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

Financial Statements

March 31, 2011 and 2010

(With Independent Auditors' Report Thereon)

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Financial Statements

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Table of Contents

KPMG LLP
515 Broadway
Albany, NY 12207-2974

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, 2011 and 2010, 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, 2011 and 2010 and its changes in net assets 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, 2011 and 2010, and the respective changes in net assets, 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, November 29, 2011 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 12 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

November 29, 2011

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.

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, 2011 and 2010. 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 result of the March 30, 2010 enactment of the Health Care and Education Reconciliation Act (HCERA) (HR4872), new loan guarantees under the FFELP were eliminated effective July 1, 2010.

Under the FFELP, HESC was responsible for processing loans submitted for guarantee and issuing loan guarantees. HESC will continue 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 guaranty agency and other student financial aid related activities.

2011 Financial Highlights-Operating Fund

- Current assets decreased $2.6 million or 4%.
- Current liabilities decreased $1.6 million or 9%.
- Total revenue increased $3.1million or 3%.
- Operating expenses decreased $4.7 million or 7%.
- The Operating Fund provided $11.6 million for the cost of administering the New York State grant and scholarships.
- The Operating Fund provided $4.3 million toward the costs of operations for the New York Higher Education Loan Program (NYHELPs).
- The Operating Fund transferred $22.2 million to the New York State Tuition Assistance Program to subsidize grant expenditures.

2010 Financial Highlights-Operating Fund

- Current assets decreased $4 million or 6%.
- Current liabilities decreased $1.6 million or 8%.
- Total revenue decreased $15.1 million or 14%.
- Operating expenses decreased $12.4 million or 16%.
- The Operating Fund provided $11.8 million for the cost of administering the New York State grant and scholarship programs.
- The Operating Fund provided $4.6 million toward the start up costs for NYHELPs.
- The Operating Fund transferred $22.2 million to the New York State Tuition Assistance Program to subsidize grant expenditures.

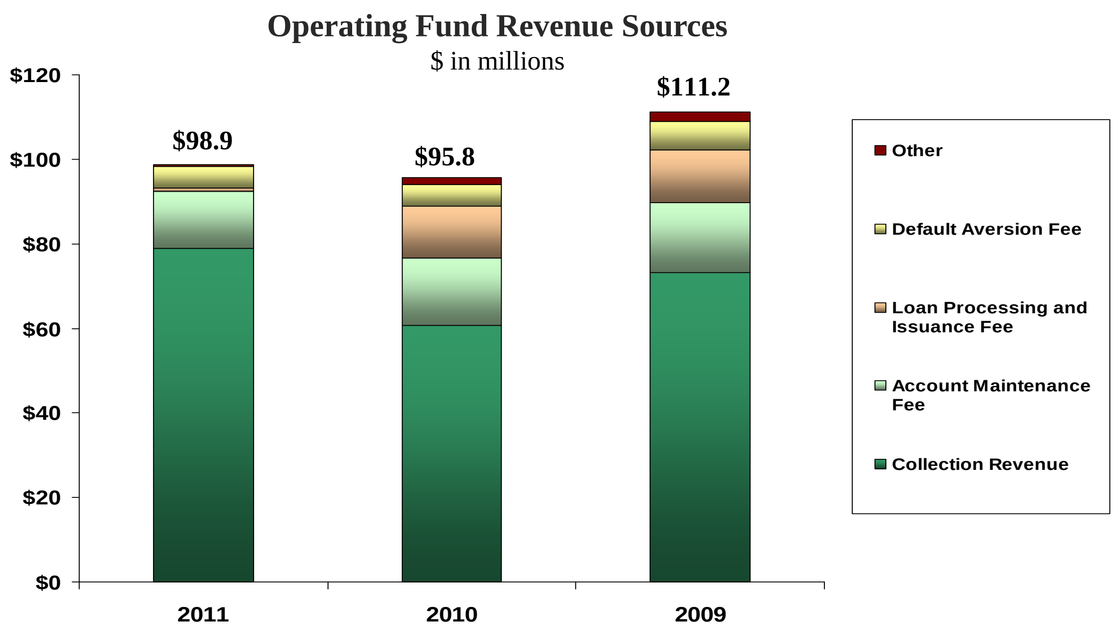
Condensed Financial Information

Amounts in thousands

		Operating Fund			Federal Fund		
		2011	2010	2009	2011	2010	2009
Current assets	$	66,066	68,683	72,721	80,443	94,983	90,335
Capital assets		382	203	38	—	—	—
Other noncurrent assets		—	—	—	4,755	5,263	4,183
Total assets		66,448	68,886	72,759	85,198	100,246	94,518
Current liabilities		17,131	18,770	20,380	2,874	—	423
Noncurrent liabilities		4,755	5,263	4,183	10,300	10,300	10,300
Total liabilities		21,886	24,033	24,563	13,174	10,300	10,723
Net assets:							
Invested in capital assets		382	203	38	—	—	—
Restricted		44,180	44,650	48,158	72,024	89,946	83,795
Total net assets	$	44,562	44,853	48,196	72,024	89,946	83,795

		Operating Fund			Federal Fund		
		2011	2010	2009	2011	2010	2009
Operating revenue:							
Default loan collections	$	78,894	60,662	73,272	236,916	204,007	207,136
Reimbursement on defaulted loans		—	—	—	612,241	561,625	514,279
Other		19,651	33,285	35,780	1,580	29,952	29,908
Non Operating revenues		315	1,821	2,185	94	61	746
Total revenues		98,860	95,768	111,237	850,831	795,645	752,069
Operating expenses:							
Administrative		59,974	64,677	77,116	—	—	—
Default loan purchases		—	—	—	637,200	584,411	534,694
Collection payments to ED		—	—	—	226,430	195,313	199,040
Fee subsidies		—	—	—	5,208	4,984	6,842
Other		89	43	43	20	6	—
Non Operating expenses		38,983	39,171	13,370	—	—	6
Total expenses		99,046	103,891	90,529	868,858	784,714	740,582
Transfers		(105)	4,780	5,705	105	(4,780)	(5,705)
Change in net assets	$	(291)	(3,343)	26,413	(17,922)	6,151	5,782

HESC Total Operating Fund Revenue



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

2011

- Collection revenue represents 80% of total revenue, an increase from last year as a result of increased rehabilitation sales and decreased administrative revenue.
- Portfolio administration fee revenue decreased by $2.4 million as a result of a decrease in outstanding principal balance of loans outstanding due to the Federal Loan Purchase Commitment (PUT) program.
- HESC guaranteed $86 million in new loans, a decrease of $3.43 billion in loan volume which resulted in a $11.5 million decrease in loan processing revenue.
- Default aversion fee (DAF) revenue increased $.2 million to $5.2 million.

