Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation
Kentucky's Affordable Prepaid Tuition
and the
Kentucky Education Savings Plan Trust

Audited Financial Statements

For the Fiscal Year Ended June 30, 2013

KENTUCKY HIGHER EDUCATION ASSISTANCE AUTHORITY
KENTUCKY HIGHER EDUCATION STUDENT LOAN CORPORATION

JUNE 30, 2013

Financial Statements

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation

June 30, 2013

Mountjoy
Chilton
Medley

INDEPENDENT AUDITOR'S REPORT

Board of Directors
Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation
Frankfort, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Kentucky Higher Education Assistance Authority and the Kentucky Higher Education Student Loan Corporation (the Authority/Corporation), component units of the Commonwealth of Kentucky, as of and for the year ended June 30, 2013, and the related notes to the financial statements which collectively comprise the Authority/Corporation's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is express opinions on these financial statements based on our audit. We did not audit the financial statements of the Kentucky Education Savings Plan Trust, which statements reflect total assets of $152,762,614 as of June 30, 2013, and increase to fiduciary net position of $16,017,703 for the year ended June 30, 2013. Those financial statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Kentucky Education Savings Plan Trust, is based solely on the report of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinions

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregated remaining fund information of the Authority/Corporation as of June 30, 2013, and the respective changes in financial position, and where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 15 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated September 23, 2013, on our consideration of the Authority/Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority/Corporation's internal control over financial reporting and compliance.

Lexington, Kentucky
September 23, 2013

Description of the Business

The Kentucky Higher Education Assistance Authority (the “Authority” or “KHEAA”) was established in 1966 as the Commonwealth of Kentucky’s agency for improving higher education opportunities. The Authority also guarantees, performs default aversion activities and performs collection activities on eligible student loans. The Kentucky Educational Savings Plan Trust (the “Trust”) and the Commonwealth Postsecondary Education Prepaid Trust Fund, Kentucky’s Affordable Prepaid Tuition Plan (the “Plan”) offer savings and investment opportunities for Kentuckians to save for higher education. The Kentucky Higher Education Student Loan Corporation (the “Corporation” or “KHESLC”) makes student loans directly to parents and students as part of the Kentucky Advantage loan programs, purchases and services eligible Federal and Kentucky Advantage student loans and performs collection activities on eligible Federal student loans. The Authority and the Corporation maintain bundled operations to maximize the efficiency of loan guarantee and servicing operations. Accordingly, all senior management positions have responsibilities related to both the Authority and the Corporation. Additionally, the Plan and the Trust are governed by the Authority and Corporation’s combined Board of Directors. Throughout the accompanying financial statements, the “Authority/Corporation” refers to the combined group of operations.

The Authority/Corporation maintains the following operations:

Outreach - Outreach operations provide resources to make higher education accessible to Kentucky’s current and future generations. Outreach counselors at the Authority/Corporation are available year-round to provide free college planning and financial aid assistance. They conduct scholarship and other funding searches, help students with the admissions and financial aid application processes and increase motivation for at-risk students. Outreach services are offered through financial aid nights, career fairs, college nights, adult education programs, Kentucky Educational Excellence Scholarship (“KEES”) workshops, Free Application for Federal Student Aid (“FAFSA”) workshops, PTA and other meetings, financial literacy workshops, professional development/staff training, and other programs and camps. Personnel, professional and administrative costs associated with the outreach operation are accounted for as a program benefit in a proprietary fund of the Authority/Corporation.

Student Aid - Student aid operations provide some or all levels of administration of fifteen student aid programs: (1) the Kentucky Tuition Grant (“KTG”) program, (2) College Access Program (“CAP”) grant, (3) Kentucky Educational Excellence Scholarship program, (4) Teacher Scholarship program, (5) Osteopathic Medicine Scholarship program, (6) the KHEAA Work-Study program, (7) Kentucky Coal County College Completion Scholarship, (8) Early Childhood Development Scholarship program, (9) the Go Higher Grant program, (10) the Coal County Scholarship for Pharmacy Students program, (11) the Mary Jo Young Scholarship program, (12) John R. Justice grant, (13) the Drive the Dream Scholarship program, (14) the Kentucky National Guard Tuition Award program, and (15) the Minority Educator Recruitment and Retention Scholarship program.

Personnel, professional and administrative costs associated with student aid operations are accounted for as a program benefit in a proprietary fund of the Authority/Corporation. Direct benefits to students are accounted for in the governmental fund.

College Savings Plan - The college savings plan operation administers two savings plans for the Commonwealth of Kentucky; (1) the Trust and (2) the Plan.

The Trust was formed on July 15, 1988, by Kentucky law, to help families save for the costs of education after high school. The Trust is administered by the Authority/Corporation's Board of Directors. The Authority/Corporation has contracted with TIAA-CREF Tuition Financing, Inc. ("TFI"), a wholly-owned subsidiary of Teachers Insurance and Annuity Association of America ("TIAA"), for management services for the Trust. The Trust is operated in a manner such that it is exempt from registration as an investment company under the Investment Company Act of 1940. The Trust offers certain federal and state tax advantages to purchasers.

An individual participating in the Trust establishes an account in the name of a beneficiary. Contributions can be made among six investment options: the Managed Allocation Option, the Fixed Income Option, the Balanced Option, the Equity Index Option, the Active Equity Option, and the Guaranteed Option.

Contributions in the Managed Allocation Option are allocated among six age bands, based on the age of the beneficiary. Each age band invests in varying percentages in the Institutional Class of the International Equity, International Equity Index, Large-Cap Value Index, Large-Cap Growth Index, S&P 500 Index, Mid-Cap Growth Fund, Small-Cap Equity, Mid-Cap Value, Short-Term Bond, Bond Index, Large-Cap Growth, Inflation-Linked Bond, Equity Index, Small-Cap Blend Index, Bond, Large-Cap Value Index, Real Estate Securities, Emerging Market Equity, Emerging Market Equity Index and Money Market Funds of the TIAA-CREF Institutional Mutual Funds.

These percentages are determined by the Authority/Corporation's Board of Directors and are subject to change. The assets of the Guaranteed Option are allocated to a funding agreement issued by TIAA-CREF Life Insurance Company, a subsidiary of TIAA, which offers a guarantee of principal and a minimum rate of return to the Trust.

The college savings plan operation also administers the Plan, which was created by the 2000 Kentucky General Assembly and is governed under Kentucky Revised Statutes ("KRS") 164A.700-709.

The Plan was established to provide families with an opportunity to save for future postsecondary education expenses. The Plan investment strategy is to earn rates of return that exceed anticipated tuition inflation rates so that the Plan is able to meet its obligation to pay benefits at future tuition rates. The Plan offers certain federal and state tax advantages to purchasers.

Participants purchased annual tuition units at current tuition levels, or current tuition levels plus a premium, and receive benefits equal to tuition rates in place at the time that the student attends a qualified postsecondary education institution. The Plan offers three tuition plans – the Value Plan, the Standard Plan, and the Premium Plan. In the Value Plan, participants buy tuition units and receive benefits indexed to the tuition rate of the Kentucky Community and Technical College System. The Standard Plan offers tuition units and benefits indexed to the tuition rate of Kentucky's most expensive public university. The Premium Plan offers tuition units at the current average tuition cost of Kentucky's private colleges and universities and guarantees a return on a participant's investment equal to the tuition inflation rate for the University of Kentucky.

Participants were allowed to elect to spread payments to the Plan over three, five or seven years or until the anticipated year of the student's enrollment in a qualified postsecondary education institution. Participants may use Plan benefits for eligible educational expenses at any eligible public or private vocational school, college or university in the United States. If a beneficiary attends an eligible educational institution with tuition rates in excess of Plan benefits, the Plan will not be responsible for the difference. If a beneficiary attends an eligible educational institution with tuition rates less than Plan benefits, participants may use the difference for other qualified educational expenses such as room, board, books, and supplies.

Participants may withdraw from the Plan at any time for any reason. Terminating participants are refunded any contract payments made less benefits received, administrative and cancellation fees. Participants who withdraw after July 1 of the beneficiary's college entrance year receive the tuition payout value of the contract less benefits received, administrative and cancellation fees. Non-qualified withdrawals are subject to a 10% penalty in accordance with Section 529 of the Internal Revenue Code ("IRC") except in cases where the withdrawal is: (1) made on account of the death or disability of the student; (2) made on account of a scholarship received by a student, or (3) a non-taxable transfer to another account or to another IRC Section 529 program for a different student who is a family member of the original student.

As of June 30, 2013, the Plan maintained a present value fund deficit of $52.9 million. Based on actuarial estimates, the Plan's assets will be exhausted in fiscal year 2020, at which time the liability of the Plan becomes a General Obligation of the Commonwealth of Kentucky. Per KRS 164A.708, once a real liability is expected to accrue, the General Assembly shall appropriate the necessary funds to meet the liability. Over the remaining estimated life of the program, through fiscal year 2032, actuarial estimates show the Commonwealth of Kentucky will need to transfer approximately $95 million.

Personnel, professional and administrative costs associated with administering the Trust and the Plan are accounted for in the Student Aid Fund, a governmental fund of the Authority/Corporation. All assets, liabilities and net asset additions and deductions for the Trust are accounted for in the Kentucky Educational Savings Plan Trust fund, a fiduciary fund of the Authority/Corporation. All assets, liabilities and net asset additions and deductions for the Plan are accounted for in the Kentucky Affordable Prepaid Tuition fund, a fiduciary fund of the Authority/Corporation.

Loan Guarantee - Loan guarantee operations maintain loan guarantees for qualified students and parents of qualified students made by approved lenders, under the Federal Family Education Loan Program ("FFELP"). The loan guarantee operation is responsible for providing default aversion assistance to lenders for delinquent loans, reporting loan information to the National Student Loan Data System ("NSLDS"), paying lender claims for loans in default, paying lender claims for death, disability or bankruptcy, and collecting loans on which default claims have been paid

Personnel, professional and administrative costs associated with loan guarantee operations are accounted for in the Agency Operating Fund ("AOF"), a proprietary fund of the Authority/Corporation. All federal program activities related to default aversion, claim payment, claim reinsurance from the U.S. Department of Education ("USDE"), defaulted loan recoveries and other federally mandated program sources and uses of funds are accounted for in the Federal Student Loan Reserve Fund ("FSLRF"), a fiduciary fund of the Authority/Corporation.

Loan Origination and Disbursement – Loan origination and disbursement operations consist of credit underwriting, loan origination, and issuing disbursements directly to schools for the Kentucky Advantage Education Loan ("KAEL") and Kentucky Advantage Parent Loan programs ("KAPL"). KAEL and KAPL are the state based supplemental loans provided by the Authority/Corporation.

Personnel, professional and administrative costs associated with loan origination and disbursement operations are accounted for in the proprietary fund of the Authority/Corporation.

Loan Finance - The Authority/Corporation's loan finance operation is authorized to refinance existing long-term debt and to acquire private supplemental student loans, rehabilitated FFELP loans, and certain other FFELP loans required to be repurchased by the Higher Education Act. The Authority/Corporation may issue bonds and notes not to exceed $5 billion in order to carry out these corporate powers and duties. The FFELP student loans held by the Authority/Corporation include Federal Stafford Loans ("Stafford"), Unsubsidized Stafford Loans ("Unsubsidized Stafford"), Federal Supplemental Loans for Students ("SLS"), Federal Parent Loans for Undergraduate Students ("PLUS"), and Federal Consolidation Loans ("Consolidations"). As of June 30, 2013, the loan finance operation owned approximately $1.34 billion of student loans.

Most FFELP loans held by the Authority/Corporation are insured by the Authority/Corporation's loan guarantee operations. FFELP loans made prior to October 1, 1993, are 100% insured. FFELP loans made between October 1, 1993 and June 30, 2006, are 100% insured against borrowers' death, disability, or bankruptcy and 98% insured against borrowers' default. FFELP loans made after June 30, 2006, are 100% insured against borrowers' death, disability, or bankruptcy and 97% insured against borrowers' default.

The Authority/Corporation's loan finance operation finances all existing FFELP loans with revenue bonds, notes payable, and lines of credit. As of June 30, 2013, the loan finance operation maintained four separate General Bond Resolutions ("GBRs") and related Series Resolutions for issues of revenue bonds. The GBRs contain provisions establishing funds and accounts for the segregation of assets and provisions restricting the use of the proceeds of bonds and other funds received. As of June 30, 2013, the loan finance operation maintained $1.28 billion of revenue bonds outstanding.

Personnel, professional and administrative costs associated with loan finance operations are accounted for in a proprietary fund of the Authority/Corporation. The state based supplemental loans and a portion of FFELP loans and all related activities are also accounted for in a proprietary fund of the Authority/Corporation. The majority of loans, however, are financed by revenue bonds and the ED Conduit Program Note Payable. These loans, bonds and note payable and all other related assets, liabilities, revenues, and expenses are accounted for in the Education Finance Funds, a proprietary fund of the Authority/Corporation.

Loan Servicing - The loan servicing operation performs servicing and default prevention activities on FFELP and alternative loans held by the Authority/Corporation's loan finance operation and other lenders. Of the loans serviced, approximately $1.34 billion in outstanding principal of loans was held by the loan finance operation. Nearly all of these loans were pledged pursuant to the 1997 GBR, the 2008 Indenture, the 2010 Indenture, and the 2013-1 Indenture. Approximately $23 million of FFELP Loans and other education loans were owned by other holders, including a holder with national lending operations. For loans owned by other holders, the loan servicing operation collects student loan remittances and subsequently disburses these remittances to the appropriate lending entities.

Personnel, professional and administrative costs associated with loan servicing operations are accounted for in a proprietary fund of the Authority/Corporation. Student loan remittances and payables to other lenders are also accounted for in a proprietary fund.

Industry Update

The Health Care and Education Reconciliation Act ("HCERA") of 2010 (H.R.4872/Public Law 111-152) was signed into law on March 30, 2010. HCERA eliminated the origination and/or guarantee of FFELP loans, effective July 1, 2010. In accordance with HCERA, the Authority/Corporation continues to provide guarantee services on $2.8 billion of FFELP loans, continues to own $1.34 billion of FFELP loans, and continues to service an additional $23 million of FFELP and other education loans. The Authority/Corporation can no longer originate, guarantee or fund any new FFELP loans.

HCERA provides for servicing opportunities for nonprofit organizations to service an initial allocation of 100,000 Federal loan borrowers. The Corporation received their initial allotment of loans in the fall of 2012. The Corporation is currently partnering with another U.S. Department of Education (USDE) federal loan servicer to service these loans.

HCERA created additional funding for the College Access Challenge Grant program ("CACG"). The Authority/Corporation was awarded $1.99 million for the CACG year 2013 award period.

