



**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Financial Statements

March 31, 2008 and 2007

(With Independent Auditors' Report Thereon)

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Financial Statements

March 31, 2008 and 2007

Table of Contents

	Page
Independent Auditors' Report	1
Management's Discussion and Analysis (Unaudited)	3
Financial Statements:	
Statements of Net Assets	14
Statements of Revenue, Expenses, and Changes in Net Assets	15
Statements of Cash Flows	16
Notes to Financial Statements	18



KPMG LLP
515 Broadway
Albany, NY 12207

Independent Auditors' Report

Board of Trustees
New York State Higher Education
Services Corporation:

We have audited the accompanying financial statements of the Operating Fund and Federal Fund of the Guaranteed Student Loan Programs of the New York State Higher Education Services Corporation (HESC), as of and for the years ended March 31, 2008 and 2007, which collectively comprise HESC's basic financial statements as listed in the table of contents. These financial statements are the responsibility of HESC'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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of HESC's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

As discussed in note 1, the financial statements present only the Operating Fund and Federal Fund of the Guaranteed Student Loan Programs of HESC and do not purport to, and do not, present fairly the financial position of the New York State Higher Education Services Corporation as of March 31, 2008 and 2007 and its changes in financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial positions of the Guaranteed Student Loan Programs' Operating Fund and Federal Fund of the New York State Higher Education Services Corporation as of March 31, 2008 and 2007, and the respective changes in financial positions, and cash flows thereof for the years then ended in conformity with U.S. generally accepted accounting principles.



In accordance with *Government Auditing Standards*, we have also issued a report dated, September 3, 2008 on our consideration of the Operating Fund's and Federal Fund's internal control over financial reporting and on our tests of their 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 accompanying management's discussion and analysis on pages 3 through 13 is not a required part of the basic financial statements but is supplementary information required by U.S. generally accepted accounting principles. 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.

KPMG LLP

September 3, 2008



Management's Discussion and Analysis

This section of the New York State Higher Education Services Corporation (HESC) Guaranteed Student Loan Programs' financial statements presents management's discussion and analysis of its operations and financial performance during the fiscal years ended March 31, 2008 and 2007. This analysis provides supplementary information on the operations and activities of HESC, and should be read in conjunction with the Operating and Federal Funds' financial statements, which follow this section.

Organization and Operations

HESC is an agency of New York State (NYS) created in 1974 under Chapter 942 of the Laws of 1974 and is responsible for the administration of New York State's student financial aid programs, including the Federal Family Education Loan Program (FFELP) and State loan guarantee program.

FFELP was established by Congress and is administered by the U.S. Department of Education (ED) through HESC and other guaranty agencies. As a guaranty agency, HESC makes loans available through lending institutions to students attending colleges, universities, post-secondary educational, and vocational schools. FFELP allows HESC to guarantee repayment of principal and accrued interest to lenders for eligible student loans.

HESC'S VALUES

- **Our Employees**
● We are committed to teamwork, excellence, initiative, personal growth and responsibility.
- **Our Customers**
● We never take our customers for granted. We ask, we listen and we respond.
- **Our Products and Services**
● We are committed to high quality, dependability, and continuous improvements to meet the changing needs of our customers.

HESC has the responsibility of processing loans submitted for guarantee, issuing loan guarantees, providing collection assistance to lenders for delinquent loans, paying lender claims for loans in default, and collection activities on loans after purchase by HESC. In addition to FFELP, the Guaranteed Student Loan Programs (GSL) include the residual activity of the State guaranteed loan program in which no new loans have been guaranteed since 1984.

HESC has a Federal Student Loan Reserve Fund (Federal Fund) and an Operating Fund to account for FFELP activity. The Federal Fund assets, and earnings on those assets, are restricted in use and are considered property of ED. The Operating Fund is considered property of HESC, and its assets and earnings may be used generally for guarantee agency and other student financial aid related activities.

New York State Higher Education Services Corporation
Management's Discussion and Analysis (unaudited)
March 31, 2008 and 2007

2008 Financial Highlights-Operating Fund

- Operating revenue increased \$2.8 million or 2%.
- Operating expenses increased \$2.6 million or 3%.
- The Operating Fund transferred \$8 million to the New York State Tuition Assistance Program (TAP) to subsidize grant expenditures.
- The Operating Fund provided \$ 13.0 million for the cost of administering the New York State grants and scholarship program.
- The Operating Fund deposited \$27.5 million into the Federal Fund for the mandatory federal default fee.

2007 Financial Highlights-Operating Fund

- Operating revenue increased \$21.7 million or 18.4%.
- Operating expenses increased \$12.3 million or 16.8%.
- The Operating Fund transferred \$5.4 million to the New York State Tuition Assistance Program (TAP) to subsidize grant expenditures.
- The Operating Fund provided \$14.4 million for the cost of administration of New York State grants and scholarship program.
- The Operating Fund provided \$6.3 million to support the New York State Aid for Part Time Study program.
- The Operating Fund transferred \$20.1 million to the Federal Fund for the mandatory federal default fee which was effective July 1, 2006.
- The Operating Fund transferred \$32.2 million to the Federal Fund in order to meet the minimum reserve requirement at September 30, 2007.

New York State Higher Education Services Corporation
Management's Discussion and Analysis (unaudited)
March 31, 2008 and 2007

Condensed Financial Information

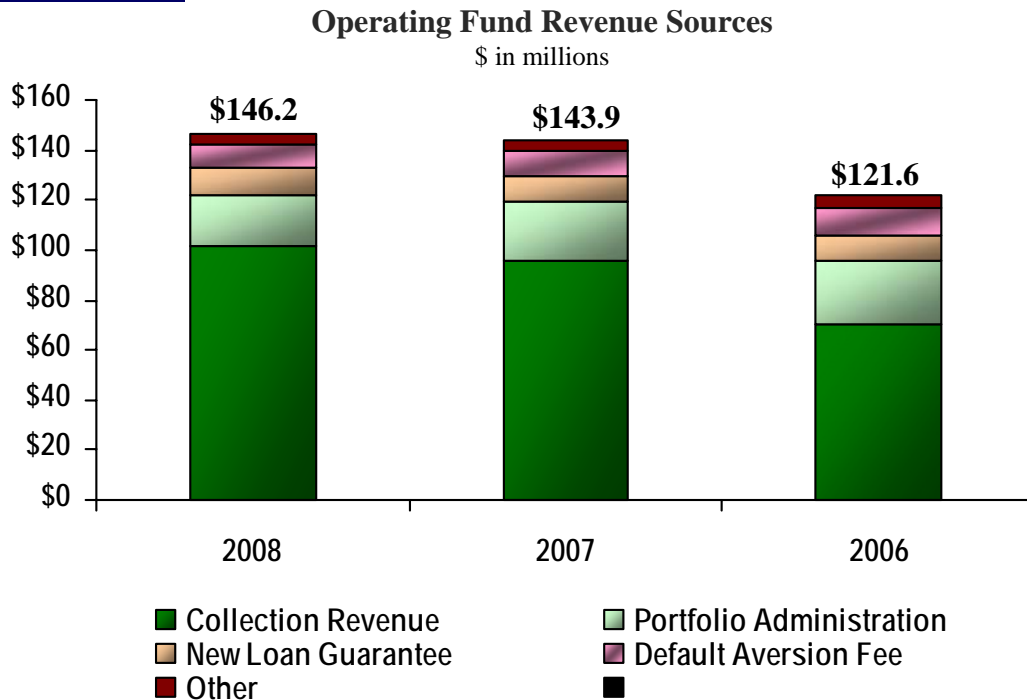
Amounts in thousands

	Operating Fund			Federal Fund		
	2008	2007	2006	2008	2007	2006
Current assets	\$ 51,698	44,828	68,109	84,373	82,609	64,074
Capital assets	81	128	228	—	—	—
Other noncurrent assets	—	—	—	3,941	6,029	7,077
Total assets	51,779	44,956	68,337	88,314	88,638	71,151
Current liabilities	26,055	29,884	31,238	—	6,013	19,890
Noncurrent liabilities	3,941	6,029	7,077	10,300	10,300	16,314
Total liabilities	29,996	35,913	38,315	10,300	16,313	36,204
Net assets:						
Invested in capital assets	81	128	228	—	—	—
Restricted	21,702	8,915	29,794	78,014	72,325	34,947
Total net assets	\$ 21,783	9,043	30,022	78,014	72,325	34,947

