

SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
COLUMBIA, SOUTH CAROLINA
FINANCIAL AND COMPLIANCE REPORT
JUNE 30, 2005 AND 2004

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
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YEARS ENDED JUNE 30, 2005 AND 2004**

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State of South Carolina

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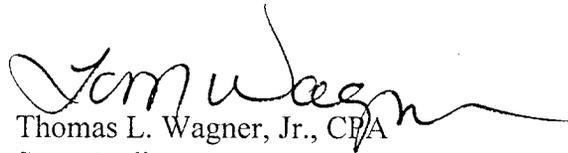
October 5, 2005

The Honorable Mark Sanford, Governor
and
Members of the Authority
South Carolina State Education Assistance Authority
Columbia, South Carolina

This report on the audit of the basic financial statements of the South Carolina State Education Assistance Authority and the accompanying schedule of expenditures of federal awards as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, for the fiscal year ended June 30, 2005, was issued by Derrick, Stubbs & Stith, L.L.P., Certified Public Accountants, under contract with the South Carolina Office of the State Auditor.

If you have any questions regarding this report, please let us know.

Respectfully submitted,


Thomas L. Wagner, Jr., CPA
State Auditor

TLWjr/trb



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INDEPENDENT AUDITOR'S REPORT

To the Members of the Authority
South Carolina State Education Assistance Authority
Columbia, South Carolina

We have audited the accompanying financial statements of the Enterprise Fund of the South Carolina State Education Assistance Authority as of and for the years ended June 30, 2005 and 2004 as listed in the table of contents. These financial statements are the responsibility of the Authority's management. Our responsibility is to express opinions 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 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 audits 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 statements presentation. We believe that our audits provide a reasonable basis for our opinions.

As discussed in Note 1, the financial statements present only the Enterprise Fund of the South Carolina State Education Assistance Authority.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Enterprise Fund of the South Carolina State Education Assistance Authority as of June 30, 2005 and 2004, and the respective changes in its financial position and cash flows, where applicable, thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated August 26, 2005, on our consideration of the Authority's internal control over financial reporting and 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* and should be considered in assessing the results of our audits.

The Management's Discussion and Analysis on pages 3 through 6 is not a required part of the basic financial statements but is supplementary information required by the accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the financial statements of the South Carolina State Education Assistance Authority taken as a whole. The schedules, listed in the table of contents as supplementary information, are presented for the purposes of additional analysis and are not a required part of the financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Derrick, Stubbs & Stith, LLP

August 26, 2005

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEAR ENDED JUNE 30, 2005**

The South Carolina State Education Assistance Authority (Authority) functions to guarantee and provide financing for education loans for students and parents. As a guarantor, the Authority processes loans submitted for guarantee, issues loan guarantees, provides collection assistance for delinquent loans, pays claims for loans in default, collects loans on which default claims have been paid, and makes appropriate responses to the Secretary. As a provider of financing, the Authority issues bonds to finance education loans.

The Authority was originally created to provide a means of making loans to students in order to enable them to attend eligible institutions, as such terms are defined in the Higher Education Act. Such loan financing has been conducted by the Authority through its Student Loan Finance Program which has been administered by the South Carolina Student Loan Corporation (Corporation) since its inception.

The Corporation and the Authority have entered into Loan Agreements pursuant to the terms of which the Authority has agreed to lend bond proceeds to the Corporation to enable the Corporation to make or acquire education loans. The obligation of the Corporation to repay the finance loans is evidenced by a promissory note of the Corporation and is secured by a pledge under the Loan Agreement.

This section of the Authority's annual financial report presents a discussion and analysis of the Authority's financial performance for the fiscal year ended June 30, 2005. Please read it in conjunction with the Authority's statement of net assets, statements of revenue, expenses and changes in net assets, statement of cash flows, and the notes to financial statements, which follow this section.

FINANCIAL HIGHLIGHTS:

| | |
|---|--|
| • | The Authority's total assets at June 30, 2005 were approximately \$ 987,995,000, which is an increase of approximately \$ 226,654,000 or 30% over June 30, 2004. |
| • | The Authority's finance loans at June 30, 2005 were approximately \$ 772,405,000, which is an increase of approximately \$ 248,855,000 or 47% over June 30, 2004. |
| • | The Authority's operating revenue for the fiscal year ended June 30, 2005 was approximately \$ 47,128,000, which is an increase of approximately \$15,930,000 or 51% over the fiscal year ended June 30, 2004. |
| • | The Authority's interest expense for the fiscal year ended June 30, 2005 was approximately \$ 17,586,000, which is an increase of approximately \$ 7,784,000 or 79% over the fiscal year ended June 30, 2004. |
| • | The Authority's total other operating expenses for the fiscal year ended June 30, 2005 was approximately \$ 25,981,000, which is a decrease of \$3,858,000 or 13% under the fiscal year ended June 30, 2004 |
| • | The Authority's change in net assets for the fiscal year ended June 30, 2005 was approximately \$ 5,477,000, which is an increase of 237% over the previous fiscal year. |

OVERVIEW OF THE FINANCIAL STATEMENTS:

The Authority's financial statements are prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied on an accrual basis. Under the accrual basis of GAAP, revenues are recognized in the period in which they are earned and expenses are recognized in the period in which they are incurred. The three basic financial statements presented within the financial statements are:

Statements of Net Assets – This statement presents information regarding the Authority's assets, liabilities and net assets. Net assets represent the total assets less the total liabilities. The statement of net assets classifies assets, liabilities and net assets as current, long-term and restricted.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEAR ENDED JUNE 30, 2005**

OVERVIEW OF THE FINANCIAL STATEMENTS (Continued):

Statements of Revenues, Expenses and Changes in Net Assets – This statement presents the Authority's interest income, cost of funds, operating expenses and changes in net assets for the fiscal year.

Statements of Cash Flows – The Authority's statement of cash flows is presented on the direct method of reporting, which reflects cash flows from operating, non-capital financing, capital and investing activities.

FINANCIAL ANALYSIS OF THE AUTHORITY:

The Authority's total net assets at June 30, 2005 were approximately \$ 129,936,000 which is an increase of approximately \$ 5,477,000 or 4% over June 30, 2004. Components of the Authority's balance sheet as of June 30, 2005 and June 30, 2004 were as follows:

| | 2005 | 2004 | Percentage Increase/(Decrease) |
|----------------------------------|-----------------------|-----------------------|---|
| Current Assets | \$ 288,627,753 | \$ 299,793,897 | -4% |
| Capital assets | 239,367 | 224,576 | 7% |
| Other Long-Term Assets | 698,732,198 | 460,770,690 | 52% |
| Restricted Assets | <u>395,300</u> | <u>551,185</u> | -28% |
| Total Assets | <u>\$ 987,994,618</u> | <u>\$ 761,340,348</u> | 30% |
| Current Liabilities | \$ 150,010,572 | \$ 54,068,271 | 177% |
| Long-Term Liabilities Payable | <u>708,047,759</u> | <u>582,812,786</u> | 21% |
| Total Liabilities | <u>\$ 858,058,331</u> | <u>\$ 636,881,057</u> | 35% |
| Net Assets: | | | |
| Invested in Capital Assets | \$ 239,367 | \$ 224,576 | 7% |
| Restricted | 128,619,521 | 123,180,027 | 4% |
| Unrestricted | <u>1,077,399</u> | <u>1,054,688</u> | 2% |
| Total Net Assets | <u>\$ 129,936,287</u> | <u>\$ 124,459,291</u> | 4% |
| Total Liabilities and Net Assets | <u>\$ 987,994,618</u> | <u>\$ 761,340,348</u> | 30% |

Please see Note 6 and Note 8 respectively for more detail on capital assets and long-term debt activity. The increase noted above in the Authority's total assets is due to the issuing of bonds and subsequent increase in finance loans. Total assets increased from approximately \$ 761,340,000 at June 30, 2004 to approximately \$ 987,995,000 at June 30, 2005.

Finance loans increased over 47% from approximately \$ 523,549,000 at June 30, 2004 to approximately \$ 772,405,000 at June 30, 2005.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEAR ENDED JUNE 30, 2005**

FINANCIAL ANALYSIS OF THE AUTHORITY (Continued):

Components of the statement of revenues, expenses and changes in net assets for these two fiscal years are as follows:

| | 2005 | 2004 | Percentage Increase/(Decrease) |
|--------------------------------------|----------------------|-----------------------|---|
| Loan Interest Income | \$ 35,512,310 | \$ 21,541,299 | 65% |
| Guaranty Agency Income | 7,163,830 | 7,087,387 | 1% |
| Investment Interest Income | <u>4,451,673</u> | <u>2,568,682</u> | 73% |
| Total Operating Revenue | <u>\$ 47,127,813</u> | <u>\$ 31,197,368</u> | 51% |
| Interest Expense | <u>\$ 17,586,492</u> | <u>\$ 9,802,740</u> | 79% |
| Other Operating Expenses: | | | |
| General Administration | 4,315,100 | 3,987,885 | 8% |
| External Loan Servicing | 4,198,752 | 3,901,624 | 8% |
| Borrower Incentives | 9,755,525 | 15,488,459 | -37% |
| Consolidation and Lender Rebate Fees | 3,084,861 | 3,150,063 | -2% |
| Other Fees | <u>4,626,425</u> | <u>3,310,689</u> | 40% |
| Total Other Operating Expenses | <u>\$ 25,980,663</u> | <u>\$ 29,838,720</u> | -13% |
| Total Operating Expenses | \$ 43,567,155 | \$ 39,641,460 | 10% |
| Total Non-Operating (Income)Expenses | <u>(1,916,338)</u> | <u>(4,445,119)</u> | -57% |
| Change in Net Assets | <u>\$ 5,476,996</u> | <u>\$ (3,998,973)</u> | 237% |

The increase noted above in the Authority's change in net assets of approximately \$ 9,476,000 over the past year relates primarily to the increase in short term interest rates and decrease in the Authority's borrower incentive programs. By continuing to offer incentives, the Authority has lowered its arbitrage liability by approximately \$ 2,180,000 from last fiscal year ended, 6/30/2004.

The increase in loan interest income, investment interest income and interest expense during the year ended June 30, 2005 are due to an increase in short term interest rates.

As noted above, the Authority's other operating expenses for the fiscal year ended June 30, 2005 decreased by 13% over the previous fiscal year.

The Authority prepares an annual operating budget that is used as a management control device for tracking the various expenses. Accounting principles generally accepted in the United States of America do not require a comparison of budget to actual expenses for enterprise funds.

Non-operating income decreased approximately \$ 2,529,000 or 57% due to a decrease in the effect of the Authority's borrower incentive programs reducing arbitrage payable.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEAR ENDED JUNE 30, 2005**

DEBT ADMINISTRATION:

The Authority has funded student loan notes by issuing tax-exempt bonds. The bonds must be approved by the Authority's and the Corporation's boards prior to being issued. Tax-exempt bonds also must receive an allocation of the State of South Carolina private activity volume ceiling or "cap". In addition, the issues must comply with federal statutes and with the rules and regulations of the United States Treasury Department.

At June 30, 2005, the Authority had \$ 745,715,000 principal amount of bonds payable, an increase of 26% from the \$ 592,010,000 principal amount outstanding at June 30, 2004. Detailed information on the Authority's debt is presented in Note 8 to the financial statements.

All \$ 745,715,000 of Authority debt is publicly held and has long-term credit ratings assigned by Moody's Investors Service (Moody's) and Standard and Poor's (S&P) based on the type of security as shown in the table below. The credit ratings have been maintained, and periodically the ratings have been confirmed in connection with new parity debt issues or extensions of recycling periods.

| Credit Rating(s) | Principal Amount | Type of Security |
|------------------------|------------------|------------------|
| AAA S&P or Aaa Moody's | \$692,180,000 | Senior Lien |
| A S&P or A2 Moody's | \$ 53,535,000 | Subordinate Lien |

CONDITIONS AFFECTING FINANCIAL POSTION:

The Authority has experienced significant growth in all aspects of its operations. With the increase in the volume of student loan applications being processed, the Authority's fiscal year 2006 reflects continued growth. The Authority has added additional staff to handle the additional work associated with this growth. The Authority's budgeted administrative expenses for the fiscal year 2006 reflect the additional costs to be incurred as a result of the increase in staff.

Higher interest rates at June 30, 2005 will result in student loan interest rates being increased during the fiscal year ending June 30, 2006, which will cause an increase in loan interest income to the Authority.

SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
STATEMENTS OF NET ASSETS
ENTERPRISE FUND
JUNE 30, 2005 AND 2004

| ASSETS | 2005 | 2004 | LIABILITIES | 2005 | 2004 |
|--|-----------------------|-----------------------|---|-----------------------|-----------------------|
| Current Assets | | | Current Liabilities | | |
| Cash and cash equivalents | \$ 145,448,489 | \$ 194,404,117 | Accounts payable | \$ 326,895 | \$ 99,390 |
| Cash and cash equivalents - restricted | 51,481,180 | 30,937,052 | Arbitrage payable to federal government | 344,553 | 292,978 |
| Receivables | | | Compensated absences | 211,087 | 173,585 |
| Current portion of finance loans | 76,400,000 | 64,800,000 | Due to South Carolina Student Loan Corporation | 93,170,694 | 28,808,236 |
| Due from South Carolina Student Loan Corporation | 9,678,139 | 8,214,023 | Consolidation rebate fee payable | 645,869 | 565,685 |
| Accrued interest receivable | 132,682 | 142,459 | Payable from restricted assets | | |
| Federal reinsurance receivable | 5,160,587 | 662,732 | Current maturities of bonds payable | 48,035,000 | 20,995,000 |
| Loan processing issuance fee receivable | 133,570 | 108,249 | Accrued bond interest payable | 7,276,474 | 3,133,397 |
| Account maintenance fee receivable | 193,106 | 525,265 | Total current liabilities | 150,010,572 | 54,068,271 |
| Total current assets | 288,627,753 | 299,793,897 | | | |
| | | | Long-Term Liabilities | | |
| Long-Term and Other Assets | | | Bonds payable, less current maturities, deferred amount | | |
| Receivables | | | of debt refunding of \$ 195,476 in 2005 and \$ 400,683 in | | |
| Finance loans, less current portion | 696,004,853 | 458,749,393 | 2004 and bond premium and discounts of \$ 1,436,980 in | | |
| Deferred cost of issuance of bonds | 2,727,345 | 2,021,297 | 2005 and \$ 1,725,147 in 2004 | 696,047,544 | 568,889,170 |
| Restricted assets | | | Provision for losses on student loans | 308,193 | |
| Investments | 395,300 | 551,185 | Federal reserve funds payable | 1,148,283 | 1,148,283 |
| Total long-term and other assets | 699,127,498 | 461,321,875 | Arbitrage payable to federal government payable from | | |
| | | | restricted funds | 10,464,005 | 12,068,186 |
| | | | Arbitrage payable to federal government, less | | |
| | | | current portion | 79,734 | 707,147 |
| | | | Total long-term liabilities | 708,047,759 | 582,812,786 |
| | | | | | |
| | | | Total liabilities | 858,058,331 | 636,881,057 |
| | | | | | |
| Property, Plant & Equipment | | | Net Assets | | |
| Furniture and equipment | 374,793 | 293,220 | Invested in capital assets | 239,367 | 224,576 |
| Automobile | 17,000 | 17,000 | Restricted for | | |
| Less: accumulated depreciation | (152,426) | (85,644) | Debt service | | |
| Total property, plant & equipment | 239,367 | 224,576 | Bond indentures - 1993 resolution | 94,256,405 | 90,346,072 |
| | | | Bond indentures - 2002 resolution | 2,391,448 | 1,764,308 |
| | | | Other | | |
| | | | Federal government | 7,679,808 | 9,881,700 |
| | | | Guaranty agency operating account | 24,291,860 | 21,187,947 |
| | | | Unrestricted | 1,077,399 | 1,054,688 |
| | | | | | |
| Total assets | \$ 987,994,618 | \$ 761,340,348 | Total net assets | \$ 129,936,287 | \$ 124,459,291 |

See notes to financial statements.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
STATEMENTS OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS
ENTERPRISE FUND
YEARS ENDED JUNE 30, 2005 AND 2004**

| | <u>2005</u> | <u>2004</u> |
|---|------------------------------|------------------------------|
| Operating Revenue | | |
| United States Department of Education | | |
| Loan processing and issuance fee | \$ 1,720,026 | \$ 1,899,291 |
| Account maintenance fee | 2,269,878 | 2,259,479 |
| Default aversion fee income | 868,597 | 915,929 |
| Retention on default collections (net of payments to federal government of \$ 3,192,341 in 2005 and \$ 3,133,363 in 2004) | 2,231,668 | 1,968,487 |
| Income from South Carolina Student Loan Corporation | | |
| Subsidized Interest | 3,331,798 | 2,598,123 |
| Special allowance | 15,321,834 | 9,662,846 |
| Non-subsidized interest | 6,918,847 | 4,222,336 |
| Late charges | 42,148 | 11,750 |
| Miscellaneous payments of student loans | 331 | 272 |
| Reimbursement of bond expense | 9,897,352 | 5,045,972 |
| Reinsurance recoveries | 57,049 | 44,201 |
| Miscellaneous income | 16,612 | |
| Interest/investment income | 4,404,805 | 2,665,405 |
| Net increase (decrease) in the fair value of investments | 46,868 | (96,723) |
| Total operating revenue | <u>47,127,813</u> | <u>31,197,368</u> |
| Operating Expenses | | |
| Personnel | 3,121,655 | 2,896,970 |
| Contractual | 536,763 | 450,000 |
| General operating | 656,682 | 640,915 |
| South Carolina Student Loan Corporation for operating costs | 4,198,752 | 3,901,624 |
| Bond interest expense | 17,586,492 | 9,802,740 |
| Amortization - deferred cost of bond issuance | 179,882 | 152,961 |
| Default aversion fee expense | 868,597 | 915,929 |
| Loan fees | 3,084,861 | 3,150,063 |
| Borrower incentives | 9,755,525 | 15,488,459 |
| Broker/dealer fees | 1,944,217 | 1,383,377 |
| Reinsurance expense | 753,299 | |
| Other fees | 880,430 | 858,422 |
| Total operating expenses | <u>43,567,155</u> | <u>39,641,460</u> |
| Operating income (loss) | 3,560,658 | (8,444,092) |
| Non-operating revenues (expenses) | | |
| Arbitrage income (expense) | <u>1,916,338</u> | <u>4,445,119</u> |
| Change in Net Assets | 5,476,996 | (3,998,973) |
| Net Assets | | |
| Beginning | <u>124,459,291</u> | <u>128,458,264</u> |
| Ending | <u><u>\$ 129,936,287</u></u> | <u><u>\$ 124,459,291</u></u> |

See notes to financial statements.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
STATEMENTS OF CASH FLOWS
ENTERPRISE FUND
YEARS ENDED JUNE 30, 2005 AND 2004**

| | <u>2005</u> | <u>2004</u> |
|--|-------------------------------------|------------------------------|
| Cash flows from operating activities | | |
| Receipts from borrowers and U.S. Department of Education | \$ 87,352,770 | \$ 39,789,114 |
| Receipts from SCSLC services provided | 34,630,908 | 32,292,929 |
| Payments to suppliers | (42,094,213) | (41,782,179) |
| Payments to employees | (3,084,153) | (2,874,856) |
| Net cash provided by operating activities | <u>76,805,312</u> | <u>27,425,008</u> |
| Cash flows from non-capital financing activities | | |
| Finance loan advances to South Carolina Student Loan Corporation for student loans | (647,181,032) | (648,162,256) |
| Finance loan payments received from South Carolina Student Loan Corporation | 398,325,572 | 385,685,638 |
| Arbitrage paid | (263,681) | (496,696) |
| Payment on bonds payable | (20,995,000) | (13,750,000) |
| Proceeds from issuing revenue and refunding bonds for student loans | 174,700,000 | 100,150,000 |
| Costs of bond issuance paid from refunding bond proceeds | (885,930) | (570,207) |
| Interest paid on revenue bonds | (13,443,415) | (9,751,117) |
| Net cash (used in) non-capital financing activities | <u>(109,743,486)</u> | <u>(186,894,638)</u> |
| Cash flows from capital and related financing activities | | |
| Purchase of capital assets | <u>(90,661)</u> | <u>(205,749)</u> |
| Cash flows from investing activities | | |
| Interest received on investment securities | 4,414,583 | 2,850,597 |
| Sale of investments | 155,884 | 1,252,178 |
| Net increase (decrease) in fair value of investments reported as cash equivalents | 46,868 | (96,723) |
| Net cash provided by investing activities | <u>4,617,335</u> | <u>4,006,052</u> |
| Net (decrease) in cash and cash equivalents | (28,411,500) | (155,669,327) |
| Cash and cash equivalents | | |
| Beginning | <u>225,341,169</u> | <u>381,010,496</u> |
| Ending | <u><u>\$ 196,929,669</u></u> | <u><u>\$ 225,341,169</u></u> |

See notes to financial statements.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
STATEMENTS OF CASH FLOWS
ENTERPRISE FUND
YEARS ENDED JUNE 30, 2005 AND 2004**

| | <u>2005</u> | <u>2004</u> |
|---|--------------------------|--------------------------|
| Reconciliation of operating income (loss) to net cash provided by (used in) operating activities | | |
| Operating income (loss) | \$ 3,560,658 | \$ (8,444,092) |
| Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities | | |
| Purchase of student loans due to loan guarantees | (25,908,477) | (14,142,618) |
| Payments received from U.S. Department of Education under federal reinsurance program | 21,410,622 | 14,420,260 |
| Amortization of deferred cost of bond issuance | 179,882 | 152,961 |
| Amortization of deferred amount on refunding - interest expense | 205,207 | 365,562 |
| Amortization of premiums and discounts on bonds payable - interest expense | 288,168 | 347,180 |
| Interest/investment income (investing activities category) | (4,404,805) | (2,665,405) |
| Depreciation expense | 75,870 | 75,959 |
| Provision for loan losses | 308,193 | |
| Net (increase) decrease in fair value of investments reported as cash equivalents (investing activities category) | (46,868) | 96,722 |
| Bond interest expense (non-capital financing activities category) | 17,586,492 | 9,802,739 |
| Changes in assets and liabilities | | |
| (Increase) decrease in due from South Carolina Student Loan Corporation | (1,464,116) | (1,931,163) |
| (Increase) decrease in loan processing and issuance fee receivable | (25,321) | 56,056 |
| (Increase) decrease in account maintenance fee receivable | 332,159 | (52,806) |
| Increase (decrease) in due from other funds | | 279,722 |
| (Increase) decrease in miscellaneous receivables | | 189,512 |
| Increase (decrease) in accounts payable | 227,504 | (158,719) |
| Increase (decrease) in compensated absences liability | 37,502 | 22,114 |
| Increase (decrease) in consolidation rebate fee payable | 80,184 | 565,685 |
| Increase (decrease) in due to other funds | | (279,722) |
| Increase (decrease) in due to South Carolina Student Loan Corporation | 64,362,458 | 28,725,061 |
| Net cash provided by operating activities | <u>76,805,312</u> | <u>27,425,008</u> |
| Supplemental disclosures of cash flow information | | |
| Interest collected on finance loans - operating activities | <u>11,714,761</u> | <u>4,889,296</u> |
| Arbitrage income incurred and liability accrued - non-capital financing activity | <u>1,916,338</u> | <u>4,445,119</u> |
| Principal amounts of bonds - refunded - non-capital financing activity | <u>3,000,000</u> | <u>8,150,000</u> |
| Retirement of fixed assets - capital and related financing activity | <u>9,088</u> | <u>21,911</u> |
| Write-off of accumulated depreciation related to retired assets - capital and related financing activity | <u>\$ 9,088</u> | <u>\$ 21,911</u> |

See notes to financial statements

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies

Reporting entity: The South Carolina State Education Assistance Authority (Authority) is a body politic and corporate and a public instrumentality of the State of South Carolina. The Authority is a part of the State of South Carolina created by Act No. 433 of the Acts and Joint Resolutions of the General Assembly for the year 1971, now codified as Chapter 115, Title 59 of the Code of Laws of South Carolina, 1976, as amended. The Authority is governed by its members, who under the Act are the members of the State Budget and Control Board (Board). The Board consists of five (5) members by virtue of their position in state government. They are the Governor, Treasurer, Comptroller General, Chairman of Senate Finance Committee and Chairman of South Carolina House of Representatives Ways and Means Committee.

The Authority is considered to be part of the State of South Carolina because of the common Board and its financial accountability over the Authority. The funds of the Authority are included in the Comprehensive Annual Financial Report of the State of South Carolina. The financial statements of the Authority present the financial position, results of operations and cash flows solely of the Authority and do not include any component units, organizations, or other funds of the State of South Carolina.

The Authority discharges its statutory obligations through two distinct programs. The program through which the Authority conducts its guarantee activities is herein referred to as the "Student Loan Insurance Program." The program through which the Authority finances the making of education loans by South Carolina Student Loan Corporation (SCSLC) is herein referred to as the "Student Loan Finance Program."

The Authority was originally created in order to provide a means of making loans to students in order to enable them to attend eligible institutions, as such terms are defined in the Higher Education Act. Such loan financing has been conducted by the Authority through its Student Loan Finance Program which has, since its inception, been administered by SCSLC.

The Authority has been authorized by the State of South Carolina to issue revenue bonds for the purpose of making student loans. The Authority has approved SCSLC as an eligible lender under its program and has designated it as the private, non-profit agency to administer these loans. It is the duty of SCSLC to process applications, make student loans and collect principal, interest, fees and penalties on such loans. Loans may or may not be subsidized. Interest is paid on subsidized loans during the enrolled, grace, and deferred periods by the U.S. Department of Education. Upon entering the repayment period, the interest is paid by the borrower. Also, the U.S. Department of Education pays SCSLC a special allowance which is based on a variable percentage of the unpaid principal of the loans. This income is a reimbursement to help offset administrative expenses and payments of bonds. SCSLC remits this income along with the principal and interest collected on loans to the Authority as it is received for bonds under the 1993 resolution. Under the 2002 resolution, the amount necessary to pay debt service on the Authority's bonds is required to be reimbursed as defined by the 2002 bond resolution.