USDE currently contracts with Private Collection Agencies ("PCAs") to collect student loans, including defaulted Direct Loans that have been assigned or referred to USDE. In March 2012, the Authority/Corporation contracted with one of the PCAs to collect loans on their behalf. The Authority/Corporation plans to leverage this experience, as well as its experience collecting defaulted FFELP loans, in its pursuit to become one of the PCAs selected by USDE as part of the current PCA Request for Proposal process. In anticipation of this selection process, the Authority/Corporation sought and received state legislative approval from the Commonwealth of Kentucky to create the Asset Resolution Corporation ("ARC") as the entity that would contract with USDE to become a PCA. ARC was created by the Kentucky General Assembly effective July 12, 2012.

On May 6, 2013, the KHESLC entered into a voluntary closing agreement (the "VCA") with the Internal Revenue Service (the "IRS") relating to certain of its tax-exempt bonds (collectively, the "Subject Bond Issues"). The VCA resulted from a request that was submitted by KHESLC on July 31, 2012 pursuant to IRS Announcement 2012-14, 2012-14 I.R.B. 721, titled TEB Voluntary Closing Agreement Program: Relief from Allocation and Accounting Errors for Certain Issuers of Tax-Exempt

Student Loan Bonds (the "Announcement"). KHESLC expects the VCA to finally and conclusively resolve all matters that were addressed in the Request.

A notice was published in the Federal Register on August 14, 2013, inviting guaranty agencies with agreements to participate in FFELP to submit proposals to enter into a Voluntary Flexible Agreement ("VFA") with the Secretary, as authorized by section 428A of the Higher Education Act of 1965, as amended ("HEA"). The invitation requested agencies interested to submit evidence as to their scalability and capacity to assume full responsibility for all or part of the FFELP portfolio of agencies whose agreements with the Secretary have been, or would be, terminated. The Authority/Corporation submitted a letter of interest to the Secretary on September 12, 2013 prior to the September 13, 2013 deadline indicating the Authority/Corporation's willingness to potentially assume responsibility for the FFELP portfolio of other guarantors. The letter of interest does not obligate the Authority/Corporation to assume any such responsibility.

Overview of Financial Statements

This discussion and analysis is intended to serve as an introduction to the Authority/Corporation's combined financial statements. The Authority/Corporation's combined financial statements are comprised of the following three components: 1) combined government-wide financial statements, 2) combined fund financial statements, and 3) notes to combined financial statements.

The combined government-wide statement of net position and statement of activities include the Governmental Funds and Proprietary Funds. The combined government-wide financial statements can be found on pages 16 and 17 of this report. The combined fund financial statements can be found on pages 18 through 23 of this report.

Fiduciary funds are used to account for resources held for the benefit of parties outside the Authority/Corporation. Fiduciary funds are not reflected in the combined government-wide financial statements because the resources are not available to support the Authority/Corporation's programs. The fiduciary fund statement of net position (deficit) and changes in fiduciary net position (deficit) can be found on pages 24 and 25 of this report.

The Trust publishes separate financial statements and footnotes.

To obtain a copy of the financial statements and footnotes, please contact the Authority at (502) 696-7421.

The following is a condensed summary of financial information for the years ended June 30, 2013 and 2012, respectively.

Condensed Financial Information - Governmental Fund and Proprietary Funds

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation

	Governmental Fund		Proprietary Funds	
	2013	2012	2013	2012
Net Position Information				
Capital assets	$	$	$ 4,500,499	$ 4,332,499
Other assets	27,959,655	19,409,469	1,544,447,553	1,748,146,457
Total Assets	27,959,655	19,409,469	1,548,948,052	1,752,478,956
Long-term liabilities			1,290,869,840	1,517,068,808
Other liabilities	290,899	1,036,388	17,753,430	22,972,954
Deferred gain on debt retirements, net			24,772,621	0
Total Liabilities and Deferred Inflows of Resources	290,899	1,036,388	1,333,395,891	1,540,041,762
Invested in capital assets, net of expended debt proceeds			4,500,499	4,332,499
Unrestricted			43,585,902	51,704,872
Restricted, other			93,145,111	87,695,246
Restricted for program benefits	27,668,756	18,373,081		
Restricted for student aid and related activities			74,320,649	68,704,577
Total Net Positon	$ 27,668,756	$ 18,373,081	$ 215,552,161	$ 212,437,194
Activity Information				
Interest and investment income fund	$ 755,271	$ 279,579	$ 500,437	$ 437,072
Student aid & advancement fund revenue	195,437,075	193,585,870		
Tobacco settlement revenue	1,099,805	1,000,000		
Unclaimed lottery revenue	10,600,000	7,000,000		
Contributions from Agency Operating Fund	2,770,728	3,155,384		
Federal funds revenue	161,947	240,379		
Servicing Fees from external sources			1,646,074	162,131
Servicing Fees from Education Finance Funds			8,600,008	9,561,870
Conversion fees			1,000,000	0
SAFRA revenue			203,640	404,677
Debt recovery commission			23,916,732	25,482,439
Early retirement of debt			4,718,437	3,480,335
Federal fees earned			1,921,685	2,193,241
Federal grant revenue			1,802,896	2,536,854
Default aversion fee income			629,785	908,652
Interest income on loans			21,760,139	26,033,086
Amortization of deferred gain on debt retirements			18,465,693	18,465,693
Guarantee fee			195,426	98,710
Gain on the sale of loans			153,234	9,146
Late payment penalties			1,546,097	1,455,242
School Services			137,461	109,487
Other income	1,191,475	279,125	116,533	332,040
Total Revenue	212,016,301	205,540,337	87,314,277	91,670,675
Kentucky Tuition Grants	30,074,117	31,403,472		
College Access Program Grants	57,549,144	59,044,286		
Robert C. Byrd Scholarship	0	219,396		
Mary J Young Scholarships	497,020	416,933		
Early Childhood Development Scholarships	906,695	1,245,345		
National Guard Tuition Awards	4,670,292	4,798,881		
Kentucky Education Excellence Scholarships	102,759,512	99,142,626		
Teacher Scholarships	1,376,372	880,971		
Teacher Loan Forgiveness	1,400,000	2,050,000		
Osteopathic Medicine Scholarships	642,222	635,862		
Work Study Benefits	448,384	580,481		
Go Higher Grant Program	219,042	206,086		
Pharmacy Scholarship Program	253,800	159,800		
Drive the Dream Scholarship	558,491	448,500		
Kentucky Coal County College Completion Scholarship	1,197,828			
John R. Justice Grant	121,209	57,544		
State General Fund expenditure	0	447,414		
Loan guarantee operations			3,458,272	3,747,137
Default collections			5,275,384	6,090,275
Default fee expense				
Loan finance and servicing activities			47,120,468	47,246,659
Outreach			3,956,706	3,341,667
Contribution to FSLRF			5,500,000	2,874,310
Student aid administration			1,889,023	2,358,884
Contribution to student aid programs			881,705	796,500
School services			1,921,564	109,487
Other activities	46,498	219,978	(19,850)	124,388
Total Expenditures	202,720,626	201,957,575	69,983,272	66,689,307
Net Operating income (loss) before Operating Transfers	9,295,675	3,582,762	17,331,005	24,981,368
Transfer to State General Fund			0	(147,000)
Transfer to KAPT (the "Plan")			(24,855)	(102,646)
Change in Net Position	$ 9,295,675	$ 3,582,762	$ 17,306,150	$ 24,731,722

Financial Analysis – Governmental and Proprietary Funds

As previously noted, the Authority and the Corporation maintain bundled operations to maximize the efficiency of operations. Throughout the financial analysis, the "Authority/Corporation" refers to the combined group of operations for both organizations. Financial results for specific operating activities may be discussed as needed to provide appropriate disclosure.

This section of the annual financial report presents a discussion and analysis of the Authority/Corporation's government-wide performance for the fiscal year ended June 30, 2013. Please read it in conjunction with the Authority/Corporation's combined financial statements and notes to the combined financial statements, which follow this section.

Financial Overview

- The Authority/Corporation's proprietary fund total assets decreased approximately $203 million (11%), from $1.7 billion to $1.5 billion. The decrease was caused primarily by a $173 million decrease in loans, a $4.7 million decrease in accrued interest income, a $2.6 million decrease in receivables, a decrease in cash and investments of $8 million, and a $14 million decrease in deferred assets (see Note T).

- The Authority/Corporation's proprietary fund liabilities and deferred inflows decreased by $206 million (15%), from $1.5 billion to $1.3 billion. The decrease in liabilities resulted primarily from a decrease in bonds payable and the ED Conduit Program Note Payable combined of $182 million and decreases in deferred gain on early retirement of debt and various payables of $18.4 million and $5.7 million, respectively.

- The Authority/Corporation's proprietary fund revenues decreased $4.4 million (4.8%), the majority of which related to decreases in debt recovery commissions and net interest revenues of $1.5 million and $4.2 million, respectively, and various other decreases offset primarily by an increase on gains of early retirement of debt of $1.2 million.

- The Authority/Corporation's total proprietary fund expenditures increased $3.2 million (5%), resulting primarily from a $2.6 million increase in the contribution to FSLRF and an increase in operating expenses of $0.6 million.

- The Authority/Corporation's governmental fund assets increased by $8.6 million (44%) resulting primarily from increase in accounts receivable related to student aid programs and an increase in cash and cash equivalents of $6.8 million and $2.0 million, respectively.

- The Authority/Corporation's governmental fund liabilities decreased by $745,000 primarily due to timing differences related to student aid disbursements.

- The Authority/Corporation's governmental fund revenues increased $6.4 million (3%), resulting from additional state General Funds for student aid programs of $1.8 million, increases in unclaimed lottery revenue of $3.6 million, an decrease in the contribution from the Agency Operating Fund of $.4 million, an increase in investment income of $0.5 million and an increase in other income related to prior year student aid refunds of $0.9 million.

- The Authority/Corporation's governmental fund expenditures remained relatively consistent with the prior year. Expenditure changes primarily included reductions in College Access Program and Kentucky Tuition Grant of $2.8 million offset by increases in the Kentucky Educational Excellence Scholarships of $3.6 million.

Combined Statement of Net Position – Governmental Fund and Proprietary Funds

Total governmental fund balance increased from $18.4 million to $27.6 million. Total proprietary fund net position increased $3.0 million (1.5%) comprised of a $18.5 million increase from default collection operations (compared to $19.3 million in prior year), $530,000 decrease from loan guarantee operations (compared to $313,000 contribution in prior year), $2.2 million contribution for outreach activities (compared to $805,000 million contribution in prior year), $2.8 million contribution for student aid and administration (compared to $3.1 million in prior year), $11.6 million gain in loan finance and servicing activities (compared to $12.7 million gain in prior year) and $5.5 million contribution to the FSLRF (compared to $2.8 million in prior year). Additionally there was a $14 million decrease related to deferred assets (see Note T). Also, the proprietary fund contributed $24,855 to administer the Plan.

Certain highlights related to the combined statement of net position as of June 30, 2013, are as follows:

- The Authority/Corporation purchased $97.05 million of its own auction rate securities on the secondary market for a discount, resulting in other income of $4.7 million.

- The Authority/Corporation maintained $2.8 billion of FFELP guarantees outstanding.

- The Authority/Corporation maintained $1.34 billion of FFELP loans.

- The Authority/Corporation maintained $429.3 million of defaulted loans in its collection portfolio.

- Unrestricted net position decreased from $51.7 million to $43.6 million.

- Net position, restricted other increased from $87.7 million to $93.1 million.

- Net position restricted for student aid and related activities increased from $68.7 million to $74.3 million.

Combined Statement of Revenues, Expenses and Changes in Net Position

In fiscal year 2013, the KEES program was fully funded. Certain other Student Aid programs, including CAP and KTG, incurred a reduction in General Fund appropriations as a result of the 2012-2014 biennial budget process. In fiscal year 2012, USDE awarded $2,058,032 of CACG funds to the Authority/Corporation, with an award period from August 14, 2011 through August 13, 2012. In fiscal year 2013, USDE awarded another $1,995,549 CACG grant to the Authority/Corporation with an award period from August 14, 2012 through August 13, 2013. The Authority/Corporation is required to provide 1/3rd match for CACG grant, and outreach expenses increased $615,000 during the fiscal year ended June 30, 2013. Outreach activities (including CACG activities) for both fiscal years were accounted for in a proprietary fund of the Authority/Corporation.

The $17.3 million increase in proprietary fund net position during FY 2013 was $7.4 million less than the $24.9 million increase during FY 2012. The decrease resulted from an approximate $6.3 million decrease in the Authority's net position and an approximate $1.1 million decrease in the Corporation's net position. The Authority's $6.3 million decrease was due primarily to decreases in revenue of $2.8 million combined with increases in expenses $3.5 million, $2.6 million of which pertains to an increase in the Contribution to FSLRF. The reduction in the overall increase in net position of the Corporation in FY 2013 compared to FY 2012 resulted primarily from the net of the following changes: a decrease in net interest revenues net of financing expenses of $3.9 million resulting primarily from a lower average loans receivable balance, an increase in other operating revenues of $3 million associated primarily from additional servicing and conversion fees, an increase in total operating expenses of $5.1 million due largely to the settlement of a contingency previously disclosed but not recorded, and a decrease in program benefits of $4.8 million. $4.3 million of the program benefit decrease is attributable to the current year elimination of amortization of front end borrower benefits due to the early adoption of GASB Statement No. 65 (see Note T).

Certain other highlights related to the combined statement of revenues, expenses and changes in net position for the year ended June 30, 2013, are as follows:

- The Authority/Corporation provided $19 million for program benefits for citizens of the Commonwealth of Kentucky.
- The defaulted loan collection operation received $23.8 million in commissions on the $128.8 million collected on behalf of the USDE.