	Operating Fund			Federal Fund		
	2008	2007	2006	2008	2007	2006
Operating revenue:						
Default loan collections	\$ 101,876	96,084	70,110	242,674	201,479	125,366
Reimbursement on defaulted loans	—	—	—	472,537	421,198	371,442
Other	40,542	43,552	47,812	4	11	29
Non Operating revenues	3,778	4,255	3,699	2,871	2,591	1,681
Total revenues	146,196	143,891	121,621	718,086	625,279	498,518
Operating expenses:						
Administrative	88,103	85,496	73,162	—	—	—
Default loan purchases	—	1	13	491,519	437,429	383,399
Collection payments to ED	—	—	—	233,822	191,835	120,857
Fee subsidies	—	—	—	9,567	10,919	30,611
Other	98	101	152	—	—	8
Non Operating expenses	22,742	26,990	70,916	—	—	—
Total expenses	110,943	112,588	144,243	734,908	640,183	534,875
Transfers	(22,512)	(52,282)	(3,500)	22,512	52,282	3,500
Change in net assets	\$ 12,741	(20,979)	(26,122)	5,690	37,378	(32,857)

New York State Higher Education Services Corporation
 Management's Discussion and Analysis (unaudited)
 March 31, 2008 and 2007

HESC Total Operating Fund Revenue... Continued Growth for Seventh Consecutive Year



Operating Fund Revenue Highlights for the fiscal year ending March 31,

2008

- Collection revenue represents 70% of total revenue.
- Portfolio administration revenue decreased by \$3.0 million as a result of a decrease in the Account Maintenance Fee (AMF) rate from .10% to .06%, effective 10/01/07. The loss in revenue from the rate change was partially offset by an increase in the loan portfolio balance of 3.5% to \$24.48 billion.
- HESC guaranteed \$3.2 billion in new loans, an increase of \$.2 billion in loan volume.
- Default aversion revenue decreased \$.4 million to \$9.6 million as a result of a decrease in the number of default aversion assistance requests processed during 2007-2008 and an increase in refunds required during the same period.

2007

- Collection revenue represents 67% of total revenue.
- Portfolio administration revenue decreased by \$2.5 million as a result of a decline in the outstanding loan portfolio of 2.4% to \$23.65 billion.
- HESC guaranteed \$3.0 billion in new loans, an increase of \$.2 billion in loan volume, causing an increase in revenue of \$.7 million.
- Default aversion revenue decreased \$1.2 million to \$10.0 million as a result of a decrease in the number of default aversion assistance requests processed during 2006-2007.

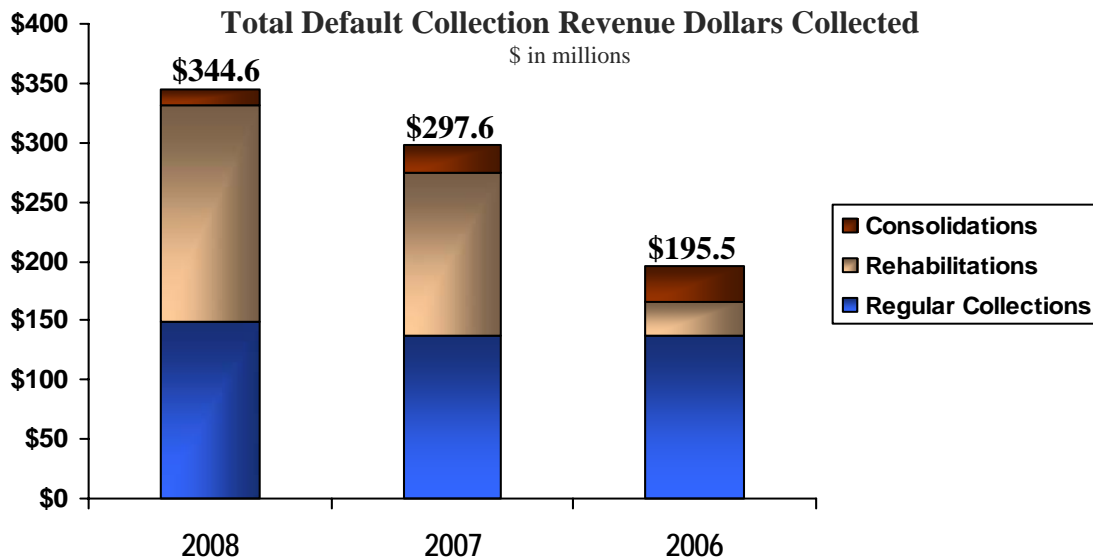
New York State Higher Education Services Corporation

Management's Discussion and Analysis (unaudited)

March 31, 2008 and 2007

Collection Revenue – Showing Shift in Collections Focus

As a FFEL guarantor, HESC retains a percentage determined by ED to collect defaulted student loans. Collection revenue shown below is the gross collection receipts by HESC in the respective years. HESC's primary source of revenue continues to be collection related revenue, accounting for more than half of total HESC operating fund revenue for the past three fiscal years.



Fiscal Year Ending March 31, 2008

- Collections on rehabilitated loans increased 33% to \$181.5 million in 2008. This increase is a result of the continued shift in collection focus to rehabilitations.
- Total regular collections increased 9% from \$137.3 million in 2007 to \$149.3 million in 2008. Administrative wage garnishment collections increased 39% due to the full implementation of the allowable garnishment percentage increase from 10% to 15% effective July 2006.
- Federal direct default consolidation revenue decreased \$9.8 million during the fiscal year from \$23.0 million in 2007 to \$13.2 million in 2008, due to the decrease in lenders consolidating loans for borrowers.

Fiscal Year Ending March 31, 2007

- Collections on rehabilitated loans increased 385% from \$28.1 million in 2006 to \$136.4 million in 2007. The increase is a result of the continued shift in collections focus to rehabilitations.
- Total regular collections remained constant from fiscal year 2006 to 2007. HESC is continually adding regular monthly paying borrowers and removing monthly borrowers through the loan rehabilitation process.
- Federal direct default consolidation revenue decreased during the fiscal year from \$29.5 million in 2006 to \$23.0 million in 2007. In addition, the agency retention on these consolidation loans declined from 18.5% to 10.0% effective October 1, 2006.

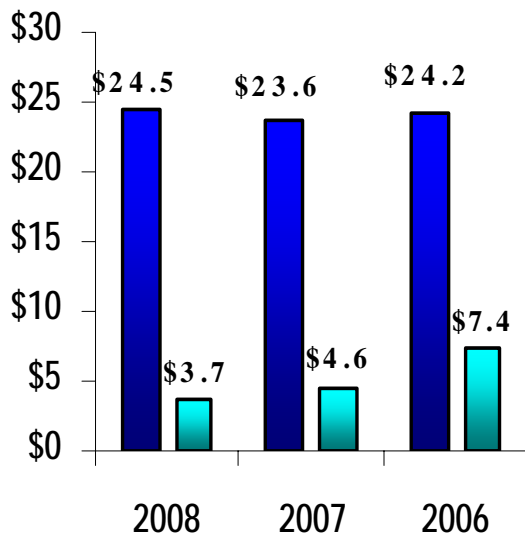
New York State Higher Education Services Corporation
 Management's Discussion and Analysis (unaudited)
 March 31, 2008 and 2007

Operating Fund Administration Revenue on FFEL Guaranteed Loans

As a FFEL guarantor, HESC receives fee revenue for issuing new loan guarantees and for administering the outstanding guarantee loan portfolio. Administrative fee income decreased \$3.0 million and \$3.1 million respectively for the fiscal years ended March 31, 2008 and March 2007.

Loan Guarantee Volume

Fiscal Year Ending March 31
 \$'s in billions



■ Outstanding Loan Guarantee Portfolio
 ■ Annual Dollars Guaranteed

Loan Guarantee Volume

HESC guaranteed \$3.7 billion in student loans during the fiscal year ending March 31, 2008, a decrease of \$0.9 billion or 20% from 2007. New loan guarantees increased \$243 million or 8.1% to \$3.2 billion, and consolidation loans decreased \$1.2 billion or 71.2% to \$468 million.

Guarantees for 2007 were \$4.6 billion, a decrease of 38% or \$2.8 billion from 2006. New loan guarantees were \$3.0 billion, up \$0.3 billion from 2006. Consolidation loan guarantees declined 66% during state fiscal year 2006-2007.

Loan Guarantee Revenue

HESC's outstanding portfolio balance increased by \$0.9 billion or 4% for the current fiscal year ending March 31, 2008. This increase was completely offset by the AMF rate reduction of .04%, effective 10/01/07 and resulted in a decrease in the Administrative revenue of \$3.0 million. A decrease in AMF revenue of \$0.6 million was experienced in 2007 due to decreased consolidation loans in the portfolio.

New loan guarantee revenue grew \$1.0 million for the fiscal year ending March 31, 2008, due to a slight increase in new guarantees. An increase in new loan guarantees of \$0.7 million was experienced during fiscal year ending March 31, 2007.