The operations of the Authority are administered by employees of SCSLC. The Authority reimburses SCSLC upon request for the actual operating expenses incurred in the administration of the program in accordance with a previously approved budget. All leases are in the name of SCSLC and the Authority pays its pro rata share based on space occupied, equipment usage, and loan servicing costs.

Neither the Authority nor SCSLC is considered a component unit of the other because each is a legal separate organization and not financially accountable to/for the other.

In May 1978, the Authority initiated its Student Loan Insurance Program and commenced guaranteeing Guaranteed Loans as the guaranty agency for the State under §428(c) of the Higher Education Act. In order to administer its Student Loan Insurance Program effectively, the Authority processes loans submitted for guarantee, issues loan guarantees, provides collection assistance for delinquent loans, pays claims for loans in default, collects loans on which default claims have been paid, and makes appropriate responses to the Secretary. The Authority is also responsible for initiating policy and performing compliance reviews as required by the Higher Education Act with respect to certain schools participating in the Student Loan Insurance Program.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Business – type activity: The accounts of the Authority are organized on the basis of funds, each of which is considered a separate accounting entity. The operation of each account uses a separate set of self-balancing accounts that comprise its assets, liabilities, net assets, revenue and expenses.

The Authority's Enterprise Fund, called "Education Assistance Fund", reports the activities to fulfill the entity's authorized purposes of issuing revenue bonds to finance student loans which are handled by South Carolina Student Loan Corporation and guaranteeing guaranteed loans. The Authority's Enterprise Fund is composed of the collection account prior unpledged, 1993 resolution, 2002 resolution, agency operating account, and the federal student loan reserve account. These accounts, except for the federal student loan reserve account, agency operating account and collection account prior unpledged, constitute pledged income for the liquidation of outstanding bonds after transfers for operations.

The Authority reports net assets reserved for current debt service as the accrued interest plus ten months of the outstanding bond principal due as of year end as required by the bond indentures (see Note 8). Under the 1993 Bond Resolution, restricted for bond indentures represents net assets for future debt service and includes six months interest to become due on the principal amount or three percent of the outstanding bond principal as specified under each bond series plus principal and interest collected on student loans not yet required to meet current debt service or used to make student loans. Under the 2002 Bond Resolution, restricted for bond indentures represents net assets for future debt service and includes one percent (1%) of the outstanding bond principal as specified under each bond series plus principal and interest allocated on student loans not yet required to meet current debt service. Under the bond resolutions, the restricted for bond indentures also includes one to four months projected operating expenses and any unamortized costs of issuances. The unrestricted is the residual equity not legally reserved for bond indentures.

The 1993 and 2002 resolution accounts each include a sinking account that is used to deposit the proceeds from the sale of bonds and collections on loans including federal interest and income from SCSLC which, as lender, bills the Department of Education directly. All investment income on investments in the debt reserve fund of the sinking account is recorded in the sinking account as required by the bond indentures. The sinking account is used to make transfers to the debt reserve and loan accounts.

The 1993 and 2002 resolution accounts each include a debt reserve account that is a part of the sinking account. Simultaneously with the issuance and delivery of any series of bonds, the Authority is required to deposit monies equal to the debt reserve requirements, based on a percentage of outstanding bonds, into the debt reserve account. These requirements include the forward funding of the debt service monies necessary to make debt service account interest, principal and cumulative sinking fund payments when due and payable. The current debt service account must contain accrued interest payable and a portion of the outstanding bond principal as of June 30, as required in the bond indentures. The balance of the account for future debt service consists of a portion of the original bond issue and a portion of the outstanding balance.

The 1993 and 2002 resolution accounts each include a loan account that is used to deposit bond proceeds which are transferred from the sinking account for the purpose of making loans and paying the cost of issuance of bonds. Other transfers from the sinking account are deposited into the loan account to reimburse monies which have been transferred to SCSLC for operations.

The Collection Account Prior Unpledged collects all payments on loans on behalf of the Authority and SCSLC. The account is required to disburse to each Authority account and to SCSLC by the tenth of each month for the prior month.

The Federal Student Loan Reserve Account (FSLRF) is used to account for activity as required by the 1998 reauthorization of the Higher Education Act. This account is used to account for investment income and insurance premiums withheld from borrowers' loans. The Authority has not charged insurance premiums for

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Business – type activity (continued):

loans guaranteed since March 1, 1999; however, the Authority reserves the right to reinstate such charges at such times and in such lawful amounts as it deems appropriate. Amounts in the Federal Student Loan Reserve Account can only be used to pay lender claims on defaulted loans and to disburse default aversion fees to the Agency Operating Account for default aversion activities. Upon payment to lenders for defaulted loans, these funds are then reimbursed to the Federal Student Loan Reserve Account by the U. S. Department of Education at a percentage determined by the Authority's default rate. Payments to lenders for defaulted loans are recorded as Federal Reinsurance Receivables. Reimbursement by the U. S. Department of Education reduces the Federal Reinsurance Receivable. The Authority has always received the maximum reimbursement allowable under the Supplemental Guarantee Agreement and does not anticipate falling below this level (See Note 3).

The Agency Operating Account is used to account for all loan processing and issuance fees, account maintenance fees, default aversion fees, and the retention on default collections. The U. S. Department of Education pays all of the fees except the default aversion fees reimbursed by the Federal Student Loan Reserve Account. The loan processing issuance fee was equal to 0.65% of the total principal amount of loans originated prior to October 1, 2003. As of October 1, 2003 the loan processing fee changed to 0.40%. The account maintenance fee is equal to 0.10% of the average original principal balance of loans outstanding for the fiscal year. The default aversion fee is equal to one percent of the principal and interest of a loan upon which default aversion activity was performed. This is reimbursed from the Federal Student Loan Reserve Account. Should this loan subsequently default, the default aversion fee is refunded back to the FSLRF. Retention on Default Collections is reported by the Authority directly to the Department of Education for services it performs in its role as guarantor. The Authority recognizes income related to a specified portion (23% as of October 1, 2003 and 24% prior to October 1, 2003) of collections adjusted for certain items made on behalf of the Federal government on defaulted loans. The remaining balance of collections is remitted to the Federal government. The total cumulative value at June 30, 2005 and 2004 of all defaulted student loans purchased by the Authority is \$169,248,000 and \$143,339,523, respectively (See Note 3). The Authority records the purchased defaulted loans as assets, but only recognizes its portion of the share of any recoveries in the year of collection. Funds in the Agency Operating Account can only be used for application processing, loan disbursement, enrollment and repayment status management, permitted default prevention activities, default collection activities, school and lender training, compliance monitoring and other student financial aid related activities as determined by the Secretary and for voluntary irrevocable transfers to the FSLRF. Except for funds transferred from the Federal Student Loan Reserve Account, the Agency Operating Account is considered to be the property of the guaranty agency. To date, no funds have been transferred from the FSLRF to the Agency Operating Account.

Basis of accounting: The accrual basis of accounting is used for the Education Assistance Fund. Under the accrual basis of accounting, revenue is recognized when earned, and expenses are recorded when incurred. Investment income is recorded at stated interest rates with no amortization of premiums or discounts. Net increase (decrease) in the fair value of investments include unrealized and realized gains and losses. Bond payable premiums and discounts are amortized over the life of the bonds and netted against interest expense. The Authority applies all Government Accounting Standards Board (GASB) pronouncements and all Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989, when not in conflict with GASB pronouncements. In accordance with GASB Statement 20, the Authority has elected not to implement FASB Statements 103 and after.

Budget and budgetary accounting: Certain expenses for the Enterprise Fund are budgeted as a management control device. However, the cost of issuing bonds, SCSLC expenses, interest expense, reinsurance and other fees and revenue are not budgeted. Accounting principles generally accepted in the United States of America do not require a comparison of budget to actual expenses.

These budgets are approved by the SCSLC Board and the State Treasurer and are not adopted by the Legislature or printed in the Appropriations Act. The Authority is subject to State laws and regulations.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Budget and budgetary accounting (continued):

Expenditures in excess of the budgeted amounts are not in violation of State laws. However, these are approved by the Board.

Compensated absences: Depending on length of employment, employees earn annual vacation at the rate of twelve (12) to twenty-five (25) days per year. Employees are expected to use at least one week (5 consecutive days) each year. An employee may not carry forward more than five (5) vacation days to the next year without the supervisor's permission. Earned, but unused, annual vacation will be paid when an employee terminates employment except when this termination is involuntary or inadequate notice is given. Sick leave is earned at the rate of 7 to 10 days per year depending on length of employment. An employee may not carry forward more than sixty (60) sick days to the next year without the supervisor's approval. Employees are not paid for earned, but unused, sick days upon termination of employment. The Authority calculates the gross compensated absences liability based on recorded balances of unused vacation leave, compensatory holiday, and overtime leave for those specific SCSLC employees who administer Authority operations. The entire unpaid liability for which the employer expects to compensate employees through paid time off or cash payments, inventoried at fiscal year-end current salary costs and the cost of the salary-related benefit payments, is recorded. The net change in the liability is recorded in the current year in the personnel expenses.

Non-exchange transactions: The Authority adheres to GASB Statement No. 33, *Accounting and Financial Reporting for Non-exchange Transactions* which standardizes the accounting and financial reporting for non-exchange transactions involving financial or capital resources. For the Authority, there generally are two types of non-exchange transactions, *Government-mandated non-exchange transactions* which occur when a government at one level provides resources to a government at another level and requires the recipient to use the resources for a specific purpose and *voluntary non-exchange transactions* which result from legislative or contractual agreements, other than exchanges, entered into willingly by the parties to the agreement. The Authority recognizes non-exchange transactions when they are both measurable and probable of collection. For *Government-mandated non-exchange transactions* and *voluntary non-exchange transactions*, the Authority recognizes assets when all applicable eligibility requirements are met or resources are received, whichever is first, and revenue when all applicable eligibility requirements are met.

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 date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and cash equivalents: The amounts shown in the financial statements as "cash and cash equivalents" represent cash on deposit in banks, cash on hand with the State Treasurer and cash invested in various instruments by the State Treasurer as part of the State's internal cash management pool and cash invested in various instruments by the Bank of New York..

Because the State's internal cash management pool operates as a demand deposit account, amounts invested in the pool are classified as cash and cash equivalents. The State Treasurer administers the cash management pool. The pool includes some long-term investments such as obligations of the United States and certain agencies of the United States, obligations of domestic corporations, certificates of deposit and collateralized repurchase agreements. Most State agencies participate in the cash management pool; however, some agency accounts are not included in the pool because of restrictions on the use of the funds. For those accounts, cash equivalents include investments in short-term, highly liquid securities including those that are classified as restricted having a maturity at the time of purchase of three months or less.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Cash and cash equivalents (continued):

The State's internal cash management pool consists of a general deposit account and several special deposit accounts. The State records each fund's equity interest in the general deposit account; however, all earnings on that account are credited to the General Fund of the State.

The Authority records and reports its deposits in the general deposit account at cost. The Authority reports its deposits in the special deposit accounts at fair value. Investments held by the pool are recorded at fair value. Interest earned by the Authority's special deposit accounts is posted to the Authority's account at the end of each month and is retained by the Authority. Interest earnings are allocated based on the percentage of the Authority's accumulated daily interest receivable to the total undistributed interest received by the pool. Reported interest income includes interest earnings, realized gains/losses, and unrealized gains/losses arising from changes in fair value of investments in the pool. Realized gains and losses are allocated monthly and are included in the accumulated income receivable. Unrealized gains and losses are allocated at year-end based on the Authority's percentage ownership in the pool.

Although the State's internal cash management pool includes some long-term investments, it operates as a demand deposit account; therefore, for credit risk information pertaining to the State's internal cash management pool, see the deposits disclosures in Note 2.

For the Authority's funds not held by the State Treasurer, cash equivalents include investments in short-term, highly liquid securities having a maturity at the time of purchase of three months or less.

Amortization of deferred cost of issuance of bonds and bond premiums and discounts: Cost of issuance of bonds is being amortized over the lives of the bond issues on a straight-line basis and are included in operating expenses. Bond premiums and discounts are amortized over the terms of the bonds using the straight-line method and are recorded as an addition or deduction to interest expense.

Deferred amount of debt refunding: The deferred amount of debt refunding is the difference between the reacquisition price and the net carrying amount of the old debt. Reacquisition price is the amount required to repay previously issued debt in a refunding transaction and it includes principal of the old debt plus any call premium. The net carrying amount is the amount due at maturity, adjusted for any unamortized premium or discount and issuance costs related to the old debt. The amount is being amortized as a component of interest expense on the straight line basis over the shorter of the remaining life of the old debt or the life of the new debt. It is being charged to operations using the effective - interest method. This treatment applies to debt refunding after July 1, 1994.

Risk management: The Authority is exposed to various risks of losses related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Authority pays insurance premiums to certain other State agencies to cover risks that may occur in normal operations. Several State funds accumulate assets and the State itself assumes all risks for claims of State employees for unemployment compensation benefits. In addition, the Authority pays premiums to the State's Insurance Reserve Fund which accumulates assets to cover general tort claims.