2010

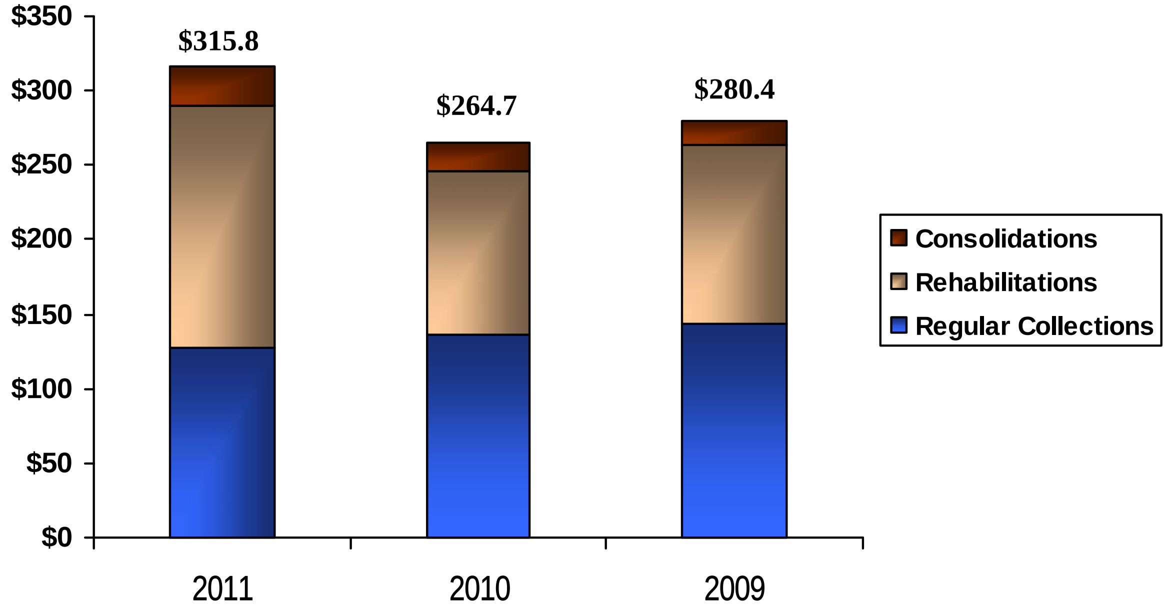
- Collection revenue represents 63% of total revenue, a decrease from last year as a result of lender rehabilitation loan discounts.
- Portfolio administration revenue decreased by $0.4 million as a result of a decrease in principal amount of loans outstanding due to the PUT program.
- HESC guaranteed $3.4 billion in new loans, a decrease of $.3 billion in loan volume which resulted in a slight decrease in loan processing revenue.
- DAF revenue decreased $1.9 million to $5.0 million primarily as a result of a decrease in DAF revenue and an increase in DAF refunds.

Collection Revenue

As a FFEL guarantor, HESC retains a percentage determined by ED for collections on 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 five fiscal years.

