



MICHIGAN

OFFICE OF THE AUDITOR GENERAL

AUDIT REPORT



THOMAS H. McTAVISH, C.P.A.
AUDITOR GENERAL

The auditor general shall conduct post audits of financial transactions and accounts of the state and of all branches, departments, offices, boards, commissions, agencies, authorities and institutions of the state established by this constitution or by law, and performance post audits thereof.

– Article IV, Section 53 of the Michigan Constitution

Audit report information can be accessed at:

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Michigan
Office of the Auditor General
REPORT SUMMARY

Financial Audit

Michigan Higher Education Assistance Authority
(A Discretely Presented Component Unit of the State of Michigan)
October 1, 2008 through September 30, 2009

Report Number:
271-0272-10

Released:
December 2009

A financial audit determines if the financial statements are fairly presented; considers internal control over financial reporting; and determines compliance with requirements material to the financial statements. This financial audit of the Michigan Higher Education Assistance Authority was conducted as part of the constitutional responsibility of the Office of the Auditor General.

Financial Statements:

Auditor's Report Issued

We issued an unqualified opinion on the Michigan Higher Education Assistance Authority's financial statements.

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**Internal Control Over Financial Reporting
and on Compliance and Other Matters**

In accordance with *Government Auditing Standards*, we will issue a report on our consideration of the Michigan Higher Education Assistance Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters.

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Background:

The Michigan Higher Education Assistance Authority was created under Act 77 of the Public Acts of 1960 and is comprised of two divisions, the Michigan Guaranty Agency and the Office of Scholarships and Grants.

The Authority's activities are intended to enhance educational opportunities and improve the chance of success for participants. The Authority's primary activities include the administration of State scholarship programs, the guarantee of qualified loans, acquiring defaulted loans, and performing certain default aversion and loan rehabilitation activities.

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<http://audgen.michigan.gov>



Michigan Office of the Auditor General
201 N. Washington Square
Lansing, Michigan 48913

Thomas H. McTavish, C.P.A.
Auditor General

Scott M. Strong, C.P.A., C.I.A.
Deputy Auditor General



STATE OF MICHIGAN
OFFICE OF THE AUDITOR GENERAL
201 N. WASHINGTON SQUARE
LANSING, MICHIGAN 48913
(517) 334-8050
FAX (517) 334-8079

THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

December 30, 2009

Mr. Robert J. Kleine, Chair
Michigan Higher Education Assistance Authority
Richard H. Austin Building
Lansing, Michigan

Dear Mr. Kleine:

This is our report on the financial audit of the Michigan Higher Education Assistance Authority, a discretely presented component unit of the State of Michigan, for the period October 1, 2008 through September 30, 2009.

This report contains our report summary, our independent auditor's report on the financial statements, the Authority management's discussion and analysis, the Authority's basic financial statements, and a glossary of acronyms and terms.

We appreciate the courtesy and cooperation extended to us during this audit.

AUDITOR GENERAL

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INDEPENDENT AUDITOR'S REPORT



STATE OF MICHIGAN
OFFICE OF THE AUDITOR GENERAL
201 N. WASHINGTON SQUARE
LANSING, MICHIGAN 48913
(517) 334-8050
FAX (517) 334-8079

THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

Independent Auditor's Report on the Financial Statements

Mr. Robert J. Kleine, Chair
Michigan Higher Education Assistance Authority
Richard H. Austin Building
Lansing, Michigan

Dear Mr. Kleine:

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Michigan Higher Education Assistance Authority, a discretely presented component unit of the State of Michigan, as of and for the fiscal year ended September 30, 2009, which collectively comprise the Authority's basic financial statements as identified in the table of contents. These financial statements are the responsibility of the Michigan Higher Education Assistance Authority's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the 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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As described in Note 1, the financial statements present only the Michigan Higher Education Assistance Authority and do not purport to, and do not, present fairly the financial position of the State of Michigan or its component units as of September 30, 2009 and the changes in financial position and cash flows, where applicable, thereof for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Michigan Higher Education Assistance Authority as of September 30, 2009 and the respective changes in financial position and cash flows, where applicable, for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2 to the financial statements, the Authority changed the timing of the recognition of federal default fee revenue.

In accordance with *Government Auditing Standards*, we will issue a report on our consideration of the Michigan Higher Education Assistance Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and 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 audit.

The management's discussion and analysis on pages 11 through 20 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

AUDITOR GENERAL

December 22, 2009

MANAGEMENT'S DISCUSSION AND ANALYSIS

The Michigan Higher Education Assistance Authority (the Authority) is comprised of two divisions, the Office of Scholarships and Grants (OSG) and the Michigan Guaranty Agency (MGA).

Office of Scholarships and Grants (OSG)

Higher Education Programs Fund

OSG administers State and federal programs for scholarships, grants, work-study, and reimbursement. Funding for these programs and administrative costs are derived from the State of Michigan's General Fund and restricted funds, the U.S. Department of Education, the Merit Award Trust Fund, federal funds from the Michigan Department of Human Services, and the Michigan Guaranty Agency's Operating Fund. The following programs are administered by OSG:

- **Michigan Competitive Scholarship** - This scholarship is a merit/need based program for students at Michigan public/private institutions.
- **Leveraging Educational Assistance Partnership (LEAP) Program** - This program provides federal matching funds for states administering comprehensive need-based student financial assistance programs.
- **Special Leveraging Educational Assistance Partnership (SLEAP) Program** - This program is an additional component of the LEAP program. In Michigan, this program increases the number of LEAP program recipients.
- **Gear Up Michigan** - The Gaining Early Awareness and Readiness for Undergraduate Program (Gear Up) is designed to significantly increase the number of low-income students who are prepared to enter and succeed in post-secondary education. The U.S. Department of Education awarded Michigan grant funds to support early college awareness activities. A portion of this award is dedicated to a post-secondary student scholarship program.
- **Michigan Tuition Grant** - This grant is a need-based award for students attending a Michigan independent, nonprofit college.
- **Robert C. Byrd Honors Scholarship Program** - This federally funded program provides scholarships up to \$1,500 per year to academically exceptional high

school graduates for undergraduate study at approved U.S. colleges and universities.

