recognized ratably over the period during which the related educational services are provided.
>
> Private gifts: Private gifts, including unconditional promises to give, are recognized as revenue in the period the related commitments are received. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met. Private gifts of assets other than cash are recorded at their estimated fair value.
>
> Federal grants: Federal grants are recognized ratably over the period during which the related educational services are provided; or as earned by federal work-study employees.
>
> Other income: Other income primarily consists of education related content and services provided to other colleges and universities. Revenues are recognized upon delivery and acceptance of the related content and services.

Deferred Revenue: Deferred revenue at July 31, 2017 and 2016 is primarily comprised of tuition and fees paid in advance by students for the fall trimester and other income that will be recognized upon delivery and acceptance of the related content and services.

Pension Plan: The University sponsors defined contribution pension plans covering generally all full-time administrative officers, faculty and certain support staff. The University's policy is to fund the pension cost accrued. Pension expense for 2017 and 2016 was approximately $2,691,000 and $2,840,000, respectively.

(Continued)

NOTE 1 – NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

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 affecting the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenditures during the reporting periods. Actual results could differ from those estimates.

Upcoming Accounting Pronouncements:

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. ASU No. 2016-14 requires significant changes to the financial reporting model of organizations that follow FASB not-for-profit rules, including changing from three classes of net assets to two classes: net assets with donor restrictions and net assets without donor restrictions. The ASU will also require changes in the way certain information is aggregated and reported by the University, including required disclosures about the liquidity and availability of resources. The new standard is effective for the University's year ending July 31, 2019 and thereafter and must be applied on a retrospective basis. As part of implementing this standard, the University is currently evaluating the consolidation of its net asset classifications and the development of a new expense matrix and new liquidity footnote disclosures.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers* (Topic 606), which will supersede the current revenue recognition requirements in Topic 605, *Revenue Recognition*. The ASU is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. The new guidance will be effective for the University's year ending July 31, 2020. The ASU permits application of the new revenue recognition guidance to be applied using one of two retrospective application methods. The University does not believe the implementation of the new standard will have a significant impact on any of its methods and timing of revenue recognition.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*, which will supersede the current lease requirements in ASC 840. The ASU requires lessees to recognize a right-of-use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the statement of activities. Currently, leases are classified as either capital or operating, with only capital leases recognized on the statement of financial position. The reporting of lease-related expenses in the statements of activities and cash flows will be generally consistent with the current guidance. The new lease guidance will be effective for the University's year ending July 31, 2021 and will be applied using a modified retrospective transition method to the beginning of the earliest period presented. The new lease standard is expected to have a significant effect on the University's financial statements as a result of the leases described in Note 9 and currently classified as operating leases.

NOTE 1 – NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

Upcoming Accounting Pronouncements: (Continued)

In December 2015, the FASB issued ASU No. 2015-07, *Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (Or its Equivalent)*. ASU No. 2015-07 removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share (NAV) practical expedient. The ASU also requires information to allow for the reconciliation of fair value of investments from the hierarchy disclosure to the line item presented on the statement of financial position. The new guidance will be effective for the University's year ending July 31, 2018 and will be applied retrospectively for all periods presented. The University is currently assessing its investments to create the additional disclosures necessary under the new standard.

NOTE 2 – INVESTMENTS

Investments at July 31, 2017 and 2016 are summarized as follows:

	2017	2016
	(In thousands)	
Cash	$ 1,196	$ 2,811
Equities	42,775	45,897
Bonds	30,158	22,750
Mutual funds – Equities	4,798	4,566
Mutual funds – Bonds	3,286	1,448
Hedge funds	145	176
Limited partnerships	3,118	1,637
Investments at fair value	$ 85,476	$ 79,285

The composition of investment return for the years ended July 31, 2017 and 2016 consisted of the following:

	2017	2016
	(In thousands)	
Interest and dividends	$ 1,656	$ 2,244
Investment fees	(415)	(430)
Net realized gains (losses) on investments	3,853	(1,029)
Net unrealized gains on investments	3,463	2,908
Total investment return	8,557	3,693
Investment return designated for current operations	617	368
Investment return not designated for current operations	$ 7,940	$ 3,325

(Continued)

NOTE 3 – FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value measurements are determined by the University pursuant to guidance issued by the FASB. This guidance defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. FASB guidance established a fair value hierarchy that distinguishes between (A) market participant assumptions developed based on market data obtained from independent sources (observable inputs) and (B) an entity's own assumptions about market participant assumptions based on the best information available in the circumstances (unobservable inputs). The fair value hierarchy consists of three broad levels, which gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3).