Total Default Collection Recovery Dollars Collected

$ in millions



Collection Recovery Highlights for the fiscal year ending March 31,

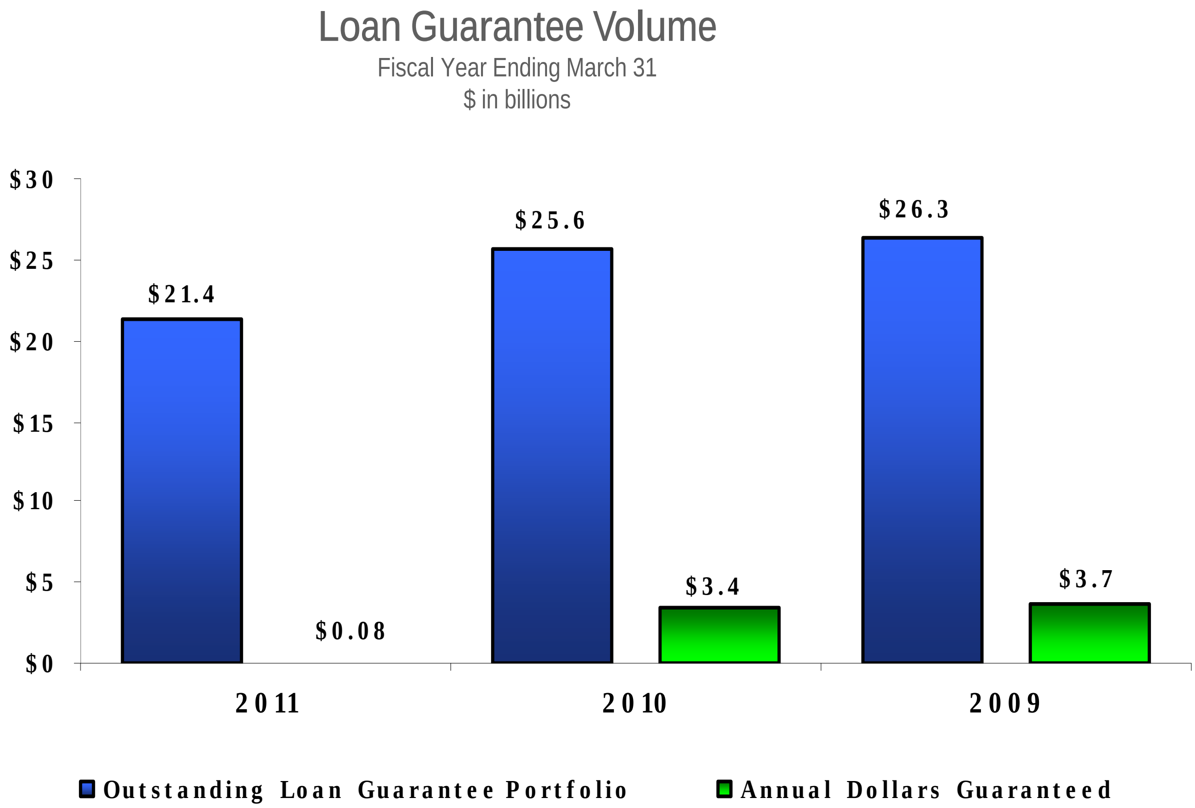
2011

- Collections on rehabilitated loans increased 49% to $163 million as a result of HESC collection efforts.
- Total regular collections decreased 6% from $135.8 million in 2010 to $127.6 million in 2011, due to current economic conditions.
- Federal direct default consolidation revenue increased $5.9 million during the fiscal year from $19.3 million in 2010 to $25.2 million in 2011, as part of HESC's collection strategy.

2010

- Collections on rehabilitated loans decreased 9% to $109.5 million due to a discount paid to HESC's rehabilitation lender.
- Total regular collections decreased 5% from $143.3 million in 2009 to $135.8 million in 2010, due to current economic conditions.
- Federal direct default consolidation revenue increased $3 million during the fiscal year from $16.3 million in 2009 to $19.3 million in 2010, as part of HESC's collection strategy.

Operating Fund Administration Revenue on FFEL Guaranteed Loans



Loan Guarantee Volume

- HESC guaranteed $85 million in student loans during the fiscal year ending March 31, 2011. New loan guarantees decreased $3.3 billion or 98%, and consolidation loans decreased $1.4 million or 62% during fiscal year 2010-2011. The elimination of the FFELP effective July 1, 2010 caused these significant decreases.
- Loan guarantees for fiscal year ending 2010 were $3.4 billion. New loan guarantees decreased $266 million from $3.7 billion in 2009. Consolidation loan guarantees declined $21.5 million or 90.2% during fiscal year 2009-2010.

Loan Guarantee Revenue

- HESC's outstanding portfolio balance decreased by $4.2 billion or 16% for the current fiscal year ending March 31, 2011. The AMF revenue, based on outstanding portfolio balance, decreased approximately $2.5 million as a result of the PUT program. HESC's outstanding portfolio decreased by $700 million in 2009-2010.
- New loan guarantee revenue decreased $11.5 million from fiscal year 2009-2010 to 2010-2011. New loan guarantee revenue fell $.25 million for the fiscal year ending March 31, 2010.

Total HESC Operating Fund Expenses

2011

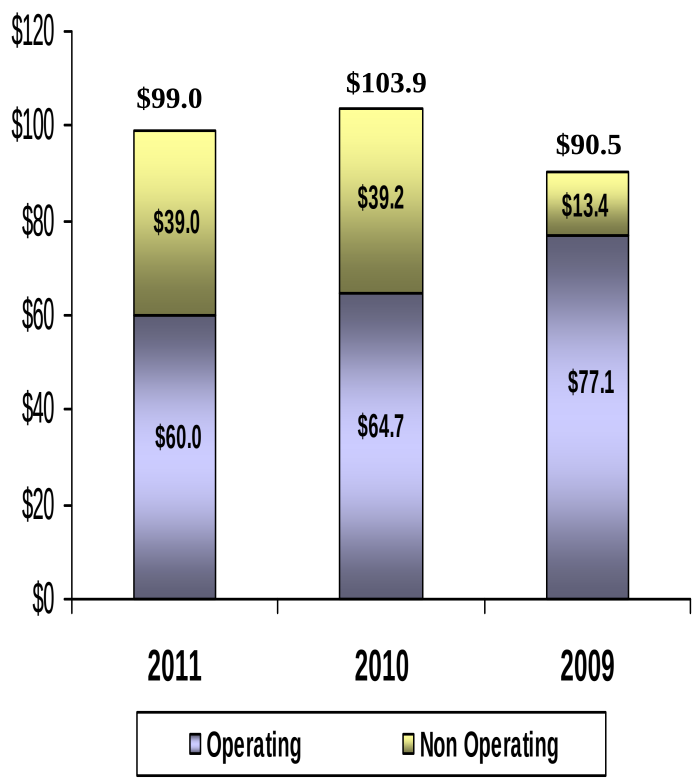
Operating Expenses

- Outsourced vendor collection fees increased $3.3 million or 29% as a result of increased collections attributable to outside collection agencies.
- Contract programmer expenses decreased approximately $1.1 million or 52% as a result of cost cutting measures implemented by management.
- Payroll and fringe benefits decreased $3.9 million or 11% due to a reduction in full time equivalent employees.
- Allowance for default aversion fee refunds decreased $1.2 million as a result of reduced projected revenue.

Non Operating Expenses

- The Operating Fund contributed $22.2 million to subsidize the Tuition Assistance Program.
- Grant and scholarship program expenses decreased $.17 million.
- HESC incurred $4.3 million in expenses related to the NYHELPs program.