- **Adult Part-Time Grant** - This grant provides up to \$600 per year for undergraduate independent part-time students who demonstrate financial need attending a Michigan public or private institution.
- **Michigan Educational Opportunity Grant** - This grant provides up to \$1,000 per year for undergraduate students who are enrolled at least half-time at a Michigan public college or university and demonstrate financial need.
- **Michigan Work-Study Programs** - These programs provide needy undergraduate and graduate students the opportunity to earn money toward their education while enrolled in school.
- **Tuition Incentive Program** - This reimbursement program specifically targets students who have or have had Medicaid coverage for 24 months within a consecutive 36-month period as identified by the Department of Human Services. This program will pay for the first two years of college and beyond for these identified students who graduate from high school or complete their general equivalency diploma (GED) before age 20.
- **Children of Veterans Tuition Grant Program** - Students are eligible if they meet program requirements and are the natural or adopted child of a Michigan veteran who died in a war or war condition, is totally and permanently disabled from a service-connected illness or injury, or is listed as missing in action. Students must enroll at an approved Michigan post-secondary institution. Awards are up to \$2,800 per academic year.
- **Nursing Scholarship Program** - This program provides scholarships for students enrolled in approved programs that lead to a licensed practical nurse (LPN), Associate Degree in Nursing (ADN), or Bachelor of Science in Nursing (BSN) degree. Students can receive up to \$4,000 per academic year for up to four years. Recipients are required to work at the profession in Michigan for one year for each year of assistance.

The Higher Education Programs Fund is included in the Authority's financial statements as a governmental fund.

Michigan Guaranty Agency (MGA)

MGA was established by Act 77 of the Public Acts of 1960. Under the Federal Family Education Loan Program (FFELP), MGA administers five loan guarantee programs in Michigan:

- **Subsidized Stafford Loans** - These loans are awarded based on a federal formula that includes income and other assets. The federal government pays the interest on these loans while the student is in school and during grace or deferment periods.
- **Unsubsidized Stafford Loans** - These loans are available regardless of income as long as financial need is demonstrated per the federal formula. The student is responsible for all interest which accrues.
- **Parent Loan for Undergraduate Students (PLUS)** - This is a supplemental loan available to parents of dependent students.
- **Graduate PLUS Loans** - These loans are available to graduate and professional students under the Federal PLUS Loan Program.
- **Consolidation Loans** - These loans allow a borrower the opportunity to combine various federally authorized student loans into a single loan with the benefits of a fixed rate and an extended repayment period.

The interest rate charged to a borrower under these programs varies based on the type of program and the federal regulations in effect at the time of borrowing. The loans are made by banks, credit unions, savings and loan associations, insurance companies, certain federal agencies, and the Michigan Higher Education Student Loan Authority (MHESLA).

MGA loan guarantee programs are intended to enhance educational opportunities and improve the chance of success for the programs' participants. The mission of MGA is to provide Michigan residents with optimum access to post-secondary educational opportunities through low-interest, long-term educational loans.

The federal Higher Education Act Amendments of 1998 created the current guaranty agency administrative and financial model. Under the model, MGA was required to

establish two funds, an Operating Fund and a Federal Fund, which are described as follows.

Operating Fund

The Operating Fund is included in the Authority's financial statements as a proprietary fund. This Fund holds and accounts for funds considered to be the property of MGA. Sources of revenue include investment income, retention on collection of defaulted loans, and default aversion fees, along with account maintenance fees and loan processing and issuance fees received from the federal government. Expenses include personnel-related and collection costs, loan servicer fees, federal default fees, and other administrative expenses.

Federal Fund

The federal Higher Education Act Amendments of 1998 created the current financial model, as discussed previously. At this time, the Federal Fund was established with all net assets of MGA prior to October 1, 1998. Monies in this Fund are used to reimburse lenders for defaulted student loans and to pay the Operating Fund for default aversion activities. The federal government, through reinsurance, subsequently reimburses the Federal Fund for defaulted student loans purchased from lenders. Other sources of additions are federal retention on collections of defaulted loans and investment income. Effective July 1, 2006, the Federal Fund receives a federal default fee. This fee is derived by applying 1.0% to all MGA guaranteed loans disbursed each month. From July 1, 2006 to June 30, 2007, the 1.0% default fee was paid from the Operating Fund on behalf of borrowers. Effective July 1, 2007, the Operating Fund paid 0.75% and MGA's participating lenders paid the remaining 0.25% of the default fee on behalf of borrowers. Effective July 1, 2008, the full 1.0% is paid from MGA's Operating Fund on behalf of borrowers. Effective July 1, 2009, the full 1.0% is paid either by the lender or by the borrower at the time of disbursement.

The Federal Fund is a fiduciary fund. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the Authority's own programs.

Overview of the Basic Financial Statements

This discussion and analysis is intended to serve as an introduction to the Authority's basic financial statements. The basic financial statements are comprised of three components:

1. Government-wide financial statements
 - Statement of net assets
 - Statement of activities

2. Fund financial statements
 - Governmental fund
 - Higher Education Programs Fund (major fund)
 - Proprietary fund
 - Operating Fund (major fund)
 - Fiduciary fund
 - Federal Fund

3. Notes to the financial statements

The basic financial statements present the Authority's financial position, revenues, expenses, changes in net assets, and cash flows. The following is a condensed summary of financial information for the fiscal years ended September 30, 2009 and September 30, 2008.

Condensed Financial Information

Net Assets	2009		
	Governmental Activities	Business-Type Activities	Fiduciary Activities
	Higher Education Programs Fund	Operating Fund	Federal Fund
Assets			
Cash and cash equivalents		\$ 1,259,500	\$ 17,120,342
Investments		7,500,000	1,570,780
Receivable from U.S. Department of Education		1,300,299	21,240,909
Other assets	\$ 1,167,345	1,445,158	1,035,652
Capital assets - Net	673,035	15,963	
Total assets	\$ 1,840,380	\$ 11,520,920	\$ 40,967,683
Liabilities			
Claims payable			\$ 17,831,571
Payable to U.S. Department of Education			2,618,235
Other liabilities	\$ 867,345	\$ 511,975	1,164,556
Total liabilities	\$ 867,345	\$ 511,975	\$ 21,614,362
Invested in capital assets	\$ 673,035	\$ 15,963	
Unrestricted	300,000		
Restricted		10,992,982	\$ 19,353,321
Total net assets	\$ 973,035	\$ 11,008,945	\$ 19,353,321
Change in Net Assets			
Revenues/additions			
Loan recoveries		\$ 3,244,177	\$ 27,440,052
U.S. Department of Education	\$ 2,295,938	5,490,079	149,428,680
Loans repurchased and rehabilitated		2,482,912	10,221,891
Loan consolidation fees		2,757,725	
Other revenues/additions	140,109,806	2,966,390	7,737,709
Total revenues/additions	\$142,405,744	\$ 16,941,283	\$194,828,332
Expenses/deductions			
Scholarships, grants, and other higher education programs	\$139,364,729		
Loan claims			\$156,717,144
U.S. Department of Education			36,218,393
Student loan servicer fees		\$ 8,807,523	
Federal default fees		5,614,584	
Other expenses/deductions	2,898,343	6,105,834	2,680,308
Total expenses/deductions	\$142,263,072	\$ 20,527,941	\$195,615,846
Net change	\$ 142,672	\$ (3,586,658)	\$ (787,514)