Condensed Financial Information - Fiduciary Funds

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation

	Federal Student Loan Reserve Fund		Kentucky's Affordable Prepaid Tuition		Kentucky Education Savings Plan Trust	
	2013	2012	2013	2012	2013	2012
Net Position Information						
Other assets	$ 20,541,989	$ 21,072,284	$ 119,082,448	$ 121,667,135	$ 152,762,614	$ 136,977,448
Total Assets	**20,541,989**	**21,072,284**	**119,082,448**	**121,667,135**	**152,762,614**	**136,977,448**
Total Liabilities	12,139,873	14,705,359	171,985,473	176,172,487	173,569	406,106
Restricted net position (deficit)	8,402,116	6,366,925	(52,903,025)	(54,505,352)	152,589,045	136,571,342
Total Net Position	**$ 8,402,116**	**$ 6,366,925**	**(52,903,025)**	**(54,505,352)**	**$ 152,589,045**	**$ 136,571,342**
Changes in Fiduciary Net Position Information						
Federal reinsurance	$ 95,392,394	$ 121,456,219	$	$	$	$
Contribution from Agency Operating Fund	5,500,000	2,874,310				
Fee revenue	0	(1,108)				
Contributions			310,439	649,997		
Subscriptions					47,998,799	43,420,053
Investment revenue	1,080	2,540	12,858,989	7,740,033	11,502,563	3,520,446
Other income	2,747,959	2,887,176				
Total Additions	103,641,433	127,219,137	13,169,428	8,390,030	59,501,362	46,940,499
Administrative expenses			425,447	500,226	611,036	557,770
Refunds			948,279	632,135		
Trustee expense			319,566	240,268		
Tuition benefits expense, net			9,898,664	10,661,806		
Loan claims	100,976,457	129,021,794				
Redemptions					42,872,623	40,407,608
Default aversion	629,785	908,652				
Total Deductions	101,606,242	129,930,446	11,591,956	12,034,435	43,483,659	40,965,378
Change in Net Position Before Operating Transfers	2,035,191	(2,711,309)	1,577,472	(3,644,405)	16,017,703	5,975,121
Operating Transfers						
Transfer from Agency Operating Fund			24,855	102,646		
Change in Net Position After Operating Transfers	**$ 2,035,191**	**$ (2,711,309)**	**$ 1,602,327**	**$ (3,541,759)**	**$ 16,017,703**	**$ 5,975,121**

Financial Analysis – Fiduciary Funds

This section of the annual financial report presents a discussion and analysis of the Authority/Corporation's fiduciary fund performance for the fiscal year ended June 30, 2013. Please read it in conjunction with the Authority/Corporation's combined financial statements and notes to the combined financial statements, which follow this section.

Financial Overview

- Loan claims paid decreased from $129 million in fiscal year 2012 to $101 million in fiscal year 2013 (22% increase).

- The Plan noted a decrease in tuition benefits payable of $4.2 million in fiscal year 2013, due primarily to a lower than expected tuition rate, higher than expected investment experience, and the continued maturity of a program that has not been open for new enrollments since fiscal year 2005.

Statement of Fiduciary Net Position (Deficit)

The FSLRF net position increased $2 million compared to prior year. Assets decreased approximately 2.5% ($530,000), while liabilities decreased 17.4% ($2.5 million). The increase in net position is primarily comprised of a $5.5 million contribution from the Agency Operating Fund offset by a $3.4 million decrease associated with claim payments.

The Plan recognized a decrease in the net deficit of $3.96 million for fiscal year 2013 compared to a $3.6 million increase in net deficit in the prior year. Overall, the current year decrease in net deficit from prior year is a progression of several additions and subtractions with the overall decrease resulting primarily from gains associated with both favorable tuition inflation and investment experience.

The Plan's total assets decreased $2.6 million, from $121.7 million as of June 30, 2012 to $119.1 million as of June 30, 2013. Cash and investments decreased from $116.8 million to $115.2 million, a $1.6 million decrease. The change in tuition and investment return assumptions are as follows:

- 2013-thereafter – investment return decreased from 6.25% to 5.94%

- 2012-2013 academic year – tuition increase assumption was 6.75%, while actual tuition increases were 3.8% for the Value Plan and 6% for the Standard Plan and the Premium Plan

- 2014-thereafter – tuition increase assumption remained at 6.75%

The Trust is an Internal Revenue Code 529 plan managed by the Authority and administered on behalf of the Authority by TFI. Trust assets are entirely comprised of cash and pooled investments. Total net position increased approximately $16 million, due to subscriptions received ($48 million) and investment gain ($11.5 million), net of expenses and redemptions ($43.4 million).

Statement of Changes in Fiduciary Net Position (Deficit)

The FSLRF net position increased $2 million compared to prior year. Assets decreased approximately 2.5% ($530,000), while liabilities decreased 17.4% ($2.5 million). The increase in net position is primarily comprised of a $5.5 million contribution from the Agency Operating Fund offset by a $3.4 million decrease associated with claim payments.

The Plan recognized a decrease in the net deficit of $1.6 million for fiscal year 2013 compared to a $3.6 million increase in net deficit in the prior year. Overall, the current year decrease in net deficit from prior year is a progression of several additions and subtractions with the overall decrease resulting primarily from gains associated with both favorable tuition inflation and investment experience.

Combined Government-Wide Statement of Net Position

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation

June 30, 2013

ASSETS	Governmental Activities	Business-Type Activities	Total
Current:			
Cash and cash equivalents	$ 2,676,169	$ 39,819,439	$ 42,495,608
Accounts receivable and prepaid expenses	16,456,476	1,989,168	18,445,644
Accrued interest income		10,368,726	10,368,726
Investments		6,422,639	6,422,639
Teacher and Osteopathic Medicine scholarship loans	450,000		450,000
Loans, net		221,423,557	221,423,557
Total Current Assets	19,582,645	280,023,529	299,606,174
Noncurrent:			
Restricted cash and cash equivalents		77,114,367	77,114,367
Restricted from Federal Student Loan Reserve Fund		8,035,026	8,035,026
Investments		51,889,664	51,889,664
Fixed assets, net		8,785,499	8,785,499
Loans, net		1,110,250,188	1,110,250,188
Teacher and Osteopathic Medicine scholarship loans, net	4,648,108		4,648,108
Teacher and Osteopathic Medicine scholarship advances	3,728,902		3,728,902
Accrued interest income, net		12,849,779	12,849,779
Total Noncurrent Assets	8,377,010	1,268,924,523	1,277,301,533
Total Assets	27,959,655	1,548,948,052	1,576,907,707
LIABILITIES			
Current:			
Accounts payable and accrued expenses	290,899	5,472,454	5,763,353
Accrued interest expense		2,264,750	2,264,750
Payable to US Department of Education		9,491,226	9,491,226
Capital lease payable		525,000	525,000
Total Current Liabilities	290,899	17,753,430	18,044,329
Noncurrent:			
Allowance for arbitrage liabilities		94,840	94,840
Capital lease payable		3,760,000	3,760,000
Bonds payable		1,287,015,000	1,287,015,000
Total Noncurrent Liabilities		1,290,869,840	1,290,869,840
Total Liabilities	290,899	1,308,623,270	1,308,914,169
Deferred Inflows of Resources:			
Deferred gain on debt retirements, net		24,772,621	24,772,621
Total Liabilities and Deferred Inflows of Resources	290,899	1,333,395,891	1,333,686,790
NET POSITION			
Invested in capital assets, net of expended debt proceeds		4,500,499	4,500,499
Unrestricted		43,585,902	43,585,902
Restricted, other		93,145,111	93,145,111
Restricted for program benefits	27,668,756		27,668,756
Restricted for student aid and related activities		74,320,649	74,320,649
Total Net Position	$ 27,668,756	$ 215,552,161	$ 243,220,917

See accompanying notes

Combined Government-Wide Statement of Activities

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation

For Year Ending June 30, 2013

			Program Revenue		Net (Expenses) Revenues and Changes in Net Position		
	Direct Expenses	Indirect Expenses	Charges for Services	Operating Grants and Contributions	Governmental Activities	Business-Type Activities	Total
Governmental Activities:							
Kentucky Tuition Grant	$ 29,820,457	$ 253,660	$	$ 32,537,955	$ 2,463,838	$	$ 2,463,838
College Access Program Grant	57,182,311	366,833		62,779,316	5,230,172		5,230,172
Mary Jo Young Scholarship	405,385	91,635		475,335	(21,685)		(21,685)
Early Childhood Development Scholarship	853,505	53,190		1,185,874	279,179		279,179
Kentucky National Guard Tuition Award Program	4,618,029	52,263		5,283,801	613,509		613,509
Kentucky Educational Excellence Scholarship	102,273,471	486,041		102,986,610	227,098		227,098
Teacher Scholarship	1,099,326	277,046		2,521,885	1,145,513		1,145,513
Teacher Loan Forgiveness	1,400,000			-	(1,400,000)		(1,400,000)
Osteopathic Medicine Scholarship	595,782	46,440		1,161,125	518,903		518,903
KHEAA Work Study Program	401,282	47,102		647,102	198,718		198,718
Go Higher Grant Program	190,270	28,772		238,263	19,221		19,221
Pharmacy Scholarship Program	253,800			1,047	(252,753)		(252,753)
Kentucky Coal County College Completion Scholarship	1,115,471	82,357		1,432,357	234,529		234,529
Drive the Dream Scholarship	525,580	32,911		532,911	(25,580)		(25,580)
John R. Justice Grant	96,934	24,275		186,222	65,013		65,013
Kentucky Education Savings Plan Trust		46,498		46,498	-		
Total Governmental Activities	200,831,603	1,889,023		212,016,301	9,295,675		9,295,675
Business-Type Activities:							
Loan guarantee operations	3,458,272		2,927,911			(530,361)	(530,361)
Default collections	5,275,384		23,756,772			18,481,388	18,481,388
Loan finance and servicing activities	47,120,468		58,709,087			11,588,619	11,588,619
Outreach	3,956,706		1,802,896			(2,153,810)	(2,153,810)
Contribution to student aid programs	881,705					(881,705)	(881,705)
Student aid administration	1,889,023					(1,889,023)	(1,889,023)
Contribution to FSLRF	5,500,000					(5,500,000)	(5,500,000)
School services	1,921,564		137,461			(1,784,103)	(1,784,103)
Other activities	(19,850)		(19,850)				
Total Business-Type Activities	69,983,272		87,314,277			17,331,005	17,331,005
Total Primary Government	$ 270,814,875	$ 1,889,023	$ 87,314,277	$ 212,016,301	9,295,675	17,331,005	26,626,680
Transfers:							
Transfer to KAPT (the "Plan")						(24,855)	(24,855)
Total Transfers						(24,855)	(24,855)
Change in Net position					9,295,675	17,306,150	26,601,825
Net position, July 1, 2012, as restated (Note T)					18,373,081	198,246,011	216,619,092
Net position, June 30, 2013					$ 27,668,756	$ 215,552,161	$ 243,220,917

Combined Statement of Net Position - Proprietary Funds

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation

June 30, 2013

	Authority			Corporation			Combined
ASSETS	**Internal Service Fund**	**Agency Operating Fund**	**Authority Total**	**Education Finance Funds**	**Operating Fund**	**Corporation Total**	**Total**
Current:							
Cash and cash equivalents	$ 2,529,971	$ 13,336,680	$ 15,866,651	$	$ 23,952,788	$ 23,952,788	$ 39,819,439
Investments		6,422,639	6,422,639		-	-	6,422,639
Accounts receivable and prepaid expenses	1,005,962	78,470	1,084,432	23,035	881,701	904,736	1,989,168
Accrued interest income		185,530	185,530	10,082,481	100,715	10,183,196	10,368,726
Loans, net				217,519,205	3,904,352	221,423,557	221,423,557
Total Current Assets	3,535,933	20,023,319	23,559,252	227,624,721	28,839,556	256,464,277	280,023,529
Noncurrent:							
Restricted cash and cash equivalents	500,795		500,795	76,613,572		76,613,572	77,114,367
Internal receivable (payable) for Gear Up Scholarships	(500,795)	500,795	-				-
Receivable from Federal Student Loan Reserve Fund		8,035,026	8,035,026				8,035,026
Investments		43,782,154	43,782,154		8,107,510	8,107,510	51,889,664
Fixed assets, net		8,499,974	8,499,974		285,525	285,525	8,785,499
Loans, net				1,088,105,276	22,144,912	1,110,250,188	1,110,250,188
Accrued interest income, net				12,583,509	266,270	12,849,779	12,849,779
Total Noncurrent Assets		60,817,949	60,817,949	1,177,302,357	30,804,217	1,208,106,574	1,268,924,523
Total Assets	3,535,933	80,841,268	84,377,201	1,404,927,078	59,643,773	1,464,570,851	1,548,948,052
LIABILITIES							
Current:							
Accounts payable and accrued expenses	1,117,367	422,835	1,540,202	531,113	3,401,139	3,932,252	5,472,454
Interfund payable (receivable)	2,418,566	(1,982,642)	435,924	(6,698,927)	6,263,003	(435,924)	-
Accrued interest expense		36,452	36,452	2,228,298	-	2,228,298	2,264,750
Payable (receivable) to U.S. Department of Education		(456,000)	(456,000)	9,839,022	108,204	9,947,226	9,491,226
Capital lease payable		525,000	525,000				525,000
Total Current Liabilities	3,535,933	(1,454,355)	2,081,578	5,899,506	9,772,346	15,671,852	17,753,430
Noncurrent:							
Capital lease payable		3,760,000	3,760,000				3,760,000
Allowance for arbitrage liabilities				94,840		94,840	94,840
Bonds payable				1,287,015,000		1,287,015,000	1,287,015,000
Total Noncurrent Liabilities		3,760,000	3,760,000	1,287,109,840	-	1,287,109,840	1,290,869,840
Total Liabilities	3,535,933	2,305,645	5,841,578	1,293,009,346	9,772,346	1,302,781,692	1,308,623,270
Deferred Inflows of Resources:							
Deferred gain on debt retirements, net				24,772,621		24,772,621	24,772,621
Total Liabilities and Deferred Inflows of Resources	3,535,933	2,305,645	5,841,578	1,317,781,967	9,772,346	1,327,554,313	1,333,395,891
NET POSITION							
Invested in capital assets, net		4,214,974	4,214,974		285,525	285,525	4,500,499
Unrestricted					43,585,902	43,585,902	43,585,902
Restricted, other				87,145,111	6,000,000	93,145,111	93,145,111
Restricted for student aid and related activities		74,320,649	74,320,649			-	74,320,649
Total Net Position	$ -	$ 78,535,623	$ 78,535,623	$ 87,145,111	$ 49,871,427	$ 137,016,538	$ 215,552,161

See accompanying notes

Combined Statement of Revenues, Expenditures and Changes
in Net Position - Proprietary Funds