State Fiscal Year Ended March 31
$ in millions



2010

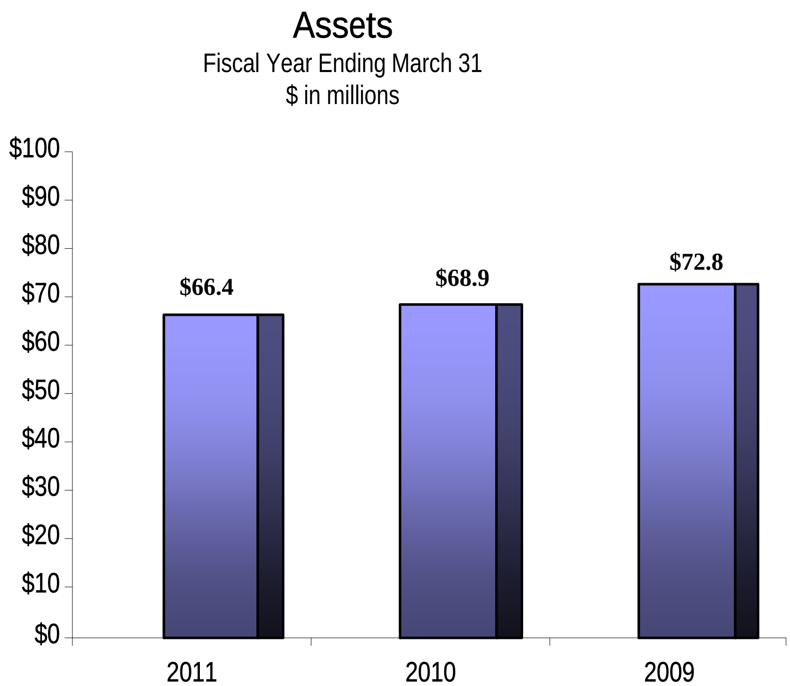
Operating Expenses

- Outsourced vendor collection fees decreased $3 million or 20% as a result of a renegotiated rate paid to vendors on rehabilitation recoveries.
- Payments to Office for Technology decreased $1.4 million or 36.5% due to the transfer of the printing of FFELP default bills to an external system and streamlining in house processing.
- Contract programmer expenses decreased approximately $2 million or 48% as a result of cost cutting measures implemented by management.
- Payroll and fringe benefits decreased $6.7 million or 15% due to a reduction in full time equivalent employees.

Non Operating Expenses

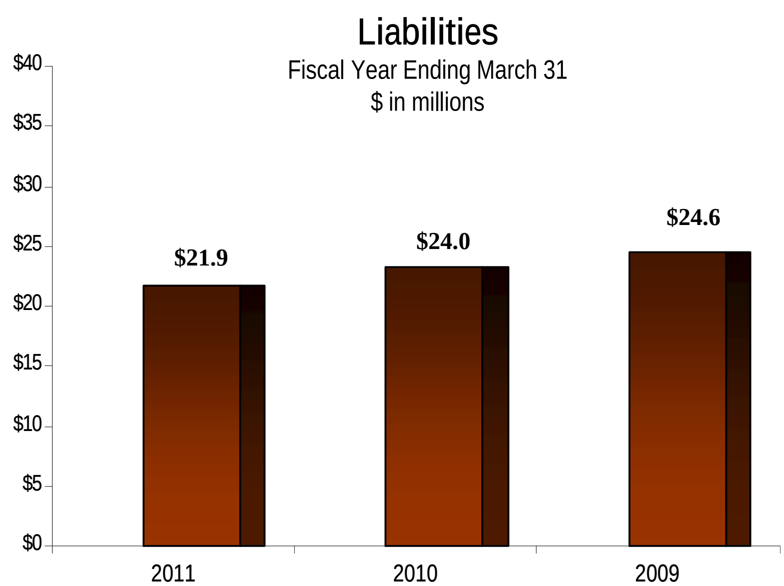
- The Operating Fund was not required to subsidize $22.2 million to the Tuition Assistance Program.
- Grant and scholarship program related expenses decreased $.5 million.
- HESC incurred $4.6 million in expenses as a result of the NYHELPs program.

Operating Fund Assets & Liabilities



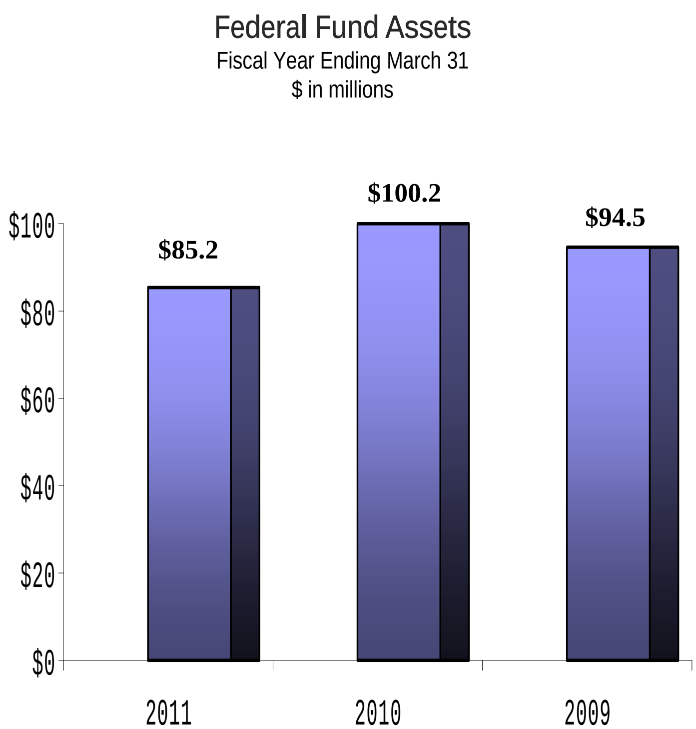
- Total operating assets are primarily current assets, consisting of cash and cash equivalents, receivables due from the U.S. Department of Education and the Federal Fund.
- Total assets decreased $2.4 million or 4%, primarily due to the $5.7 million reduction in administrative fee receivables, offset by an increase in interfund receivables of $3.3 million. Administrative fee receivables declined due to the elimination of new loan originations under FFELP effective June 30, 2010. Interfund balances fluctuate due to the timing of transfers between the Federal Fund and Operating Fund.

- Accounts payable and accrued liabilities represented 77% of total liabilities for the fiscal year ending March 31, 2011 and 70% of total liabilities for the fiscal year ending March 31, 2010.
- Accounts payable and interfund payables decreased $.3 million in fiscal year 2011.
- Amounts payable through the EFT system declined $1.3 million.
- Non current liabilities decreased $.5 million, as a result of the decrease in the allowance for default aversion fee refund.