2008		2008 - Restated
Governmental Activities	Business-Type Activities	Fiduciary Activities
Higher Education Programs Fund	Operating Fund	Federal Fund
	\$ 5,240,300	\$ 10,062,533
	7,500,000	1,509,429
	1,579,023	30,185,370
\$ 443,434	789,956	182,741
830,363	43,176	
<u>\$ 1,273,797</u>	<u>\$15,152,455</u>	<u>\$ 41,940,073</u>
		\$ 18,771,700
		2,749,052
\$ 443,434	\$ 556,852	278,484
<u>\$ 443,434</u>	<u>\$ 556,852</u>	<u>\$ 21,799,236</u>
\$ 830,363	\$ 43,176	
	14,552,427	\$ 20,140,837
<u>\$ 830,363</u>	<u>\$14,595,603</u>	<u>\$ 20,140,837</u>
\$ 1,547,118	\$ 2,890,114	\$ 24,875,789
	5,640,118	128,235,444
	5,880,986	20,499,579
	2,142,908	224,742
131,637,697	3,044,550	8,738,611
<u>\$133,184,815</u>	<u>\$19,598,676</u>	<u>\$182,574,164</u>
\$130,383,466		\$135,179,970
		44,808,156
	\$ 9,929,282	
	6,065,854	
2,958,677	7,242,678	2,509,406
<u>\$133,342,143</u>	<u>\$23,237,814</u>	<u>\$182,497,532</u>
<u>\$ (157,328)</u>	<u>\$ (3,639,138)</u>	<u>\$ 76,632</u>

Financial Analysis

Office of Scholarships and Grants (OSG)

Higher Education Programs Fund

OSG had total expenses of \$142.1 million in fiscal year 2008-09. Approximately \$139.4 million includes payments to students, colleges, and universities for financial aid scholarships, grants, work-study, and degree reimbursement. The remaining \$2.7 million relates to expenses for salaries and employee benefits and other administrative expenses. The following represents the program expenditures for the fiscal year ended September 30, 2009 (in millions):

Michigan Competitive Scholarship	\$ 34.4
Gear Up Michigan	0.9
Michigan Tuition Grant	58.9
Robert C. Byrd Honors Scholarship Program	1.4
Adult Part-Time Grant	2.7
Michigan Educational Opportunity Grant	2.1
Michigan Work-Study Programs	7.0
Tuition Incentive Program	26.7
Children of Veterans Tuition Grant Program	0.9
Nursing Scholarship Program	4.4
	<hr/>
Total program expenditures - Higher education programs	<u><u>\$139.4</u></u>

Michigan Guaranty Agency (MGA)

Operating Fund

The Operating Fund total assets decreased by \$3.6 million in fiscal year 2008-09. The \$3.6 million decrease is primarily attributable to MGA paying the federal default fee from the Operating Fund to the Federal Fund, thus a decrease in cash and cash equivalents.

Operating Revenues and Expenses

Operating revenues decreased by \$2.4 million in fiscal year 2008-09. In fiscal year 2008-09, revenue from loans repurchased and rehabilitated reflected a substantial decrease by \$3.4 million. This decrease in loans rehabilitated is due to the inability of MGA to find a buyer for rehabilitated loans as a result of capital market disruptions.

Also, in fiscal year 2008-09, loan recoveries, account maintenance fees, loan consolidation fees, and default aversion fees all reflected minimal increases.

Operating income for fiscal year 2008-09 was \$1.7 million compared to \$3.0 million in fiscal year 2007-08. This \$1.3 million decrease is attributable to a decrease in revenue from loans repurchased and rehabilitated and a decrease in collection fees.

Nonoperating Revenues and Expenses

Nonoperating revenues and expenses for fiscal year 2008-09 were a net amount of \$5.3 million in expenses compared to a net amount of \$6.7 million in expenses in fiscal year 2007-08. This \$1.4 million decrease is mostly attributable to a transfer to the Higher Education Program Fund of \$1.2 million in fiscal year 2007-08, which was not required in fiscal year 2008-09.

Net assets decreased approximately \$3.6 million in fiscal year 2008-09.

Federal Fund

The Federal Fund total assets decreased by \$972,000 in fiscal year 2008-09 primarily from a decrease in reinsurance receivable from the U.S. Department of Education.

Total liabilities decreased by \$185,000 in fiscal year 2008-09. The \$185,000 decrease in fiscal year 2008-09 is attributable to an offset of an increase in amounts payable to the U.S. Department of Education for loan recoveries and loans repurchased and rehabilitated and a decrease in claims payable.

Additions increased by \$12.3 million in fiscal year 2008-09. The \$12.3 million increase reflects increases in the amounts received from the U.S. Department of Education for loan recoveries and loans reinsured. Loans repurchased and rehabilitated decreased by \$10.3 million in fiscal year 2008-09.

Deductions increased by \$13.1 million in fiscal year 2008-09. This increase is due to a substantial increase of \$21.5 million in loan claims and \$2.3 million in amounts paid to the U.S. Department of Education for loan recoveries and a decrease of \$10.6 million in amounts paid to the U.S. Department of Education for loans repurchased and rehabilitated. Due to the current economic climate, claims for loan defaults increased to an all-time high of \$156.7 million in fiscal year 2008-09, whereas loan claims were \$135.2 million in fiscal year 2007-08.

Net assets decreased by \$788,000 in fiscal year 2008-09, which was primarily due to the change in accounting principle for recording federal default fees (Note 2).

BASIC FINANCIAL STATEMENTS

MICHIGAN HIGHER EDUCATION ASSISTANCE AUTHORITY

Statement of Net Assets

September 30, 2009

	Governmental Activities	Business-Type Activities	Total
Assets			
Cash and cash equivalents (Note 4)		\$ 1,259,500	\$ 1,259,500
Investments (Note 4)		7,500,000	7,500,000
Accrued interest		218,863	218,863
Amounts receivable from U.S. Department of Education:			
Account maintenance fees		691,175	691,175
Loan processing and issuance fees		609,124	609,124
Due from the State of Michigan		374,378	374,378
Due from fiduciary - Federal Fund		851,917	851,917
Due from other governmental units	\$ 367,345		367,345
Other current assets	300,000		300,000
Capital assets (Note 3)	673,035	15,963	688,998
Other noncurrent assets	500,000		500,000
	\$ 1,840,380	\$ 11,520,920	\$ 13,361,300
Total assets			
Liabilities			
Due to the State of Michigan	\$ 367,345		\$ 367,345
Deferred revenue	500,000		500,000
Noncurrent liabilities		\$ 511,975	511,975
	\$ 867,345	\$ 511,975	\$ 1,379,320
Total liabilities			
Net Assets			
Invested in capital assets (Note 3)	\$ 673,035	\$ 15,963	\$ 688,998
Unrestricted	300,000		300,000
Restricted - Student financial aid-related activities		10,992,982	10,992,982
	\$ 973,035	\$ 11,008,945	\$ 11,981,980
Total net assets			

The accompanying notes are an integral part of the financial statements.