The three levels of the fair value hierarchy under the FASB guidance are as follows:

Level 1 – Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2 – Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 – Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The fair values of equity investments that are readily marketable are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs). If quoted prices in active markets for identical assets are not available to determine fair value, then quoted prices for similar assets are used (Level 2 inputs). This valuation methodology applies to investments such as corporate and government bonds, mutual funds, mortgage-backed securities, and agency securities.

The fair values of bonds and mutual funds are determined primarily based on Level 2 inputs. The University estimates the fair values of the bonds using quoted prices for identical or similar assets in inactive markets, with additional consideration to contractual cash flows, benchmark yields, and credit spreads. The University estimates the fair values of the mutual funds based on the fair value of the underlying investments with consideration of any restrictions on the interest in the fund that exist

(Continued)

NOTE 3 – FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

The fair values of the University's hedge fund investments have been estimated using the net asset value per share of the investment, or its equivalent. Due to current market conditions as well as the limited trading activity of these securities, the market value of the securities is highly sensitive to assumption changes and market volatility (Level 3 inputs). Redemption restrictions are greater than three months. There are no unfunded commitments on these funds. The investment objectives of the various hedge funds are as follows:

- Focus on institutional quality managers who invest in historically uncorrelated strategies such as relative value, event-driven, equity market neutral, credit, distressed securities, and various arbitrage-based approaches.
- Enhance return through an extensive manager selection process and manage risk through an intensive quantitative and qualitative due diligence and monitoring process. The highly diversified, noncorrelated, multi-manager/multi-strategy portfolio focuses on inefficiencies and anomalies in the financial markets across a broad spectrum of unique liquid alternative investment strategies.
- Preserve capital and superior risk-adjusted returns. Engage principally in a diversified investment strategy utilizing a multi-manager approach to invest in securities.

For other investments for which there is no active market, University management and the Investment Committee review the valuations and returns in comparison to industry benchmarks and other information (income approach). Due to current market conditions as well as the limited trading activity of these securities, the market value of the securities is highly sensitive to assumption changes and market volatility (Level 3 inputs). At July 31, 2017 and 2016, these investments consist solely of limited partnerships (primarily private equity funds), which are valued at net asset value. There are no redemption options on these funds. University management expects approximately 25% of the investments to be distributed within one to three years. The remaining investments are expected to be distributed within three to ten years. There are unfunded commitments on certain of these funds totaling approximately $3,303,000 and $4,350,000 at July 31, 2017 and 2016, respectively. The investment objectives of these funds are as follows:

- Achieve attractive risk-adjusted absolute returns by focusing on certain transaction types in certain key markets.
- Offer investors an opportunity to access the private equity market through a much smaller commitment than would be feasible investing directly in funds.

NOTE 3 – FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

Assets and Liabilities Measured on a Recurring Basis: Assets and liabilities measured at fair value on a recurring basis are summarized below:

	Fair Value Measurements at July 31, 2017 Using		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(In thousands)	
Cash	$ 1,196	$ -	$ -
Equities:			
Consumer discretionary	5,995	-	-
Consumer staples	4,283	-	-
Energy	787	-	-
Financials	1,197	-	-
Health care	10,102	-	-
Industrials	992	-	-
Information technology	12,980	-	-
Materials	5,370	-	-
Other	1,069	-	-
Corporate Bonds	-	7,454	-
Mortgage-backed Securities	-	10,057	-
US Treasury and Gov't Agency Bonds	-	12,647	-
Mutual funds - Equities	-	4,798	-
Mutual funds - Bonds	-	3,286	-
Hedge funds	-	-	145
Limited partnerships	-	-	3,118
Total investments	$ 43,971	$ 38,242	$ 3,263

(Continued)