Premiums for worker's compensation, property insurance including fixed assets, group life, fidelity bonds, and employee health insurance are paid to private insurance carriers and the Authority's coverage is subject to the limits of these policies. The expense for these items is charged to the enterprise fund. Settled claims have not exceeded this commercial coverage in any of the past three fiscal years.

Property and equipment: Furniture, equipment and automobiles costing over \$ 5,000 are capitalized at cost when purchased. Depreciation has been provided using the straight-line method over useful lives of three to ten years for furniture and equipment and three years for automobiles and computers.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Operating and non-operating revenues/expenses: Balances classified as operating revenues and expenses are those which comprise the Authority's principle ongoing operations. Since the Authority's operations are similar to those of any other finance company, all revenues and expenses are considered operating except the recall of Federal Reserve Funds and arbitrage expense.

Applying restricted or unrestricted resources: The Authority's policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

Provision for losses on student loans: The provision for losses on student loans represents the Authority's estimate of the costs related to the 2% to 5% risk sharing on FFELP loans and losses related to servicing of loans by the Authority. In making the estimate, the Authority considers the trend in default rates in the loan guarantee portfolio, past and anticipated loss experience, current operating information, and changes in economic conditions. The provision is based on total guaranteed loans times the default rate times 3%. However, the evaluation is inherently subjective and the provisions may significantly change in the future. The allowance for loan losses was \$ 308,193 and \$ 0 at June 30, 2005 and 2004, respectively.

Note 2. Deposits and Investments

All deposits and investments of the Authority are under the control of the State Treasurer who, by law, has sole authority for investing State funds. Certain of the Authority's deposits and investments are deposited with the Bank of New York or Wachovia Bank, N.A. as authorized by the State Treasurer. Deposits and investments of \$ 84,859,233 and \$ 193,302,303 at June 30, 2005 and 2004, respectively, are held by the Bank of New York as trustee or custodian for the Authority.

The following schedule reconciles deposits and investments within the footnotes to the balance sheet amounts:

| | <u>2005</u> | <u>2004</u> | | <u>2005</u> | <u>2004</u> |
|---------------------------|------------------------------|------------------------------|----------------------------|------------------------------|------------------------------|
| Statement of Net Assets | \$ 145,448,489 | \$ 194,404,117 | Footnotes | | |
| Cash and Cash Equivalents | | | Cash at banks | \$ 165,154 | \$ 32,611 |
| | | | Deposits - STO ICM pool | 112,300,582 | 32,557,440 |
| | | | Investments | | |
| Restricted Assets | | | Bank repurchase agreements | 26,192,021 | 61,493,395 |
| Cash and cash equivalents | 51,481,180 | 30,937,052 | U.S. treasury notes | 53,150,047 | 98,740,142 |
| Investments | 395,300 | 551,185 | U.S. agency bonds | 5,517,165 | 7,713,675 |
| | | | Commercial notes | | 5,092,541 |
| | | | Money market funds | | 20,262,550 |
| Total | <u>\$ 197,324,969</u> | <u>\$ 225,892,354</u> | Total | <u>\$ 197,324,969</u> | <u>\$ 225,892,354</u> |

Deposits: State law requires full collateralization of all State Treasurer balances. The State Treasurer must correct any deficiencies in collateral within seven (7) days. At June 30, 2005 and 2004, all State Treasurer bank balances were fully insured or collateralized with securities held by the State or by its agents in the State's name.

With respect to investments in the State's internal cash management pool, all of the State Treasurer's investments are insured or are investments for which the securities are held by the State or its agents in the State's name. Information pertaining to the reported amounts, fair values, and credit risk of the State Treasurer's investments is disclosed in the Comprehensive Annual Financial Report of the State of South Carolina.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 2. Deposits and Investments (Continued)

Deposits (continued):

At June 30, 2005 and 2004, Wachovia Bank, N.A. carried a bank balance at \$ 72,679 and \$ 32,611, respectively, of unspent federal grants for the Authority. These accounts are covered by FDIC insurance up to \$ 100,000.

At June 30, 2005 and 2004, the Bank of New York carried a bank balance at \$ 92,475 and \$ 0. These accounts are covered by FDIC insurance up to \$ 100,000.

All other deposits are in the State Treasurer Internal Cash Management Account. The value of the Authority's investment in the State's Internal Cash Management Account is determined based on the fair value of the Pool's underlying portfolio.

The reported amount and fair value of deposits held for the various accounts of the Authority were as follows at June 30, 2005 and 2004:

| | <u>2005</u> | <u>2004</u> |
|----------------------------|-----------------------|----------------------|
| Collection/unpledged prior | \$ 112,300,559 | \$ 32,555,879 |
| 1993 resolution | 23 | 1,561 |
| Total | \$ 112,300,582 | \$ 32,557,440 |

Investments: Investments are valued and reported at fair value based on quoted market prices when available or otherwise at the amount at which the instrument could be exchanged in a current transaction. Investment income on investments is recorded when earned. Purchases and sales are accounted for on the trade date. Unrealized gains and losses on investments have been recorded. Realized gains and losses on securities transactions are recorded on the accrual basis.

The reported amount and fair value of investments held for the various accounts of the Authority were as follows at June 30, 2005 and 2004:

| | <u>2005</u> | <u>2004</u> |
|---|-------------------|--------------|
| Collection/unpledged prior account - Bank of New York | | |
| Money market funds | \$ | \$ 1,052,907 |
| Bank repurchase agreements | 1,077,144 | |
| Total | 1,077,144 | 1,052,907 |
| 1993 resolution account - Bank of New York | | |
| U.S. treasury notes | 42,569,137 | 79,929,300 |
| U.S. agency bonds | 539,300 | 734,300 |
| Bank repurchase agreements | 1,772,929 | 61,424,172 |
| Total | 44,881,366 | 142,087,772 |
| 2002 resolution account - Bank of New York | | |
| U.S. treasury notes | 9,591,893 | 18,810,842 |
| Bank repurchase agreements | 443,092 | 69,223 |
| Total | 10,034,985 | 18,880,065 |
| Agency operating account - Bank of New York | | |
| U.S. treasury notes | 989,017 | |
| U.S. agency bonds | 3,984,330 | 5,481,563 |
| Bank repurchase agreements | 19,512,856 | |
| Commercial notes | | 5,092,541 |
| Money market funds | | 10,249,189 |
| Total | 24,486,203 | 20,823,293 |

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 2. Deposits and Investments (Continued)

Investments (continued):

| | <u>2005</u> | <u>2004</u> |
|---|----------------------|-----------------------|
| Federal student loan reserve account - Bank of New York | | |
| U.S. agency bonds | 993,535 | 1,497,812 |
| Bank repurchase agreements | 3,386,000 | |
| Money market funds | | 8,960,454 |
| Total | <u>4,379,535</u> | <u>10,458,266</u> |
| | | |
| Totals | <u>\$ 84,859,233</u> | <u>\$ 193,302,303</u> |

Investments are restricted by bond indentures to direct obligations of (or obligations guaranteed by) the United States of America, interest bearing time deposits, certificates of deposit or repurchase agreements fully secured by direct obligations of the United States of America, and obligations of certain Federal Agencies and instrumentalities.

Interest rate risk: In accordance with its investment policy, the Authority manages its exposure to declines in fair values by limiting the weighted average maturity of its investment portfolio to less than twelve months.

Credit risk: The Authority adheres to the State of South Carolina's investment policy, and invests in primarily U.S. government-backed obligations. Investments in commercial paper or corporate bonds and equities are not done.

Concentration of credit risk: The Authority's investment policy does not allow for an investment in any one issuer that is in excess of five percent (5%) of the total investments. Most investments are U.S. governmental obligations.

Foreign currency risk: The Authority has no foreign currency investments.

Custodial credit risk: This is the risk that the Authority will not be able to recover the value of investment or collateral securities that are in the possession of an outside party if the counter party to the investment transaction fails. The investments at Bank of New York are categorized to give an indication of the level of the custodial credit risk assumed by the Authority at June 30, 2005 and 2004. All Bank of New York investments are insured or registered by the Authority or its agent in the Authority's name. There are no uninsured investments.

Note 3. Student Loans, Federal Family Education Loans (FFEL), and Federal Reinsurance of FFEL Loans

In 2005 and 2004, these loans bear interest at a fixed rate of 2.875% to 12% or an annual variable rate of 2.77% to 4.32%, which is reset each July 1 and which is equal to the bond equivalent rate of the 91-day or 52-week Treasury Bill, determined at the final auction held prior to the immediately preceding June 1, plus 1.7 to 3.25 percent with a cap on the rate of 8.25 to 12.00 percent. These loans are repayable over a period of five (5) to thirty (30) years with a minimum payment of \$ 360 or \$ 600 per year. Repayment of principal may be scheduled to begin within sixty (60) days of final disbursement or six (6) to ten (10) months after the student graduates or ceases to be enrolled on at least a half-time basis in an eligible institution.

Loans disbursed for the 1978-79 Academic year and subsequent years appear on SCSLC's financial statements. These loans are guaranteed by the Authority and reinsured by the U.S. Department of Education. (See Note 12.) Up until March 1, 1999, the Authority charged loan recipients an amount equal to one-half to 1% of the principal amount as an insurance premium to remedy defaults on guaranteed student loans. The Authority can start charging an insurance premium at any time, but current funds are deemed sufficient to pay defaults. Since the Authority entered into a Supplemental Guaranty Agreement with the

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 3. Student Loans, Federal Family Education Loans (FFEL), and Federal Reinsurance of FFEL Loans (Continued)

U.S. Department of Education in 1978, under which the Federal government reinsures the Authority for amounts paid in connection with defaulted loans, the Authority has received cumulative payments to date of \$ 164,087,405 and \$ 142,676,791 as of June 30, 2005 and 2004, respectively, of federal reinsurance. The percentage of the defaulted claims to be reimbursed by the federal government is dependent upon the Authority's default rate experience, as follows:

| <u>Claims Rate</u> | <u>Federal Payment for Loans made prior to October 1, 1993</u> | <u>Federal Payment for Loans made on or after October 1, 1993</u> | <u>Federal Payment for Loans made on or after October 1, 1998</u> |
|--------------------|---|--|--|
| 0% up to 5% | 100% of claims | 98% of claims | 95% of claims |
| 5% up to 9% | 100% of all claims up to 5%; and 90% of claims 5% and over | 98% of all claims up to 5%; and 88% of claims 5% and over | 95% of claims up to 5%; and 85% of claims 5% and over |
| 9% and over | 100% of claims up to 5%; 90% of claims 5% and over up to 9%; and 80% of claims 9% and over | 98% of claims up to 5%; 88% of claims 5% and over up to 9%; and 78% of claims 9% and over | 95% of claims up to 5%; 85% of claims 5% and over up to 9%; and 75% of claims 9% and over |

The calculation of the default rate is based upon the claims paid in a given year as of the Federal government's fiscal year ending September 30 to the total loans in collection on the previous October 1. Based upon data maintained by the Authority, the default rate in the period ended September 30, 2004 and 2003 was approximately .60% and .73%, respectively. The Authority expects the default rate to remain about 1%.

Note 4. Note Receivable Finance Loans

Each bond resolution of the Authority requires that all funds advanced to SCSLC by the Authority for the purpose of making student loans be evidenced by a loan agreement, assignment of collateral and assignment of revenues between the two parties, with the student loans providing security to the bond trustee. Increases (decreases) to SCSLC from the Authority's 1993 General Resolution are made pursuant to a loan agreement dated August 31, 1993, and increases (decreases) to SCSLC from the Authority's 2002 General Resolution are made pursuant to a loan agreement dated June 12, 2002. Each loan is calculated as set forth in the respective loan agreements. The finance loans as of June 30, 2005 and 2004 are as follows:

| Authority Bond Resolution | <u>2004</u> | | | <u>2005</u> | | | <u>Balance 6/30/2005</u> |
|---------------------------------|------------------------------|-----------------------|-----------------------|------------------------------|-----------------------|-----------------------|------------------------------|
| | <u>Balance 6/30/2003</u> | <u>Increases</u> | <u>Decreases</u> | <u>Balance 6/30/2004</u> | <u>Increases</u> | <u>Decreases</u> | |
| 1993 | \$ 151,747,899 | \$ 557,000,000 | \$ 384,852,305 | \$ 323,895,594 | \$ 457,800,000 | \$ 392,853,572 | \$ 388,842,022 |
| 2002 | 109,324,876 | 91,162,256 | 833,333 | \$ 199,653,799 | 189,381,032 | 5,472,000 | 383,562,831 |
| Total | <u>\$ 261,072,775</u> | <u>\$ 648,162,256</u> | <u>\$ 385,685,638</u> | <u>\$ 523,549,393</u> | <u>\$ 647,181,032</u> | <u>\$ 398,325,572</u> | <u>\$ 772,404,853</u> |

Note 5. Amounts Due from/to SCSLC

The \$ 9,678,139 and \$ 8,214,023 at June 30, 2005 and 2004, respectively, amount due from SCSLC represents funds due for income earned, but not yet received, from the U.S. Department of Education and borrowers thus not remitted to the Authority and funds collected on behalf of the Authority. The Authority also owes SCSLC for funds collected on their behalf of \$ 93,170,694 and \$ 28,808,236 at June 30, 2005 and 2004, respectively. Funds collected on behalf of SCSLC are required to be paid to SCSLC by the tenth of each month.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 6. Capital Assets