New York State Higher Education Services Corporation
 Management's Discussion and Analysis (unaudited)
 March 31, 2008 and 2007

Total HESC Operating Fund Expenses

March 31, 2008

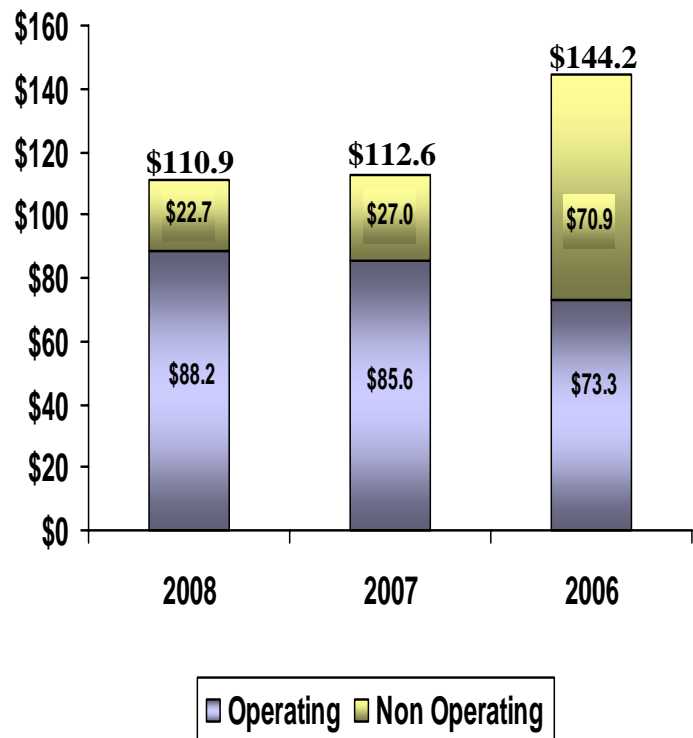
Operating Expenses

- Outsourced vendor collection service fees decreased \$1.4 million or 7% as a result of decreased vendor collections of 15%, as well as a negotiated rate reduction resulting from the guaranty agency's retention reduction from 23% to 16%, on regular collections.
- Payroll and fringe benefits increased \$2.8 million due to an increase in full time equivalent employees.
- Payments to Office for Technology decreased \$1.3 million from 2007 to 2008 as a result of rate and volume changes from 2007.
- HESC spent \$2.5 million on a web based, self service, multi-year debt planning financial aid tool as part of its student financial literacy initiative.

Non Operating Expenses

- The Operating Fund contributed \$8.0 million to subsidize the Tuition Assistance Program.
- The administrative costs of the grants and scholarship program totaling \$11.8 million was paid by the Operating Fund in 2008.
- The Operating Fund continued to provide funds for the GEAR UP program's operational expenses administered by the state in 2008.
- The Operating Fund disbursed \$.6 million in default prevention grants during 2007-2008.

Fiscal Year Ended March 31
\$ in millions



March 31, 2007

Operating Expenses

- Outsourced vendor collection service fees increased \$8.7 million or 66% as a result of increased vendor collections.
- Payroll and fringe benefits increased \$1.6 million due to an increase in full time equivalent employees.
- Payments to Office for Technology increased \$1.0 million from 2006 to 2007 as a result of rate and volume changes from 2006.
- Default Management Initiative Program operational expenses of \$1.0 million was paid in 2007, this expense was paid from restricted funds in the past.

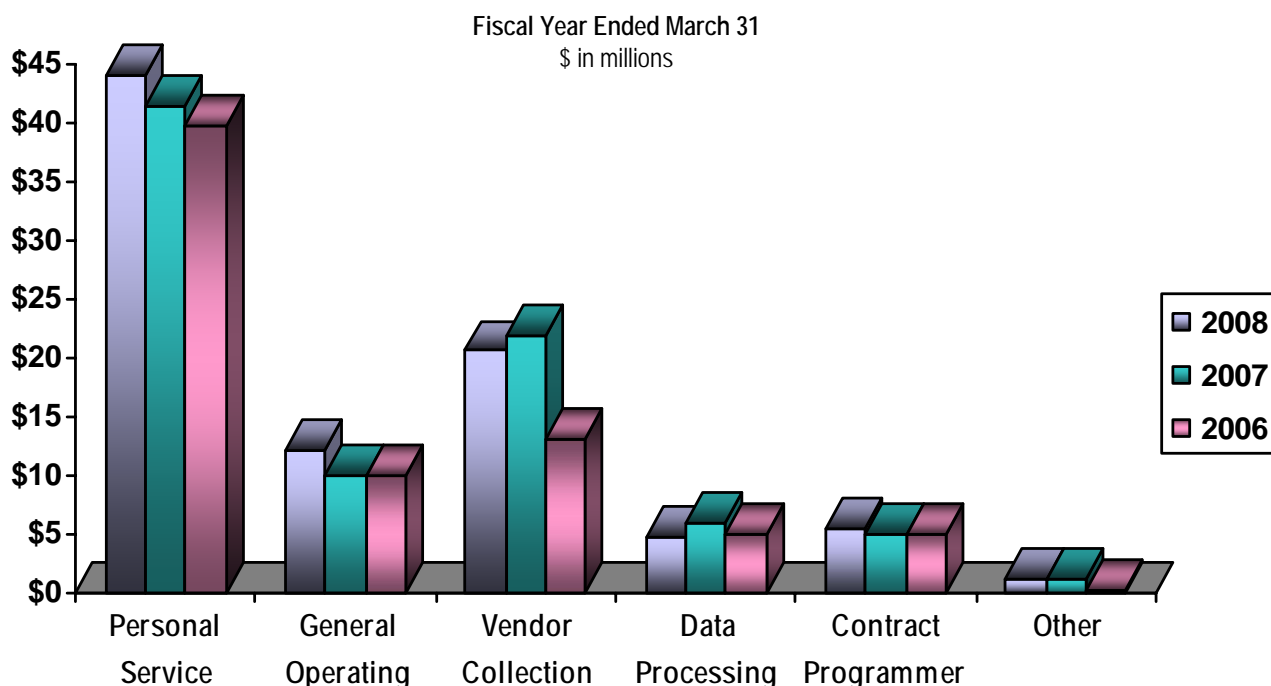
Non Operating Expenses

- The Operating Fund contributed \$5.4 million to subsidize the TAP program and \$6.3 million for the Aid for Part Time Study program (APTS).
- The administrative costs of the grants and scholarship program totaling \$14.3 million was paid by the Operating Fund in 2007.
- The Operating Fund provided funds for the GEAR UP program's operational expenses administered by the state for the first time in 2007.

New York State Higher Education Services Corporation
 Management's Discussion and Analysis (unaudited)
 March 31, 2008 and 2007

Operating Fund Administrative Expenses

Operating fund administrative expenses increased from \$85.5 to \$88.1 million for the fiscal year ended March 31, 2008.



Personal Service

Personal service costs include salaries and fringe benefits. Fringe benefits for 2008 represent \$14.4 million or 32.7% of personal services. The increase in personal service and fringe benefits is a result of an increase in full time equivalent employees from 579 in 2007 to 584 in 2008. Full time equivalent employees increased from 530 in 2006 to 579 in 2007.

General Operating

General operating expenses increased \$ 2.1 million during the fiscal year ending March 31, 2008. A decrease in rent expense was partially offset by an increase in postage and supplies expense. Also included is \$ 2.5 million for the web based, financial aid planning program, implemented during 2007-2008. General operating expenses remained constant during the fiscal year ended March 31, 2007. An increase in rent expense was offset by the removal of the Financial Aid Training Grant expense in 2007.

Vendor Collection

Vendor collection expense decreased in fiscal year 2007-2008 as a result of decreased vendor collections. During the year ending March 31, 2008, vendor collection expense decreased \$1.4 million dollars or 7%. For the period ended March 31, 2007, vendor collection expense increased \$8.7 million dollars or 66%.

Data Processing

Data processing costs decreased approximately \$1.3 million during fiscal year ended March 31, 2008, as a result of the reduced rate charged by the Office for Technology and transition of programs from mainframe to web processes. The change in expense from 2006 to 2007 was \$900,000.