MICHIGAN HIGHER EDUCATION ASSISTANCE AUTHORITY
Statement of Activities
Fiscal Year Ended September 30, 2009

	Program Revenues		Net (Expenses) Revenues and Changes in Net Assets			
	Expenses	Charges for Service	Operating Grants and Contributions	Governmental Activities	Business-Type Activities	Total
Governmental Activities -						
Higher education programs	\$ 142,263,072		\$ 142,405,744	\$ 142,672		\$ 142,672
Business-Type Activities -						
Student loan services	20,527,941	\$ 16,607,272	334,011		\$ (3,586,658)	(3,586,658)
Total primary government	<u>\$ 162,791,013</u>	<u>\$ 16,607,272</u>	<u>\$ 142,739,755</u>			
Net Assets - Beginning of fiscal year				830,363	14,595,603	15,425,966
Net Assets - End of fiscal year				<u>\$ 973,035</u>	<u>\$ 11,008,945</u>	<u>\$ 11,981,980</u>

The accompanying notes are an integral part of the financial statements.

MICHIGAN HIGHER EDUCATION ASSISTANCE AUTHORITY
 Governmental Fund - Balance Sheet
September 30, 2009

	Higher Education Programs Fund
Assets	
Due from other governmental units	\$ 367,345
Other current assets	300,000
Total current assets	\$ 667,345
Other noncurrent assets	500,000
Total assets	\$ 1,167,345
Liabilities	
Due to the State of Michigan	\$ 367,345
Deferred revenue	500,000
Total liabilities	\$ 867,345
Fund Balance	
Unreserved fund balance	\$ 300,000
Total fund balance	\$ 300,000
Total liabilities and fund balance	\$ 1,167,345
Net assets on the statement of net assets	
Amounts reported for governmental activities in the statement of net assets are different than fund balance because capital assets used in governmental activities are not financial resources and are not reported in the funds (Note 3)	\$ 673,035
Net assets of governmental activities	\$ 973,035

The accompanying notes are an integral part of the financial statements.

MICHIGAN HIGHER EDUCATION ASSISTANCE AUTHORITY
 Governmental Fund - Statement of Revenues, Expenditures, and Changes in Fund Balance
September 30, 2009

	Higher Education Programs Fund
Revenues	
U.S. Department of Education	\$ 2,295,938
State of Michigan's General Fund	13,786,935
Merit Award Trust Fund	6,763,937
Michigan Department of Human Services (Note 7)	119,021,061
Other	537,873
Total revenues	\$ 142,405,744
Expenditures	
Salaries and employee benefits	\$ 2,212,181
Scholarships, grants, and other higher education programs	139,364,729
Other administrative expenses	528,834
Total expenditures	\$ 142,105,744
Excess of Revenues Over Expenditures	\$ 300,000
Fund Balance - Beginning of fiscal year	
Fund Balance - End of fiscal year	\$ 300,000
Net assets on the statement of activities	
Amounts reported for governmental activities in the statement of activities are different than excess of revenues over expenditures because governmental funds report capital outlays as expenditures; however, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which depreciation exceeds capital outlay in the current period.	\$ (157,328)
Change in net assets of governmental activities	\$ 142,672

The accompanying notes are an integral part of the financial statements.

MICHIGAN HIGHER EDUCATION ASSISTANCE AUTHORITY
Proprietary Fund - Statement of Net Assets
September 30, 2009

	<u>Operating Fund</u>
Assets	
Current assets:	
Cash and cash equivalents (Note 4)	\$ 1,259,500
Investments (Note 4)	7,500,000
Accrued interest	218,863
Amounts receivable from U.S. Department of Education:	
Account maintenance fees	691,175
Loan processing and issuance fees	609,124
Due from the State of Michigan	374,378
Due from fiduciary - Federal Fund	851,917
Total current assets	\$ 11,504,957
Capital assets - Net (Note 3)	15,963
Total assets	\$ 11,520,920
Liabilities	
Compensated absences	\$ 511,975
Total liabilities	\$ 511,975
Net Assets	
Invested in capital assets (Note 3)	\$ 15,963
Restricted - Student financial aid-related activities	10,992,982
Total net assets	\$ 11,008,945
Total liabilities and net assets	\$ 11,520,920

The accompanying notes are an integral part of the financial statements.

MICHIGAN HIGHER EDUCATION ASSISTANCE AUTHORITY
Proprietary Fund - Statement of Revenues, Expenses, and Changes in Net Assets
September 30, 2009

	<u>Operating Fund</u>
Operating Revenues	
Loan recoveries	\$ 3,244,177
U.S. Department of Education:	
Account maintenance fees (Note 1)	2,706,866
Loan processing and issuance fees (Note 1)	2,783,213
Loans repurchased and rehabilitated fees	2,482,912
Loan consolidation fees	2,757,725
Default aversion fees (Note 1)	2,632,379
	<u>16,607,272</u>
Total operating revenues	\$ 16,607,272
 Operating Expenses	
Salaries and employee benefits	\$ 4,395,638
Collection fees (Note 7)	2,883,360
Servicer fees	5,924,163
Depreciation	27,213
Other administrative expenses (Note 9)	1,682,983
	<u>14,913,357</u>
Total operating expenses	\$ 14,913,357
 Operating Income	<u>\$ 1,693,915</u>
 Nonoperating Revenues and Expenses	
Investment income	\$ 334,011
Federal default fees (Note 1)	(5,614,584)
	<u>(5,280,573)</u>
Total nonoperating expenses	\$ (5,280,573)
 Change in Net Assets	<u>\$ (3,586,658)</u>
 Net Assets - Beginning of fiscal year	<u>14,595,603</u>
 Net Assets - End of fiscal year	<u>\$ 11,008,945</u>

The accompanying notes are an integral part of the financial statements.