The following is a summary of changes in capital assets for fiscal years ended June 30, 2005 and 2004:

| | Balance 6/30/2003 | Additions | Deletions | Balance 6/30/2004 | Additions | Deletions | Balance 6/30/2005 |
|--------------------------------|----------------------|-------------------|-----------------|----------------------|------------------|----------------|----------------------|
| Cost | | | | | | | |
| Furniture and equipment | \$ 114,479 | \$ 188,749 | \$ (10,008) | \$ 293,220 | \$ 90,661 | \$ (9,088) | \$ 374,793 |
| Automobiles | 11,903 | 17,000 | (11,903) | 17,000 | - | - | 17,000 |
| Total | <u>126,382</u> | <u>205,749</u> | <u>(21,911)</u> | <u>310,220</u> | <u>90,661</u> | <u>(9,088)</u> | <u>391,793</u> |
| Accumulated Depreciation | | | | | | | |
| Furniture and equipment | (19,693) | (71,237) | 10,008 | (80,922) | (70,203) | 9,088 | (142,037) |
| Automobiles | (11,903) | (4,722) | 11,903 | (4,722) | (5,667) | - | (10,389) |
| Less, accumulated depreciation | <u>(31,596)</u> | <u>(75,959)</u> | <u>21,911</u> | <u>(85,644)</u> | <u>(75,870)</u> | <u>9,088</u> | <u>(152,426)</u> |
| Net Capital Assets | <u>\$ 94,786</u> | <u>\$ 129,790</u> | <u>\$ -</u> | <u>\$ 224,576</u> | <u>\$ 14,791</u> | <u>\$ -</u> | <u>\$ 239,367</u> |

Note 7. Loan Guarantees

As an incentive for the states to set up state guaranty agencies, the U.S. Department of Education has made certain funds available to the states to assist in establishing a federal student loan reserve account which replaced the loan guarantee account by the 1998 Reauthorization of the Higher Education Act (Act) on July 1, 1998. Maintenance of the federal student loan reserve account will depend upon possible further Federal and State advances, investment income, insurance premium on student loans if collected, and reinsurance payments from the U.S. Department of Education. Prior to July 1, 1998, the account accumulated retention of default collections, administrative cost allowance and supplemental preclaims assistance. The Act eliminated this format (See Note 14). The U.S. Department of Education reserved the right to request repayment of advances under the Advance Agreement within such period as it deemed appropriate in light of the maturity and solvency of the Authority's federal student loan reserve account. As of June 30, 2005 and 2004, the Authority has reimbursed all such advances to the U.S. Department of Education that they have requested.

The 1993 Amendments to the Higher Education Act, Section 422 of the Higher Education Act of 1965, as amended, provides that the federal student loan reserve account of all guaranty agencies under the Act shall be considered the property of the United States to be used in connection with the Federal Family Education Loan Programs and Consolidation Loan Programs under Parts B and C of Title IV of the Act. The Act further provides that the Secretary may direct a guaranty agency to return to the Secretary a portion of its federal student loan reserve account which the Secretary determines is unnecessary to pay the program expenses and contingent liabilities of the guaranty agency. (See Note 14).

Effective July 1, 1998, the Act allowed a new account called the Agency Operating Account to be established. As described in Note 1, this account accumulates funds to operate the guaranty agency.

Note 8. Bonds and Other Payable and Restricted Assets

The Authority issues Guaranteed Student Loan Revenue Bonds or Education Loan Revenue Bonds as needed to make finance loans to the South Carolina Student Loan Corporation to make student loans (See Note 4). The finance loans to the South Carolina Student Loan Corporation are secured by loans funded by bond proceeds, related revenue from such loans, investments in accounts and earnings thereon. The bond resolutions permit the Authority to accumulate borrowers' payments during the year to pay principal and interest on bonds as due. The bonds do not constitute a debt, liability or obligation of the State of South Carolina or a pledge of the faith and credit of the State of South Carolina. As of June 30, 2005, the current debt service account must contain

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 8. Bonds and Other Payable and Restricted Assets (Continued)

assets equal to the accrued interest payable plus ten months of the outstanding bond principal due the following September 1 plus four (4) months principal due following March 1 as required in the bond indentures. As of June 30, 2005 and 2004, the Authority was required to have assets deposited in the current debt service account of \$ 40,837,388 and \$ 16,939,076, respectively. The Authority has more on deposit in investments recorded in the Debt Reserve Account than the current debt service requirement in 2005 and 2004. Restricted assets in the debt reserve account are \$ 51,876,480 in 2005 and \$ 31,488,237 in 2004, and will be used to pay future debt service.

The Student Loan Revenue bonds as of June 30, 2005 and 2004 follow:

| Issued | Original Amount | Interest Rate | Maturity Date | Balance Outstanding 6/30/2003 | Issued (Retired) During FY 04 | Balance Outstanding 6/30/2004 | Issued (Retired) During FY 05 | Balance Outstanding 6/30/2005 |
|-----------|-----------------|---------------|---------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|
| 8/31/1993 | 99,495,000 | 3.50-5.55% | 9/1/96-2008 | \$ 40,365,000 | (11,250,000) | \$ 29,115,000 | \$ (10,995,000) | \$ 18,120,000 |
| 8/31/1994 | 86,845,000 | 4.75-6.30% | 9/1/96-2014 | 67,335,000 | (2,500,000) | 64,835,000 | (2,500,000) | 62,335,000 |
| 8/30/1995 | 62,055,000 | 5.00-6.00% | 9/1/99-2015 | 55,010,000 | | 55,010,000 | | 55,010,000 |
| 6/17/1998 | 49,850,000 | Auction | 9/1/05-2033 | 49,850,000 | | 49,850,000 | | 49,850,000 |
| 6/16/1999 | 67,300,000 | Auction | 9/1/07-2019 | 67,300,000 | | 67,300,000 | | 67,300,000 |
| 6/29/2000 | 59,050,000 | Auction | 3/1/05-2020 | 59,050,000 | | 59,050,000 | (2,500,000) | 56,550,000 |
| 6/20/2001 | 49,200,000 | Auction | 3/1/05-2021 | 49,200,000 | | 49,200,000 | (2,500,000) | 46,700,000 |
| 6/12/2002 | 117,500,000 | Auction | 3/1/05-2022 | 117,500,000 | | 117,500,000 | (2,500,000) | 115,000,000 |
| 8/20/2003 | 100,150,000 | Auction | 9/1/05-2023 | | 100,150,000 | 100,150,000 | | 100,150,000 |
| 8/11/2004 | 174,700,000 | Auction | 3/1/06-2024 | | | | 174,700,000 | 174,700,000 |
| | | | | <u>\$ 505,610,000</u> | <u>\$ 86,400,000</u> | <u>\$ 592,010,000</u> | <u>\$ 153,705,000</u> | <u>\$ 745,715,000</u> |

The 1994, 1995, 1998, 1999, 2000, 2001, 2002, 2003 and 2004 bond issues include auction rate bonds totaling \$ 692,200,000. The interest rate on these bonds varies every thirty-five days depending on auction rate bond markets. The effective interest rates for 2005 and 2004 fiscal years have been approximately 2.05% and 1.1%, respectively. The maximum interest rate is 12%. Future interest payment projections are based upon the weighted average rate of 2.92% at June 30, 2005.

Optional redemption features are available for certain of the various outstanding bonds. The Authority's auction rate bonds can be optionally redeemed in full on any auction date without any call premium due. Certain of the Authority's fixed rate bonds can be optionally redeemed from September 1, 2004 to August 31, 2006 depending on the series with a call premium of 1% to 2% of the principal redeemed. Each of the Authority's remaining fixed rate bonds may be redeemed on and after September 1, 2006 with no call premiums.

The changes in debt for the years ending June 30, 2005 and 2004 follow:

| Long-Term Liabilities | 6/30/2003 | Increases | Decreases | 6/30/2004 | Increases | Decreases | 6/30/2005 | One Year |
|---|-----------------------|-----------------------|------------------------|-----------------------|-----------------------|------------------------|-----------------------|----------------------|
| Bonds payable | \$ 505,610,000 | \$ 100,150,000 | \$ (13,750,000) | \$ 592,010,000 | \$ 174,700,000 | \$ (20,995,000) | \$ 745,715,000 | \$ 48,035,000 |
| Compensated absences payable | 151,471 | 158,400 | (136,286) | 173,585 | 296,102 | (258,600) | 211,087 | 211,087 |
| Arbitrage payable to federal government | 18,010,126 | | (4,941,815) | 13,068,311 | | (2,190,019) | 10,878,292 | 344,553 |
| Deferred amount of debt refunding | (766,244) | | 365,561 | (400,683) | | 205,207 | (195,476) | (128,108) |
| Unamortized bond revenues retirement | (2,072,327) | | 347,180 | (1,725,147) | | 288,167 | (1,436,980) | (256,981) |
| Total | <u>\$ 520,933,026</u> | <u>\$ 100,308,400</u> | <u>\$ (18,115,359)</u> | <u>\$ 603,126,066</u> | <u>\$ 174,996,102</u> | <u>\$ (22,950,245)</u> | <u>\$ 755,171,923</u> | <u>\$ 48,205,551</u> |

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 8. Bonds and Other Payable and Restricted Assets (Continued)

The annual requirements to retire these bonds as of June 30, 2005 are as follows:

| <u>Year Ended June 30,</u> | <u>Principal</u> | <u>Interest</u> | <u>Totals</u> |
|----------------------------|-----------------------|-----------------------|-----------------------|
| 2006 | \$ 48,035,000 | \$ 17,811,285 | \$ 65,846,285 |
| 2007 | 3,745,000 | 20,966,161 | 24,711,161 |
| 2008 | 37,465,000 | 19,849,034 | 57,314,034 |
| 2009 | 95,470,000 | 17,616,368 | 113,086,368 |
| 2010 | 59,100,000 | 15,837,487 | 74,937,487 |
| 2011 | | 14,646,280 | 14,646,280 |
| 2012 | | 14,646,280 | 14,646,280 |
| 2013 | | 14,646,280 | 14,646,280 |
| 2014 | | 14,646,280 | 14,646,280 |
| 2015 | 52,050,000 | 13,379,730 | 65,429,730 |
| 2016 | 29,900,000 | 12,398,853 | 42,298,853 |
| 2017 | | 12,253,340 | 12,253,340 |
| 2018 | | 12,253,340 | 12,253,340 |
| 2019 | 23,700,000 | 12,022,660 | 35,722,660 |
| 2020 | 20,000,000 | 11,366,633 | 31,366,633 |
| 2021 | 30,000,000 | 10,685,300 | 40,685,300 |
| 2022 | 79,000,000 | 9,332,367 | 88,332,367 |
| 2023 | 92,000,000 | 7,571,400 | 99,571,400 |
| 2024 | 171,700,000 | 103,660 | 171,803,660 |
| 2025 | | 103,660 | 103,660 |
| 2026 | | 103,660 | 103,660 |
| 2027 | | 103,660 | 103,660 |
| 2028 | | 103,660 | 103,660 |
| 2029 | | 103,660 | 103,660 |
| 2030 | | 103,660 | 103,660 |
| 2031 | | 103,660 | 103,660 |
| 2032 | | 103,660 | 103,660 |
| 2033 | 3,550,000 | 69,107 | 3,619,107 |
| | <u>\$ 745,715,000</u> | <u>\$ 252,931,125</u> | <u>\$ 998,646,125</u> |

On August 11, 2004, the Authority had outstanding bonds of \$ 592,010,000 and then issued \$ 174,700,000 in Guaranteed Student Loan Revenue and Refunding Bonds with a variable auction interest rate which is capped at 12.0 percent to refund \$ 3,000,000 of outstanding 1993 and 1994 Bonds with an average interest rate of 5.2 percent and to provide financing for student loans. The gross proceeds of \$ 174,700,000 after payment for issuance costs (\$ 896,024), certain deposits to funds (\$ 1,747,000) and purchase of new student loans (\$ 169,056,976) were used to fund an irrevocable trust with an escrow agent to provide remaining debt service payments on the old bonds on September 1, 2004. As a result, these bonds are considered to be defeased and the liability for these bonds has been removed from bonds payable. The advance refunding resulted in no difference between the reacquisition price and the net carrying amount of the old debt. The Authority completed the refunding to have bonds under the 2002 bond resolution which has lower reserve requirements and allows the financing of alternative or non-federal loans. The refunding increases its total debt payments by \$ 449,833 over the next seven (7) years and obtains an economic loss (difference between the present values of the old and new debt service payments) of \$ 17,127. Defeased bonds in the amount of \$ 3,000,000 were paid in full on September 1, 2004.

The deferred amount of debt refunding at June 30, 2005 and 2004 is \$ 195,476 and \$ 400,683, respectively. The amount of the unamortized bond discounts at June 30, 2005 and 2004 is \$ 1,436,980 and \$ 1,725,147, respectively.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 9. Paul Douglas Teacher Scholarship Program

The Authority administers the Paul Douglas Teacher Scholarship Program (formerly the Congressional Teacher Scholarship Program). This is a federally funded scholarship program designed to attract bright high school students and encourage them to enter the field of teaching. As of June 30, 1995, the federal government has suspended the loan program and the Authority will reimburse all funds collected for the program.