NOTE 3 – FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

	Fair Value Measurements at July 31, 2016 Using		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(In thousands)	
Cash	$ 2,811	$ -	$ -
Equities:			
Consumer discretionary	11,576	-	-
Consumer staples	3,870	-	-
Energy	1,764	-	-
Financials	3,024	-	-
Health care	5,958	-	-
Industrials	1,275	-	-
Information technology	14,440	-	-
Materials	3,990	-	-
Corporate Bonds	-	8,612	-
Mortgage-backed Securities	-	6,668	-
US Treasury and Gov't Agency Bonds	-	7,470	-
Mutual funds - Equities	-	4,566	-
Mutual funds - Bonds	-	1,448	-
Hedge funds	-	-	176
Limited partnerships	-	-	1,637
Total investments	$ 48,708	$ 28,764	$ 1,813

The tables below present a reconciliation and income statement classification of gains and losses for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the years ended July 31, 2017 and 2016:

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)	
	Hedge Funds	Limited Partnerships
	(In thousands)	
2017		
Beginning balance, July 31, 2016	$ 176	$ 1,637
Redemptions/distributions	(36)	(194)
Purchases/capital contributions	-	1,028
Realized/unrealized gain included in earnings	5	647
Ending balance, July 31, 2017	$ 145	$ 3,118
2016		
Beginning balance, July 31, 2015	$ 346	$ 1,336
Redemptions/distributions	(139)	-
Purchases/capital contributions	-	322
Realized/unrealized loss included in earnings	(31)	(21)
Ending balance, July 31, 2016	$ 176	$ 1,637

(Continued)

NOTE 3 – FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

The University records transfers in and/or out of the various levels as of the end of the respective reporting period.

Unrealized gains and (losses) generated from Level 3 investments still held at July 31, 2017 and 2016, and reported in the University's statement of activities were $589,000 and ($151,000), respectively.

The various investments in equity securities, bonds, mutual funds and other investments are exposed to a variety of uncertainties, including interest rate, market and credit risks. Due to the level of risk associated with certain investments, it is possible that changes in the value of these investments could occur.

NOTE 4 – PLEDGED CONTRIBUTIONS RECEIVABLE

Contributions receivable are promises to give from various donors that are unconditional. At July 31, 2017 and 2016, approximately $83,000 and $118,000, respectively, was recognized on the consolidated statement of financial position, net of allowance for uncollectible promises of $60,000 and $61,000, respectively.

The University expects to receive the pledged contributions as follows at July 31, 2017 and 2016:

	2017	2016
	(In thousands)	
Gross amounts to be received in:		
Less than one year	$ 35	$ 30
One to five years	38	94
More than five years	70	61
	143	185
Less net present value discount	-	6
Net present value of pledge contributions receivable	$ 143	$ 179

The net present value discount of expected future cash flows is based on a discount rate of 3.25%.

NOTE 5 – CAPITALIZED LEASE OBLIGATIONS PAYABLE

The University had the following capitalized lease obligations at July 31, 2017 and 2016:

	2017	2016
	(In thousands)	
January 2010 Issue	$ 1,453	$ 1,993
February 2016 Issue	17,011	17,756
	$ 18,464	$ 19,749

(Continued)

NOTE 5 – CAPITALIZED LEASE OBLIGATIONS PAYABLE (Continued)

On January 1, 2010, the University entered into a lease agreement with the Ohio Higher Educational Facility Commission (the “Commission”) to finance the renovation of various buildings and the purchase of information technology equipment. The University’s lease serves as security for the Commission’s $5,000,000 State of Ohio Higher Educational Facility Revenue Bonds (Franklin University January 2010 Project). The interest rate on the lease is fixed at 4.2102%. The estimated fair value of the outstanding balance of the bonds was approximately $908,000 and $2,073,000 as of July 31, 2017 and 2016, respectively. The capitalized lease obligation is due in January 2020.

On December 1, 2010, the University entered into a lease agreement with the Commission to fund certain capital expenditure projects and to redeem the December 2007 Issue, with a then-outstanding principal balance of $4,500,000. The University’s lease serves as security for the Commission’s $9,500,000 State of Ohio Higher Educational Facility Revenue Bond (Franklin University December 2010 Project). The interest rate on the lease was fixed at 2.31% until February 1, 2016. The University’s obligation under this lease was refunded through the February 2016 Issue discussed below.