MICHIGAN HIGHER EDUCATION ASSISTANCE AUTHORITY
Proprietary Fund - Statement of Cash Flows
September 30, 2009

	<u>Operating Fund</u>
Cash Flows from Operating Activities	
Operating receipts	\$ 16,137,087
Payments to vendors	(10,625,580)
Payments to employees	(4,305,441)
	<u>\$ 1,206,066</u>
Cash Flows from Noncapital Financing Activities	
Default fees paid to the Federal Fund	\$ (5,614,584)
	<u>\$ (5,614,584)</u>
Cash Flows from Investing Activities	
Proceeds from maturity of investments	\$ 5,500,000
Purchase of investments	(5,500,000)
Interest received on investments	427,718
	<u>\$ 427,718</u>
Net Decrease in Cash and Cash Equivalents	\$ (3,980,800)
Cash and Cash Equivalents - Beginning of fiscal year	<u>5,240,300</u>
Cash and Cash Equivalents - End of fiscal year	<u>\$ 1,259,500</u>
Reconciliation of Operating Income (Loss) to Net Cash from Operating Activities	
Operating income	\$ 1,693,915
Adjustments to reconcile operating income to net cash from operating activities:	
Depreciation	27,213
Change in assets:	
Account maintenance fees	183,335
Loan processing and issuance fees	95,389
Due from the State of Michigan	103,008
Due from federal government	(851,917)
Change in liabilities:	
Due to federal government	(135,074)
Compensated absences	90,197
	<u>\$ 1,206,066</u>

Noncash Investing, Capital, and Financing Activities - There were no noncash investing, capital, and financing activities during the fiscal year ended September 30, 2009.

The accompanying notes are an integral part of the financial statements.

MICHIGAN HIGHER EDUCATION ASSISTANCE AUTHORITY
 Fiduciary Fund - Private Purpose Trust
 Statement of Fiduciary Net Assets
September 30, 2009

	<u>Federal Fund</u>
Assets	
Cash and cash equivalents (Note 4)	\$ 17,120,342
Investments (Note 4)	1,570,780
Accrued interest	46,970
Reinsurance receivable from U.S. Department of Education	21,240,909
Due from the State of Michigan	923
Default fee receivable	987,759
	<u>987,759</u>
Total assets	<u>\$ 40,967,683</u>
Liabilities	
Accounts payable	\$ 312,638
Claims payable	17,831,571
Due to Operating Fund	851,918
Amounts payable to U.S. Department of Education:	
Loan Recoveries	1,522,297
Loans repurchased and rehabilitated	1,095,938
	<u>1,095,938</u>
Total liabilities	<u>\$ 21,614,362</u>
Net Assets - Available for student loan services	<u>\$ 19,353,321</u>

The accompanying notes are an integral part of the financial statements.

MICHIGAN HIGHER EDUCATION ASSISTANCE AUTHORITY
Fiduciary Fund - Private Purpose Trust
Statement of Changes in Fiduciary Net Assets
Fiscal Year Ended September 30, 2009

	Federal Fund
Additions	
Loan recoveries	\$ 27,440,052
U.S. Department of Education - Loans reinsured (Note 5)	149,428,680
Loans repurchased and rehabilitated	10,221,891
Investment income	64,931
Increase in fair value of investments	61,351
Federal default fees	6,815,803
Reinsurance rate complement (Note 1)	795,624
	<u>\$ 194,828,332</u>
Deductions	
Loan claims	\$ 156,717,144
U.S. Department of Education:	
Loan recoveries	27,410,579
Loans repurchased and rehabilitated	8,807,814
Default aversion expense (Note 1)	2,632,379
Other	47,929
	<u>\$ 195,615,846</u>
Change in Net Assets	\$ (787,514)
Net Assets - Beginning of fiscal year - Restated (Note 2)	20,140,835
Net Assets - End of fiscal year	\$ 19,353,321

The accompanying notes are an integral part of the financial statements.

Notes to the Financial Statements

Note 1 **Summary of Significant Accounting Policies**

Organization - The Michigan Higher Education Assistance Authority (the Authority) is comprised of two divisions, the Michigan Guaranty Agency and the Office of Scholarships and Grants.

Michigan Guaranty Agency (MGA) - MGA was formed for the purpose of guaranteeing loans to qualified students and parents of qualified students made through approved financial institutions. Commencing in 1969, retroactive to 1965, the federal government agreed to reinsure 80% of such guaranteed student loans under the Guaranteed Student Loan Program (now known as the Federal Family Education Loan Program (FFELP)). FFELP, under which MGA operates, was established by Congress and is administered by the U.S. Department of Education as a means of making loans available to students attending colleges, universities, and vocational institutions. FFELP provides for MGA to guarantee the repayment of principal and accrued interest to lenders for each eligible student loan. MGA is responsible for processing loans submitted for guarantee, issuing loan guarantees, providing collection assistance to lenders for delinquent loans, paying lender claims for loans in default, and collecting loans on which default claims have been paid. MGA also informs schools and lenders of FFELP requirements and regulatory changes and encourages lender participation.

Effective January 10, 1977, MGA entered into a supplemental guaranty agreement with the federal government, which provided up to 100% reimbursement, depending upon default experience as specified in the agreement. Federal reinsurance on guaranteed loans made from October 1, 1993 to September 30, 1998 was reduced to a maximum of 98%. Federal reinsurance on guaranteed loans made on or after October 1, 1998 was reduced to a maximum of 95%.

The Higher Education Act Amendments of 1998 (the 1998 Amendments) that were enacted on October 7, 1998, with an effective date of October 1, 1998, changed the manner in which FFELP is administered. Under the 1998 Amendments, MGA established an Operating Fund and a Federal Fund, as

required, to account for FFELP activities. The result of this federal legislation was that MGA's net assets of approximately \$36.1 million were transferred to the newly established Federal Fund and the Operating Fund commenced activities with \$0 in net assets.

Operating Fund - The Operating Fund assets and earnings on those assets are the property of MGA and may be used only for MGA and other student financial aid-related activities. The assets, liabilities, net assets, and operations of the Operating Fund are presented in the accompanying proprietary fund statements of the Authority.

Federal Fund - The Federal Fund assets and earnings on those assets are the property of the federal government and are presented in the accompanying statement of fiduciary net assets. The funds in the Federal Fund pay for the reimbursements to the lenders for defaulted student loan claims and default aversion fees. The funds are replenished from reimbursements from the federal government and several other sources. All of the other sources and uses of monies not related to the Federal Fund are recorded in the Operating Fund. Both the Operating Fund and Federal Fund are subject to federal oversight.

Office of Scholarships and Grants (OSG) - OSG is responsible for administering financial aid programs to benefit students, colleges, and universities. The programs that are administered by OSG include Michigan Competitive Scholarship, Michigan Tuition Grant, Robert C. Byrd Honors Scholarship Program, Michigan Work-Study Programs, Adult Part-Time Grant, Leveraging Educational Assistance Partnership Program, Special Leveraging Assistance Partnership Program, Michigan Educational Opportunity Grant, Nursing Scholarship Program, Tuition Incentive Program, Children of Veterans Tuition Grant Program, and Gear Up Michigan. The main focus of the staff at OSG is to disburse monies of the program to the colleges and universities or directly to the students. The staff is required to ensure that students, colleges, and universities adhere to strict eligibility requirements prior to disbursement. These programs are funded from amounts provided from the State of Michigan's General Fund and restricted funds, the U.S. Department of Education, the Merit Award Trust Fund, the Michigan Department of Human Services, and the Michigan Guaranty Agency's Operating Fund.