During the fiscal years ended June 30, 2005 and 2004, collections were \$ 74,782 and \$ 33,661, respectively, from repayments by participants. The Authority repaid these amounts to the Federal Government during the years ended June 30, 2005 and 2004 due to suspension of the program. Any repayments not repaid to the Federal Government are recorded as a liability.

Note 10. Related Party Transactions

The Authority has significant transactions with the State of South Carolina and SCSLC. Services received at no cost from State Agencies include maintenance of certain accounting records from the Comptroller General, investment and banking functions from the State Treasurer, and legal services from the Attorney General.

The Authority paid the University of South Carolina \$ 13,945 and \$ 19,081 for the years ended June 30, 2005 and 2004, respectively, for data processing services and the expense is recorded as contractual expenses.

See Note 1 regarding transactions with SCSLC.

Note 11. Employee Benefit Plans

The Authority provides retirement benefits through the South Carolina Student Loan Corporation Money Purchase Pension Plan for all employees who have completed one year of service and attained age 21. SCSLC has adopted the Branch Banking & Trust Co. (BB&T) Money Purchase Pension Plan, a single employer plan. BB&T is the Trustee of the Plan. The authority under which benefits provisions are established or amended is provided in the Plan document as administered by the Plan Trustee. The Plan issues a stand-alone report annually and may be obtained by writing to the South Carolina Student Loan Corporation, Post Office Box 21487, Columbia, S.C. 29221 or by calling (803) 772-9480.

This is a defined contribution plan in which the employer is required to contribute 5.6% of the participant's total annual compensation plus 5.6% of compensation exceeding the Social Security wage base. Contributions are paid monthly. A participant is 20% vested after three years service and 100% vested after seven years. A participant receives normal retirement at age sixty-five. At termination of employment or reaching normal retirement age, the participant has the right to elect to receive all or any portion of his vested benefit derived from employer contributions. Voluntary contributions are not permitted. Under the plan, the portion of an employee's account that has not vested when an employee terminates, called forfeitures, reduces the employer's contribution in the year following the Plan year in which the forfeiture occurs. The total pension expense is fully funded and is included in personnel expenses under the retirement category.

Pension expense, total salary and covered salary are as follows:

| | | |
|---|---------------------|--------------|
| | 2005 | 2004 |
| Total Salary | \$ 2,094,800 | \$ 1,960,481 |
| Total Covered Salary | 1,848,207 | 1,816,281 |
| Pension Expense (Actual and Required) | 108,632 | 102,269 |
| Percent Pension Expense to Covered Salary | 5.88% | 5.63% |

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 11. Employee Benefit Plans (Continued)

The Authority participates in a supplemental retirement plan. The Plan is called the South Carolina Student Loan Corporation Defined Benefit Plan, a single employer plan. The authority under which benefit provisions are established or amended is provided in the Plan document as administered by the Plan Trustee. The Plan is a defined benefit pension plan covering substantially all employees with one year of service and over 21 years of age. The Plan provides benefits based on years of service and compensation. The benefit formula uses one percent (1%) of the average of the five highest consecutive years' pay of each eligible employee multiplied by the number of years of service not to exceed 30 years. The Corporation's funding policy is to make at least the minimum annual contribution that is actuarially computed by the projected unit credit method required by the Plan. The Authority will contribute the amount billed to them by the Corporation. The Corporation issues a publicly available financial report that includes financial statements and required supplementary information for the South Carolina Student Loan Corporation Defined Benefit Plan. That report may be obtained by writing to South Carolina Student Loan Corporation, Post Office Box 21487, Columbia, South Carolina 29221 or by calling (803) 772-9480.

The total required and paid contributions for the years ended June 30, 2005 and 2004 were \$ 161,372 and \$ 244,035, respectively, representing 8.73% and 13.44% of covered salary of \$ 1,848,207 and \$ 1,816,281, respectively. Total salaries for the years ended June 30, 2005 and 2004 were \$ 2,096,525 and \$ 1,960,481, respectively. Contributions are included in the personnel expense category.

The Authority participates in the 403 (b) Defined Contribution Plan established by the South Carolina Student Loan Corporation on November 5, 2002. The Plan provides for a 5% contribution based on the participant's total annual compensation. The total amount contributed under the plan was \$ 75,753 in 2005 and \$ 88,553 in 2004. All employees are eligible who have completed one year of service and attainment of age 21. Contributions are 100% vested when made. Employees are eligible to make voluntary contributions to the Plan.

Certain health care, dental, long-term disability and life insurance benefits are provided to active employees by various private insurers. All full-time and part-time employees who worked at least 32 hours per week are eligible to receive these benefits. Employer contributions applicable to those benefits were \$ 535,551 and \$ 354,417 in 2005 and 2004, respectively, and are recorded as expenses under the personnel expense category, and are paid monthly as billed by insurers.

Note 12. Student Loan Guarantees

The total approved amount and outstanding balance of student loans that the Authority has under guarantee is as follows at June 30:

| | <u>2005</u> | <u>2004</u> |
|---------------------------|------------------|------------------|
| Approved Amount for Loans | \$ 4,977,918,869 | \$ 4,180,521,330 |
| Outstanding Balance | 2,117,886,699 | 1,903,061,100 |

Note 13. Arbitrage

The Internal Revenue Code (IRC) and arbitrage regulations issued by the IRS require rebate to the federal government of excess investment earnings on bond proceeds if the yield on those earnings exceeds the effective yield on the related tax-exempt bonds issued. Regulations also exist for calculating rebate earnings in connection with the accounting for bond proceeds, refunding issues, and proceeds that are commingled with other funds for investment purposes. Rebates are payable every five years from date of bond issue or upon maturity of the bonds, whichever is earlier.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 13. Arbitrage (Continued)

The IRC and U. S. Treasury Regulations permit issuers of qualified student loan tax-exempt obligations to earn no more than 1.5% to 2.0% above the bond yield on the qualified student loans financed with such tax-exempt obligations. For excess earnings on qualified student loans, issuers may elect to pay such excess to the U. S. Treasury or return such excess to the borrowers of qualified student loans financed by the tax-exempt obligations. The Authority has elected to implement a program of borrower benefits in order to return such excess to borrowers and the program resulted in decreasing the liability.

The South Carolina State Treasurer had computations made to determine the liability at June 30, 2005 and 2004. Based on those results, the Authority incurred expense (income) of \$ (1,916,338) for 2005 and \$ (4,445,119) for 2004. This expense is determined using the "Future Value" method of determining cumulative arbitrage liability, as set forth in the U.S. Treasury Regulations and is based on cash flows created by investment, sale, maturity of and earnings on gross bond proceeds. As of June 30, 2005 and 2004, the Authority reports \$ 10,888,292 and \$ 13,068,311, respectively, arbitrage liability.

Note 14. Recall of FFELP (Federal Student Loan) Reserve Funds

The net restricted for federal student loan reserves is the accumulated portion of net assets derived from the Federal Family Education Loan Program (FFELP) guarantee operations of the Authority and may only be used in support of FFELP (See Note 3). On August 5, 1997, the Higher Education Act was amended by the Balanced Budget Act of 1997. Under this amendment, the Secretary of Education (the Secretary) was required to recall \$ 1 billion on September 1, 2002 of FFELP reserve funds. The amount owed by each guarantor was based on the agency's reserves and reserve ratio as of September 30, 1996. For purposes of calculation, the reserves include any Federal Student Loan Reserve Account funds in cash or liquid assets held by the agency. The reserve ratio is defined as the amount of the agency's Federal Student Loan Reserve Account as of September 30, 1996 divided by the original principal amount of all outstanding insured loans on that date. Each agency must transfer its required share to a separate account in five equal annual installments for the federal fiscal years 1998 through 2002. The Authority's estimated amount of prorated share of the \$ 1 billion is approximately \$ 6,830,214 as determined by the U.S. Department of Education. During 2001 – 2002 fiscal year, the Authority's estimated liability was increased by \$ 1,739,823 as determined by the U.S. Department of Education. The \$ 1,739,823 increase resulted in a revised liability of \$ 8,570,037 due to the U.S. Department of Education.

The Authority deposited \$ 1,366,043 each fiscal year beginning December 1997 into a separate account for a total of \$ 6,830,214 at June 30, 2002 and could not use the funds for any purpose without the express written permission of the Secretary. The interest earnings on the account may be used for performing certain default reduction activities as outlined in the Balanced Budget Act of 1997. The funds are reflected in the cash and cash equivalents of the Federal Student Loan Reserve Account. As of June 30, 2003, the reserve funds totaling \$ 7,421,754 were transferred to the U.S. Department of Education leaving a balance due of \$ 1,148,283. The balance due is payable in two equal installments of \$ 574,141 in 2006 and 2007.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
YEARS ENDED JUNE 30, 2005 AND 2004**

Notes to Financial Statements

Note 15. Required Information on Business Type Activity for State of South Carolina

The Authority is only one major enterprise fund which is not required to present government-wide financial statements. However, the State of South Carolina requires business type activities for the State's government-wide Statement of Activities. The required information follows:

| | <u>2005</u> | <u>2004</u> |
|--|------------------------------|------------------------------|
| Charges for Services | | |
| United States Department of Education | | |
| Loan processing and issuance fee | \$ 1,720,026 | \$ 1,899,291 |
| Account maintenance fee | 2,269,878 | 2,259,479 |
| Default aversion fee income | 868,597 | 915,929 |
| Retention on default collections | 2,231,668 | 1,968,487 |
| Income from South Carolina Student Loan Corporation | | |
| Subsidized interest | 3,331,798 | 2,598,123 |
| Special allowance | 15,321,834 | 9,662,846 |
| Non-subsidized interest | 6,918,847 | 4,222,336 |
| Late charges | 42,148 | 11,750 |
| Miscellaneous payments of student loans | 331 | 272 |
| Reimbursement of bond expense | 9,897,352 | 5,045,972 |
| Reinsurance recoveries | 57,049 | 44,201 |
| Total charges for services | <u>42,659,528</u> | <u>28,628,686</u> |
| Operating grants and contributions | | |
| Interest/investment income | 4,404,805 | 2,665,405 |
| Net increase (decrease) in the fair value of investments | 46,868 | (96,723) |
| Miscellaneous income | 16,612 | |
| Arbitrage income (expense) | 1,916,338 | 4,445,119 |
| Total operating grants and contributions | <u>6,384,623</u> | <u>7,013,801</u> |
| Total program revenue | <u>49,044,151</u> | 35,642,487 |
| Less, expenses | <u>43,567,155</u> | <u>39,641,460</u> |
| Change in net assets | 5,476,996 | (3,998,973) |
| Net assets | | |
| Beginning | <u>124,459,291</u> | <u>128,458,264</u> |
| Ending | <u>\$ 129,936,287</u> | <u>\$ 124,459,291</u> |

Note 16. Reclassifications

Certain reclassifications were made on 2004 amounts by statement of net assets and/or operating statement accounts for comparability to 2005 with no effect on net income.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
SCHEDULE OF NET ASSETS BY ACCOUNTS
ENTERPRISE FUND
JUNE 30, 2005**

| | Collection Account Prior Unpledged | 93 Resolution | 02 Resolution | Agency Operating Account | Federal Student Loan Reserve Account | Total |
|--|---------------------------------------|-----------------------|-----------------------|--------------------------------|--|-----------------------|
| ASSETS | | | | | | |
| Current Assets | | | | | | |
| Cash and cash equivalents | \$ 113,450,382 | \$ 2,570,252 | \$ 469,642 | \$ 24,545,382 | \$ 4,412,831 | \$ 145,448,489 |
| Cash and cash equivalents - restricted | | 41,915,837 | 9,565,343 | | | 51,481,180 |
| Receivables | | | | | | |
| Current portion of finance loans | | 41,256,000 | 35,144,000 | | | 76,400,000 |
| Due from South Carolina Student Loan Corporation | 36,416 | 4,937,655 | 4,704,068 | | | 9,678,139 |
| Accrued interest receivable | 911 | 92,545 | 16,854 | 20,977 | 1,395 | 132,682 |
| Federal reinsurance receivable | | | | | 5,160,587 | 5,160,587 |
| Loan processing issuance fee receivable | | | | 133,570 | | 133,570 |
| Account maintenance fee receivable | | | | 193,106 | | 193,106 |
| Due from other funds | (19,025,499) | 19,095,469 | | 35,240 | (105,210) | |
| Total current assets | <u>94,462,210</u> | <u>109,867,758</u> | <u>49,899,907</u> | <u>24,928,275</u> | <u>9,469,603</u> | <u>288,627,753</u> |
| Long-term and other assets | | | | | | |
| Receivables | | | | | | |
| Finance loans, less current portion | | 347,586,022 | 348,418,831 | | | 696,004,853 |
| Deferred cost of issuance of bonds | | 786,545 | 1,940,800 | | | 2,727,345 |
| Restricted assets | | | | | | |
| Investments | | 395,300 | | | | 395,300 |
| Total long-term and other assets | <u>-</u> | <u>348,767,867</u> | <u>350,359,631</u> | <u>-</u> | <u>-</u> | <u>699,127,498</u> |
| Property, plant & equipment | | | | | | |
| Furniture and equipment | | | | 374,793 | | 374,793 |
| Automobile | | | | 17,000 | | 17,000 |
| Less: accumulated depreciation | | | | (152,426) | | (152,426) |
| Total property, plant & equipment | <u>-</u> | <u>-</u> | <u>-</u> | <u>239,367</u> | <u>-</u> | <u>239,367</u> |
| Total assets | <u>\$ 94,462,210</u> | <u>\$ 458,635,625</u> | <u>\$ 400,259,538</u> | <u>\$ 25,167,642</u> | <u>\$ 9,469,603</u> | <u>\$ 987,994,618</u> |