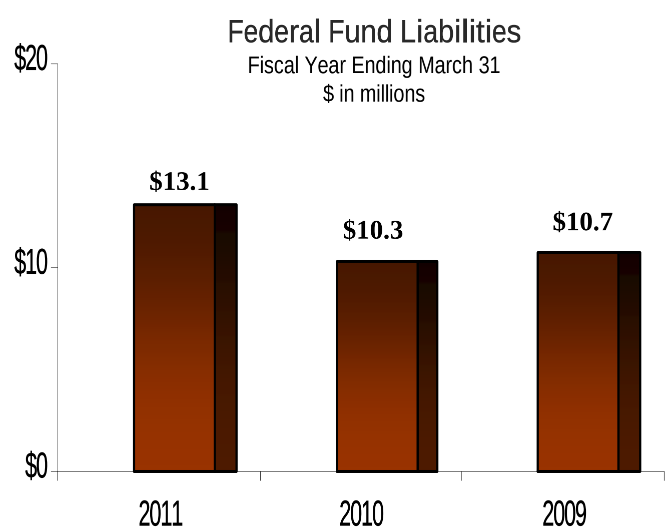
The Federal Student Loan Reserve Fund (Federal Fund)

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 cash and cash equivalents decreased $26.9 million or 37% in fiscal year 2010-2011 as a result of cash used in operations of $27.1 million.
- The reinsurance receivable increased $14.8 million as a result of increased default purchases in fiscal year 2011.
- The interfund receivable in 2010 of $477 thousand became an interfund payable in fiscal year 2011 in the amount of $2.8 million.
- The interfund DAF allowance decreased $.5 million in fiscal year 2011 based on current refund statistics.

- Fiscal year 2010-2011 current liabilities include $2.8 million in interfund payables to the Operating Fund which will settle during the fiscal year 2011-2012.
- Non current liabilities include $10.3 million for non-interest bearing advances from the US Department of Education, for the purpose of helping to strengthen FFELP through the infusion of additional working capital.



Significant Known Facts, Decisions, or Conditions

- As a result of the March 30, 2010 enactment of the Health Care and Education Reconciliation Act (HCERA) (HR4872), the Federal Family Education Loan Program (FFELP) was eliminated effective July 1, 2010. No new (first disbursed) Stafford, PLUS or consolidated loans were disbursed through the FFELP after June 30, 2010. Existing FFELP loans will continue to be eligible for program benefits. As of July 1, 2010, all new Stafford, PLUS and consolidation loans were made under the U.S. Department of Education's Direct Loan Program.

- HESC will remain responsible for the administration of its existing FFELP portfolio of both active and defaulted loans and in addition is actively pursuing the possibility of providing the Department of Education additional post default collection services.

- HESC was designated by Governor Paterson as the agency to administer the New York Higher Education Loan Program (NYHELPs), in partnership with private lenders and SONYMA. NYHELPs is a private student loan program for New York State residents attending participating institutions in the State. The first NYHELPs loan was disbursed January 2010.

- The Operating Fund will continue to support the operational expenses of the Grants and Scholarship program in the amount of approximately $11.1 million for the fiscal year 2011-2012.

- HESC's fringe benefit rate for state fiscal year 2011-2012 has decreased to 46.32% from 47.2% in state fiscal year 2010-2011.

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 detailed 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, Matthew Downey at (518) 474-8893 or **mdowney@hesc.org**.

**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, 2011 and 2010

		2011		2010	
Assets		**Operating Fund**	**Federal Fund**	**Operating Fund**	**Federal Fund**
Current assets:					
Cash and cash equivalents (note 4)	$	59,704,478	45,511,488	59,220,817	72,440,025
Receivables due from U.S. Department of Education:					
Administrative fees (note 5)		3,208,901	—	8,942,246	—
Reinsurance		—	34,916,482	—	20,158,096
EFT fees receivable from lenders		20,886	—	217,032	—
Interfund balances (note 7)		2,874,119	—	—	477,394
Due from lenders for default fee billing (note 13)		—	15,062	—	1,908,153
Prepaid expenses and other assets		257,196	—	301,216	—
Accrued interest		83	71	1,283	—
Total current assets		66,065,663	80,443,103	68,682,594	94,983,668
Noncurrent assets:					
Interfund default aversion fee allowance (note 5)		—	4,755,209	—	5,262,740
Capital assets, net (note 10)		381,813	—	203,550	—
Total noncurrent assets		381,813	4,755,209	203,550	5,262,740
Total assets		66,447,476	85,198,312	68,886,144	100,246,408
Liabilities and Net Assets					
Current liabilities:					
Accounts payable and accrued liabilities		16,814,673	—	16,681,411	—
Interfund balances (note 7)		—	2,874,119	477,394	—
Amounts payable to lenders through EFT (note 4)		315,938	—	1,611,455	—
Total current liabilities		17,130,611	2,874,119	18,770,260	—
Noncurrent liabilities:					
Advance from U.S. Department of Education (note 11)		—	10,300,348	—	10,300,348
Interfund default aversion fee allowance (note 5)		4,755,209	—	5,262,740	—
Total noncurrent liabilities		4,755,209	10,300,348	5,262,740	10,300,348
Total liabilities		21,885,820	13,174,467	24,033,000	10,300,348
Net assets:					
Invested in capital assets		381,813	—	203,550	—
Restricted – property of U.S. Department of Education		—	72,023,845	—	89,946,060
Restricted – for student aid related activities		44,179,843	—	44,649,594	—
Total net assets	$	44,561,656	72,023,845	44,853,144	89,946,060