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation

For Year Ending June 30, 2013

	Authority			Corporation			Combined
	Internal Service Fund	Agency Operating Fund	Authority Total	Education Finance Funds	Operating Fund	Corporation Total	Total
Operating revenues:							
Interest Revenues:							
Interest on loans	$	$	$	$ 31,469,556	$ 1,109,269	$ 32,578,825	$ 32,578,825
Interest and investment income		376,441	376,441	82,513	41,483	123,996	500,437
Amortization of deferred gain on debt retirements				18,465,693		18,465,693	18,465,693
Interest expense on bonds				(10,818,686)		(10,818,686)	(10,818,686)
Total net interest revenues		376,441	376,441	39,199,076	1,150,752	40,349,828	40,726,269
Financing Expenses:							
Provision for loan losses				1,329,952	(156,917)	1,173,035	1,173,035
Long-Term debt credit facility and remarketing fees				3,643,523		3,643,523	3,643,523
Debt issuance costs				3,158,628		3,158,628	3,158,628
Total financing expenses				8,132,103	(156,917)	7,975,186	7,975,186
Interest revenues net of financing expenses		376,441	376,441	31,066,973	1,307,669	32,374,642	32,751,083
Other Operating Revenues:							
Servicing fees from external sources					1,646,074	1,646,074	1,646,074
Servicing fees from Education Finance Funds					8,600,008	8,600,008	8,600,008
Conversion fees					1,000,000	1,000,000	1,000,000
SAFRA revenue					203,640	203,640	203,640
Debt recovery commission		23,756,772	23,756,772		159,960	159,960	23,916,732
Federal fees earned		1,921,685	1,921,685				1,921,685
Federal grant revenue		1,802,896	1,802,896				1,802,896
Default aversion fee income		629,785	629,785				629,785
Guarantee fee					195,426	195,426	195,426
Gain on early retirement of debt				4,718,437		4,718,437	4,718,437
Gain on sale/purchase of loans				149,464	3,770	153,234	153,234
Late payment penalties				1,509,542	36,555	1,546,097	1,546,097
School services		137,461	137,461				137,461
Other income	(19,850)		(19,850)		136,383	136,383	116,533
Total operating revenues	(19,850)	28,625,040	28,605,190	37,444,416	13,289,485	50,733,901	79,339,091
Operating Expenses:							
Administrative expenses	(142,864)	8,220,233	8,077,369		17,118,022	17,118,022	25,195,391
Servicing fees for Operating Fund				8,600,008		8,600,008	8,600,008
Depreciation and amortization		488,925	488,925		78,774	78,774	567,699
Other expenses	123,014	24,498	147,512	486,458	7,888,639	8,375,097	8,522,609
Total operating expenses	(19,850)	8,733,656	8,713,806	9,086,466	25,085,435	34,171,901	42,885,707
Net operating income (loss) before program benefits		19,891,384	19,891,384	28,357,950	(11,795,950)	16,562,000	36,453,384
Program Benefits:							
Principal and interest benefits				1,056,210	3,917,171	4,973,381	4,973,381
School Service		1,921,564	1,921,564				1,921,564
Outreach		3,956,706	3,956,706				3,956,706
Contribution to FSLRF		5,500,000	5,500,000				5,500,000
Contribution to student aid programs		881,705	881,705				881,705
Student aid administration		1,889,023	1,889,023				1,889,023
Total program benefits		14,148,998	14,148,998	1,056,210	3,917,171	4,973,381	19,122,379
Operating income (loss) before transfers		5,742,386	5,742,386	27,301,740	(15,713,121)	11,588,619	17,331,005
Transfers (to) from other funds							
Interfund transfers		-	-	(8,208,505)	8,208,505	-	-
Transfer to KAPT (the "Plan")		(24,855)	(24,855)				(24,855)
Increase (decrease) in Net position after transfers		5,717,531	5,717,531	19,093,235	(7,504,616)	11,588,619	17,306,150
Net position, July 1, 2012, as restated (NoteT)		72,818,092	72,818,092	68,051,876	57,376,043	125,427,919	198,246,011
Net position, June 30, 2013	$	$ 78,535,623	$ 78,535,623	$ 87,145,111	$ 49,871,427	$ 137,016,538	$ 215,552,161

See accompaning notes

Combined Statement of Cash Flows - Proprietary Fund

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation

For Year Ending June 30, 2013

	Authority			Corporation			Combined
	Internal Service Fund	Agency Operating Fund	Authority Total	Education Finance Funds	Operating Fund	Corporation Total	Total
Cash Flows from Operating Activities:							
Principal received on loans	$	$	$	$ 209,971,735	$ 8,030,592	$ 218,002,327	$ 218,002,327
Interest received on loans				45,784,934	1,752,928	47,537,862	47,537,862
Special allowance paid				(31,104,127)	(825,368)	(31,929,495)	(31,929,495)
Servicing fees received, internal sources	(19,850)	(498,851)	(518,701)	(8,600,008)	8,600,008	-	(518,701)
School services fees received		137,461	137,461				137,461
Servicing fees received, external sources				-	2,424,092	2,424,092	2,424,092
Debt recovery commission received		23,756,772	23,756,772		30,497	30,497	23,787,269
Federal fees received		1,921,685	1,921,685				1,921,685
Federal grant revenue received		1,802,896	1,802,896				1,802,896
Default aversion fees received		629,785	629,785				629,785
Outreach		(3,956,706)	(3,956,706)				(3,956,706)
School services		(1,921,564)	(1,921,564)				(1,921,564)
SARFA revenue received					(1,216)	(1,216)	(1,216)
Internal activity-payments to other funds	(560,048)	560,048	-	646,081	(646,081)	-	-
Loans originated, including costs				5,826	(7,885,116)	(7,879,290)	(7,879,290)
Administrative expenses paid		(5,756,462)	(5,756,462)	(5,753,367)	(33,098,634)	(38,852,001)	(44,608,463)
Contribution to FSLRF		(5,500,000)	(5,500,000)				(5,500,000)
Credit facility fees paid				(3,643,820)		(3,643,820)	(3,643,820)
Loans purchased, including premiums				(12,094,868)	(25,082,992)	(37,177,860)	(37,177,860)
Contribution to student aid programs		(881,705)	(881,705)				(881,705)
Student aid administration		(1,889,023)	(1,889,023)	-	-	-	(1,889,023)
Interfund loan sales and purchases				(34,920,153)	34,920,153	-	-
Client loan receipts				-	4,746,576	4,746,576	4,746,576
Loan receipts remitted to clients					(4,951,134)	(4,951,134)	(4,951,134)
Net Cash Provided by (Used in) Operating Activities	(579,898)	8,404,336	7,824,438	160,292,233	(11,985,695)	148,306,538	156,130,976
Cash Paid from Noncapital Financing Activities:							
Proceeds from debt issued				563,800,000	-	563,800,000	563,800,000
Debt principal payments				(746,235,654)	-	(746,235,654)	(746,235,654)
Principal received on loans PUT to USDE				27,402,494		27,402,494	27,402,494
Interest on debt				(12,253,234)		(12,253,234)	(12,253,234)
Debt issuance costs				(3,158,628)		(3,158,628)	(3,158,628)
Gain on early retirement of debt				4,718,437		4,718,437	4,718,437
Interfund transfers				(8,208,505)	8,208,505	-	-
Transfer to KAPT (the "Plan")		(24,855)	(24,855)	-			(24,855)
Increase in Federal Student Loan Reserve receivable		2,188,523	2,188,523				2,188,523
Net Cash Provided by (Used in) Noncapital Financing Activities		2,163,668	2,163,668	(173,935,090)	8,208,505	(165,726,585)	(163,562,917)
Cash Flows From Capital and Related Financing Activities:							
Capital expenditures		(407,620)	(407,620)		(204,507)	(204,507)	(612,127)
Debt Issuance costs		(67,512)	(67,512)				(67,512)
Interest paid on capital lease		(4,144)	(4,144)				(4,144)
Bond principal payments		(500,000)	(500,000)				(500,000)
Net Cash Used in Capital and Related Financing Activities		(979,276)	(979,276)		(204,507)	(204,507)	(1,183,783)
Cash Flows From Investing Activities:							
Proceeds from sales/maturities of investments		27,088,242	27,088,242		4,096,288	4,096,288	31,184,530
Purchases of investments		(46,767,455)	(46,767,455)		(4,222,296)	(4,222,296)	(50,989,751)
Investment income		589,505	589,505	86,756	77,488	164,244	753,749
Net Cash Provided by (Used in) Investing Activities		(19,089,708)	(19,089,708)	86,756	(48,520)	38,236	(19,051,472)
Net Increases (Decrease) in Cash and Cash Equivalents	(579,898)	(9,500,980)	(10,080,878)	(13,556,101)	(4,030,217)	(17,586,318)	(27,667,196)
Cash and Cash Equivalents, July 1, 2012	3,610,664	22,837,660	26,448,324	90,169,673	27,983,005	118,152,678	144,601,002

See accompanying notes

Combined Statement of Cash Flows - Proprietary Fund

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation

For Year Ending June 30, 2013

	Authority			Corporation			Combined
	Internal Service Fund	Agency Operating Fund	Authority Total	Education Finance Funds	Operating Fund	Corporation Total	Total
Cash and Cash Equivalents, June 30, 2013	$ 3,030,766	$ 13,336,680	$ 16,367,446	$ 76,613,572	$ 23,952,788	$ 100,566,360	$ 116,933,806
Reconciliation of Operating Income to Net Cash Provided by (Used in) Operating Activities							
Operating income (loss) before transfers	$	$ 5,742,386	$ 5,742,386	$ 27,301,740	$ (15,713,121)	$ 11,588,619	$ 17,331,005
Adjustments to reconcile operating income to net cash provided by (used in) operating activities:							
Investment income		(376,441)	(376,441)	(86,756)	(45,189)	(131,945)	(508,386)
Depreciation and amortization		873,973	873,973	3,158,628	78,774	3,237,402	4,111,375
Amortization of deferred gain on debt retirements				(18,465,693)		(18,465,693)	(18,465,693)
Gain on early retirement of debt				(4,718,437)		(4,718,437)	(4,718,437)
Interest expense		4,144	4,144	10,818,686	-	10,818,686	10,822,830
Provision for loan losses				1,329,952	(156,917)	1,173,035	1,173,035
Borrower interest converted to principal				(28,540,366)	(506,289)	(29,046,655)	(29,046,655)
Loan forgiveness				1,056,210	7,990	1,064,200	1,064,200
Loss on equipment disposal			0		(8,622)	(8,622)	(8,622)
(Increases) decreases in assets:							
Accounts receivables and prepaid expenses	922,171	(558,278)	363,893	47,171	(495,496)	(448,325)	(84,432)
Accrued interest receivable		59,427	59,427	4,535,844	279,853	4,815,697	4,875,124
Principal received on loans				209,971,736	8,030,592	218,002,328	218,002,328
Loans purchased, including premiums				(12,094,868)	(25,082,992)	(37,177,860)	(37,177,860)
Loans originated, including costs				5,826	(7,885,116)	(7,879,290)	(7,879,290)
Interfund loan sales and purchases				(34,920,153)	34,920,153	-	-
Increases (decreases) in liabilities:							
Accounts payable and accrued expenses	13,915	876,696	890,611	(348,710)	(4,281,717)	(4,630,427)	(3,739,816)
Payable to U.S. Department of Education				715,713	(210,928)	504,785	504,785
Interfund receivable/payable	(1,515,984)	1,786,573	270,589	646,081	(916,670)	(270,589)	-
Accrued interest payable		(4,144)	(4,144)				(4,144)
Allowance for arbitrage liabilities				(120,371)		(120,371)	(120,371)
Net Cash Provided by (Used in) Operating Activities	$ (579,898)	$ 8,404,336	$ 7,824,438	$ 160,292,233	$ (11,985,695)	$ 148,306,538	$ 156,130,976

Balance Sheet - Governmental Fund

Kentucky Higher Education Assistance Authority

June 30, 2013

ASSETS	Governmental Fund Student Aid
Current:	
Cash and cash equivalents	$ 2,676,169
Accounts receivable	16,456,476
Teacher and Osteopathic Medicine scholarship loans	450,000
Total Current Assets	19,582,645
Noncurrent:	
Teacher and Osteopathic Medicine scholarship loans, net of allowance of $3,600,000	4,648,108
Teacher and Osteopathic Medicine scholarship advances	3,728,902
Total Noncurrent Assets	8,377,010
Total Assets	27,959,655
LIABILITIES	
Current:	
Accounts payable	290,899
Total Liabilities	290,899
FUND BALANCE	
Restricted for program benefits	$ 27,668,756

See accompanying notes

Statement of Revenues, Expenditures and Changes
in Fund Balance - Governmental Fund

Kentucky Higher Education Assistance Authority

For Year Ending June 30, 2013

	Governmental Fund
	Student Aid
Revenues:	
Interest and investment income fund	$ 755,271
Tobacco settlement revenue	1,099,805
Unclaimed lottery revenue	10,600,000
State General Fund revenue	195,437,075
Federal funds revenue	161,947
Other income	1,191,475
Contribution from Agency Operating Fund	2,770,728
Total Revenues	212,016,301
Expenditures:	
Kentucky Tuition Grant	30,074,117
College Access Program Grant	57,549,144
Mary Jo Young Scholarship	497,020
Early Childhood Development Scholarship	906,695
Kentucky National Guard Tuition Award Program	4,670,292
Kentucky Educational Excellence Scholarship	102,759,512
Teacher Scholarship	1,376,372
Teacher Loan Forgiveness	1,400,000
Osteopathic Medicine Scholarship	642,222
Pharmacy Scholarship Program	253,800
KHEAA Work Study Program	448,384
Go Higher Grant Program	219,042
Drive the Dream Scholarship	558,491
Kentucky Coal County College Completion Scholarship	1,197,828
John R. Justice Grant	121,209
Kentucky Education Savings Plan Trust	46,498
Total Expenditures	202,720,626
Net Change in Fund Balance	9,295,675
Fund Balance, July 1, 2012	18,373,081
Fund Balance, June 30, 2013	$ 27,668,756

See accompanying notes

Statement of Fiduciary Net Position (Deficit)

Kentucky Higher Education Assistance Authority

June 30, 2013

ASSETS	**Federal Student Loan Reserve Fund**	**Kentucky's Affordable Prepaid Tuition**	**Kentucky Education Savings Plan Trust**
Current:			
Cash and cash equivalents	$ 11,046,290	$ 1,895,451	$ 30
Contributions receivable		977,011	
Fees receivable		192,212	
Receivable from U.S. Department of Education	9,490,769		
Investments		113,332,787	152,638,031
Other current assets	4,930		124,553
Total Current Assets	20,541,989	116,397,461	152,762,614
Noncurrent:			
Contributions receivable		2,684,987	
Total Assets	20,541,989	119,082,448	152,762,614
LIABILITIES			
Current:			
Accounts payable	120,887	70,578	124,550
Accrued expenses			49,019
Current portion of reinsurance reserve	487,597		
Total Current Liabilities	608,484	70,578	173,569
Noncurrent:			
Reinsurance reserve, less current portion	3,496,362		
Payable to Agency Operating Fund	8,035,027		
Tuition benefits payable		171,914,895	
Total Liabilities	12,139,873	171,985,473	173,569
NET POSITION (DEFICIT)			
Restricted for program benefits		(52,903,025)	152,589,045
Restricted for other purposes	8,402,116		
Total Net Position (Deficit)	$ 8,402,116	$ (52,903,025)	$ 152,589,045

Statement of Changes in Fiduciary Net Position (Deficit)