Contract Programmers

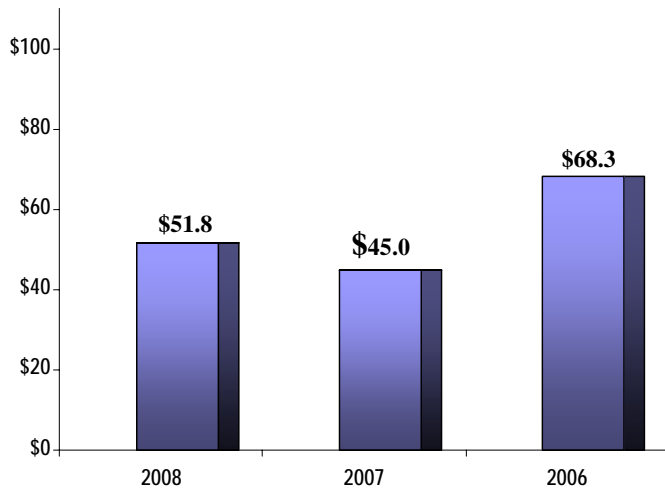
Contract programmer expenses increased \$.5 million during 2007- 2008 due to the implementation of program changes required by the College Cost Reduction and Access Act. The cost for 2007 had increased \$60,000 from 2006.

New York State Higher Education Services Corporation
 Management's Discussion and Analysis (unaudited)
 March 31, 2008 and 2007

Assets & Liabilities- Operating Fund

Assets

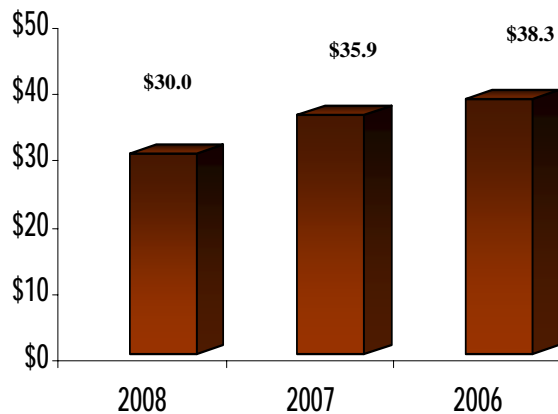
Fiscal Year Ending March 31
 \$ in millions



- Total operating assets are primarily current assets, consisting of cash and cash equivalents, receivables due from the U.S. Department of Education and the Federal Fund.
- Current assets increased \$6.9 million or 15% as a result of cash provided from operations of \$8.6 million in fiscal year 2007-2008.
- Administrative fees receivable increased \$6.6 million in 2007 as a result of the account maintenance fee payment for March 2007 paid in June.

Liabilities

Fiscal Year Ending March 31
 \$ in millions

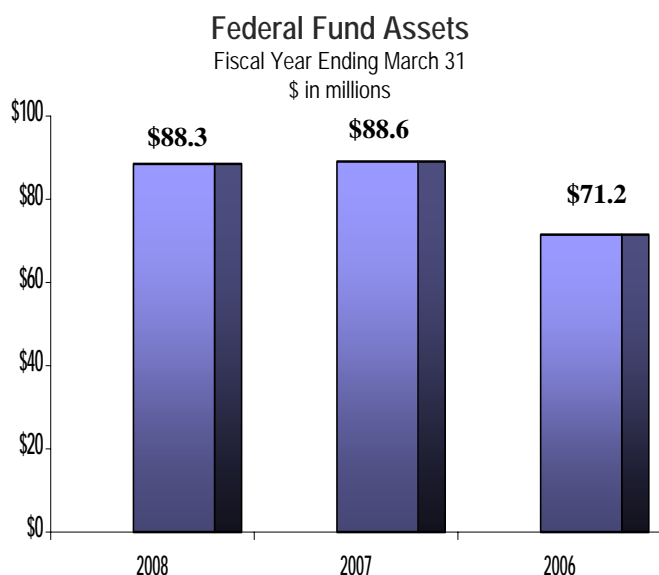


- Accrued liabilities represented 76% of total liabilities for the year ended March 31, 2008 and 67% of total liabilities in 2007.
- Accounts payable increased \$1.1 million in fiscal year 2008 primarily due to increases in personal service related expenses.
- Interfund balances for 2008 represent a \$1.4 million liability, a decrease of \$2.8 million from 2006-2007.
- Non current liabilities for the year ended March 31, 2008 and 2007 decreased \$2.0 million and \$1.0 million respectively, as a result of the decrease in the allowance for default aversion fee refund.

New York State Higher Education Services Corporation
 Management's Discussion and Analysis (unaudited)
 March 31, 2008 and 2007

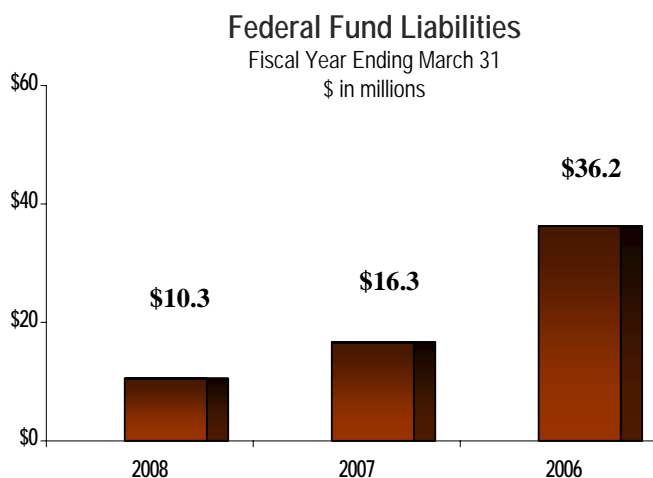
The Federal Student Loan Reserve Fund (Federal Fund)

The Federal Fund assets are owned by the U.S. Department of Education (ED) and have restricted use, primarily to reimburse lender claims for defaulted student loans.










- The Federal Fund's current assets stayed constant in fiscal year 2008. A transfer of funds from the Operating Fund on September 30, 2006 of \$32.2 million to meet the minimum reserve requirement caused the increase in 2007.
- The reinsurance receivable decreased in 2007 as a result of monthly reinsurance billings being filed twice a month.

- Federal Fund liabilities for the fiscal years ended 2007 and 2006 included \$6 million and \$12 million respectively, representing reserve recall amounts. The reserve recall amount was transferred to ED in two equal installments of \$6 million in September of 2006 and then in August 2007.
- Non current liabilities in 2008 include \$10.0 million for account maintenance fee earned in fiscal year 2006 which was transferred from the Federal Fund in May 2006.



New York State Higher Education Services Corporation
Management's Discussion and Analysis (unaudited)
March 31, 2008 and 2007

Significant Known Facts, Decisions, or Conditions

-  The Operating Fund will continue to support the operational expenses of the Grants and Scholarship program in the amount of approximately \$13.4 million for 2008-2009.
-  HESC's fringe benefit rate for 2008-2009 has decreased 2% to 46.5%.
-  HESC reached an agreement with the Federal Department of Education on an outstanding payment regarding HESC's rehabilitation revenue retention from 1996 – 2004. The agreement will allow HESC to recapture \$16.9 million in Agency Operating Fund revenue when revenue in the Federal Fund exceeds the required minimum reserve level. As of March 31, 2008, HESC transferred \$5.0 million of the \$16.9 million settlement.
-  The Operating Fund will continue to pay the federal default fee on behalf of the students for loans guaranteed prior to May 1, 2008. As a result of New York State facing more than a \$4 billion budget deficit, the funds earmarked for the payment of the federal default fee subsequent to May 2008 will be redirected to support the TAP at a cost of approximately \$27 million for state fiscal year 2008-2009.
-  In May 2008, HESC submitted to the Federal Department of Education updated rules and operating procedures for implementing a Lender of Last Resort Program (LLR) if necessary to ensure borrowers access to student loans. Under the Higher Education Act a guaranty agency can request an advance of federal funds from the Secretary if it is unable to otherwise fund LLR funds.
-  The College Cost Reduction and Access Act enacted October 1, 2007 significantly reduced revenue to guarantors for account maintenance fee and collection retention of defaulted loans. The Act also significantly reduced interest allowances paid to lenders and increased insurance fees paid by them.
-  In response to a request from the Governor for reduction in state spending, HESC developed an agency spending reduction/financial management plan to demonstrate how it would meet expected target savings. The plan was approved by the Division of Budget.

Contacting Financial Management

This financial report is designed to provide our customers, business partners and creditors with a general overview of the Guaranteed Student Loan Programs' finances. For further detail information regarding the FFEL Program, you may also review our annual report on the web at www.hesc.org.