Reporting Entity - The Authority is a discretely presented component unit of the State of Michigan and is reported as such in the *State of Michigan Comprehensive Annual Financial Report*. The accompanying financial statements present only the Michigan Higher Education Assistance Authority. Accordingly, they do not purport to, and do not, present fairly the financial position and the changes in financial position and cash flows of the State of Michigan or its component units in conformity with accounting principles generally accepted in the United States of America.

Measurement Focus, Basis of Accounting, and Basis of Presentation - The accounts of the Authority are organized and operated on the basis of the underlying funds. A fund is an independent fiscal and accounting entity with a self-balancing set of accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with finance-related legal and contractual provisions.

The Authority has the following fund types:

Governmental Fund (Higher Education Programs Fund) - The Higher Education Programs Fund, a major fund, is used to account for the inflows and outflows of funds within OSG. Governmental funds are accounted for on the flow of current resources measurement and use the modified accrual basis of accounting. Under this method, revenues should be recorded in the period when they become available and measurable to finance the expenditures of the fiscal period and expenses are recorded at the time the liabilities are incurred.

Revenue from the Michigan Department of Human Services - In the fiscal years ended September 30, 2009 and September 30, 2008, the Authority received approximately \$119.0 million and \$108.2 million, respectively, from the Michigan Department of Human Services (DHS) as appropriated in Act 140 of the Public Acts of 2009 and Act 279 of the Public Acts of 2008. These funds were used for the scholarship and grant program expenditures for the Nursing Scholarship and Grant Program, State competitive scholarships, tuition grants, and the Tuition Incentive Program. DHS determined that these scholarships and grants were eligible for the federal Temporary Assistance for Needy Families (TANF) program. Prior to 2008, the Authority had been appropriated

funding from the State of Michigan's General Fund and Michigan Merit Award Trust Fund for education scholarships administered by OSG and the Authority.

Proprietary Fund (Operating Fund) - The Operating Fund, a major fund, is accounted for on the flow of economic resources measurement focus and uses the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The Authority applies all applicable Governmental Accounting Standards Board (GASB) pronouncements, as well as all Financial Accounting Standards Board statements and interpretations, Accounting Principles Board opinions, and Accounting Research Bulletins issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. After November 30, 1989, the Authority only applies applicable GASB pronouncements.

Fiduciary Fund (Federal Fund) - The Federal Fund is used to account for funds and property received from various sources and held by the Authority on behalf of the U.S. Department of Education for the conduct of FFELP. Such fund utilizes the accrual basis of accounting, which requires that revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Operating Revenues and Expenses - The Authority's primary operations include providing guarantees of qualified loans; acquiring defaulted loans from financial institutions; performing certain default aversion and loan rehabilitation activities; performing collection activities on defaulted student loans; and administering the scholarship and grant programs to students, colleges, and universities.

Cash and Cash Equivalents - The Authority considers cash and money market funds to be cash and cash equivalents for the purpose of the statement of cash flows.

Investments - The Authority reports investments at fair value based on quoted market prices with gains and losses included in the statement of revenues, expenses, and changes in net assets and the statement of changes in fiduciary net assets.

Reserves - Pursuant to reauthorization, the Authority maintains cash and cash equivalents and investments as a reserve of FFELP loan guarantee claim obligations. The Higher Education Act of 1965, as amended, states that the Authority must maintain a 0.25% minimum reserve level requirement. Assets of the Federal Fund must be at least 0.25% of the Authority's guaranteed loan portfolio's original principal balance outstanding. The Authority was in compliance with its minimum reserve level requirement as follows as of September 30, 2009 (in thousands):

Outstanding loans (original principal balance)	\$4,408,441
Minimum reserve requirement	\$ 11,021
Federal Fund cash and investments	\$ 18,691

Capital Assets - Purchases by the Authority for use in its operations that meet the requirements of the State of Michigan's capitalization policy are capitalized in accordance with GASB Statement No. 34. For the fiscal year ended September 30, 2009, the Authority had no capitalized equipment purchases. Costs incurred for computer software developed or obtained for internal use are capitalized and amortized over its useful life of 12 years. Costs incurred for office equipment are capitalized and depreciated over the equipment's useful life of five years.

Account Maintenance Fee (AMF) - The 1998 Amendments established an AMF based on 0.12% of the original principal amount of outstanding loans. The AMF is paid to the Authority on a quarterly basis by the federal government. This fee is recognized as revenue and recorded in the Operating Fund. Effective October 1, 2003, the AMF was reduced to 0.10% of the original principal amount of outstanding loans. Effective October 1, 2007, the AMF was reduced to 0.06% of the original principal amount of outstanding loans.

Loan Processing and Issuance Fee (LPIF) - The 1998 Amendments established an LPIF. LPIF payments are based on the net guarantee amount, less cancellations, multiplied by 0.65%. The LPIF is paid to the Authority on a quarterly basis by the federal government. This fee is recognized as revenue and recorded in the Operating Fund. Effective October 1, 2003, the LPIF was reduced to 0.40% of net guarantees, less cancellations.

Default Aversion Fee (DAF) - The DAF was established under the 1998 Amendments. The Authority receives the DAF for its aversion activities on delinquent loans at the time lenders request default aversion assistance. The DAF is equal to 1.0% of principal and interest on the loan at the time the Authority receives a request from a lender for preclaim assistance. The DAF is paid monthly from the Federal Fund to the Operating Fund and is recognized as a deduction in the Federal Fund and as revenue in the Operating Fund.

Federal Default Fee - The Higher Education Reconciliation Act of 2005 created a new federal default fee. This fee is equal to 1% of the principal amount of the loan, by deduction proportionately from each installment payment of the proceeds of the loan to the borrower for loans made on or after July 1, 2006. The fee must be deposited into the Federal Fund. This fee shall be collected either by deduction from the proceeds of the loan or by payment of other nonfederal sources such as the lender or MGA's Operating Fund. Approval of the Authority was granted to pay the federal default fee from the Operating Fund on behalf of borrowers. Effective July 1, 2007, 0.75% was paid from the Operating Fund and 0.25% was received from MGA's participating lenders on behalf of borrowers. Effective July 1, 2008, the full 1.0% fee was paid from MGA's Operating Fund. Effective July 1, 2009, the full 1.0% fee is paid by either the lender or the borrower at the time of disbursement.

Reinsurance - The Authority's Federal Fund will receive federal loan reinsurance revenue from the U.S. Department of Education according to the following schedule for all eligible default claims purchased by the Federal Fund:

Annual Default Rate	Federal Reinsurance
0% to less than 5%	95%
5% to less than 9%	95% of claims up to 5% and 85% of claims equal to or greater than 5%, but less than 9%
9% or greater	95% of claims up to 5%; 85% of claims equal to or greater than 5%, but less than 9%; and 75% of claims equal to or greater than 9%

For claims filed on loans guaranteed prior to October 1, 1998, the reinsurance rates of 95%/85%/75% reflected in the schedule above are increased to 98%/88%/78%, respectively. For claims filed on loans guaranteed prior to October 1, 1993, the reinsurance rates are increased to 100%/90%/80%, respectively.