Kentucky Higher Education Assistance Authority

For Year Ending June 30, 2013

	Federal Student Loan Reserve Fund	Kentucky's Affordable Prepaid Tuition	Kentucky Education Savings Plan Trust
Additions:			
Federal reinsurance	$ 95,392,394	$	$
Contribution from Agency Operating Fund	5,500,000		
Fee revenue	-		
Contract income, net		310,439	
Subscriptions			47,998,799
Investment Revenues:			
Net unrealized gain on investments		4,906,528	8,962,662
Interest and investment income	1,080	7,952,461	2,539,901
Other income	2,747,959		
Total Additions	103,641,433	13,169,428	59,501,362
Deductions:			
Program benefits:			
Loan claims	100,976,457		
Default aversion fee expense	629,785		
Redemptions			42,872,623
Administrative expenses		51,150	611,036
Personnel and professional expenses		374,297	
Refunds		948,279	
Trustee fee expense		319,566	
Tuition benefits expense, net		9,898,664	
Total Deductions	101,606,242	11,591,956	43,483,659
Change in Net Position before Transfers	2,035,191	1,577,472	16,017,703
Transfer from Agency Operating Fund		24,855	
Change in Net Position	2,035,191	1,602,327	16,017,703
Net Position (Deficit), July 1, 2012	6,366,925	(54,505,352)	136,571,342
Net Position (Deficit), June 30, 2013	$ 8,402,116	$ (52,903,025)	$ 152,589,045

Note A--Description of Business

The Kentucky Higher Education Assistance Authority (the “Authority”) was established in 1966 as the Commonwealth of Kentucky’s agency for improving higher education opportunities. The Authority guarantees loans, performs default aversion activities and performs collection activities on eligible student loans. The Kentucky Educational Savings Plan Trust (the “Trust”), and the Commonwealth Postsecondary Education Prepaid Trust Fund, Kentucky’s Affordable Prepaid Tuition Plan (the “Plan”) offer savings and investment opportunities for Kentuckians to save for higher education. The Kentucky Higher Education Student Loan Corporation (the “Corporation”) makes student loans directly to parents and students as part of the Kentucky Advantage Education Loan Program (“KAEL”), which includes the Kentucky Advantage Parent Loan. The Corporation also purchases, services and performs collection activities on eligible education loans. The Authority and the Corporation maintain bundled operations to maximize the efficiency of loan guarantee and servicing operations. Accordingly, all senior management positions have responsibilities related to both the Authority and the Corporation. Additionally, the Plan and the Trust are governed by the Authority and Corporation’s combined Board of Directors. Throughout the accompanying financial statements, the “Authority/Corporation” refers to the combined group of operations.

The Health Care and Education Reconciliation Act (“HCERA”) of 2010 was signed into law on March 30, 2010. HCERA eliminated the origination and/or guarantee of Federal Family Education Loan Program (“FFELP”) loans, effective July 1, 2010. HCERA did allow lenders to make subsequent disbursements on loans originated on or before June 30, 2010. The Authority/Corporation can no longer originate, guarantee or fund any new FFELP loans. However, the Authority/Corporation continues to operate under existing FFELP regulations for loans originated and guaranteed prior to July 1, 2010.

HCERA does provide for servicing opportunities for qualified nonprofit organizations to service an initial allocation of 100,000 federal loan borrowers. The Corporation received their initial allotment of loans in the fall of 2012. The Corporation is currently partnering with another U.S. Department of Education (“USDE”) federal loan servicer to service these loans (see Note R).

Loan Guarantee Operations

The Authority/Corporation’s loan guarantee operations guarantees existing FFELP loans to qualified students and parents of qualified students made by approved lenders in Kentucky and Alabama. Commencing in 1969, retroactive to 1965, the federal government agreed to insure 80% of such guarantee student loans. FFELP was established by Congress and is administered by the USDE as a means of making loans available to students attending colleges, universities and vocational institutions. FFELP provides for the Authority/Corporation’s loan guarantee operations to guarantee the repayment of principal and accrued interest to lenders for each eligible student loan. The Authority/Corporation’s loan guarantee operation is responsible for maintaining loan guarantees, providing default aversion assistance to lenders for delinquent loans, paying lender claims for loans in default, paying lender claims for death, disability or bankruptcy and collecting loans on which default claims have been paid. The Authority/Corporation also educates lenders about FFELP requirements and regulatory changes.

Note A--Description of Business--Continued

Effective January 10, 1977, the Authority/Corporation's loan guarantee operation entered into a supplemental guaranty agreement with the federal government, which provided up to 100% reimbursement, depending upon default experience as specified in the agreement. Subsequently, federal reinsurance on guaranteed loans made from October 1, 1993 to September 30, 1998 was reduced to a maximum of 98% and federal reinsurance on guaranteed loans made on or after October 1, 1998, was reduced to a maximum of 95% (see Note E).

The Higher Education Amendments of 1998 (the "1998 Amendments") which were enacted on October 7, 1998, with an effective date of October 1, 1998, changed the manner in which FFELP is administered. Under the 1998 Amendments, the Authority/Corporation established a Federal Student Loan Reserve Fund (the "FSLRF") and an Agency Operating Fund (the "AOF") to account for all FFELP guarantee activities. The FSLRF assets and all earnings on those assets (except investment income on the 1998 Balance Budget Act set-aside funds) are the property of the federal government.

The guarantee reserves of the Authority/Corporation were required to be deposited in the new Federal Fund no later than 60 days after enactment. The result of this federal legislation was that the Authority/Corporation's guarantee reserve fund equity of approximately $40.6 million was transferred to the newly established FSLRF and the Authority/Corporation's AOF commenced activities with a zero fund equity. The funds in the newly established FSLRF were used to pay for the reimbursements to the lenders for student loan claims and pay the AOF for default aversion fees, Account Maintenance Fee shortfall and any U.S. Treasury recall amounts. Funds used to pay loan claims are mostly replenished from reimbursements from the federal government.

Other sources of revenues to the FSLRF include the federal compliment on collections of defaulted loans and investment income. All of the other sources and uses of funds not related to the FSLRF are recorded in the AOF. The AOF assets and earnings on those assets are the property of the Authority/Corporation and may generally be used for all guaranty agency and other student financial aid related activities.

Sources of funds to the AOF include investment income, agency retention on collections of defaulted loans, default aversion fees and account maintenance fees.

Expenditures from the AOF include personnel, professional and other administrative expenses directly related to the loan program operations and outreach activities. The AOF provides funding to the governmental fund to pay administration costs for fifteen student aid programs, administrative costs for the Trust, and direct benefits for the Mary Jo Young Scholarship program. The AOF also transfers funds to the Plan to pay some of the Plan's administration costs. Both the FSLRF and AOF are subject to federal oversight.

Note A--Description of Business--Continued

Loan Finance and Servicing Operations

The Corporation is an independent *de jure* municipal corporation established by the Kentucky General Assembly in 1978 to provide a loan finance program for post-secondary students in the Commonwealth of Kentucky. The Corporation is authorized to finance loans for students attending eligible post-secondary institutions, service and collect education loans, and issue bonds and notes not to exceed $5 billion in order to carry out its corporate powers and duties.

The Authority/Corporation's finance, servicing and collection activities include: (i) the origination and acquisition of education loans; (ii) the financing of FFELP and KAEL loans; (iii) the servicing of FFELP and other education loans; and (iv) the collection of FFELP and other education loans for other holders on a commission or cost reimbursement basis. FFELP student loans held, serviced and collected by the Authority/Corporation include Federal Stafford Loans ("Stafford"), Unsubsidized Stafford Loans ("Unsubsidized Stafford"), Federal Supplemental Loans for Students ("SLS"), Federal Parent Loans for Undergraduate Students ("PLUS") and Federal Consolidation Loans ("Consolidations").

Most FFELP loans held by the Authority/Corporation are insured by a guarantee agency. Loans made prior to October 1, 1993, are 100% insured. Loans made between October 1, 1993 and June 30, 2006, are 100% insured against borrowers' death, disability, or bankruptcy and 98% insured against borrowers' default. Loans made after June 30, 2006, are 100% insured against borrowers' death, disability, or bankruptcy and 97% insured against borrowers' default. KAEL loans are self-insured by the Authority/Corporation. KAEL borrowers are charged a guarantee fee at the time their loan is originated to fund any future losses on defaulted KAEL loans.

The Authority/Corporation's General Bond Resolution ("GBR"), Indentures, and separate series resolutions for issuance of revenue bonds and notes payable contain provisions establishing funds and accounts for the segregation of assets and provisions restricting the use of the proceeds of bonds and other funds received.

Note A--Description of Business--Continued

As of June 30, 2013 the Authority/Corporation held and serviced approximately $1.34 billion outstanding principal amount of FFELP and other education loans. $1.31 billion of loans were pledged pursuant to the 1997 GBR, the 2008 Indenture, the 2010 Indenture, and the 2013-1 Indenture. The remaining $29 million of loans were funded by the Corporation's Operating Fund. Also, the Authority/Corporation services approximately $20 million of FFELP and other education loans on behalf of other holders, including a holder with national lending operations. The majority of such education loans are serviced by the Authority/Corporation pursuant to servicing agreements which do not provide for the acquisition by the Authority/Corporation of the education loans serviced. As a servicer of FFELP and other education loans, the Authority/Corporation collects student loan remittances and subsequently disburses these remittances to the appropriate lending entities. The Authority/Corporation's obligations pursuant to such servicing and collection agreements are without recourse to assets pledged to collateralize any Authority/Corporation financings.

In addition to operations related to FFELP program, the Authority/Corporation administers the Trust, the Plan and fifteen grant and scholarship programs.

Kentucky Educational Savings Plan Trust

The Trust was formed on July 15, 1988 by Kentucky law, to help families save for the costs of education after high school. The Trust is administered by the Board of Directors. The Authority/Corporation has contracted with TIAA-CREF Tuition Financing, Inc. ("TFI"), a wholly-owned subsidiary of Teachers Insurance and Annuity Association of America ("TIAA"), for management services over the Trust's operations. The Trust is operated in a manner such that it is exempt from registration as an investment company under the Investment Company Act of 1940.

An individual participating in the Trust establishes an account in the name of a Beneficiary. Contributions can be made among six investment options: the Managed Allocation Option, the Fixed Income Option, the Balanced Option, Equity Index Option, Active Equity Option and the Guaranteed Option.

Contributions in the Managed Allocation Option are allocated among six age bands, based on the age of the beneficiary. Each age band invests in varying percentages in the Institutional Class of the International Equity, International Equity Index, Large-Cap Value Index, Large-Cap Growth Index, S&P 500 Index, Mid-Cap Growth, Small-Cap Equity, Mid-Cap Value, Short-Term Bond, Bond Index, Large-Cap Growth, Inflation-Linked Bond, Equity Index, Small-Cap Blend Index, Bond, Large-Cap Value Index, Real Estate Securities, Emerging Market Equity, Emerging Market Equity Index and Money Market Funds of the TIAA-CREF Institutional Mutual Funds.

The Equity Options invests in varying percentages in the Institutional Class of the International Equity and Growth & Income Funds of the TIAA-CREF Institutional Mutual Funds.

The Guaranteed Option is contractually obligated to pay a minimum rate of return of 1%.

Note A--Description of Business--Continued

All allocation percentages are determined by the Authority/Corporation's Board of Directors and are subject to change. The assets of the Guaranteed Option are allocated to a funding agreement issued by TIAA-CREF Life Insurance Company, a subsidiary of TIAA, which offers a guarantee of principal and a minimum rate of return to the Trust.

Prepaid Tuition Plan

The Authority/Corporation also administers the Plan, which was created by the 2000 Kentucky General Assembly and is governed under Kentucky Revised Statutes ("KRS") 164A.700-709.

On July 1, 2005, governance of the Plan permanently transferred to the Authority/Corporation. The Plan was established to provide families with an opportunity to save for future postsecondary education expenses. The Plan investment strategy is to earn rates of return that exceed anticipated tuition inflation rates so that the Plan is able to meet its obligation to pay benefits at future tuition rates. The Plan offered enrollment periods in fiscal years 2002, 2003 and 2005, for purchasers to buy prepaid tuition contracts. The Plan offers certain federal and state tax advantages to purchasers. There have been no enrollment periods since fiscal year 2005 as the Plan currently maintains an accumulated net deficit of approximately $52.9 million.

Participants purchased annual tuition units at current tuition levels, or current tuition levels plus a premium, and receive benefits equal to tuition rates in place at the time that the student attends a qualified postsecondary education institution. The Plan offers three tuition plans – the Value Plan, the Standard Plan and the Premium Plan. In the Value Plan, participants buy tuition units and receive benefits indexed to the tuition rate of the Kentucky Community and Technical College System. The Standard Plan offers tuition units and benefits indexed to the tuition rate of Kentucky's most expensive public university. The Premium Plan offers tuition units at the current average tuition cost of Kentucky's private colleges and universities and guarantees a return on a participant's investment equal to the tuition inflation rate for the University of Kentucky.

Participants were allowed to elect to spread payments to the Plan over three, five or seven years or until the anticipated year of the student's enrollment in a qualified postsecondary education institution.

Participants may use Plan benefits for eligible educational expenses at any eligible public or private vocational school, college or university in the United States.

If a beneficiary attends an eligible educational institution with tuition rates in excess of Plan benefits, the Plan will not be responsible for the difference. If a beneficiary attends an eligible educational institution with tuition rates less than Plan benefits, participants may use the difference for other qualified educational expenses such as room, board, books and supplies.

Note A--Description of Business--Continued

Participants may withdraw from the Plan at any time for any reason. Terminating participants are refunded any contract payments made less benefits received, administrative and cancellation fees. Participants who withdraw after July 1 of the beneficiary's college entrance year receive the tuition payout value of the contract less benefits received, administrative and cancellation fees. Non-qualified withdrawals are subject to a 10% penalty in accordance with Section 529 of the Internal Revenue Code ("IRC") except in cases where the withdrawal is: (i) made on account of the death or disability of the student; (ii) made on account of a scholarship received by a student; or (iii) a non-taxable transfer to another account or to another IRC Section 529 program for a different student who is a family member of the original student.

As of June 30, 2013, the Plan maintained an accumulated net deficit of approximately $52.9 million. Based on actuarial estimates, the Plan's assets will be exhausted in fiscal year 2020, at which time the liability of the Plan becomes a General Obligation of the Commonwealth of Kentucky. Per KRS 164A.708, once a real liability is expected to accrue, the General Assembly shall appropriate the necessary funds to meet the liability. Over the remaining estimated life of the program, through fiscal year 2032, actuarial estimates show the Commonwealth of Kentucky will need to transfer approximately $95 million.