Questions about this report can be directed to HESC's Chief Financial Officer, Warren E. Wallin at (518) 473-1200 or wwallin@hesc.com.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Statements of Net Assets

March 31, 2008 and 2007

Assets	2008		2007	
	Operating Fund	Federal Fund	Operating Fund	Federal Fund
Current assets:				
Cash and cash equivalents (note 4)	\$ 42,169,852	54,591,586	33,553,943	55,349,961
Receivables due from U.S. Department of Education:				
Administrative fees (note 5)	8,785,089	—	10,720,182	—
Reinsurance	—	28,367,095	—	22,985,354
EFT fees receivable from lenders	151,901	—	276,340	—
Interfund balances (note 7)	—	1,412,340	—	4,255,392
Due from other sources (note 8)	—	—	63,398	—
Prepaid expenses and other assets	589,642	—	207,625	—
Accrued interest	1,097	2,365	6,460	18,714
Total current assets	51,697,581	84,373,386	44,827,948	82,609,421
Noncurrent assets:				
Interfund Default Aversion Fee Allowance (note 5)	—	3,940,630	—	6,028,872
Capital assets, net (note 12)	81,229	—	127,642	—
Total noncurrent assets	81,229	3,940,630	127,642	6,028,872
Total assets	\$ 51,778,810	88,314,016	44,955,590	88,638,293
Liabilities and Net Assets				
Current liabilities:				
Accounts payable and accrued liabilities	\$ 21,009,317	—	19,991,934	—
Interfund balances (note 7)	1,412,340	—	4,255,392	—
Amounts payable to lenders through EFT (note 4)	3,633,561	—	5,636,944	—
Federal reserve return (note 13)	—	—	—	6,013,293
Total current liabilities	26,055,218	—	29,884,270	6,013,293
Noncurrent liabilities:				
Advance from U.S. Department of Education (note 13)	—	10,300,348	—	10,300,348
Interfund Default Aversion Fee Allowance (note 5)	3,940,630	—	6,028,872	—
Total noncurrent liabilities	3,940,630	10,300,348	6,028,872	10,300,348
Total liabilities	29,995,848	10,300,348	35,913,142	16,313,641
Net assets:				
Invested in capital assets	81,229	—	127,642	—
Restricted – property of U.S. Department of Education	—	78,013,668	—	72,324,652
Restricted – for student aid related activities	21,701,733	—	8,914,806	—
Total net assets	\$ 21,782,962	78,013,668	9,042,448	72,324,652

See accompanying notes to financial statements.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Statements of Revenue, Expenses, and Changes in Net Assets
Years ended March 31, 2008 and 2007

	2008		2007	
	Operating Fund	Federal Fund	Operating Fund	Federal Fund
Operating revenues:				
Defaulted loan collections (note 6)	\$ 101,875,848	242,674,192	96,084,420	201,479,362
Administrative and program fee income (note 5)	40,542,429	—	43,552,444	—
Reimbursement on purchases of default loans from lenders (note 14)	—	472,536,582	—	421,197,722
Other revenue	1,224,455	4,467	1,172,105	11,212
Total operating revenues	<u>143,642,732</u>	<u>715,215,241</u>	<u>140,808,969</u>	<u>622,688,296</u>
Operating expenses:				
Salaries and employee benefits	44,048,457	—	41,352,527	—
General and administrative	17,617,672	—	15,126,587	—
Collections	20,567,033	—	21,928,522	—
NYS Office for Technology equipment usage charges	4,765,574	—	6,048,626	—
D.M.I. program expenses	1,104,125	—	1,040,255	—
Default aversion fee subsidy	—	9,562,760	—	9,967,752
Account maintenance fee subsidy	—	—	—	951,422
Purchases of default loans from lenders (note 14)	—	491,518,997	—	437,429,395
Defaulted loan collections paid to U.S. Department of Education	—	233,822,374	—	191,834,670
Depreciation	98,191	—	100,529	—
Other expense	—	4,565	—	250
Purchases of defaulted State loans from lenders	—	—	1,490	—
Total operating expenses	<u>88,201,052</u>	<u>734,908,696</u>	<u>85,598,536</u>	<u>640,183,489</u>
Operating income (loss)	<u>55,441,680</u>	<u>(19,693,455)</u>	<u>55,210,433</u>	<u>(17,495,193)</u>
Nonoperating revenues (expenses):				
Interest income	2,553,125	2,870,922	3,082,376	2,590,814
Default prevention grant (note 10)	(611,096)	—	—	—
Gear Up operational expenses	(1,005,636)	—	(931,888)	—
New York State initiatives (note 9)	(21,126,010)	—	(26,058,167)	—
Total nonoperating (expenses) revenues	<u>(20,189,617)</u>	<u>2,870,922</u>	<u>(23,907,679)</u>	<u>2,590,814</u>
Transfer from/(to) Federal Fund (note 11)	5,000,000	(5,000,000)	(32,183,883)	32,183,883
Transfer of Federal Default Fee (note 15)	(27,511,549)	27,511,549	(20,098,261)	20,098,261
Increase (decrease) in net assets	12,740,514	5,689,016	(20,979,390)	37,377,765
Net assets, beginning	9,042,448	72,324,652	30,021,838	34,946,887
Net assets, ending	<u>\$ 21,782,962</u>	<u>78,013,668</u>	<u>9,042,448</u>	<u>72,324,652</u>

See accompanying notes to financial statements.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Statements of Cash Flows

Years ended March 31, 2008 and 2007

	2008		2007	
	Operating Fund	Federal Fund	Operating Fund	Federal Fund
Cash flows from operating activities:				
Receipts from:				
Collections	\$ 104,705,220	240,170,515	96,795,131	200,837,916
Administrative fees	39,091,130	—	47,842,239	—
Other sources	1,412,291	4,467	1,409,376	11,212
Reimbursement on purchases of default loan purchases	—	467,142,924	—	430,174,341
Payments for:				
Salaries and employee benefits	(46,800,788)	—	(40,786,330)	—
Administrative fees	—	(6,176,367)	—	(21,813,777)
Purchases of default loans from lenders	—	(491,518,997)	(1,490)	(437,429,395)
Collections paid to U.S. Department of Education	—	(233,810,457)	—	(191,719,360)
General, administrative and other expenses	(42,315,812)	(4,565)	(45,011,314)	(249)
Net cash provided by (used in) operating activities	<u>56,092,041</u>	<u>(24,192,480)</u>	<u>60,247,612</u>	<u>(19,939,312)</u>
Cash flows from noncapital financing activities:				
Payments to NYS – other student aid activities	(22,811,619)	—	(32,219,773)	—
Transfer to Federal Fund	(31,560,128)	31,560,128	(46,733,819)	46,733,819
Payment to DOE for Federal Recall	—	(6,013,293)	—	(6,013,293)
Payment from DOE for additional rehabilitated loans	5,000,000	(5,000,000)	—	—
Payments to schools for financial aid training grant	(611,096)	—	—	—
Net cash (used in) provided by noncapital financing activities	<u>(49,982,843)</u>	<u>20,546,835</u>	<u>(78,953,592)</u>	<u>40,720,526</u>
Cash flows from capital and related financing activities:				
Purchases of capital assets	(51,778)	—	—	—
Net cash used in capital and related financing activities	<u>(51,778)</u>	<u>—</u>	<u>—</u>	<u>—</u>
Cash flows from investing activities:				
Interest received	2,558,489	2,887,270	3,079,198	2,576,018
Net cash provided by investing activities	<u>2,558,489</u>	<u>2,887,270</u>	<u>3,079,198</u>	<u>2,576,018</u>
Increase (decrease) in cash and cash equivalents	8,615,909	(758,375)	(15,626,782)	23,357,232
Cash and cash equivalents, beginning	<u>33,553,943</u>	<u>55,349,961</u>	<u>49,180,725</u>	<u>31,992,729</u>
Cash and cash equivalents, ending	<u>\$ 42,169,852</u>	<u>54,591,586</u>	<u>33,553,943</u>	<u>55,349,961</u>

See accompanying notes to financial statements.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Statements of Cash Flows

Years ended March 31, 2008 and 2007

	2008		2007	
	<u>Operating Fund</u>	<u>Federal Fund</u>	<u>Operating Fund</u>	<u>Federal Fund</u>
Operating income (loss)	\$ 55,441,680	(19,693,455)	55,210,433	(17,495,193)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:				
Depreciation	98,191	—	100,529	—
Change in assets and liabilities:				
Receivables	1,935,093	(5,381,741)	(6,604,808)	9,091,930
Other assets	(257,578)	—	336,296	—
Interfund balances	1,268,924	(1,205,526)	12,584,229	(12,584,229)
Accounts payable and accrued liabilities	1,697,356	—	487,634	—
Other liabilities	(2,003,383)	—	(818,521)	—
Allowance for default aversion refunds	(2,088,242)	2,088,242	(1,048,180)	1,048,180
Total adjustments	<u>650,361</u>	<u>(4,499,025)</u>	<u>5,037,179</u>	<u>(2,444,119)</u>
Net cash provided by (used in) operating activities	<u>\$ 56,092,041</u>	<u>(24,192,480)</u>	<u>60,247,612</u>	<u>(19,939,312)</u>

See accompanying notes to financial statements.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Notes to Financial Statements

March 31, 2008 and 2007

(1) Organization and Operations

New York State Higher Education Services Corporation (HESC) is an agency of New York State (the State) created in 1974 under Chapter 942 of the Laws of 1974 and is responsible for the administration of the State's student financial aid programs, including the Federal Family Education Loan Program (FFELP) and State loan guarantee program.