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, 2011 and 2010

		2011		2010	
		Operating Fund	**Federal Fund**	**Operating Fund**	**Federal Fund**
Operating revenues:					
Defaulted loan collections (note 6)	$	78,893,948	236,916,311	60,662,495	204,006,782
Administrative and program fee income (note 5, 13)		19,651,171	1,580,295	33,284,593	29,951,609
Reimbursement on purchases of default loans from lenders (note 12)		—	612,240,690	—	561,625,491
Other revenue		208,781	12,646	1,663,166	4,029
Total operating revenues		98,753,900	850,749,942	95,610,254	795,587,911
Operating expenses:					
Salaries and employee benefits		33,499,839	—	37,359,802	—
General and administrative		7,916,132	—	11,915,047	—
Collections		15,248,792	—	11,912,097	—
NYS Office for Technology equipment usage charges		2,225,681	—	2,435,732	—
D.M.I. program expenses		1,065,432	—	1,031,883	—
Default aversion fee subsidy		—	5,207,517	—	4,984,022
Purchases of default loans from lenders (note 12)		—	637,200,138	—	584,411,391
Defaulted loan collections paid to U.S. Department of Education (note 6)		—	226,430,399	—	195,312,889
Depreciation (note 10)		89,338	—	42,609	—
Other expense		—	20,415	—	5,933
Purchases of defaulted State loans from lenders		18,234	—	22,086	—
Total operating expenses		60,063,448	868,858,469	64,719,256	784,714,235
Operating income (loss)		38,690,452	(18,108,527)	30,890,998	10,873,676
Nonoperating revenues (expenses):					
Interest income		105,969	81,790	158,125	56,850
Gear Up operational expenses		(855,290)	—	(559,533)	—
New York State initiatives (note 8)		(38,128,097)	—	(38,612,277)	—
Total nonoperating (expenses) revenues		(38,877,418)	81,790	(39,013,685)	56,850
Transfer (to) from Federal Fund (note 9)		(165,475)	165,475	4,925,705	(4,925,705)
Transfer of Federal default fee (note 13)		60,953	(60,953)	(146,012)	146,012
(Decrease) increase in net assets		(291,488)	(17,922,215)	(3,342,994)	6,150,833
Net assets, beginning		44,853,144	89,946,060	48,196,138	83,795,227
Net assets, ending	$	44,561,656	72,023,845	44,853,144	89,946,060

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, 2011 and 2010

	2011		2010	
	Operating Fund	**Federal Fund**	**Operating Fund**	**Federal Fund**
Cash flows from operating activities:				
Receipts from:				
Collections	$ 76,690,395	240,674,341	62,146,505	202,928,376
Administrative fees	25,253,714	—	34,688,282	—
Other sources	389,888	12,644	1,700,983	4,030
Reimbursement on purchases of default loan purchases	—	597,474,711	—	571,971,998
Federal default fee income from lenders	—	3,473,387	—	29,813,489
Payments for:				
Salaries and employee benefits	(35,139,276)	—	(39,785,622)	—
Administrative fees	—	(5,076,715)	—	(5,943,120)
Purchases of default loans from lenders	(18,234)	(637,200,138)	(22,086)	(584,411,391)
Collections paid to U.S. Department of Education (ED)	—	(226,422,805)	—	(195,344,394)
General, administrative and other expenses	(28,082,073)	(20,415)	(28,213,987)	(5,933)
Net cash provided by (used in) operating activities	39,094,414	(27,084,990)	30,514,075	19,013,055
Cash flows from noncapital financing activities:				
Payments to NYS – other student aid activities	(38,375,586)	—	(38,041,528)	—
Interfund transfers	(74,734)	74,734	(203,780)	203,780
Payment from ED for additional rehabilitated loans	—	—	4,925,705	(4,925,705)
Net cash (used in) provided by noncapital financing activities	(38,450,320)	74,734	(33,319,603)	(4,721,925)
Cash flows from capital and related financing activities:				
Purchases of capital assets	(267,601)	—	(207,600)	—
Net cash used in capital and related financing activities	(267,601)	—	(207,600)	—
Cash flows from investing activities:				
Interest received	107,168	81,719	156,921	57,009
Net cash provided by investing activities	107,168	81,719	156,921	57,009
Increase (decrease) in cash and cash equivalents	483,661	(26,928,537)	(2,856,207)	14,348,139
Cash and cash equivalents, beginning	59,220,817	72,440,025	62,077,024	58,091,886
Cash and cash equivalents, ending	$ 59,704,478	45,511,488	59,220,817	72,440,025

**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, 2011 and 2010

		2011		2010	
		Operating Fund	**Federal Fund**	**Operating Fund**	**Federal Fund**
Operating income	$	38,690,452	(18,108,527)	30,890,998	10,873,676
Adjustments to reconcile operating income to net cash provided by (used in) operating activities:					
Depreciation		89,338	—	42,609	—
Change in assets and liabilities:					
Receivables		5,733,345	(14,758,386)	444,591	10,315,000
Other assets		240,166	1,893,091	315,482	(138,117)
Interfund balances		(3,381,301)	3,381,301	958,222	(958,222)
Accounts payable and accrued liabilities		(474,538)	—	(663,898)	—
Other liabilities		(1,295,517)	—	(2,553,211)	—
Allowance for default aversion refunds		(507,531)	507,531	1,079,282	(1,079,282)
Total adjustments		403,962	(8,976,463)	(376,923)	8,139,379
Net cash provided by (used in) operating activities	$	39,094,414	(27,084,990)	30,514,075	19,013,055

See accompanying notes to financial statements.

(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 guaranty agencies. As a guaranty agency, HESC made 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 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.

On March 30, 2010, the President signed into law H.R. 4872 – The Health Care and Education Reconciliation Act of 2010, which terminated new loan originations in the FFELP on June 30, 2010. Effective July 1, 2010, all new Stafford, PLUS or consolidated loans are originated under the U.S. Department of Education Direct Loan Program. Existing FFELP loans will continue to be eligible for program benefits. The Guaranteed Student Loan Programs' Operating Fund and Federal Fund of HESC continues to administer its existing FFELP portfolio of both active and default student loans. As a result of the new legislation, loan processing and issuance fee revenue and federal default fee revenue were reduced and ultimately will be eliminated as a revenue source.

The accompanying financial statements only reflect the Operating Fund and Federal Fund of the Guaranteed Student Loan Programs of HESC. The Federal Fund assets, and earnings on those assets, are restricted in use and are property of the U.S. Department of Education. The Operating Fund is property of HESC and its assets and earnings are restricted in use for student financial aid related activities as required by the Higher Education Amendments of 1998 (1998 Amendments).