Student Aid Programs

The Authority/Corporation provides administration of fifteen student aid programs: (1) the Kentucky Tuition Grant program, (2) College Access Program grant, (3) Kentucky Educational Excellence Scholarship program, (4) Teacher Scholarship program, (5) Osteopathic Medicine Scholarship program, (6) the KHEAA Work-Study program, (7) Kentucky Coal County College Completion Scholarship, (8) Early Childhood Development Scholarship program, (9) the Go Higher Grant program, (10) the Coal County Scholarship for Pharmacy Students program, (11) the Mary Jo Young Scholarship program, (12) John R. Justice grant, (13) the Drive the Dream Scholarship program, (14) the Kentucky National Guard Tuition Award program, and (15) the Minority Educator Recruitment and Retention Scholarship program. Direct benefits for grant, scholarship, and work-study programs are funded by appropriations from the Kentucky General Assembly, federal grants, funding from the Authority/Corporation, allocation of revenues from the Kentucky Lottery Corporation, Coal Severance Tax and Tobacco Settlement funds.

Note B--Summary of Significant Accounting Policies

Basis of Presentation - The Authority/Corporation reports its financial information in accordance with the Government Accounting Standard Board ("GASB") Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis – for State and Local Governments* as amended by GASB No. 37 and modified by GASB No. 38, *Certain Financial Statement Disclosures*, (collectively "GASB No. 34"). The Authority/Corporation's basic financial statements are prepared in accordance with GASB No. 34 and are comprised of the following three components: 1) government-wide financial statements; 2) fund financial statements, and 3) notes to financial statements. The government-wide financial statements are comprised of a statement of net assets and a statement of activities. Prepared using the economic resources measurement focus and the accrual basis of accounting, these statements reflect all of the assets, liabilities, deferred inflows of resources, deferred outflows of resources, revenues, expenses, gains and losses of the combined Authority/Corporation's governmental and business-type activities. The Authority/Corporation's governmental activities reflect the activities of administering the various student grant, scholarship, advance/loan and work-study programs for the Commonwealth of Kentucky and the Federal Government.

The Authority/Corporation's business-type activities include administering loan guarantees, default collection, borrower assistance, loan finance and servicing, student aid administration and contributions, and other activities.

Also included in the business-type activities are funds related to the Student Aid and Fiscal Responsibility Act ("SAFRA"). SAFRA provides payments to federal student loan servicers operating in FFELP on January 1, 2010 to retain jobs at locations in the United States. Assets related to SAFRA are held by the Authority/Corporation and transferred to the Operating Fund quarterly to offset permissible job retention related costs. All SAFRA funds must be expended on or before September 30, 2012. As of September 30, 2012 all SAFRA funds except for $1,216 were utilized for allowable job retention related costs. The $1,216 was remitted back to the USDE prior to September 30, 2012.

The combined government-wide financial statements do not reflect fiduciary activities whose resources are not available to finance the Authority/Corporation's programs.

The Authority/Corporation's combined fund financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America applicable to state government entities, which provide that accounting systems be organized by funds to account for specific activities consistent with legal and operating requirements. The Authority/Corporation's governmental fund includes the activities of administering grant, scholarship, advance/loan programs and the work-study program for the Commonwealth of Kentucky and the Federal Government.

The Authority/Corporation's loan guarantee, default collection, borrower assistance, loan finance and servicing, student aid administration and contributions, and other business-type activities are presented as proprietary funds. Proprietary funds also include internal service funds, which are used to report activity that provides goods or services on a cost reimbursement basis predominantly to the Authority/Corporation's other business-type activities. The Authority/Corporation follows all applicable GASB pronouncements

Note B--Summary of Significant Accounting Policies--Continued

Fiduciary activities include private-purpose trust and agency funds administered by the Authority/Corporation pursuant to FFELP, the Trust and the Plan. The fiduciary fund financial statements are comprised of a statement of net position and a statement of changes of net position. Prepared using the economic resources measurement focus and the accrual basis of accounting, these statements reflect all of the assets, liabilities, revenues, expenses, gains and losses of the FSLRF, the Trust and the Plan.

The Authority/Corporation's Fiduciary Funds are held in a custodial capacity. Assets of the Trust are held by the Authority/Corporation on behalf of program participants. Assets of the Plan are held by the Authority/Corporation to offset future tuition obligations of participants.

Cash and Cash Equivalents - The Authority/Corporation considers cash and cash equivalents to include highly liquid investments, which mature within one month or less of purchase.

Investments - Investments for all funds consist primarily of securities of the federal government or its agencies, corporate bonds, commercial paper collateralized mortgage obligations and mutual funds, which are stated at fair market value. Fair market value is determined by using quoted market prices as of the last day of the fiscal year.

The Plan maintains a separate investment policy with the current following target asset allocation:

Large Cap U.S. stocks	37%
Mid Cap U.S. stocks	6%
Small Cap U.S. stocks	5%
Non-U.S. stocks	9%
Total Equity	57%
Inflation indexed bonds	7%
Domestic fixed income	36%
Total Fixed Income	43%

Note B--Summary of Significant Accounting Policies--Continued

To decrease overall investment risk, the following restrictions apply to the Plan's investments:

i. No more than 5% of the total amount of the equity portion of the investment account in the securities of any one issuer;

ii. No more than 25% of the total amount of the equity portion of the investment account in any one industry, as defined by Standard & Poors;

iii. For portfolios invested in major-market countries, no more than 25% of the total amount of the equity portion of the investment account in any one country with the exception of those countries whose weighting in the Europe, Australia, and Far East ("EAFE") index is greater than 25%, where a maximum weight of the current country weight in the EAFE benchmark plus 10% is permitted;

iv. For portfolios invested in emerging markets, no more than 20% of the equity portion of the investment account shall be invested in one country;

v. A minimum of eight countries shall be represented in each investment account; and

vi. No more than 10% of the total amount of the fixed-income portion of the investment account shall be committed to the securities of any one issuer at the time of purchase, with the exception of securities issued or guaranteed by the full faith and credit of the United States of America or AAA-related securities issued by government agencies as to which there is no limit.

Under the Kentucky Revised Statutes, the Authority/Corporation's Board of Directors is charged with selecting the various options in which the participants of the Trust can invest their funds. An individual participating in the Trust establishes an account in the name of a Beneficiary. Contributions can be made among six investment options: the Managed Allocation Option, the Fixed Income Option, the Balanced Option, Equity Index Option, Active Equity Option and the Guaranteed Option.

Contributions in the Managed Allocation Option are allocated among six age bands, based on the age of the beneficiary. Each age band invests in varying percentages in the Institutional Class of the International Equity, International Equity Index, Large-Cap Value Index, Large-Cap Growth Index, S&P 500 Index, Mid-Cap Growth, Small-Cap Equity, Mid-Cap Value, Short-Term Bond, Bond Index, Large-Cap Growth, Inflation-Linked Bond, Equity Index, Small-Cap Blend Index, Bond, Large-Cap Value Index, Real Estate Securities, Emerging Market Equity, Emerging Market Equity Index and Money Market Funds of the TIAA-CREF Institutional Mutual Funds.

Teacher and Osteopathic Medicine Scholarship Loan and Advances - Teacher Scholarship advances to students may be repaid via eligible service credits granted for specified teaching in primary or secondary schools. The disbursements are recorded as advances and charged to program benefits over the period that the teaching service is performed. If the teaching requirements are not satisfied, the advances are converted to loans, which are repayable with interest.

Note B--Summary of Significant Accounting Policies--Continued

Osteopathic medicine scholarship advances to students may be repaid via eligible service credits granted for working as a doctor in Kentucky. The expenditures are recorded as advances and charged to program benefits over the period that the medical services are provided. If the medical requirements are not satisfied, the advances are converted to loans, which are repayable with interest.

Fixed Assets, Net - Fixed assets are stated at cost, less accumulated depreciation. Fixed assets are depreciated beginning when the assets are placed in service and continuing over the estimated useful lives of the respective asset using the straight-line method.

Defaulted Student Loans - All collections on defaulted loans are recorded as income when received. The portion of collections due to the federal government is treated as a contra-revenue. Federal defaulted loans outstanding are accounted for by the Authority/Corporation but are not presented on the accompanying combined statement of net assets.

Allowance for Uncollectible Loans - As discussed in Note A, most FFELP loans held by the Authority/Corporation are insured by guarantee agencies and the USDE. Management of the Authority/Corporation believes that all of the respective guarantee agencies and the USDE will be able to honor all loan claims submitted. However, the Authority/Corporation records a provision for loan losses based upon its expected default claims with respect to 98% and 97% insured loans and for loans with certain loan servicing violations. The allowance for loan loss on all loans funded through normal operations was $3.1 million for loan principal and $463,000 for accrued interest as of June 30, 2013. Furthermore, the Authority/Corporation is required to purchase loans owned by third party customers with certain loan servicing violations. As of June 30, 2013, the allowance for third party servicing loan losses for loans that have been purchased was $1.4 million for loan principal and $513,000 for accrued interest. In addition, the Authority/Corporation records a provision for loan loss related to Teacher and Osteopathic Medicine advances that have converted to loans. As of June 30, 2013, the allowance for advances converted to loans was $3.7 million.

Interest Income on Loans - The Authority/Corporation earns interest income on loans from the following three sources: (1) subsidized interest from USDE earned while certain students are in school, in grace or in deferment status; (2) special allowance from USDE (discussed in Note G); and (3) borrower interest. All interest is recorded when earned and is shown in the combined financial statements net of the interest related portion of the provision for loan losses.

Servicing Fees - The Authority/Corporation's fees for servicing loans held by third parties are recorded as servicing fee revenue when earned.

Third party loans serviced by the Authority/Corporation are not presented on the combined statement of net position, as they are not owned by the Authority/Corporation.

Note B--Summary of Significant Accounting Policies--Continued

Deferred Debt Issuance Costs - Debt issuance costs are expensed when incurred (see Note T).

Deferred Gain on Early Retirement of Debt - In accordance with GASB No. 23, *Accounting and Financial Reporting of Debt Reported by Proprietary Activities*, the Authority/Corporation defers any gains related to early retirement associated with a refinancing of debt over the shorter of the remaining life of the old debt or the life of the new debt.

Income Taxes - The Authority is a state government agency established by the Kentucky General Assembly and the Corporation is an independent *de jure* municipal corporation and political subdivision of the Commonwealth of Kentucky, therefore they are not subject to federal or state income taxes. The Trust and the Plan are state sponsored IRC Section 529 education savings plans and therefore, are also not subject to federal or state income taxes.

Use of Estimates - Generally Accepted Accounting Principles in the United States (“GAAP”) 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 combined financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Interfund Eliminations - Interfund receivables and payables are eliminated in the governmental and business-type activities column of the combined government-wide statement of net assets. Net residual amounts due between governmental and business-type activities are reflected as receivable (payable) for internal balances. Amounts reported in funds as receivable from or payables to fiduciary funds are reflected in the combined government-wide statement of net position. Eliminations are made in the combined government-wide statement of activities to remove the doubling-up effect of internal service fund activity.

Program Revenues - Program revenues are reported in two categories including (1) charges for services and (2) program-specific operating grants and contributions. Charges for services include revenues received in the form of fees and charges for the Authority/Corporation loan guarantee, default collection, interest income the corporate loan finance and servicing activities, and other activities.

Program-specific operating grants and contributions include revenues from mandatory and voluntary non-exchange transactions with other governments and organizations that are restricted for use in a particular program. Program-specific operating grant and contribution services include the interest earned on scholarship loans.

Note B--Summary of Significant Accounting Policies--Continued

Contribution Receivable - As discussed in Note A, participants in the Plan may elect to make payments on executed tuition contracts over a specific period. Contributions receivable are recorded at their net realizable value in the period in which a tuition contract is purchased. A finance charge of 7.25% per annum of the outstanding balance is charged to participants who enrolled in the Plan during fiscal year 2005.

Tuition Benefits and Other Payable **-** Tuition benefits payable are reported at the actuarial net present value of estimated future benefits to be paid on behalf of participants of the Plan. The reported amount reflects actuarial assumptions, including anticipated tuition and fee increases, expected investment earnings, and refunds and other terminations.

Indirect Costs **-** Indirect costs are allocated among functions/programs utilizing a full cost allocation approach with the objective of allocating all expenses to the Authority/Corporation's various functions and programs.

Risk Management - The Authority/Corporation is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries. Coverage against various risks of loss is obtained through participation in the State of Kentucky's Risk Management Fund, State Sponsored Group Insurance Fund, and policies purchased from outside insurance corporations.

Restricted Net Position - Restricted net position is comprised of net position with legal or contractual restrictions and thus cannot be used in operations of the Authority/Corporation.

Unrestricted Net Position - Unrestricted net position is comprised of net position available to be used in operations or transfers of the Authority/Corporation.

Subsequent Events - In preparing these combined financial statements, the Authority/Corporation has evaluated events and transactions for potential recognition or disclosure through the date of the Independent Auditor's Report which represents the date the financial statements were available to be issued. (See Note R.)

Note C--Cash and Investments

The Authority/Corporation has adopted provisions of GASB Statement No. 40, *Deposits and Investment Risk Disclosures*. This statement adds certain additional disclosures about cash and investments, including common areas of investment risk.

The Authority/Corporation's operating funds and investments comply with the Operating Funds Investment Policy. The policy permits investments in bank time deposits, certificates of deposit, commercial paper, asset-backed commercial paper, bankers acceptance and floating-rate notes with a coupon reset of 30 days or less, direct obligations of the United States of America (which are unconditionally guaranteed by the United States of America), indebtedness issued by certain Federal agencies, U.S. dollar denomination corporate bonds and obligations of foreign governments, asset-backed securities, and taxable and tax-exempt municipal bonds. All securities must have a minimum rating of investment grade BBB or better by a nationally recognized credit rating agency at the time of purchase. Money market instruments must be rated A-1 or P-1 or better at the time of purchase. An average rating of A must be maintained by the total portfolio.

The investments in the Authority/Corporation's Education Finance Funds comply with the underlying bond resolution and indenture requirements, as applicable. In accordance with those requirements, all deposits and investments meet the requirements and approval of bond underwriters and rating agencies. Additionally, such requirements mandate specific classes of investment vehicles including bank time deposits, certificates of deposit, direct obligations of the United States of America (which are unconditionally guaranteed by the United States of America), indebtedness issued by certain Federal agencies, collateralized repurchase agreements or investment funds secured by obligations of the United States of America with collateral held by or at the direction of the trustee.

Continued

Note C--Cash and Investments--Continued

Custodial Credit Risk and Interest Rate Risk - Custodial credit risk is the risk that in the event of a bank failure, the Authority/Corporation's deposits may not be returned to it. The Authority/Corporation's investment policy does not contain a requirement for the collateralization of cash and investments nor does it require investments to be maintained in the Authority/Corporation's name. As of June 30, 2013, Authority/Corporation's Proprietary Funds, Governmental Fund and Fiduciary Funds maintained cash on deposit is as follows:

Of the $118.1 million of cash and cash equivalents maintained in the Proprietary Funds, $16.5 million was held for guarantee operations and the remaining $101.6 million was held for loan finance and servicing activities.