FFELP was established by Congress and is administered by the U.S. Department of Education (ED) through HESC and other guarantee agencies. As a guarantee agency, HESC makes loans available through lending institutions to students attending colleges, universities, postsecondary educational, and vocational schools. FFELP allows HESC to guarantee repayment of principal and accrued interest to lenders for eligible student loans. HESC has the responsibility of processing loans submitted for guarantee, issuing loan guarantees, providing collection assistance to lenders for delinquent loans, paying lender claims for loans in default, and performing certain collection activities on loans after purchase by HESC. In addition to FFELP, the Guaranteed Student Loan Programs include the residual activity of the State guaranteed loan program in which no new loans have been guaranteed since 1984.

The accompanying financial statements only reflect the Operating Fund and Federal Fund of the Guaranteed Student Loan Programs of HESC. The Higher Education Amendments of 1998 (1998 Amendments) were enacted on October 6, 1998 and changed the manner in which FFELP is administered. Under the Amendments, HESC established a Federal Student Loan Reserve Fund (Federal Fund) and an Operating Fund as required to account for FFELP activity. The Federal Fund assets, and earnings on those assets, are restricted in use and are considered property of the U.S. Department of Education. The Operating Fund is considered property of HESC and its assets and earnings may be used generally for all guarantee agency and other student financial aid related activities.

HESC also administers the Tuition Assistance Program, State Scholarship Programs, Federal Gear Up Program and Robert L. Byrd Federal Scholarship Program under which students apply for payments to attend particular educational institutions based on family income and/or academic achievement. These programs are not included in the accompanying financial statements.

(2) Significant Accounting Policies

Basis of Accounting

The Guaranteed Student Loan Programs' Operating Fund and Federal Fund follow fund accounting under U.S. generally accepted accounting principles in which resources are classified for accounting and reporting purposes into funds established according to their purpose.

The Guaranteed Student Loan Programs' funds consist of the Federal Fund and the Operating Fund. The Federal Fund finances FFELP insurance activities, while the Operating Fund accounts for substantially all FFELP operational costs as well as financial aid awareness and related outreach activities. The two funds together constitute the Guaranteed Student Loan Programs and are accounted for as business type activities using the flow of economic resources measurement focus and the accrual basis of accounting. Revenues

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Notes to Financial Statements

March 31, 2008 and 2007

are recognized when earned and expenses are recognized when the liability is incurred regardless of the timing of the related cash flow.

In accordance with Government Accounting Standards Board (GASB) Statement Number 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting*, the Operating and Federal Fund have elected to apply all applicable GASB pronouncements as well as Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. These Funds have also elected not to apply accounting standards issued after November 30, 1989 by FASB and APB.

Cash and Cash Equivalents

Cash and cash equivalents consisting of United States Treasury Bills and collateralized short-term repurchase agreements are carried at fair value. Investment income represents interest on deposits and gains and losses.

Operating Revenues and Expenses

Operating revenues and expenses result generally from activities associated with FFELP, including collection on defaulted loans, default prevention, and default loan purchase activities. All revenues and expenses not derived from the administration of FFELP are reported as nonoperating revenues and expenses.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles 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. Management estimates include useful lives in depreciating capital assets, and anticipated future default aversion fee refunds. Actual results could differ from those estimates.

(3) Guaranteed Loans Outstanding and Respective Unpaid Balances

As of March 31, 2008 and 2007, the Federal Fund was the guarantor of loans outstanding with original principal amounts of approximately \$24,484,000,000 and \$23,646,000,000, respectively, made to students by participating lending institutions. Substantially all of that amount is guaranteed by the U.S. Department of Education, with an amount representing less than 1% guaranteed by the State. At March 31, 2008 and 2007, the unpaid balances were approximately \$22,306,000,000 and \$21,597,000,000, respectively.

HESC's management anticipates that a certain portion of the loans outstanding as of March 31, 2008 and 2007 will go into default status, requiring the Federal Fund to purchase loans from lenders. Because the majority of these loans are Federally guaranteed, the Federal Fund will be reimbursed by the U.S. Department of Education.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Notes to Financial Statements

March 31, 2008 and 2007

(4) Cash and Cash Equivalents

In accordance with HESC's investment policy, investments are made in low risk securities that are fully collateralized by the dealer. Cash equivalents are short-term investments with remaining maturities of three months or less when purchased and are generally short-term United States Treasury Bills and collateralized repurchase agreements. Cash equivalents are recorded at cost plus accrued interest, which approximates the fair value at March 31, 2008 and 2007. Federal Fund amounts and reserve recall amounts are restricted in use and are property of the U.S. Department of Education. HESC actively manages the investments of its cash balances to minimize its uninvested funds. Excess cash balances are generally invested in short-term repurchase agreements until such time that HESC anticipates the funds will be required for operational needs. Cash balances in an administrative account in the Operating Fund are invested in the New York State Comptroller's short-term investment pool. These cash balances are available to HESC upon demand.

Custodial credit risk for cash and cash equivalents is the risk that in the event of the failure of the counterparty to a transaction, HESC will not be able to recover the value of cash and cash equivalents that are in the possession of an outside party. In order to manage this risk, HESC requires collateral consisting of Federal government obligations or agency instruments guaranteed by the Federal government pursuant to its investments in repurchase agreements and delivery to its Trustee (agent) of all securities purchased and collateral for repurchase agreements, regardless of the seller institution. To manage custodial credit risk on deposits, HESC requires that its depository banks pledge collateral based on available bank balances. Additionally, HESC's investment policy limits the amount of funds which may be invested at any given dealer to \$75 million.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of a cash equivalent. HESC's policy for managing this risk is to hold cash equivalents to maturity, at which time the fair value of the investment is equal to its stated maturity value.

Included in Operating Fund bank balances are \$3,633,561 for 2008 and \$5,636,944 for 2007, which were deposited by lenders, to be forwarded to schools generally within three business days under an electronic funds transfer program (EFT). The offsetting liability is shown as amounts due to lenders, which are held by HESC for future disbursement.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Notes to Financial Statements

March 31, 2008 and 2007

Cash and cash equivalents at March 31 were as follows:

	2008	2007
Operating Fund:		
Repurchase agreements	\$ 31,587,250	23,026,564
Cash in State Comptroller's short-term investment pool	10,551,602	10,496,379
Petty cash and travel imprest accounts	31,000	31,000
Operating Fund cash and cash equivalents	\$ 42,169,852	33,553,943
Federal Fund:		
Repurchase agreements	\$ 65,501,594	65,989,275
Cash-net of outstanding bank checks	(10,910,008)	(10,639,314)
Federal Fund cash and cash equivalents	\$ 54,591,586	55,349,961

As of March 31, the cost and fair value of cash equivalents are as follows:

Operating Fund	2008		2007	
	Cost	Fair value	Cost	Fair value
Held by HESC's agent in HESC's name	\$ 31,587,250	31,587,250	23,026,564	23,026,564

Federal Fund	2008		2007	
	Cost	Fair value	Cost	Fair value
Held by HESC's agent in HESC's name	\$ 65,501,594	65,501,594	65,989,275	65,989,275

(5) Administrative Fees

The 1998 Amendments established three fees recorded in the Operating Fund for administering the loan program on behalf of the Federal Government based on performance as a guarantee agency.

A Default Aversion Fee is recognized for default aversion activities on delinquent loans at the time the lenders request aversion assistance between the 60th and 120th days of a borrower's delinquency. A fee of 1% of principal and interest on the loan may be charged to the Federal Fund at the time the guarantee agency receives a request from a lender for preclaim assistance. However, the fee must be refunded by the Operating Fund to the Federal Fund in the event the loan is later paid as a default claim. Accordingly, an estimate of default aversion fee refunds has been calculated and is presented as a liability in the Operating Fund and a receivable in the Federal Fund. The net default aversion fee is transferred from the Federal Fund to the Operating Fund on a monthly basis.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Notes to Financial Statements

March 31, 2008 and 2007

A Loan Processing and Issuance Fee is paid based on the original principal amount of new loans guaranteed and disbursed during the period at a rate of 0.40%. This fee is paid to the Operating Fund on a quarterly basis.