HESC also administers the Tuition Assistance Program, State Scholarship Programs, and Robert L. Byrd Federal Scholarship Program under which students apply for payments to attend eligible educational institutions based on family income and/or academic achievement. In addition, HESC partners with colleges, universities, school districts and other educational organizations in administering the Federal GEAR UP and College Access and Challenge Grants which are designed to increase the number of low income students who are prepared to enter and succeed in postsecondary education. These programs are not included in the accompanying financial statements.

In 2009 the State legislature created the New York Higher Education Loan Program (NYHELPs), a State sponsored student loan program for New York residents attending participating institutions in the State. HESC administers the program in partnership with the State of New York Mortgage Agency (SONYMA) and participating lending institutions. HESC's responsibilities include but are not limited to: monitoring the origination and servicing of loans, marketing the program to various audiences, providing financial literacy education, default aversion services and collecting on defaulted accounts. The financial activities of NYHELPs are not included in the accompanying financial statements.

(2) Significant Accounting Policies

(a) Basis of Accounting

The Guaranteed Student Loan Programs' Operating Fund and Federal Fund follow U.S. generally accepted accounting principles as promulgated by the Governmental Accounting Standards Board (GASB). The Guaranteed Student Loan Programs' Operating Fund and Federal Fund follow fund accounting 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 are recognized when earned and expenses are recognized when the cost is incurred regardless of the timing of the related cash flow.

In accordance with GASB Statement Number 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting*, the Operating Fund and Federal Fund apply all applicable 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. The Funds have elected not to apply accounting standards issued after November 30, 1989 by FASB and APB.

(b) Cash and Cash Equivalents

Cash and cash equivalents consisting of United States Treasury Bills and collateralized short-term repurchase agreements with original maturities of 90 days or less, are carried at cost plus accrued interest, which approximates fair value. Investment income represents interest on deposits and gains and losses.

(c) 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.

(d) 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, 2011 and 2010, the Federal Fund was the guarantor of loans outstanding with original principal amounts of approximately $21,399,000,000 and $25,562,000,000, respectively, made to students by participating lending institutions. A substantial portion 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, 2011 and 2010, the unpaid balances were approximately $18,734,000,000 and $22,930,000,000, respectively.

HESC's management anticipates that a certain portion of the loans outstanding as of March 31, 2011 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.

(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 original maturities of three months or less when purchased and generally consist of 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, 2011 and 2010. Federal Fund 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

(Continued)

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 $315,938 for 2011 and 1,611,455 for 2010, which were deposited by lenders, to be forwarded to schools generally within one business day 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.

Cash and cash equivalents at March 31 were as follows:

		2011	2010
Operating Fund:			
Repurchase agreements	$	58,261,299	30,000,000
Cash in State Comptroller's short-term investment pool and cash in bank		1,423,179	29,200,817
Petty cash and travel imprest accounts		20,000	20,000
Operating Fund cash and cash equivalents	$	59,704,478	59,220,817
Federal Fund:			
Repurchase agreements	$	46,231,407	—
Cash-net of outstanding bank checks		(719,919)	72,440,025
Federal Fund cash and cash equivalents	$	45,511,488	72,440,025

At March 31, 2010, all Federal Fund cash was held at Key Bank due to a lack of available collateral amongst the repurchase agreement dealers that HESC uses for investments. At the time, all balances at Key Bank were covered by the FDIC's Transaction Account Guarantee Program, which temporarily removed the insurance cap on balances. The Operating Fund daily liquid cash was also held at Key Bank at the time, however, a term repurchase agreement purchased earlier was outstanding as of March 31, 2010. As of March 31, the cost and fair value of cash equivalents are as follows:

		2011		2010	
Operating Fund		**Cost**	**Fair value**	**Cost**	**Fair value**
Held by HESC's agent in HESC's name	$	58,261,299	58,261,299	30,000,000	30,000,000

Federal Fund		2011 Cost	2011 Fair value	2010 Cost	2010 Fair value
Held by HESC's agent in HESC's name	$	45,511,488	45,511,488	—	—

(5) Operating 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 guaranty 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 guaranty 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 of $4,755,209 and $5,262,740 at March 31, 2011 and 2010, respectively, are reported 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.

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 by the U.S. Department of Education. As a result of HCERA, the last payment of Loan Processing and Issuance Fee was paid for the quarter ended December 31, 2010.

An Account Maintenance Fee is calculated on the original principal amount of loans outstanding at a rate of 0.06%. This fee is paid to the Operating Fund either 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, 2011 and 2010, the administrative fees receivable from U.S. Department of Education consisted of the following:

		2011	2010
Operating Fund:			
Loan processing and issuance fee receivable	$	—	5,107,270
Account maintenance fee receivable		3,208,901	3,834,976
	$	3,208,901	8,942,246

For years ended March 31, 2011 and 2010, administrative fee income is as follows:

		2011	2010
Operating Fund:			
Default aversion fee, net of estimated refunds	$	5,207,517	4,984,022
Loan processing and issuance fee		792,521	12,259,720
Account maintenance fee		13,651,133	16,040,851
	$	19,651,171	33,284,593

Gross default aversion fee income for the years ended March 31, 2011 and 2010 was $10,417,118 and $11,431,620, respectively. The estimated reserve for default aversion fee refunds is netted against default aversion fee income. In 2011 and 2010, the default aversion fee allowance estimate was 50% and 45% of default aversion fee income, respectively. The estimate of the refunds for 2011 is based on the current year's refunds to revenue, which reflects actual experience.

(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 retained 16% of borrower payments, approximately 37% of rehabilitation collection payments and 10% of principal and interest at the time of consolidation.

(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.

At March 31, 2011, the Operating Fund had a net interfund receivable balance of $2,874,119 which included a receivable from the Federal Fund for overpayment of collections activity of $2,460,964. At March 31, 2010, the Operating Fund had a net interfund payable balance of $477,394 which included a payable to the Federal Fund for underpayment of collections activity of $1,297,065, 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 $428,237 and $804,965 at March 31, 2011 and 2010, respectively. In 2011, loan cancellations resulted in a federal default fee receivable of $15,082 in the Operating Fund. The federal default fee payable from the Operating Fund to the Federal Fund totaled $14,706 at March 31, 2010.