On February 1, 2016, the University entered into a lease agreement with the Commission to fund certain capital expenditure projects and to redeem the December 2010 Issue, with a then-outstanding principal balance of $7,496,000. The University’s lease serves as security for the Commission’s $18,000,000 State of Ohio Higher Educational Facility Revenue Bonds (Franklin University 2016 Project). The interest rate on the lease is fixed at 2.00%. The estimated fair value of the outstanding balance of the bonds was approximately $16,739,000 and $16,826,000 as of July 31, 2017 and 2016, respectively. The capitalized lease obligation is due in February 2036.

Bond proceeds restricted for buildings and equipment are held in escrow in a bank savings account. Funds are made available to the University, upon request, to reimburse capital expenditures within the scope of the project.

The cost and accumulated amortization of the assets under capital leases are as follows at July 31, 2017 and 2016:

	2017	2016
	(In thousands)	
Equipment, furniture and software	$ 17,258	$ 14,843
Less: Accumulated amortization	7,345	6,468
Educational property, net	$ 9,913	$ 8,375

Amortization of the assets under capital leases is included with depreciation expense.

Total interest expense on all debt obligations for 2017 and 2016 was approximately $422,000 and $353,000, respectively.

In the event of default by the University on its obligation pursuant to the January 2010 Issue, the assets that were acquired with the proceeds from the bonds may be repossessed by the trustee of the bonds. The University has provided a general pledge of its revenues as collateral for the February 2016 Issue. In addition, pursuant to these agreements, the University has agreed to certain financial and operating covenants, with which the University has complied.

(Continued)

NOTE 5 – CAPITALIZED LEASE OBLIGATIONS PAYABLE (Continued)

The future minimum lease payments under capital lease obligations for each of the next five years and in the aggregate, less the amount representing interest, are as follows as of July 31, 2017 (in thousands):

2018	$ 1,684
2019	1,684
2020	1,376
2021	1,070
2022	1,070
Remaining amount due	15,135
Total minimum lease payments	22,019
Less amounts representing interest	3,555
Net present value of capital lease obligations payable	$ 18,464

NOTE 6 – LINE OF CREDIT

At July 31, 2017, the University has a $5,000,000 unsecured revolving line of credit with a bank. Advances on the line bear interest at LIBOR plus 1.25%. In addition, pursuant to these agreements, the University has agreed to certain financial and operating covenants, with which the University has complied. The line of credit is due on demand and had no amounts outstanding at July 31, 2017 and 2016. The line of credit expires on August 31, 2018.

NOTE 7 – NET ASSETS

Unrestricted net assets at July 31, 2017 and 2016 consist of the following:

	2017	2016
	(In thousands)	
Investment in educational property	$ 26,701	$ 29,285
Board-designated for endowment	1,227	1,113
Board-designated for other purposes	21	21
Undesignated	79,820	71,951
Total	$ 107,769	$ 102,370

Temporarily restricted net assets consist of net assets restricted for scholarships, the Franklin University Leadership Center, and capital additions.

Permanently restricted net assets consist of endowed funds for scholarships and the Franklin University Leadership Center.

(Continued)

NOTE 8 – ENDOWMENT COMPOSITION

The University's endowment primarily consists of funds held in trust by Key Bank. Its endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. As required by applicable standards, net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Endowment net assets are composed by type of fund as follows as of July 31, 2017:

	(In thousands)			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Totals
Donor-restricted endowment funds	$ -	$ 1,782	$ 3,372	$ 5,154
Board-designated funds	1,227	-	-	1,227
Total funds	$ 1,227	$ 1,782	$ 3,372	$ 6,381

Changes in endowment net assets for the year ended July 31, 2017 were as follows:

	(In thousands)			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Totals
Endowment assets, beginning of year	$ 1,113	$ 1,312	$ 3,255	$ 5,680
Investment income, net	120	494	8	622
Contributions	-	-	109	109
Appropriation of endowment assets	(6)	(24)	-	(30)
Endowment assets, end of year	$ 1,227	$ 1,782	$ 3,372	$ 6,381

Endowment net assets are composed by type of fund as follows as of July 31, 2016:

	(In thousands)			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Totals
Donor-restricted endowment funds	$ -	$ 1,312	$ 3,255	$ 4,567
Board-designated funds	1,113	-	-	1,113
Total funds	$ 1,113	$ 1,312	$ 3,255	$ 5,680

(Continued)

NOTE 8 – ENDOWMENT COMPOSITION (Continued)

Changes in endowment net assets for the year ended July 31, 2016 were as follows:

	(In thousands)			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Totals
Endowment assets, beginning of year	$ 1,068	$ 1,167	$ 3,262	$ 5,497
Investment income, net	47	188	4	239
Contributions	-	-	4	4
Appropriation of endowment assets	(2)	(43)	(15)	(60)
Endowment assets, end of year	$ 1,113	$ 1,312	$ 3,255	$ 5,680

Interpretation of UPMIFA: The Board of Trustees of the University has interpreted the Uniform Prudent Management of Institutional Funds Act ("UPMIFA") as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary.

As a result of this interpretation, the University classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the University in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the University considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

(1) The duration and preservation of the fund

(2) The purposes of the University and the donor-restricted endowment fund

(3) General economic conditions

(4) The possible effect of inflation and deflation

(5) The expected total return from income and the appreciation of investments

(6) Other resources of the University

(7) The investment policies of the University

Return Objectives and Risk Parameters: The University has adopted investment policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment. Endowment assets include those assets of donor-restricted funds that the University must hold in perpetuity or for a donor-specified period(s) as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of the S&P 500 index while assuming a moderate level of investment risk.

(Continued)

NOTE 8 – ENDOWMENT COMPOSITION (Continued)

Strategies Employed for Achieving Objectives: The purpose of the Endowment Fund is to facilitate donors' desires to make substantial long-term gifts to the community and to develop a new and significant source of revenue for the University. In so doing, the Endowment Fund will provide a secure, long-term source of funds to: (i) stabilize funding during periods of below normal annual campaigns; (ii) fund special grants; (iii) ensure long-term growth; (iv) enhance the University's ability to meet changing community needs in both the short and long term; and (v) support the administrative expenses of the University as deemed appropriate.

Spending Policy and How the Investment Objectives Relate to Spending Policy: The Board of Trustees approves all major spending decisions of the University. Although no formal spending policy has been adopted, historically the University has never used endowment funds to pay for operational expenses.

Funds with Deficiencies: From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or UPMIFA requires the University to retain as a fund of perpetual duration. Deficiencies of this nature that are in excess of related temporarily restricted amounts are reported in unrestricted net assets. There were no deficiencies of this nature at July 31, 2017 and 2016.

NOTE 9 – COMMITMENTS AND CONTINGENCIES

Operating Leases: The University leases classroom space and equipment under various noncancelable operating leases that expire at various dates through February 2023. Future minimum lease payments under noncancelable operating leases at July 31, 2017 are as follows (in thousands):

2018	$ 495
2019	482
2020	455
2021	463
2022	243
Thereafter	84
	$ 2,222

Rent expense for the years ended July 31, 2017 and 2016 was approximately $787,000 and $1,047,000, respectively.

Financial Aid Compliance: The University's students receive significant financial assistance from governmental agencies in the form of grants. The disbursement of funds received under such programs generally requires compliance with terms and conditions specified in grant agreements and are subject to audit by grantor agencies. The grant agreements provide for possible auditing of expenditures by grantor agencies and possible disallowance of certain expenditures. The University has not had any disallowance of expenditures in the past.

(Continued)

NOTE 10 – SUBSEQUENT EVENTS

Management has performed an analysis of the activities and transactions subsequent to July 31, 2017 to determine the need for any adjustments to and/or disclosures within the audited financial statements as of and for the year ended July 31, 2017. Management has performed their analysis through September 29, 2017, which is the date the financial statements were available to be issued.

SUPPLEMENTAL INFORMATION

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Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

Independent Auditor's Report

To the Board of Trustees
Franklin University and Subsidiary

We have audited the consolidated financial statements of Franklin University and Subsidiary as of and for the year ended July 31, 2017 and have issued our report thereon dated September 29, 2017, which contained an unmodified opinion on those financial statements. Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. We have not performed any procedures with respect to the audited financial statements subsequent to September 29, 2017.