An Account Maintenance Fee is calculated on the original principal amount of loans outstanding at a rate of 0.10% effective through September 30, 2007. The College Cost Reduction and Access Act reduced the rate from 0.10% to 0.06% beginning October 1, 2007. This fee is paid directly by the U.S. Department of Education or as an authorized transfer from the Federal Fund on a quarterly basis.

For the years ended March 31, 2008 and 2007, the administrative fees receivable from U.S. Department of Education consisted of the following:

	2008	2007
Operating Fund:		
Loan processing and issuance fee receivable	\$ 5,065,205	4,547,153
Account maintenance fee receivable	3,719,884	6,173,029
	\$ 8,785,089	10,720,182

For years ended March 31, 2008 and 2007, administrative fee income is as follows:

	2008	2007
Operating Fund:		
Default aversion fee, net of estimated refunds	\$ 9,562,760	9,967,752
Loan processing and issuance fee	11,086,731	10,156,160
Account maintenance fee	19,892,938	23,428,532
	\$ 40,542,429	43,552,444

Gross default aversion fee income for the years ended March 31, 2008 and 2007 was \$12,853,735 and \$12,972,163, respectively. The estimated reserve for default aversion fee refunds is netted against default aversion fee income. In 2008 and 2007, the default aversion fee allowance estimate was 25.60% and 23.16% of default aversion fee income, respectively. The estimate of the amount to be refunded is based on current and historical data, which reflects actual experience over the past eight years.

(6) Collections on Defaulted Loans

HESC management is required by Federal statutes to pursue collections on loans upon default claim payment. Collections on defaulted loans and related complements are recorded at the time such collections are received. All collection receipts are initially deposited in the Operating Fund and daily estimated collection transfers are made to the Federal Fund. The Operating Fund retains 23% of borrower payments through September 30, 2007, the rate of HESC retention decreased to 16% for regular payments effective

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Notes to Financial Statements

March 31, 2008 and 2007

October 1, 2007. HESC's Operating Fund retains approximately 37% of rehabilitation collection payments. As a result of the Higher Education Reconciliation Act, the Operating Fund's retention on consolidated loans was reduced from 18.5% to 10% effective October 1, 2006.

(7) Interfund Balances

Interfund balances are monies due to and/or due from the Federal Fund to the Operating Fund and includes collection transfer balances, default aversion fees and federal default fees pending transfer. A daily transfer between funds is made based on an estimate of ED's equitable share of daily collections. A final settlement for the actual amount of collections due to the Federal Fund is made at month end.

In fiscal year 2008, the Operating Fund had a net interfund payable balance of \$1,412,340 which included a payable to the Federal Fund for underpayment of collections activity of \$492,979. In fiscal year 2007, the Operating Fund had a net interfund payable balance of \$4,255,392 which included a receivable from the Federal Fund for overpayment on collections activity of \$2,010,697. In both years, the appropriate interest earnings were transferred with the funds' settlement at the end of the month. In addition, there were interfund default aversion fee receivable balances in the Operating Fund of \$580,386 at March 31, 2008 and a payable balance of \$717,765 at fiscal year end March 2007. The default prevention fee payable from the Operating Fund to the Federal Fund totaled \$1,499,747 and \$5,548,325 at March 31, 2008 and 2007 respectively.

(8) Due from/(to) Other Sources

During fiscal year 2008, HESC determined that the receivable balance due from other sources would be charged as an expense to the Operating Fund. The receivable was established for HESC's share of expenses related to the College Choice program which HESC had previously offset against a balance owed to NYS for FFELP expenses paid for with Grants and Scholarship funds, that liability was relieved during fiscal year 2007. At March 2007, HESC had a receivable from the State in the amount of \$63,398.

(9) New York State Initiatives

The 2007-2008 New York State budget appropriated \$8 million of Operating Funds to subsidize the Tuition Assistance Plan (TAP) transferred in March 2008.

The 2006-2007 New York State budget appropriated \$11.7 million of Operating Funds to subsidize the TAP and the Aid for Part Time Study Program (APTS). The TAP funding totaled \$5.4 million transferred in March 2007, the APTS payments totaled \$6.3 million made during the first two quarters of the state fiscal year.

In addition, the Operating Fund was required to pay the operational expenses related to the administration of the State's grants and scholarship programs, which amounted to approximately \$13.0 million and \$14.4 million in 2007-2008 and 2006-2007, respectively.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Notes to Financial Statements

March 31, 2008 and 2007

(10) Default Prevention Grant

In fiscal year 2008, HESC awarded up to \$50,000 to colleges and universities, based on a competitive bid process. The grant was to be used by schools to identify risks that contribute to student loan default and to develop and implement new programs which have the best potential to significantly reduce the dollar amount of defaults. A total of \$661,096 was distributed to 29 schools throughout the State.

(11) Transfer from/(to) Federal Fund

Section 422A of the Higher Education Act states, "each agency shall maintain in the Federal Student Loan Reserve Fund a current minimum reserve level of 0.25% of the total attributable amount of all outstanding loans guaranteed by the agency" calculated at September 30 of each year. As of September 30, 2007, HESC's Federal Student Loan Reserve Fund exceeded the minimum reserve requirement at 0.2885%. As of September 30, 2006, HESC's Federal Student Loan Reserve Fund balance fell below this required minimum reserve level to 0.1269%. To remain in compliance with regulations, HESC transferred \$32.2 million from the Operating Fund to the Federal Fund, bringing the reserve level to 0.2500%.

On October 7, 2005, HESC submitted a letter for approximately \$16.9 million to the U.S. Department of Education (ED) seeking reimbursement for additional rehabilitated loan retention not previously requested, for the periods April 1996 through September 2004. The amount of reimbursement requested represents agency retention on rehabilitated loans. From April 1996 through September 2004, HESC retained only the collection costs charged borrowers on rehabilitated loans. The remaining funds, including agency retention, were transferred to ED. Subsequent to clarification by ED, HESC changed its procedures prospectively to report rehabilitated loans and calculated agency retention as instructed. On April 19, 2007, HESC received a letter from the Chief Business Operations Officer, Financial Student Aid at ED resolving the outstanding rehabilitation issue. ED authorized HESC to transfer amounts in the Federal Fund which exceed the minimum required reserve level until the full \$16.9 million is recuperated in the Operating Fund. This agreement is valid from September 30, 2007 to September 30, 2010. As the Federal Fund has had subsidies from the Operating Fund in the past two years in order to meet the required minimum reserve levels, the \$16.9 millions is contingent upon the Federal Fund having sufficient excess funds above the minimum reserve level. HESC transferred \$5.0 million from the Federal Funds to the Operating Fund as part of the rehabilitation recuperation. The remaining balance of \$11.9 million will be transferred as excess funds are available.

(12) Capital Assets

Capital assets are recorded at cost. Capital assets are defined as assets with initial, individual costs exceeding a capitalization threshold of \$25,000. Depreciation for Operating Fund assets is based on an estimated five year useful life, using an accelerated depreciation method. The majority of the Federal and Operating Funds' capital assets consists of computer equipment, while a small part of these assets are office equipment.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Notes to Financial Statements

March 31, 2008 and 2007

Capital asset activity in the Operating Fund for the year ended March 31, 2008 is as follows:

	Balance April 1, 2007	Additions	Disposals	Balance March 31, 2008
Office and computer equipment	\$ 1,318,852	51,778	—	1,370,630
Less accumulated depreciation	(1,191,210)	(98,191)	—	(1,289,401)
Net capital assets	<u>\$ 127,642</u>	<u>(46,413)</u>	<u>—</u>	<u>81,229</u>

Capital asset activity in the Operating Fund for the year ended March 31, 2007 is as follows:

	Balance April 1, 2006	Additions	Reductions	Balance March 31, 2007
Office and computer equipment	\$ 1,318,852	—	—	1,318,852
Less accumulated depreciation	(1,090,681)	(100,529)	—	(1,191,210)
Net capital assets	<u>\$ 228,171</u>	<u>(100,529)</u>	<u>—</u>	<u>127,642</u>

At March 31, 2008 and 2007, the Federal Fund had capitalized equipment with a book value of \$294,255, which was fully depreciated.

(13) Federal Reserve Recall and Federal Advances

The 1998 Amendments to the Higher Education Act contain a provision for a recall of federal reserve funds held by guarantee agencies totaling \$250 million nationwide. HESC's share of this recall is \$18,222,100. HESC transferred \$6,195,514 to the U.S. Treasury on September 3, 2002. The second payment of \$6,013,293 was paid to U.S. Treasury on September 6, 2006. The remaining payment of \$6,013,293 was paid on August 31, 2007.