(8) New York State Initiatives

The 2010-2011 New York State budget required the Operating Fund to pay the operational expenses related to the administration of the State's grant and scholarship programs, which amounted to approximately $11.6 million and $11.8 million in 2010-2011 and 2009-2010, respectively.

The 2010-2011 and 2009-2010 New York State budgets appropriated $22.2 million of operating funds to subsidize the Tuition Assistance Plan (TAP) which was transferred in March each year.

In fiscal years 2010-2011 and 2009-2010, HESC's Operating Fund incurred costs of $4.3 million and $4.6 million, respectively, as part of the implementation and administration of NYHELPs.

The activities of these programs are excluded from the accompanying financial statements.

(9) Transfer from (to) Federal Fund

In February 2011, HESC was notified by ED that loan processing and issuance fees for the quarters ended June 30, 2010 and September 30, 2010 were overpaid to guaranty agencies. HESC was instructed to transfer the overpayment of $165,475 to the federal fund. The transfer was made in June 2011.

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. 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 was valid from September 30, 2007 to September 30, 2010. HESC transferred $5 million from the Federal Fund to the Operating Fund as part of the rehabilitation recuperation in 2007-2008, and $7 million in 2008-2009. The remaining balance of $4.9 million was transferred October 15, 2009.

(10) Capital and Intangible Assets

Capital assets are recorded at cost. Capital assets are defined as assets with initial, individual costs exceeding a capitalization threshold of $40,000. 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.

Capital asset activity in the Operating Fund for the year ended March 31, 2011 is as follows:

	Balance April 1, 2010	Additions	Disposals	Balance March 31, 2011
Office and computer equipment	$ 1,578,230	267,601	—	1,845,831
Less accumulated depreciation	(1,374,680)	(89,338)	—	(1,464,018)
Net capital assets	$ 203,550	178,263	—	381,813

Capital asset activity in the Operating Fund for the year ended March 31, 2010 is as follows:

	Balance April 1, 2009	Additions	Disposals	Balance March 31, 2010
Office and computer equipment	$ 1,370,630	207,600	—	1,578,230
Less accumulated depreciation	(1,332,071)	(42,609)	—	(1,374,680)
Net capital assets	$ 38,559	164,991	—	203,550

At March 31, 2011 and 2010, the Federal Fund had capitalized equipment with a book value of $294,255 which was fully depreciated.

HESC implemented GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, effective April 1, 2010. Based on the New York State Office of the Comptroller Accounting Bulletin A-614, HESC established a $1 million threshold for capitalization and amortization of intangible assets. As of March 31, 2011, HESC did not have any projects with costs exceeding or expected to exceed the capitalization threshold.

(11) Federal Reserve Recall and Federal Advances

HESC has received, in prior years, noninterest-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.

Long-term obligation activity for the year ended March 31, 2011, is as follows:

Federal Fund		Beginning balance	Additions	Reductions	Ending balance
Federal advances	$	10,300,348	—	—	10,300,348
Total Federal Fund	$	10,300,348	—	—	10,300,348

Long-term obligation activity for the year ended March 31, 2010, is as follows:

Federal Fund		Beginning balance	Additions	Reductions	Ending balance
Federal advances	$	10,300,348	—	—	10,300,348
Total Federal Fund	$	10,300,348	—	—	10,300,348

(12) 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.

All FFELP claims are paid at 97% of the claim value. As of March 2011, HESC was processing claims for 15 servicers.

(13) 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 elected to pay the 1% default fee from the Operating Fund for loans guaranteed prior to May 1, 2008. HESC collects from lenders the 1% fee for loans guaranteed after May 1, 2008 and deposits the fee into the Federal Fund. The enactment of the Health Care and Education Reconciliation Act on March 30, 2010 eliminated the FFEL program. As of July 1, 2010 no new Stafford, PLUS or consolidated loans were disbursed through the FFELP and therefore the federal default fee deposit requirement was substantially eliminated.

For the years ended March 31, 2011 and 2010, the Federal default fee revenue consisted of the following:

		2011	2010
Federal Fund:			
Default fee revenue from lenders	$	1,580,295	29,951,609
Default fee revenue transferred (to) from HESC's Operating Fund		(60,953)	146,012
Total Federal default fee revenue	$	1,519,342	30,097,621

(14) 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 for the first ten years of employment. The Operating Fund contributes the balance payable to the System for these employees.

The Operating Fund paid to the System $3,337,823.25 for 2011, $3,292,422 for 2010, $3,203,568 for 2009 and $3,488,604 for 2008, 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 10.19%, 9.08%, and 8.58% of covered payroll for each of the years, respectively.

(15) 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. The plan under 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 three 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, 2011, 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.

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, 2011 and 2010, HESC had approximately 417 and 380 retired and/or spouses of retired employees, receiving retiree health care benefits with an annual pay-as-you-go cost of approximately $3.5 million and $3.2 million.

(16) 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 $2,153,739 and $2,641,557 as of March 31, 2011 and 2010, respectively, and is recorded in accounts payable and accrued expenses in the Operating Fund.

(17) 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.

(18) Leases

HESC leases office and storage space under noncancelable operating leases effective through 2017. Total rental expense recorded in the Operating Fund, which includes utilities for one of two major leases, for the years ended March 31, 2011 and 2010, were $1,564,183 and $1,688,180, respectively. The following is a summary of future minimum rental commitments under noncancelable leases with terms exceeding one year:

Year ending March 31:		
2012	$	1,928,676
2013		2,197,626
2014		2,251,416
2015		2,244,540
2016		2,223,912
2017		2,218,352
2018		738,524
	$	13,803,046

(19) 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.

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, 2011 and 2010, respectively.

As of the financial issuance date, HESC was working to verify the collections process performed in relations to certain classes of student loans purchased by the agency. There is the potential for a liability resultant from the activities being performed that cannot reasonably be determined at this time. Management believes, however, that the resolution of the verification and any resultant liability will not likely materially affect the financial position or operations of HESC.

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.