The accompanying schedule of expenditures of federal awards is presented for the purpose of additional analysis as required by the Uniform Guidance and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Plante & Moran, PLLC

September 29, 2017

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Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Independent Auditor's Report

To Management and the Board of Trustees
Franklin University and Subsidiary

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Franklin University and Subsidiary (the "University), which comprise the consolidated statement of financial position as of July 31, 2017 and the related consolidated statements of activities and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated September 29, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Franklin University and Subsidiary's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control. Accordingly, we do not express an opinion on the effectiveness of the University's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the University's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Franklin University and Subsidiary's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

To Management and the Board of Trustees
Franklin University and Subsidiary

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the University's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the University's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Plante & Moran, PLLC

September 29, 2017

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Report on Compliance for Each Major Federal Program; Report on Internal Control Over Compliance

Independent Auditor's Report

To the Board of Trustees
Franklin University and Subsidiary

Report on Compliance for Each Major Federal Program

We have audited Franklin University and Subsidiary's (the "University") compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Compliance Supplement that could have a direct and material effect on its major federal program for the year ended July 31, 2017. Franklin University and Subsidiary's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal program.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of Franklin University and Subsidiary's major federal programs based on our audit of the types of compliance requirements referred to above.

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 the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (the "Uniform Guidance"). Those standards and the Uniform Guidance 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 Franklin University and Subsidiary'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 on compliance for each major federal program. However, our audit does not provide a legal determination of Franklin University and Subsidiary's compliance.

Opinion on Each Major Federal Program

In our opinion, Franklin University and Subsidiary complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended July 31, 2017.

Other Matters

The results of our auditing procedures disclosed an instance of noncompliance which is required to be reported in accordance with the Uniform Guidance and which is described in the accompanying schedule of findings and questioned costs as item 2017-001. Our opinion on each major federal program is not modified with respect to this matter.

To the Board of Trustees
Franklin University and Subsidiary

Franklin University and Subsidiary's response to the noncompliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs and corrective action plan. Franklin University and Subsidiary's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on it.

Report on Internal Control Over Compliance

Management of Franklin University and Subsidiary is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered Franklin University and Subsidiary's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the University's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified a certain deficiency in internal control over compliance that we consider to be a material weakness.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention of those charged with governance. We consider the deficiency in internal control over compliance described in the accompanying schedule of findings and questioned costs as item 2017-001 to be a material weakness.

Franklin University and Subsidiary's response to the internal control over compliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs and/or corrective action plan. Franklin University and Subsidiary's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on it.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Plante & Moran, PLLC

September 29, 2017

Schedule of Expenditures of Federal Awards
Year Ended July 31, 2017

Federal Grantor/Program Title	Federal CFDA Number	Federal/Pass-through Grant Number	Total Amount Provided to Subrecipients	Disbursements/ Expenditures
U.S. Department of Education:				
Student Financial Assistance Cluster - Franklin University:				
Federal Supplemental Educational Opportunity Grants	84.007	N/A	$ -	$ 267,710
Federal Work-Study Program	84.033	N/A	-	214,740
Federal Pell Grant Program	84.063	N/A	-	6,311,684
Federal Direct Student Loans	84.268	N/A	-	36,347,993
Total student financial assistance cluster - Franklin University				43,142,127
Student Financial Assistance Cluster - Urbana University:				
Federal Supplemental Education Opportunity Grants	84.007	N/A	-	142,801
Federal Work-Study Program	84.033	N/A	-	67,616
Federal Perkins Loan Program	84.038	N/A	-	1,962,857
Federal Pell Grant Program	84.063	N/A	-	903,042
Federal Direct Student Loans	84.268	N/A	-	6,344,098
Teacher Education Assistance for College and			-	
Higher Education Grant	84.379	N/A	-	11,180
Total student financial assistance cluster - Urbana University				9,431,594
Total Student Financial Assistance Cluster expenditures				**$ 52,573,721**

See Notes to Schedule of Expenditures of Federal Awards.