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
SCHEDULE OF NET ASSETS BY ACCOUNTS
ENTERPRISE FUND
JUNE 30, 2005**

| | Collection Account Prior Unpledged | 93 Resolution | 02 Resolution | Agency Operating Account | Federal Student Loan Reserve Account | Total |
|--|---------------------------------------|----------------------|---------------------|--------------------------------|--|-----------------------|
| LIABILITIES | | | | | | |
| Current Liabilities | | | | | | |
| Accounts payable | \$ 215,862 | \$ | \$ | \$ 15,086 | \$ 95,947 | \$ 326,895 |
| Arbitrage payable to federal government | | 344,553 | | | | 344,553 |
| Compensated absences | | | | 211,087 | | 211,087 |
| Due to South Carolina Student Loan Corporation | 92,523,080 | | | 410,242 | 237,372 | 93,170,694 |
| Consolidation rebate fee payable | 645,869 | | | | | 645,869 |
| Payable from restricted assets | | | | | | |
| Current maturities of bonds payable | | 45,535,000 | 2,500,000 | | | 48,035,000 |
| Accrued bond interest payable | | 3,726,639 | 3,549,835 | | | 7,276,474 |
| Total current liabilities | <u>93,384,811</u> | <u>49,606,192</u> | <u>6,049,835</u> | <u>636,415</u> | <u>333,319</u> | <u>150,010,572</u> |
| Long-Term Liabilities | | | | | | |
| Bonds payable, less current maturities, deferred Amount of debt refunding and bond premium and discounts | | | | | | |
| | | 308,903,550 | 387,143,994 | | | 696,047,544 |
| Provision for losses on student loans | | | | | 308,193 | 308,193 |
| Federal reserve funds payable | | | | | 1,148,283 | 1,148,283 |
| Arbitrage payable to federal government, Less current portion | | | | | | |
| | | 79,734 | | | | 79,734 |
| Arbitrage payable to federal government payable from restricted funds | | | | | | |
| | | 5,789,744 | 4,674,261 | | | 10,464,005 |
| Total long-term liabilities | <u>-</u> | <u>314,773,028</u> | <u>391,818,255</u> | <u>-</u> | <u>1,456,476</u> | <u>708,047,759</u> |
| Total liabilities | <u>93,384,811</u> | <u>364,379,220</u> | <u>397,868,090</u> | <u>636,415</u> | <u>1,789,795</u> | <u>858,058,331</u> |
| Net Assets | | | | | | |
| Invested in capital assets | | | | | | |
| | | | | 239,367 | | 239,367 |
| Restricted for | | | | | | |
| Debt service | | | | | | |
| Bond indentures | | 94,256,405 | 2,391,448 | | | 96,647,853 |
| Other | | | | | | |
| Federal government | | | | | 7,679,808 | 7,679,808 |
| Guaranty agency operating account | | | | 24,291,860 | | 24,291,860 |
| Unrestricted | | | | | | |
| | 1,077,399 | | | | | 1,077,399 |
| Total net assets | <u>\$ 1,077,399</u> | <u>\$ 94,256,405</u> | <u>\$ 2,391,448</u> | <u>\$ 24,531,227</u> | <u>\$ 7,679,808</u> | <u>\$ 129,936,287</u> |

SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
SCHEDULE OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS BY ACCOUNT
ENTERPRISE FUND
YEAR ENDED JUNE 30, 2005

| | <u>Collection Account Prior Unpledged</u> | <u>1993 Resolution</u> | <u>2002 Resolution</u> | <u>Agency Operating Account</u> | <u>Federal Student Loan Reserve Account</u> | <u>Total</u> |
|--|---|----------------------------|----------------------------|-------------------------------------|---|----------------------|
| Operating Revenue | | | | | | |
| United States Department of Education | | | | | | |
| Loan processing issuance fee | \$ | \$ | \$ | \$ 1,720,026 | \$ | \$ 1,720,026 |
| Account maintenance fee | | | | 2,269,878 | | 2,269,878 |
| Default aversion fee income | | | | 868,597 | | 868,597 |
| Retention on default collections | | | | 2,229,585 | 2,083 | 2,231,668 |
| Income from South Carolina Student Loan Corporation | | | | | | |
| Subsidized interest | | 3,331,798 | | | | 3,331,798 |
| Special allowance | | 15,321,834 | | | | 15,321,834 |
| Non-subsidized interest | | 6,918,847 | | | | 6,918,847 |
| Late charges | | 42,148 | | | | 42,148 |
| Miscellaneous payments of student loans | | 331 | | | | 331 |
| Reimbursement of bond expense | | | 9,897,352 | | | 9,897,352 |
| Reinsurance recoveries | | | | | 57,049 | 57,049 |
| Miscellaneous income | | | | | 16,612 | 16,612 |
| Interest/investment income | 21,966 | 2,532,957 | 1,302,409 | 495,331 | 52,142 | 4,404,805 |
| Net increase (decrease) in the fair value of investments | 745 | 24,659 | | 17,538 | 3,926 | 46,868 |
| Total operating revenue | <u>22,711</u> | <u>28,172,574</u> | <u>11,199,761</u> | <u>7,600,955</u> | <u>131,812</u> | <u>47,127,813</u> |
| Operating Expenses | | | | | | |
| Personnel | | | | 3,121,655 | | 3,121,655 |
| Contractual services | | | | 536,763 | | 536,763 |
| General operating | | | | 656,682 | | 656,682 |
| South Carolina Student Loan Corporation for operations | | 4,198,752 | | | | 4,198,752 |
| Bond interest expense | | 9,551,869 | 8,034,623 | | | 17,586,492 |
| Amortization - deferred cost of bond issuance | | 74,698 | 105,184 | | | 179,882 |
| Default aversion fee expense | | | | | 868,597 | 868,597 |
| Loan fees | | 3,084,861 | | | | 3,084,861 |
| Borrower incentives | | 9,755,525 | | | | 9,755,525 |
| Broker/dealer fees | | 948,026 | 996,191 | | | 1,944,217 |
| Reinsurance expense | | 1,471 | | | 751,828 | 753,299 |
| Other fees | | | | 167,151 | 713,279 | 880,430 |
| Total operating expenses | <u>\$ -</u> | <u>\$ 27,615,202</u> | <u>\$ 9,135,998</u> | <u>\$ 4,482,251</u> | <u>\$ 2,333,704</u> | <u>\$ 43,567,155</u> |

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
SCHEDULE OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS BY ACCOUNT
ENTERPRISE FUND
YEAR ENDED JUNE 30, 2005**

| | <u>Collection Account Prior Unpledged</u> | <u>1993 Resolution</u> | <u>2002 Resolution</u> | <u>Agency Operating Account</u> | <u>Federal Student Loan Reserve Account</u> | <u>Total</u> |
|---------------------------------|---|----------------------------|----------------------------|-------------------------------------|---|-----------------------|
| Operating income (loss) | \$ 22,711 | \$ 557,372 | \$ 2,063,763 | \$ 3,118,704 | \$ (2,201,892) | \$ 3,560,658 |
| Non-operating income (expenses) | | | | | | |
| Arbitrage income (expense) | - | 3,352,961 | (1,436,623) | - | - | 1,916,338 |
| Change in Net Assets | 22,711 | 3,910,333 | 627,140 | 3,118,704 | (2,201,892) | 5,476,996 |
| Net assets | | | | | | |
| Beginning | 1,054,688 | 90,346,072 | 1,764,308 | 21,412,523 | 9,881,700 | 124,459,291 |
| Ending | <u>\$ 1,077,399</u> | <u>\$ 94,256,405</u> | <u>\$ 2,391,448</u> | <u>\$ 24,531,227</u> | <u>\$ 7,679,808</u> | <u>\$ 129,936,287</u> |

SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
SCHEDULE OF CASH FLOWS BY ACCOUNTS
ENTERPRISE FUND
YEAR ENDED JUNE 30, 2005

| | Collection Account Prior Unpledged | 1993 Resolution | 2002 Resolution | Agency Operating Account | Federal Student Loan Reserve Account | Total |
|--|---|----------------------------|----------------------------|-------------------------------------|---|-----------------------|
| Cash flows from operating activities | | | | | | |
| Receipts from borrowers and U.S. Department of Education | \$ 79,785,404 | \$ | \$ | \$ 7,435,554 | \$ 131,812 | \$ 87,352,770 |
| Receipts from SCSLC services provided | | 21,975,048 | 12,655,860 | | | 34,630,908 |
| Payments to suppliers, lenders and borrowers | | (29,854,125) | (4,934,018) | (1,065,848) | (6,240,222) | (42,094,213) |
| Payments to employees | | | | (3,084,153) | | (3,084,153) |
| Net cash provided by (used in) operating activities | <u>79,785,404</u> | <u>(7,879,077)</u> | <u>7,721,842</u> | <u>3,285,553</u> | <u>(6,108,410)</u> | <u>76,805,312</u> |
| Cash flows from non-capital financing activities | | | | | | |
| Finance loan increases/advances to South Carolina Student Loan Corporation for student loans | | (457,800,000) | (189,381,032) | | | (647,181,032) |
| Finance loan decreases/payments received from South Carolina Student Loan Corporation | | 392,853,572 | 5,472,000 | | | 398,325,572 |
| Proceeds from issuing revenue refunding bonds for student loans | | | 174,700,000 | | | 174,700,000 |
| Arbitrage paid | | (263,681) | | | | (263,681) |
| Payment on bonds payable | | (18,495,000) | (2,500,000) | | | (20,995,000) |
| Costs of bond issuance paid from refunding bond proceeds | | | (885,930) | | | (885,930) |
| Interest paid on revenue bonds | | (8,174,149) | (5,269,266) | | | (13,443,415) |
| Net cash (used in) non-capital financing activities | <u>-</u> | <u>(91,879,258)</u> | <u>(17,864,228)</u> | <u>-</u> | <u>-</u> | <u>(109,743,486)</u> |
| Cash flows from capital and related financing activities | | | | | | |
| Purchase of capital assets | - | - | - | (90,661) | - | (90,661) |
| Cash flows from investing activities | | | | | | |
| Interest received on investment securities | 22,835 | 2,525,733 | 1,297,306 | 509,660 | 59,049 | 4,414,583 |
| Sale of investments | | 155,884 | | | | 155,884 |
| Net increase (decrease) in fair value of investments reported as cash equivalents | 745 | 24,659 | | 17,538 | 3,926 | 46,868 |
| Net cash provided by investing activities | <u>23,580</u> | <u>2,706,276</u> | <u>1,297,306</u> | <u>527,198</u> | <u>62,975</u> | <u>4,617,335</u> |
| Net increase (decrease) in cash and cash equivalents | <u>79,808,984</u> | <u>(97,052,059)</u> | <u>(8,845,080)</u> | <u>3,722,090</u> | <u>(6,045,435)</u> | <u>(28,411,500)</u> |
| Cash and cash equivalents | | | | | | |
| Beginning | <u>33,641,397</u> | <u>141,538,148</u> | <u>18,880,065</u> | <u>20,823,293</u> | <u>10,458,266</u> | <u>225,341,169</u> |
| Ending | <u>\$ 113,450,381</u> | <u>\$ 44,486,089</u> | <u>\$ 10,034,985</u> | <u>\$ 24,545,383</u> | <u>\$ 4,412,831</u> | <u>\$ 196,929,669</u> |