As of June 30, 2013, the FSLRF maintained money market securities of $4 million held in a trust by Bank of New York Mellon.

	Governmental Fund Bank Balance	Proprietary Fund Bank Balance	Fiduciary Fund Bank Balance
FDIC Insured	$	$ 468,391	$ 502,795
Unisured		95,556	
Collateralized by securities held by the pledging financial institution		2,912,687	7,133,272
Money market demand deposits			
Money market securities		111,568,911	4,122,966
Cash deposited with Kentucky State Treasurer	2,683,639	3,030,766	44,549
	$ 2,683,639	$ 118,076,311	$ 11,803,582

Note C--Cash and Investments--Continued

As of June 30, 2013, all Proprietary Funds investments were registered in the Authority/Corporation's name and maintained by an external trustee. The investment balances as of June 30, 2013 are summarized as follows:

	Fair Value	Weighted Average Maturity (in years)
Corporate bonds	$ 26,543,918	2.50
U.S. Treasury and government agency securities	25,150,923	1.41
Collateralized mortgage obligations	6,617,462	8.82
	$ 58,312,303	

As of June 30, 2013, Trust investments of $152.6 million comprised entirely of TIAA mutual funds.

As of June 30, 2013, Plan investments of $113.3 million comprised primarily of mutual funds held by State Street Global Advisors.

Investments are made based upon prevailing market conditions at the time of the transaction with the intent to hold the instrument until maturity. If the yield of the portfolio can be improved upon sale of an investment, prior to its maturity, with the reinvestment of proceeds, then this provision is also allowed.

Concentration of Credit Risk **-** The Authority/Corporation does not maintain investments in any one issuer that represents 5% or more of the total investment base, excluding investments issued or explicitly guaranteed by the U.S government and investments in mutual funds.

Credit Risk - The Authority/Corporation's investment policy limits the credit risk for securities. Securities must have a credit rating of BBB by a nationally recognized credit rating agency. Money Market Securities must be rated A-1 or P-1 or better at the time of purchase. The investment manager is allowed to hold up to 5% in aggregate market value securities that have been downgraded below BBB, but must maintain an average rating of A for the total portfolio. The following table summarizes the Standard & Poors / Moody's rating (as applicable) for all corporate bonds held by the Authority/Corporation's Proprietary Funds as of June 30, 2013:

Note C--Cash and Investments--Continued

Rating	Fair Value
AAA / Aaa	$ 8,787,837
AA / Aa	3,003,084
A / A	7,618,426
BAA / Baa	7,134,571
	$ 26,543,918

The Plan maintains an investment policy that limits the credit risk for fixed income securities and short-term commercial paper. No more than 10% of the total amount of fixed-income portion of the investment account shall be committed to the securities of any one issuer at the time of purchase, with the exception of securities issued or guaranteed by the full faith and credit of the United States or AAA-rated securities issued by government agencies as to which there is no limit. The Plan may invest in short-term commercial paper of any domestic issuer, maturing within 9 months, with a minimum rating of A-1 by Standard & Poors or Prime 1 by Moody's. As previously noted, at June 30, 2013 the Plan primarily invested in mutual funds.

Note D--Fixed Assets

A summary of fixed assets follows:

	Beginning Balance July 1, 2012	Additions	Disposals	Ending Balance June 30, 2013
Proprietary fund:				
Furniture and equipment	$ 18,160,562	$ 522,171	$ (5,155,230)	$ 13,527,503
Building	11,986,200	86,207		12,072,407
System development	55,955			55,955
Student loan servicing	541,131			541,131
Debt recovery system	710,509	25,000		735,509
Accumulated depreciation and amortization	(22,404,671)	(884,934)	5,142,599	(18,147,006)
	$ 9,049,686	$ (251,556)	$ (12,631)	$ 8,785,499
Fiduciary Fund:				
Furniture and equipment	$ 487,243	$	$ (417,686)	$ 69,557
Accumulated depreciation	(487,243)		417,686	(69,557)
	$	$	$	$

Depreciation and amortization expense totaled $884,934 for the year ended June 30, 2013, of which $793,752 was allocated to business-type activities, $87,580 allocated to governmental activities, and $3,602 allocated to the fiduciary activities.

Depreciation and amortization expense was allocated to the business-type activities functions as follows:

	TOTAL
Loan guarantee operations	$ 616,213
Default collections	98,765
Loan finance and servicing	78,774
	$ 793,752

Note D--Fixed Assets--Continued

The Authority/Corporation has assets under capital lease agreements, as described in Note I, of $12,072,407 with related accumulated amortization of $4,084,898. Amortization of assets under capital lease is included in amortization expense in the accompanying combined financial statements. Amortization expense of assets under capital lease agreements was $400,977 for the year ended June 30, 2013.

Note E--Federal Family Education Loan Programs (Loan Guarantee Operations)

Pursuant to FFELP, the loan guarantee operating unit of Authority/Corporation insures eligible student loans for losses incurred from the default, death, disability, or bankruptcy and also insures for other losses such as school closures and false certifications. As of June 30, 2013, the outstanding balance of aggregate insured student loans was approximately $2.8 billion.

Loans insured by the Authority/Corporation are reinsured under FFELP by the federal government. Death, disability, bankruptcy, lender of last resort, and closed school claims are reinsured at 100%. Default claims are subject to the Authority/Corporation's default claims rate (reimbursed default claims for the federal fiscal year divided by the original principal amount of loans in repayment at the beginning of the fiscal year).

The Authority/Corporation's annual default claims rate is within the 5%, which allows for reimbursement rates at the highest level. Due to the reduction of the Federal reimbursement rate for loans made subsequent to October 1, 1993, the Authority/Corporation has recorded a reserve of $4.0 million at June 30, 2013 for losses on federal reinsurance.

The following schedule summarizes the reinsurance rates for guarantee agency paid default claims.

	Reimbursement Rate		
Annual Default Claims Rate	**Through September 30, 1993**	**October 1, 1993 through September 30, 1998**	**October 1, 1998 and After**
0% to 5%	100%	98%	95%
More than 5% up to 9%	90% of claims over 5% up to 9%	88% of claims over 5% up to 9%	85% of claims over 5% up to 9%
Over 9%	80% of claims over 9%	78% of claims over 9%	75% of claims over 9%

Note E--Federal Family Education Loan Programs (Loan Guarantee Operations)—Continued

The Authority/Corporation is entitled to charge certain fees associated with its reinsurance activities. A summary of those fees are as follows:

Rehabilitated Loans - The Authority/Corporation is entitled to retain 18.5% of principal and all accrued interest for rehabilitated loans, plus 18.5% of collection costs.

Consolidated Loans - For William D. Ford Consolidation, the Authority/Corporation is entitled to 10% collection costs (18.5% collected, less 8.5% rebate to USDE).

Recoveries Payable to Federal Government - The Authority/Corporation is entitled to retain 16% of defaulted loan collections received after October 1, 2007.

Account Maintenance Fees ("AMF") - The 1998 Amendments established an account maintenance fee based on 0.06% of the sum of net guarantees as of September 30. AMF is paid to the Authority/Corporation on a quarterly basis by the Federal government.

Default Aversion Fees ("DAF") - Default aversion fees were established under the 1998 Amendments. The Authority/Corporation receives DAF for its aversion activities on delinquent loans at the time lenders request default aversion assistance. DAF's are equal to 1% of principal and interest on the loan at the time the Authority/Corporation receives a request from a lender for preclaim assistance. DAF is recorded monthly and is recognized as a deduction in the FSLRF and as revenue in the AOF.

Note F--Loans (Finance and Servicing Operations)

The Authority/Corporation originates private supplemental loans, purchases loans and holds various types of student loans as described in Note A. The terms of these loans, which vary on an individual basis depending upon loan type and the date the loan was originated, generally provide for repayment in monthly installments of principal and interest over a period of up to thirty years for consolidation loans and generally up to ten years for other loans. The repayment period begins after a grace period of six months following graduation or loss of qualified student status for the Subsidized and Unsubsidized Stafford loans. The repayment period for Consolidation, SLS and PLUS loans begins within 60 days from the date the loan is fully disbursed. Statutory interest rates on student loans ranged from 1.79% to 10% for the fiscal year ended June 30, 2013 depending upon the type and date of origination of the individual loan. Actual rates may be lower due to interest rate reductions associated with payments via electronic funds transfer or for other reasons such as borrowers making a specified number of consecutive on-time payments.

Note F--Loans (Finance and Servicing Operations)--Continued

Loans consist of the following at June 30, 2013:

Stafford - Subsidized	$ 400,379,031
Stafford - Unsubsidized	430,167,098
PLUS/SLS	34,231,526
Consolidation	463,985,349
Other	13,048,348
Total gross loans	1,341,811,352
Allowance for loan losses	(4,502,547)
Loan rebate due to borrowers	(4,000,000)
Unamortized discount on purchase of loans	(1,635,060)
Loans, net	1,331,673,745
Less amount shown as current assets	221,423,557
Noncurrent loans, net	$ 1,110,250,188

All principal and accrued interest on FFELP student loans is insured against borrower death, disability, bankruptcy or default, as long as the Authority/Corporation performs all required loan servicing due diligence activities. As of June 30, 2013, $2,330,487 of student loans were no longer insured due to violations of due diligence requirements. Loan rebate due to borrowers represents the additional loan forgiveness described in Note H.

Prior to the elimination of FFELP, borrowers were required to pay certain origination fees to USDE, based on a percentage of the gross loan amount. These origination fees were typically withheld from the loan proceeds provided to the borrower and remitted to USDE on a quarterly basis. The Authority/Corporation sometimes elected to pay a portion or all of the origination fees on behalf of the borrower and therefore, would send the borrower an increased amount of loan proceeds, but was still required to remit the full amount of origination fees to USDE. All origination fees paid on behalf of the borrower, totaling $57,293,719, were capitalized as deferred origination costs and amortized over the estimated life of the loan. The remaining unamortized balance at June 30, 2012 of $6,498,189 was included in a restatement adjustment to the July 1, 2012 beginning Net Position (see Note T).

The Authority/Corporation was also required to pay to USDE certain lender fees. The amount of the lender fees was based on a certain percentage of the gross loan amount on all FFELP loans originated after October 1, 1993. Lender fees, totaling $22,500,643, were capitalized as deferred origination costs and amortized over the estimated life of the loan. The remaining unamortized balance at June 30, 2012 of $2,165,287 was included in a restatement adjustment to the July 1, 2012 beginning Net Position (see Note T).

Generally, all student loans in the Education Finance Funds of the Authority/Corporation are pledged as collateral for the various obligations of the Authority/Corporation.

Note G--Special Allowance

The Higher Education Act of 1965 provides for quarterly Special Allowance Payments to be made by USDE to holders of student loans to the extent necessary to ensure that they receive at least specified market interest rates of return. Certain FFELP loans disbursed during the period from January 1, 2000 through June 30, 2010 received special allowance at a rate based upon the average of the bond equivalent rates of the three-month commercial paper rate as reported by the U.S. Federal Reserve through March 31, 2012. Pursuant to a December 23, 2011, amendment to the Higher Education Act, the Authority/Corporation elected to change the index for special allowance calculations on its FFELP loans disbursed after January 1, 2000, from the three-month commercial paper (CP) rate to the one-month LIBOR index beginning on April 1, 2012. Other eligible loans receive special allowance based on the 91-day Treasury bill rates. The special allowance is accrued as either earned or payable, as applicable.

Note H--Loan and Other Forgiveness

During fiscal year 2012, the Authority/Corporation forgave $5.8 million in loan principal and accrued interest for teachers funded by USDE, and an additional $1.4 million in loan forgiveness for teachers funded by the Commonwealth of Kentucky. Also, during fiscal year 2013, the Authority/Corporation provided additional loan forgiveness of $1,064,200.

The Authority/Corporation’s Board of Directors approved $4 million of additional loan forgiveness for teachers, nurses and public service attorneys who were employed in the Commonwealth, which was accrued as of June 30, 2013 and is scheduled to be provided in the fall of 2013.

The Agency Operating Fund of the Authority/Corporation contributed $5,5 million to the Federal Student Loan Reserve Fund during fiscal year 2013. The contribution was facilitated through a $2.5 million reduction in the receivable/payable between the two funds with the remaining $3 million as a cash contribution.

Note I--Capital Lease Payable

On June 22, 2000, the Commonwealth of Kentucky, State Property and Building Commission (the “Commission”) issued $8,825,000 in bonds payable on behalf of the Authority/Corporation. The proceeds of the bonds are used to house the Authority/Corporation’s operations located in Frankfort, Kentucky. On October 8, 2003, the Commission issued additional bonds payable on behalf of the Authority/Corporation as a partial refunding of original bonds payable.

The original bonds had a final principal payment in May 2010. The new bonds bear interest at fixed rates which vary from 2.0% to 5.25% and have a maturity date of May 2020. The bonds are special and limited obligations of the Commission. The bonds do not constitute a debt, liability or obligation of the Commonwealth of Kentucky or a pledge of the full faith and credit or taxing power of the Commonwealth of Kentucky, but are payable solely from amounts derived from the biennially renewable lease agreement with the Authority/Corporation as described below. The bondholders have no security interest in any properties constituting the project or any amounts derived there from. The scheduled payments of principal and interest on the bonds are guaranteed under an insurance policy.

Note I--Capital Lease Payable--Continued

In connection with the issuance of the bonds, the Authority/Corporation entered into a financing/lease agreement with the Commission whereby the Authority/Corporation agreed to lease the newly constructed building. The Authority/Corporation renewed the lease for the biennium ending June 30, 2014 and has the right to renew for three additional two-year periods.

The Authority/Corporation can cancel the lease on the last business day in May immediately preceding the beginning of any renewal term.

The lease payments are equal to the debt service required by the bond indenture. In connection with the agreements, the Kentucky General Assembly appropriated sufficient spending authorization to the Authority/Corporation to pay the lease payments required through June 30, 2014. There can be no assurance to make rent payments past the two-year lease period.