Reinsurance Rate Complement - The reinsurance rate complement (2%) was established in the 1998 Amendments. This amount is recognized as an addition in the Federal Fund when the loan recoveries are made on defaulted loans. It is calculated by using the percentage amount equal to the complement of the reinsurance percentage in effect when payment under the guaranty agreement was made.

Rehabilitated and Consolidated Loans - The Authority is entitled to retain 18.5% of principal and interest for rehabilitated loans, plus an 18.5% fee for collection costs. For consolidated loans, the Authority is entitled to a 10.0% fee for collection costs. The fees and the portion of the loan recoveries are recorded in the Operating Fund. The remaining rehabilitated loan principal and interest is recorded in the fiduciary Federal Fund.

Loan Recoveries and Payable to U.S. Department of Education - Effective October 1, 2007, the retention rate decreased to 16% from 23% as required by the 2007 College Cost Reduction and Access Act. The Authority is entitled to retain 16% of collections received for defaulted loans for which federal reinsurance has been previously received. This amount is recorded as an addition, loan recoveries, when received in the fiduciary fund.

Risk Management - The Authority is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries. Coverage for these various risks of loss is obtained through the Authority's participation in the State of Michigan's Risk Management Fund and State Sponsored Group Insurance Fund.

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 and disclosure of contingent 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. The Authority uses estimates in the calculations of claims payable and the AMF and LPIF receivables.

Note 2 Change in Accounting Principle

MGA implemented a change from an acceptable accounting principle to an industry preferred accounting principle regarding the revenue from the federal default fee. In the fiscal years ended September 30, 2007 and September 30, 2008, the federal default fee revenue was recognized over the average life of a student loan. Beginning in fiscal year 2008-09, MGA recognized the revenue when received in the Federal Fund. The cumulative effect of the change in recognition of revenue is reflected in the restatement of beginning net assets of approximately \$20.1 million.

Note 3 Capital Assets

Capital asset activity for the fiscal year ended September 30, 2009 was as follows:

	Beginning Balance	Additions	Retirements	Ending Balance
Governmental Activities				
Internally developed software	\$1,887,854	\$	\$	\$1,887,854
Less accumulated depreciation for internally developed software	1,057,491	157,328		1,214,819
	<hr/>	<hr/>	<hr/>	<hr/>
Governmental activities capital assets - Net	\$ 830,363	\$(157,328)	\$ 0	\$ 673,035
	<hr/>	<hr/>	<hr/>	<hr/>
Business-Type Activities/Proprietary Fund – Operating Fund				
Equipment	\$ 173,455	\$	\$	\$ 173,455
Less accumulated depreciation for equipment	130,279	27,213		157,492
	<hr/>	<hr/>	<hr/>	<hr/>
Business-type activities capital assets - Net	\$ 43,176	\$(27,213)	\$ 0	\$ 15,963
	<hr/>	<hr/>	<hr/>	<hr/>

Note 4 Deposits and Investments

The captions on the statement of net assets and statement of fiduciary net assets relating to cash and cash equivalents, certificates of deposit, and investments as of September 30, 2009 are as follows:

	Cash and Cash Equivalents	Investments	Total
Business-type activities/Proprietary Fund:			
Deposits	\$ 62,848	\$	\$ 62,848
Certificates of deposit		7,500,000	7,500,000
Money market mutual funds	1,196,652		1,196,652
	<hr/>	<hr/>	<hr/>
Total business-type activities	\$ 1,259,500	\$ 7,500,000	\$ 8,759,500
	<hr/>	<hr/>	<hr/>
Fiduciary activities/Fiduciary Fund:			
Deposits	\$ 25,000	\$	\$ 25,000
Money market mutual funds	17,095,342		17,095,342
U.S. government securities		1,570,780	1,570,780
	<hr/>	<hr/>	<hr/>
Total fiduciary activities	\$ 17,120,342	\$ 1,570,780	\$ 18,691,122
	<hr/>	<hr/>	<hr/>
Total	\$ 18,379,842	\$ 9,070,780	\$ 27,450,622
	<hr/>	<hr/>	<hr/>

Federal and State statutes authorize the Authority to invest in obligations of, or guaranteed by, the State of Michigan, the U.S. government or federal agency obligation repurchase agreements, mutual funds or common trust funds composed of investment vehicles that are allowable for direct investment, bankers' acceptances of U.S. banks, certificates of deposit, and savings and deposit accounts of banks or credit unions which are federally insured.

The Authority has designated two banks for the deposit of its funds. The Authority's deposits and investment policies are in accordance with statutory authority.

The Authority's cash and investments are subject to several types of risk, which are examined in more detail below:

Custodial Credit Risk of Bank Deposits

Custodial credit risk is the risk that in the event of a bank failure, the Authority's deposits may not be returned to it. The Authority does not have a deposit policy for custodial credit risk. At September 30, 2009, the carrying amount of the Authority's Operating Fund deposits was \$7,562,848 and the financial institutions' balances were \$7,525,000. Of the financial institutions' balances, \$250,000 was covered by federal depository or other insurance and \$7,275,000 was uninsured and uncollateralized.

At September 30, 2009, the bank balance of the Authority's Federal Fund deposits was \$25,000, all of which was covered by federal depository insurance.

None of the \$18.3 million in the money market mutual fund was covered by collateral held in the pledging banks' federal reserve accounts in the Authority's name. The Authority believes that, due to the dollar amounts of cash deposits and the limits of the Federal Deposit Insurance Corporation (FDIC) insurance, it is impractical to insure all deposits. As a result, the Authority evaluates each financial institution with which it deposits funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

Interest Rate Risk

Interest rate risk is the risk that the value of investments will decrease as a result of a rise in interest rates. The Authority's investment policy restricts investment maturities. At fiscal year-end, the average maturities of investments were as follows:

Type of Investment	Fair Value	Less than One Year	One to Five Years
U.S. Treasury Note	\$ 1,570,780	\$1,570,780	

Credit Risk

The Authority has an investment policy that limits its investment choices. The policy allows for investments in government securities, certificates of deposit, mutual funds, and high grade commercial paper. As of fiscal year-end, the credit quality ratings of debt securities were as follows:

Type of Investment	Fair Value	Rating	Rating Organization
Money market mutual funds	\$18,291,994	AAAm	Standard & Poor's
U.S. Treasury Note	\$ 1,570,780	AAA	Standard & Poor's

Note 5 U.S. Department of Education - Loans Reinsured

Delinquent loans acquired from financial institutions consist of loans where the student defaulted and the unpaid loan has been acquired from the financial institution by MGA and is recorded as a deduction, loan claims, in the fiduciary fund. The federal government reimburses MGA between 75% and 100% of defaulted loans based on when the loan was guaranteed and MGA's default ratio. These reimbursements are recorded as additions, U.S. Department of Education - loans reinsured, in the fiduciary fund. The reinsurance detail is included in Note 1. The federal government reimburses defaulted loan claims at 100% for bankruptcy, death, and disability. The federal government has defined the default ratio to be the default claims presented to the federal government during the federal fiscal year ended September 30, divided by loans in repayment at the beginning of the federal fiscal year, plus certain other adjustments.