HESC has received, in prior years, non-interest bearing advances from the U.S. Department of Education totaling \$10,300,348, for the purpose of helping to strengthen FFELP through the infusion of additional working capital. Under the terms of the agreement, HESC will be required to repay these advances at such time as the amount of federally guaranteed loans outstanding (note 3) is reduced to less than \$54,950,000. HESC has recorded these advances as noncurrent liabilities.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Notes to Financial Statements

March 31, 2008 and 2007

Long-term obligation activity for the year ended March 31, 2008, is as follows:

<u>Federal Fund</u>	<u>Beginning balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending balance</u>
Federal Reserve recall	\$ 6,013,293	—	(6,013,293)	—
Federal advances	10,300,348	—		10,300,348
Total Federal Fund	<u>\$ 16,313,641</u>	<u>—</u>	<u>(6,013,293)</u>	<u>10,300,348</u>

Long-term obligation activity for the year ended March 31, 2007, is as follows:

<u>Federal Fund</u>	<u>Beginning balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending balance</u>	<u>Due within one year</u>
Federal Reserve recall	\$ 12,026,586	—	(6,013,293)	6,013,293	6,013,293
Federal advances	10,300,348	—	—	10,300,348	—
Total Federal Fund	<u>\$ 22,326,934</u>	<u>—</u>	<u>(6,013,293)</u>	<u>16,313,641</u>	<u>6,013,293</u>

(14) Purchase of Defaulted Federal Loans

Purchases of defaulted loans and amounts repurchased by lenders are recorded as Federal Fund activity. The reinsurance reimbursement results in a net reduction to the Federal Fund, due to reduced reinsurance rates of 98% and 95% as a result of various amendments to the Higher Education Act.

The College Cost Reduction and Access Act repealed the Secretary's authority to recognize qualified lenders, guaranty agencies and servicers as exceptional performer effect October 1, 2007. Prior to October 2007, the Higher Education Act allowed the Secretary to designate qualified lenders, guaranty agencies and servicers as exceptional performer in servicing FFELP loans making them eligible for 99% reimbursement on all claims submitted for insurance. As of October 1, 2007, all FFELP claims are paid at 97% of the claim value. As of March 2007, HESC was processing claims for 14 servicers, with multiple lenders under the exceptional performer designation.

(15) Federal Default Fee

As a result of the Deficit Reduction Act of 2005, signed into law by the President in February 2006, a 1% default fee must be deposited into the Federal fund on all Stafford and PLUS loans guaranteed after July 1, 2006. The fees are Federal Fund revenue subject to the Federal Fund's restricted use. This fee replaces the guarantee fee (insurance premium) which was not a mandatory fee. HESC has elected to pay the 1% default fee from the Operating Fund instead of charging borrowers the fee on their Stafford or PLUS loans.

HESC's Operating Fund transferred to the Federal Fund approximately \$27.5 million and \$20.0 million in Federal default fees on behalf of the borrowers during the state fiscal years ended March 31, 2008 and 2007 respectively.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Notes to Financial Statements

March 31, 2008 and 2007

(16) Pension Benefits

Substantially all employees working for the Guaranteed Student Loan Programs are members of the New York State and Local Employees' Retirement System (System), a cost-sharing, multiple employer public employee retirement system. The State Comptroller is sole trustee and administrative head of the System. The System issues a publicly available financial report that includes financial statements and required supplementary information which may be obtained by writing to the New York State and Local Employees' Retirement System, 110 State Street, Albany, New York 12236.

The System provides retirement benefits as well as death and disability benefits. All benefits vest after five years of accredited service. Retirement benefits are established by the New York State Retirement and Social Security Law. Retirement benefits and contributory requirements depend upon the point in time at which an employee last joined the system. Most members of the System who joined before July 27, 1976 are enrolled in a noncontributory plan. The Operating Fund contributes the entire amount determined to be payable to the system for these employees. Personnel who joined the System after July 27, 1976 are required by law to contribute 3% of their gross salary. The Operating Fund contributes the balance payable to the System for these employees.

The Operating Fund paid to the System \$3,488,604 for 2008, \$3,392,998 for 2007 and \$3,855,715 for 2006, to cover 100% of the required employer contributions for retirement benefits. These payments, made through application of the New York State Fringe Benefit rate calculated by the State's Division of the Budget, represent 9.61%, 9.81% and 12.12% of covered payroll for each of the years, respectively.

(17) Postretirement Benefits

As a State agency, HESC participates in the New York State Health Insurance Program (NYSHIP), which is administered by the State as an agent multiple employer defined benefit plan. Under the plan the State provides certain healthcare benefits for eligible retired employees and their dependents under a single employer noncontributory healthcare plan. The State's plan states that employees and/or their dependents become eligible for these benefits at 55 years of age when the employee has 10 years of State service. In calculating the 10 year service requirement, all of the employee's service need not be with the State, but may be a composite of State service elsewhere, with a minimum of 3 years with the State. Employees with no prior State service must work a minimum of 10 years before they and their dependents are eligible for the retirement medical benefits. Eligible retirees hired on or after November 1, 2001, contribute 10% of the cost of single coverage and 25% of the cost of dependent coverage for health insurance benefits. The State covers 100% of the cost of single and dependent coverage for employees hired before November 1, 2001. NYSHIP does not issue a stand-alone financial report and NYSHIP's agent activities are included within the financial statements of the State.

During the fiscal year ended March 31, 2008, NYSHIP provided health insurance coverage through the Empire Plan, an indemnity health insurance plan with managed care components; 12 Health Maintenance Organizations (HMOs); and through the Student Employee Health Plan (SEHP). Generally, these include hospital, medical, mental health and substance abuse benefits, and prescription drug benefits.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Notes to Financial Statements

March 31, 2008 and 2007

HESC's policy regarding retiree healthcare benefits is to pay the amounts billed through the State's fringe benefit rate on a pay-as-you-go basis. HESC has no obligation beyond the payment of the State's fringe benefit rate for retiree healthcare benefits. The State's policy is that the State is responsible for recording the annual required contribution and the actuarial accrued liability under GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* for HESC's retiree health care benefits in the State's governmental-wide financial statements.

As of March 31, 2008 and 2007, HESC has approximately 430 retired and/or spouses of retired employees, receiving retiree health care benefits with an annual pay-as-you-go cost of approximately \$2.5 million.

(18) Employees' Vacation Pay Benefits

Under the terms of HESC management's personnel policies and its union agreements, vacation pay benefits may be paid upon termination up to a combined maximum of 30 days. The Operating Fund recognizes employees' vacation pay benefits when earned. The liability for employees' vacation pay benefits is \$2,733,626 and \$2,646,298 as of March 31, 2008 and 2007, respectively, and is recorded in accounts payable and accrued expenses in the Operating Fund.

(19) Deferred Compensation

The State offers its employees, including HESC employees, a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all employees, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency. All amounts of compensation deferred under the plan are placed in trust for participants and their beneficiaries.

(20) Leases

HESC leases office space and storage space under noncancelable operating leases and month to month agreements. Total rental expense recorded in the Operating Fund, which includes utilities for one of two major leases, for the years ended March 31, 2008 and 2007, were \$1,358,008 and \$1,340,855, respectively. The major lease for office space expired on March 31, 2007, and a new lease at the same location has been executed that will be effective through 2017.

(21) Contingencies

The Operating Fund and the Federal Fund are subject to ED oversight and audit that at times may result in program issues and potential liabilities payable to ED. The issues relate to possible violations of rules and regulations established by ED to administer the federal loan program. Management diligently attempts to interpret ED's rules and regulations, and believes that its implementation of policies and procedures properly adheres to those rules and regulations, and that any resulting liabilities would not be material.

**THE GUARANTEED STUDENT LOAN PROGRAMS'
OPERATING FUND AND FEDERAL FUND OF
THE NEW YORK STATE HIGHER EDUCATION
SERVICES CORPORATION**

Notes to Financial Statements

March 31, 2008 and 2007

During the normal course of business the Guaranteed Student Loan Programs are involved in various legal proceedings and investigations, pertaining to matters relating to the Programs' operations and activities. While these proceedings and investigations may lead to a possible liability, in the opinion of HESC management, after considering all relevant facts, these possible liabilities will not in the aggregate have a material adverse effect on the financial position of the Operating Fund or Federal Fund as of March 31, 2008 and 2007, respectively.

HESC is exposed to various risks of loss related to damage and destruction of assets, injuries to employees, or noncompliance with Federal requirements and other natural and other unforeseen disasters. HESC in general does not insure its buildings, contents or related risks and does not insure its assets for claims and assessments arising from bodily injury, property damages, and other perils. Unfavorable judgments, claims, or losses incurred by HESC are covered by the State on a self-insured basis. The State does have fidelity insurance on State employees.