Note 1 - Basis of Presentation

The accompanying schedule of expenditures of federal awards (the "Schedule") includes the federal grant activity of Franklin University and Subsidiary under programs of the federal government for the year ended July 31, 2017. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (the "Uniform Guidance"). Because the Schedule presents only a selected portion of the operations of Franklin University and Subsidiary, it is not intended to and does not present the financial position, changes in net assets, or cash flows of Franklin University and Subsidiary.

For the year ended July 31, 2017, Franklin University and Subsidiary consists of Franklin University and its wholly owned subsidiary, Franklin LLC, dba Urbana University. Franklin University and Urbana University have separate Student Financial Assistance programs with the U.S. Department of Education. As such, the Student Financial Assistance cluster has been audited as a separate major program for both Franklin University and Urbana University.

Note 2 - Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Pass-through entity identifying numbers are presented where available.

The University has not elected to use the 10 percent *de minimus* indirect cost rate to recover indirect costs as allowed under the Uniform Guidance.

Note 3 - Loan Balances

Loans outstanding at the beginning of the year and loans made during the year are included in the federal expenditures presented in the schedule of expenditures of federal awards. The balances of loans outstanding at July 31, 2017 consist of the following:

Cluster/Program Title	CFDA Number	Loan Balance
Urbana University - Federal Perkins Loan Program	84.038	$ 1,854,918

Note 4 - Federal Direct Loan Program

The University participates in the William D. Ford Direct Loan Program. The University originates the loans, which are then funded through the U.S. Department of Education.

Franklin University and Subsidiary

Schedule of Findings and Questioned Costs
Year Ended July 31, 2017

Section I - Summary of Auditor's Results

Financial Statements

Type of auditor's report issued: Unmodified

Internal control over financial reporting:

• Material weakness(es) identified?	____ Yes	X No
• Significant deficiency(ies) 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?	X Yes	____ No
• Significant deficiency(ies) identified that are not considered to be material weaknesses?	____ Yes	X None reported

Type of auditor's report issued on compliance for major programs: Unmodified

Any audit findings disclosed that are required to be reported in accordance with Section 2 CFR 200.516 (a)?	X Yes	____ No

Identification of major programs:

CFDA Numbers	Name of Federal Program or Cluster
84.007, 84.033, 84.063, 84.268	Student Financial Assistance Cluster - Franklin University
84.007, 84.033, 84.038, 84.063, 84.268, 84.379	Student Financial Assistance Cluster - Urbana University

Dollar threshold used to distinguish between type A and type B programs: $750,000

Auditee qualified as low-risk auditee?	____ Yes	X No

Section II - Financial Statement Audit Findings

None

Section III - Federal Program Audit Findings

Reference Number	Finding
2017-001	**CFDA Number, Federal Agency, and Program Name** - Urbana University: CFDA Nos. 84.063 and 84.268, Department of Education, Federal Pell Grant Program and Federal Direct Student Loans

Federal Award Identification Number and Year - N/A

Pass-through Entity - None

Finding Type - Material weakness and material noncompliance with laws and regulations

Repeat Finding - No

Criteria - Federal Pell Grant Program: An institution shall submit, in accordance with deadline dates established by the secretary, through publication in the Federal Register, other reports and information the secretary requires and shall comply with the procedures the secretary finds necessary to ensure that the reports are correct (34 CFR Section 690.83(b)(2)).

Federal Direct Student Loans: Changes in student status are required to be reported to the National Student Loan Data System (NSLDS) within 30 days of the change or included in a Student Status Confirmation Report (SSCR) sent to the NSLDS within 60 days of the status change (34 CFR Section 685.309(b)).

Condition - The University did not report the proper student status change for certain students that graduated.

Questioned Costs - None

Identification of How Questioned Costs Were Computed - N/A

Context - Of the 18 students tested for student status changes, seven students were not properly reported as graduations.

Cause and Effect - The reports of graduated students submitted to the National Student Clearinghouse did not include all graduations for each term. The University did not have a process in place to ensure that all graduations had been processed prior to submission to the national student clearinghouse.

Recommendation - The University should implement controls and processes to ensure that all graduations are included in student status change reporting each term.

Views of Responsible Officials and Planned Corrective Actions - Management concurs. Urbana University has revised its process to ensure that all students are reported as graduated in the system prior to reporting to the National Student Clearinghouse.