Note 6 Employee Benefits

Plan Description - The Authority participates in the State's defined benefit and defined contribution pension plans that cover most State employees, as well as related component units such as the Michigan Higher Education Assistance Authority. The defined benefit and defined contribution pension plans are part of the State Employees' Retirement System administered by the Department of Management and Budget, Office of Retirement Services. Participants in each plan are eligible for retirement, healthcare, disability, and death benefits upon meeting certain vesting requirements. The State Employees' Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the defined benefit plan. That report is available on the State's website at <http://www.michigan.gov/ors>. The financial report for the defined contribution plan may be obtained by writing to the Department of Management and Budget, Office of Retirement Services, 7150 Harris Drive, P.O. Box 30171, Lansing, MI 48909 or by calling (517) 322-5103.

Funding Policy - The defined benefit plan members are not required to make contributions; the Authority was required to contribute an actuarially determined rate for the defined benefit plan of 30.64% of payroll for the fiscal year ended September 30, 2009 and 30.12% of payroll for pension and postemployment costs for the fiscal year ended September 30, 2008. During the fiscal years ended September 30, 2009 and September 30, 2008, the Authority's contributions to the plans, including postemployment benefits as described below, were \$1,327,274 and \$1,229,772, respectively.

The Authority was required to contribute to the defined contribution plan 4.0% of payroll with an additional match of up to 3.0% for the fiscal years ended September 30, 2009 and September 30, 2008. The contribution requirements of plan members and the Authority are established and may be amended by the State Legislature. The State Legislature establishes the extent to which the employer and employees are required to make contributions and establishes the benefit provisions for the plan.

Postemployment Benefits - In addition, the Authority participates in the State's postemployment benefits. The cost of retiree healthcare benefits is an allocation calculated by the State and funded on a pay-as-you-go basis. The

State will pay 90% of healthcare benefits for employees hired on or before March 30, 1997 who participate in either the defined benefit plan or the defined contribution plan and meet certain vesting and other requirements. For employees who were hired after March 1997, the State will pay up to 90% of healthcare benefits for employees who meet certain vesting and other requirements.

Note 7 Related Party Transactions

In accordance with the terms of its agreement with the Authority, the Michigan Department of Treasury performs certain collection activities for the Authority. Fees charged by the Department of Treasury for its services are based upon the amount of collections received on defaulted student loans. The Department of Treasury's collection fees totaled approximately \$35,000 for the fiscal year ended September 30, 2009.

The Authority received approximately \$119.0 million of federal funds from the Michigan Department of Human Services (DHS) under DHS's federal Temporary Assistance for Needy Families (TANF) program (see Note 1). The use of these federal funds requires certain federal regulations and compliance requirements to be met, as disclosed in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement, Catalog of Federal Domestic Assistance*, and the *Codification of Federal Regulations*. The Authority has deemed that it serves in a vendor relationship with DHS and that DHS is required to ensure compliance with the applicable federal laws and regulations for the use of the federal funds.

Note 8 Contingencies

The Authority is contingently liable for loans made by financial institutions that qualify for guaranty. The default ratio for loans guaranteed by the Authority is below 5% for the fiscal year ended September 30, 2009. As a result, the federal government's reinsurance rate for defaults for the fiscal year ended September 30, 2008 is 100% for loans made prior to October 1, 1993 and 98% for loans made from October 1, 1993 to September 30, 1998. In the event of future adverse default experience, the Authority could be liable for up to 25% of defaulted loans. At the beginning of each fiscal year, the Authority's reinsurance rate returns to 98%; management does not expect that all guaranteed loans could default in one year.

For loans made on or after October 1, 1998, the reinsurance rate is 95%. In the event of future adverse default experience, the Authority could be liable for up to 25% of such defaulted loans.

While management believes the Authority's expected maximum contingent liability is less than 25% of outstanding guaranteed loans, the maximum contingent liability at September 30, 2009 is computed as follows (in thousands):

Original amount of guaranteed student loans outstanding at financial institutions	\$4,408,441
Less minimum federal government share (75%)	<u>3,306,331</u>
Total	<u><u>\$1,102,110</u></u>

The Authority has entered into commitment agreements with all lenders that provide, among other things, that the Authority will maintain cash and marketable securities at an amount sufficient to guarantee loans in accordance with the Higher Education Act of 1965, as amended. The Authority was in compliance with this requirement as of September 30, 2009 (Note 1 - Reserves).

Note 9 Other Administrative Expenses

Other administrative expenses of the Operating Fund for the fiscal year ended September 30, 2009 consist of the following:

Professional fees	\$ 551,462
Attorney General	74,499
Information technology	294,583
Rent	211,488
Supplies and printing	103,865
Postage	108,103
Telephone	75,105
Other	<u>263,877</u>
Total	<u><u>\$1,682,983</u></u>

GLOSSARY

Glossary of Acronyms and Terms

AMF	account maintenance fee.
DAF	default aversion fee.
DHS	Michigan Department of Human Services.
FFELP	Federal Family Education Loan Program.
financial audit	An audit that is designed to provide reasonable assurance about whether the financial schedules and/or financial statements of an audited entity are presented fairly in all material respects in conformity with the disclosed basis of accounting.
GASB	Governmental Accounting Standards Board.
Gear Up	Gaining Early Awareness and Readiness for Undergraduate Program.
internal control	A process, effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance about the achievement of the entity's objectives with regard to the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.
LEAP	Leveraging Educational Assistance Partnership.
LPIF	loan processing and issuance fee.

material misstatement	A misstatement in the financial schedules and/or financial statements that causes the schedules and/or statements to not present fairly the financial position or the changes in financial position or cash flows in conformity with the disclosed basis of accounting.
MGA	Michigan Guaranty Agency.
OSG	Office of Scholarships and Grants.
PLUS	Parent Loan for Undergraduate Student.
unqualified opinion	An auditor's opinion in which the auditor states that the financial schedules and/or financial statements presenting the basic financial information of the audited agency are fairly presented in conformity with the disclosed basis of accounting.