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
SCHEDULE OF CASH FLOWS BY ACCOUNTS
ENTERPRISE FUND
YEAR ENDED JUNE 30, 2005**

| | Collection Account Prior Unpledged | 1993 Resolution | 2002 Resolution | Agency Operating Account | Federal Student Loan Reserve Account | Total |
|---|---|----------------------------|----------------------------|-------------------------------------|---|-------------------|
| Cash flows from operating activities | | | | | | |
| Operating income (loss) | \$ 22,711 | \$ 557,372 | \$ 2,063,763 | \$ 3,118,704 | \$ (2,201,892) | \$ 3,560,658 |
| Adjustments to reconcile operating income (loss to net cash provided by (used in) operating activities | | | | | | |
| Purchase of student loans under loan guarantees | | | | | (25,908,477) | (25,908,477) |
| Payments received from U.S. Department of Education under federal reinsurance program | | | | | 21,410,622 | 21,410,622 |
| Amortization of deferred cost of bond issuance | | 74,698 | 105,184 | | | 179,882 |
| Amortization of deferred amount of refunding - interest expense | | 13,180 | 192,027 | | | 205,207 |
| Amortization of premiums and discounts on bonds payable - interest expense | | 193,084 | 95,084 | | | 288,168 |
| Interest/investment income (investing activities category) | (21,966) | (2,532,957) | (1,302,409) | (495,331) | (52,142) | (4,404,805) |
| Depreciation expense | | | | 75,870 | | 75,870 |
| Provision for loan losses | | | | | 308,193 | 308,193 |
| Net (increase) decrease in fair value of investments (investing activities category) | (745) | (24,659) | | (17,538) | (3,926) | (46,868) |
| Bond interest expense (non-capital financing activities category) | | 9,551,869 | 8,034,623 | | | 17,586,492 |
| Changes in Assets and Liabilities | | | | | | |
| (Increase) decrease in due from South Carolina Student Loan Corporation | (36,416) | 38,730 | (1,466,430) | | | (1,464,116) |
| (Increase) decrease in loan processing issuance fee receivable | | | | (25,321) | | (25,321) |
| (Increase) decrease in account maintenance fee receivable | | | | 332,159 | | 332,159 |
| (Increase) decrease in due from other funds | 15,869,586 | (15,750,394) | | (150,085) | 30,893 | |
| Increase (decrease) in accounts payable | 116,471 | | | 15,086 | 95,947 | 227,504 |
| Increase (decrease) in compensated absences liability | | | | 37,502 | | 37,502 |
| Increase (decrease) in consolidation rebate fee payable | 80,184 | | | | | 80,184 |
| Increase (decrease) in due to South Carolina Student Loan Corporation | 63,755,579 | | | 394,507 | 212,372 | 64,362,458 |
| Net cash provided by (used in) operating activities | 79,785,404 | (7,879,077) | 7,721,842 | 3,285,553 | (6,108,410) | 76,805,312 |
| Supplemental Disclosures of Cash Flow Information | | | | | | |
| Interest collected on finance loans - operating activities | - | 11,714,761 | - | - | - | 11,714,761 |
| Arbitrage income (expense) incurred and liability accrued - non-capital financing activity | - | 3,352,961 | (1,436,623) | - | - | 1,916,338 |
| Principal amounts of bonds - refunded - non-capital financing activity | - | 3,000,000 | - | - | - | 3,000,000 |
| Retirement of fixed assets - capital and related financing activity | - | - | - | 9,088 | - | 9,088 |
| Write-off of accumulated depreciation related to retired assets - capital and related financing activity | \$ - | \$ - | \$ - | \$ 9,088 | \$ - | \$ 9,088 |

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
SCHEDULE OF EXPENSES COMPARED TO BUDGET
YEAR ENDED JUNE 30, 2005**

| | <u>Budget</u> | <u>Actual</u> | Variance (Over) <u>Under</u> |
|---|------------------|----------------------|------------------------------------|
| Operating Expenses | | | |
| Personnel | | | |
| Staff salaries | \$ 2,094,800 | \$ 2,096,525 | \$ (1,725) |
| Social security | 155,500 | 138,084 | 17,416 |
| Group insurance | 527,000 | 535,551 | (8,551) |
| Retirement | 429,000 | 345,757 | 83,243 |
| Unemployment | 6,775 | 5,738 | 1,037 |
| Total personnel | <u>3,213,075</u> | <u>3,121,655</u> | <u>91,420</u> |
| Contractual | | | |
| Loan servicing | 356,000 | 342,916 | 13,084 |
| Legal | 2,400 | | 2,400 |
| Accounting | 2,100 | 3,828 | (1,728) |
| Credit bureau fees | 175,500 | 162,012 | 13,488 |
| Enrollment verification | 31,600 | 28,007 | 3,593 |
| Total contractual | <u>567,600</u> | <u>536,763</u> | <u>30,837</u> |
| General Operating | | | |
| Rent | 104,300 | 100,729 | 3,571 |
| Telephone | 82,400 | 76,151 | 6,249 |
| Printing | 83,200 | 78,718 | 4,482 |
| Postage | 136,950 | 134,118 | 2,832 |
| Supplies | 70,900 | 73,634 | (2,734) |
| Travel | 44,000 | 38,456 | 5,544 |
| Equipment maintenance | 17,100 | 16,854 | 246 |
| Subscriptions and fees | 23,500 | 24,838 | (1,338) |
| Meeting and conference expense | 2,300 | 2,047 | 253 |
| Insurance - general and automotive | 32,000 | 27,809 | 4,191 |
| Contingencies | 25,000 | 7,458 | 17,542 |
| Depreciation expense | 71,000 | 75,870 | (4,870) |
| Total general operating | <u>692,650</u> | <u>656,682</u> | <u>35,968</u> |
| Capital Additions | | | |
| Equipment, furniture and fixtures | <u>\$ 91,400</u> | <u>90,661</u> | <u>\$ 739</u> |
| Total personnel expenses | | 3,121,655 | |
| Total contractual | | 536,763 | |
| Total general operating | | 656,682 | |
| Total operating expenses | | <u>4,315,100</u> | |
| South Carolina Student Loan Corporation Operating Costs | | <u>4,198,752</u> | |
| Other Expenses | | | |
| Interest on bonds | | 17,586,492 | |
| Amortization - deferred cost of bond issuance | | 179,882 | |
| Default aversion fee expense | | 868,597 | |
| Borrower incentive | | 9,755,525 | |
| Reinsurance and other fees | | 6,662,807 | |
| Total other expenses | | <u>35,053,303</u> | |
| Total expenses | | <u>\$ 43,567,155</u> | |

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
SCHEDULE OF ORGANIZATIONAL DATA
YEAR ENDED JUNE 30, 2005**

CREATION

Created by Act No. 433 of the Acts and Joint Resolutions of the General Assembly for the year 1971, now codified as Chapter 115, Title 59 of the 1976 Code (the "Act"). The Constitutionality of the Act was sustained in Durham vs. McLeod, 259 S.C. 409, 192 E. 2d 202, appeal dismissed 413 U.S. 902.

To make, insure and guarantee student loans; to acquire contingent interest in student loans from eligible banks or other lending institutions (up to 100% of the face amount thereof); to develop and administer all programs and to perform all functions necessary or convenient to promote and facilitate the making, guaranteeing and insuring of student loans and to provide such other student loan assistance and services as the Authority shall deem necessary or desirable and to enable it to qualify for loans, grants, insurance and other benefits and assistance under any program of the United States now or hereafter authorized fostering student loans; to appoint one or more banking institutions as its fiscal agent to perform such functions with respect to student loans and its revenue bonds; to approve as eligible, institutions otherwise qualified as such.

MEMBERS OF THE AUTHORITY

| <u>Name</u> | <u>Office Held</u> |
|-------------------------|--|
| Mark Sanford | Governor of South Carolina |
| Grady L. Patterson, Jr. | State Treasurer of South Carolina |
| Richard Eckstrom | Comptroller General of South Carolina |
| Hugh K. Leatherman, Sr. | Chairman, South Carolina Senate Finance Committee |
| Robert W. Harrell, Jr. | Chairman, South Carolina House of Representatives Ways and Means Committee |

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2005**

| <u>Federal Grantor/Program Title</u> | <u>CFDA Number</u> | <u>Amount of Grant</u> | <u>Expenses</u> |
|---|------------------------|----------------------------|-----------------------------|
| U.S. Department of Education programs | | | |
| Federal Family Education Loan Program | | | |
| Direct | | | |
| Loan processing and issuance fee | 84.032 | | \$ 1,720,026 |
| Account maintenance fee | 84.032 | | 2,269,878 |
| Default aversion fee income | 84.032 | | 868,597 |
| Retention on default collections | 84.032 | | 2,231,668 |
| Passed through South Carolina Student Loan Corporation | | | |
| Special allowances | 84.032 | | 15,321,834 |
| Subsidized interest | 84.032 | | <u>3,331,798</u> |
| Total Federal Family Education Loan Program (major program) | | | \$ 25,743,801 |
| Paul Douglas Teachers Scholarship Program (Note 4) | | | <u> </u> |
| Total Department of Education | | | \$ <u>25,743,801</u> |

Notes - CFDA #84.032:

1. The total approved amount at June 30, 2005, of all student loans under guarantee by the South Carolina State Education Assistance Authority was \$ 4,977,918,869. The total outstanding balance of these loans was \$ 2,117,886,699. Special Allowances and Subsidized Interest are earned based on outstanding balance. The Account maintenance fee is based on average principal outstanding for the fiscal year for loans serviced. The loan processing and issuance fee is based on loans originated during the fiscal year. The default aversion fee is based on the balance of principal and interest on a loan that was prevented from defaulting.
2. The South Carolina State Education Assistance Authority received \$ 21,410,622 during the year ended June 30, 2005, under Federal Reinsurance Agreements pursuant to Sections 428A and 428(c) of the Higher Education Act of 1965, as amended.
3. The total value at June 30, 2005, since inception, of all defaulted student loans which the South Carolina State Education Assistance Authority has purchased under Federal reinsurance agreements was \$ 169,248,000. Retention of Default Collections is generated when the Authority retains a portion of the amount it collects on these loans on behalf of the Federal Government.

Notes - CFDA #84.176:

4. Program participants repaid \$ 74,782 to the Authority. The Authority owes the Federal Government \$ 74,782 at June 30, 2005.



DERRICK, STUBBS & STITH, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

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RSM McGladrey Network
An Independently Owned Member

INDEPENDENT AUDITOR'S 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

To the Members of the Authority
South Carolina State Education Assistance Authority
Columbia, South Carolina

We have audited the financial statements of the South Carolina State Education Assistance Authority as of and for the year ended June 30, 2005, and have issued our report thereon dated August 26, 2005. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the South Carolina State Education Assistance Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the South Carolina State Education Assistance Authority's financial statements are free of 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 that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the management and the U.S. Department of Education and is not intended to be and should not be used by anyone other than these specified parties.

Derrick, Stubbs & Stith, LLP

August 26, 2005



DERRICK, STUBBS & STITH, L.L.P.

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Members of the Authority
South Carolina State Education Assistance Authority
Columbia, South Carolina

Compliance

We have audited the compliance of the South Carolina State Education Assistance Authority with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to its major federal program for the year ended June 30, 2005. The South Carolina State Education Assistance Authority's major federal program is identified in the summary of auditor's result section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the South Carolina State Education Assistance Authority's management. Our responsibility is to express an opinion on the South Carolina State Education Assistance Authority's compliance based on our audit.

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

In our opinion, the South Carolina State Education Assistance Authority complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2005.

Internal Control Over Compliance

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

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

This report is intended solely for the information of the management, Board of Directors and the U.S. Department of Education and is not intended to be and should not be used by anyone other than those specified parties.

Derick, Stulke + Stith, LLP

August 26, 2005

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2005**

1. Summary of Auditor's Results:

| | | | | |
|--------|--|--------|--------------------|----------------------|
| (i) | Type of report issued on financial statements | | | Unqualified |
| (ii) | Reportable material weaknesses in internal control over financial reporting | | | None Identified |
| (iii) | Reportable conditions not considered to be material weaknesses in internal control | | | None Identified |
| (iv) | Noncompliance material to the financial statements | | | None Noted |
| (v) | Material weaknesses in internal control over major programs | | | None Identified |
| (vi) | Reportable conditions not considered to be material weaknesses in internal control over major programs | | | None Identified |
| (vii) | Type of report issued on compliance for major programs | | | Unqualified |
| (viii) | Audit findings required to be reported under paragraph .510(a) OMB 133 | | | None Disclosed |
| (ix) | Identification of major programs: | | | |
| | U.S. Department of Education | | | |
| | Federal Family Education Loan Program | | | |
| | Loan processing and issuance fee | CFDA# | <u>Expenditure</u> | |
| | Account maintenance fee | 84.032 | \$ 1,720,026 | |
| | Default aversion fee income | 84.032 | 2,269,878 | |
| | Retention on default collections | 84.032 | 868,597 | |
| | Passed Through South Carolina Student Loan Corporation | | | |
| | Special allowances | 84.032 | 15,321,834 | |
| | Subsidized interest | 84.032 | <u>3,331,798</u> | |
| | Total Federal Family Education Loan Program (major program) | | | \$ <u>25,743,801</u> |
| (x) | Dollar threshold used to distinguish between Type A and Type B programs | | | \$ 772,314 |
| (xi) | South Carolina State Education Assistance Authority qualifies as a low risk auditee under paragraph .530 OMB 133 | | | Yes |

2. Findings related to the financial statements which are required to be reported in accordance with GAGAS None Reported

3. Findings and questioned costs for Federal awards including audit findings as defined in paragraph .510(a) OMB 133

| | | |
|------|---|---------------|
| (i) | Audit findings (e.g., internal control findings, compliance findings, questioned costs, or fraud) | None Reported |
| (ii) | Audit findings which relate to both the financial statements and Federal awards | None Reported |

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
SCHEDULE OF SUMMARY OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2005**

There are no prior audit findings and questioned costs relative to Federal Awards.

**SOUTH CAROLINA STATE EDUCATION ASSISTANCE AUTHORITY
SCHEDULE OF CORRECTIVE ACTION PLAN
YEAR ENDED JUNE 30, 2005**

There is no corrective action plan required since there are no prior audit findings and questioned costs relative to Federal Awards.