A summary of the activity for the capital lease for the year ended June 30, 2013 is as follows:

	June 30, 2012	Additions	Payments	June 30, 2013
Capital Lease Payable	$ 4,785,000		$ 500,000	$ 4,285,000

Debt service requirements for the next five fiscal years and thereafter are as follows:

Year Ending June 30,	Principal	Interest
2014	$ 525,000	$ 219,905
2015	550,000	192,342
2016	580,000	164,592
2017	610,000	135,268
2018	640,000	103,663
Two Years Ending June 30,		
2019 - 2020	1,380,000	109,288
	$ 4,285,000	$ 925,058

Note J--Revenue Bonds and Notes Payable

The balance of revenue bonds and notes payable at June 30, 2013 and the related activity for the year ended June 30, 2013 is as follows:

Series		Scheduled Maturity	Interest Rate	Beginning Balance July 1, 2012	Bond Maturities & Refundings	New Issues	Ending Balance June 30, 2013
1997 General Bond Resolution							
1997 A-1		May 1, 2027	Every 35 days	$ 11,950,000	$	$	$ 11,950,000
1997 A-2		May 1, 2027	Every 35 days	36,550,000			36,550,000
1997 B	*	May 1, 2027	Every 35 days	23,900,000			23,900,000
1998 A-1		May 1, 2028	Every 28 days	36,400,000			36,400,000
1998 A-2		May 1, 2028	Every 28 days	36,400,000			36,400,000
1998 B	*	May 1, 2028	Every 35 days	42,150,000			42,150,000
1999 A		May 1, 2029	Every 28 days	39,900,000			39,900,000
1999 B	*	May 1, 2029	Every 35 days	23,550,000	(500,000)		23,050,000
2000 A-1		May 1, 2030	Every 28 days	23,500,000			23,500,000
2000 A-2		May 1, 2030	Every 28 days	36,100,000			36,100,000
2000 A-3		May 1, 2030	Every 35 days	38,950,000			38,950,000
2000 B	*	May 1, 2030	Every 35 days	3,750,000			3,750,000
2001 A-1		May 1, 2031	Every 35 days	47,400,000	(32,450,000)		14,950,000
2001 A-2		May 1, 2031	Every 35 days	47,350,000	(27,450,000)		19,900,000
2001 B	*	May 1, 2031	Every 35 days	-			-
2002 A-1		May 1, 2032	Every 28 days	31,600,000	(18,900,000)		12,700,000
2002 A-2		May 1, 2032	Every 35 days	20,150,000	(10,250,000)		9,900,000
2002 A-3	*	May 1, 2032	Every 35 days	36,600,000	(7,000,000)		29,600,000
2003 A-1	*	May 1, 2033	Every 35 days	20,400,000	(500,000)		19,900,000
				556,600,000			459,550,000
2008 Indenture							
2008 A-1	*	June 1, 2037	Weekly	124,060,000	(50,340,000)		73,720,000
2008 A-2	*	June 1, 2038	Weekly	63,525,000	(5,400,000)		58,125,000
2008 A-3		June 1, 2038	Weekly	33,985,000	(33,985,000)		-
				221,570,000			131,845,000
2010 Indenture							
2010 A-1	*	May 1, 2020	Quarterly	33,240,000	(19,985,000)		13,255,000
2010 A-2	*	May 1, 2034	Quarterly	135,660,000			135,660,000
				168,900,000			148,915,000
2013-1 Indenture							
2013-1		June 1, 2026	Monthly		(17,095,000)	563,800,000	546,705,000
ED Conduit Program							
		January 19, 2014	Weekly	522,380,654	(522,380,654)		
				$ 1,469,450,654	$ (746,235,654)	$ 563,800,000	$1,287,015,000

*This bond series is tax-exempt.

Note J--Revenue Bonds and Notes Payable--Continued

The Authority/Corporation's revenue bonds include variable rates of interest based on various index rates. Those variable rates ranged from 0% to 4.0% as of June 30, 2013.

Debt service requirements to maturity or redemption date, assuming interest rates based on variable index rates at June 30, 2013, are as follows:

	Principal Repayment Amount (Thousands)				
	97 GBR	2008 Indenture	2010 Indenture	2013-1 Indenture	Total
Year Ending June 30, 2014	$	$	$	$	$
4 Years Ending June 30, 2018					
5 Years Ending June 30, 2023			13,255		13,255
5 Years Ending June 30, 2028	187,350			546,705	734,055
5 Years Ending June 30, 2033	272,200				272,200
5 Years Ending June 30, 2038		131,845	135,660		267,505
	$ 459,550	$ 131,845	$ 148,915	$ 546,705	$1,287,015

	Interest Payments Amount (Thousands)				
	97 GBR	2008 Indenture	2010 Indenture	2013-1 Indenture	Total
Year Ending June 30, 2014	$ 5,310	$ 335	$ 2,201	$ 1,749	$ 9,595
Year Ending June 30, 2015	5,310	335	2,201	1,749	9,595
Year Ending June 30, 2016	5,310	335	2,201	1,749	9,595
Year Ending June 30, 2017	5,310	335	2,201	1,749	9,595
Year Ending June 30, 2018	5,310	335	2,201	1,749	9,595
5 Years Ending June 30, 2023	26,550	1,675	10,667	8,745	47,637
5 Years Ending June 30, 2028	25,762	1,675	10,445	5,247	43,129
5 Years Ending June 30, 2033	8,055	1,675	10,445		20,175
5 Years Ending June 30, 2038	0	1,488	2,089		3,577
	$ 86,917	$ 8,188	$ 44,651	$ 22,737	$ 162,493

Note J--Revenue Bonds and Notes Payable--Continued

The Authority/Corporation entered into an irrevocable direct pay Letter of Credit and Reimbursement Agreement ("LOC") with two banks relating to the Series 2008 Bonds in the amount of $300,000,000 issued on June 18, 2008. The LOC was issued in an amount (the "Original Stated Amount") equal to the sum of (i) the aggregate principal amount of the outstanding Series 2008A-1 Bonds and the Series 2008A-2 Bonds, plus an amount equal to 202 days of interest thereon at a rate of 14% per annum plus (ii) the aggregate principal amount of the outstanding Series 2008A-3 Bonds, plus an amount equal to 51 days of interest thereon at a rate of 18% per annum. The LOC had an original maturity date of June 17, 2011. The Authority/Corporation and the banks extended the Stated Expiration Date as defined in the LOC to October 14, 2011. On September 8, 2011, the Stated Expiration Date as defined in the LOC was extended to September 13, 2013. On February 19, 2013 a portion of the outstanding Series 2008 Bonds were redeemed pursuant to a Mandatory Tender. On February 20, 2013 an amended LOC was entered into with one of the two banks in an amount of $142,060,278 representing outstanding principal ($131,845,000) and accrued interest ($10,215,278) calculated as described above. At June 30, 2013, there was no balance nor has there been activity on the LOC.

All assets of the 1997 General Bond Resolution Fund, the 2008 Indenture, the 2010 Indenture, and the 2013-1 Indenture are pledged for repayment of the specific bond or note issues under each resolution or program.

Note K--Allowance for Arbitrage Liabilities

Certain of the Authority/Corporation's tax-exempt bond issues are subject to potential arbitrage liabilities under U.S. tax law. Arbitrage liabilities, under current federal income tax law regarding tax-exempt bond issues, consist of three types; (1) yield adjustment payments, (2) forgiveness and (3) arbitrage rebate. At June 30, 2013, the Authority/Corporation is reporting a liability for arbitrage rebate of $94,840.

The determination of excess yield on acquired purpose investments is cumulative over the life of the applicable bond series, as is the determination of arbitrage rebate on non-purpose investments, except for variable rate bonds for which arbitrage rebate is generally determined for each five-year period without retroactivity.

Note K--Allowance for Arbitrage Liabilities--Continued

Yield adjustment payments, which also relate to yield restriction on acquired purpose investments, are applicable to all tax exempt bonds. The allowable yield is 2% above the bond yield (arbitrage yield), with the federal special allowance included in income. The loss of tax-exempt status may be avoided by rebating the excess yield to the U.S. Treasury every 10 years, and upon final maturity of the bonds.

Forgiveness is applicable to all tax exempt bonds. In general, a yield restriction is imposed on acquired purpose investments, designating the allowable yield as 2% above the bond yield (arbitrage yield). The loss of tax-exempt status may be avoided by partial forgiveness of the applicable student loans. Forgiveness can be applied upon maturity of the bonds or as otherwise prescribed by the bond resolutions.

On May 6, 2013, the KHESLC entered into a voluntary closing agreement (the "VCA") with the Internal Revenue Service (the "IRS") relating to certain of its tax-exempt bonds (collectively, the "Subject Bond Issues"). The VCA resulted from a request that was submitted by KHESLC on July 31, 2012 pursuant to IRS Announcement 2012-14, 2012-14 I.R.B. 721, titled TEB Voluntary Closing Agreement Program: Relief from Allocation and Accounting Errors for Certain Issuers of Tax-Exempt Student Loan Bonds (the "Announcement"). KHESLC expects the VCA to finally and conclusively resolve all matters that were addressed in the Request. The VCA modified the application of the foregoing excess yield discussion with respect to the Subject Bond Issues.

Arbitrage rebate is applicable to all of the Authority/Corporation's tax-exempt bonds. With certain limited exceptions, income earned on non-purpose investments (investments other than student loans) which exceeds the bond yield (arbitrage yield), must be rebated to the U.S. Treasury. Payments of at least 90% are due every five years after the year of issuance, and upon final maturity of bonds.

Note L--Deferred Gain on Retirement of Debt

In fiscal year 2010, the Authority/Corporation purchased $1.198 billion of its own auction rate securities, and retired the debt. The resulting $80.2 million of gain was deferred and is being amortized over the life of the new debt. The Authority/Corporation recognized a gain of $18.5 million for the year ended June 30, 2013. The Authority/Corporation retired additional debt during fiscal year 2013 with cash and recognized approximately $4.7 million as income in the current period.

Note M--Retirement Plans

The Authority/Corporation provides retirement benefits to all full-time employees through the Kentucky Employee Retirement System ("KERS"). KERS is a multiple-employer, defined benefit plan sponsored by the Commonwealth of Kentucky, which provides retirement, disability and death benefits. The Authority/Corporation contributed 23.61% of gross wages for the year ended June 30, 2013. The employees contributed up to 6% of their gross wages to the plan for the year ended June 30, 2013. Such rates are intended to provide for normal costs on a current basis, plus an amount equal to the amortization of unfunded past service costs over thirty years, using the level percentage of payroll method. These contribution rates are determined by the Board of Trustees of KERS each biennium. The payroll of employees covered by the retirement plan was $14,903,525 for the year ended June 30, 2013. Total payroll for the year ended June 30, 2013 was $15,110,318. KERS participants have fully vested interests after the completion of sixty months of service, twelve months of which are current service. The KERS contribution requirement for the year ended June 30, 2013 was $4,232,068 which consisted of employer contributions of $3,467,460 and employee contributions of $764,608. Employer contributions for the years ended June 30, 2012 and 2011 were $3,467,460 and $2,674,236 respectively.

Although separate measurements of assets and pension benefit obligation are not available for individual employers, the Kentucky Retirement Systems' annual financial report (which is a matter of public record) contains this information for the Kentucky Retirement Systems as a whole. It may be obtained from the Kentucky Retirement Systems by writing to them at 1260 Louisville Road, Perimeter Park West, Frankfort, Kentucky 40601.

Note N--Tuition Benefit Payable

The following assumptions developed by management were used in the actuarial valuation of tuition benefits payable as of June 30, 2013. These assumptions are based on historical data for both state and national trends.

Investment Rates - The investment yield assumption is based on estimates of the yields that will be available on the investment portfolio and cash and cash equivalents. The gross investment yield assumption utilized in the calculation of the tuition benefit payable was 5.94% and 6.25% as of June 30, 2013 and June 30, 2012, respectively.

Investment Expenses - The minimum investment expense is assumed to be 20 basis points on all invested assets.

Note N--Tuition Benefit Payable--Continued

Tuition Increases - Tuition increases are based on the known increases for the next academic year and best estimates of future tuition increases for Kentucky's public colleges and universities. The historical tuition increases are as follows:

- The tuition increases for the 2003-2004 academic year were 23.4% for the Value Plan and 14.4% for the Standard Plan and the Premium Plan.
- The tuition increases for the 2004-2005 academic year were 24.2% for the Value Plan and 16.9% for the Standard Plan and the Premium Plan.
- The tuition increases for the 2005-2006 academic year were 6.5% for the Value Plan and 12.5% for the Standard Plan and the Premium Plan.
- The tuition increases for the 2006-2007 academic year were 11.2% for the Value Plan and 12% for the Standard Plan and the Premium Plan.
- The tuition increases for the 2007-2008 academic year were 5.5% for the Value Plan and 9.0% for the Standard Plan and the Premium Plan.
- The tuition increases for the 2008-2009 academic year were 5.2% for the Value Plan and 9.0% for the Standard Plan and the Premium Plan.
- The tuition increases for the 2009-2010 academic year were 3.3% for the Value Plan and 5.0% for the Standard Plan and the Premium Plan.
- The tuition increases for the 2010-2011 academic year were 4.0% for the Value Plan and 6.0% for the Standard Plan and the Premium Plan.
- The tuition increases for the 2011-2012 academic year were 3.8% for the Value Plan and 6.0% for the Standard Plan and the Premium Plan.
- The tuition increases for the 2012-2013 academic year were 3.8% for the Value Plan and 6.0% for the Standard Plan and the Premium Plan.
- As of June 30, 2013, the tuition increases for the 2013-2014 academic year were 2.9% for the Value Plan and 3% for the Standard Plan and the Premium Plan. The tuition increase assumption was 6.75% for the 2013-2014 academic year and 6.75% for each year thereafter.

Note N--Tuition Benefit Payable--Continued

For the period from inception to June 30, 2013, the annualized tuition increase for the highest-priced Kentucky public university, as applicable to the tuition benefits payout rate of Kentucky's Affordable Prepaid Tuition Standard Plan, which represents 92.3% of the Plan's enrollments, has been 8.9%. For the Kentucky Community and Technical College System ("KCTCS"), as applicable to the tuition benefits payout rate of the Value Plan, the average annualized tuition increase from inception to June 30, 2013, has been 10.50%. For the University of Kentucky, as applicable to the tuition benefits payout rate of the Premium Plan, the average annualized tuition increase from inception to June 30, 2013 has been 8.30%.

Payment of Tuition and Mandatory Fees - Payments of tuition and mandatory fees are assumed to be 128 credit hours of utilization and payments occur twice annually.

Note O--Restricted Net Assets

The following categories of restricted net assets are included in the combined statement of net assets for the following purposes:

a. **Federal Student Loan Reserve Fund:** Net assets are restricted for certain FFELP activities, primarily the payments of claims.

b. **Agency Operating Fund:** Net assets are restricted for certain FFELP activities and other student aid activities.

c. **Education Finance Funds:** Net assets are restricted as required by the 1997 General Bond Resolution Fund, the 2008 Indenture, the 2010 Indenture and the 2013-1 Indenture.

d. **Corporation Operating Fund:** Net assets are restricted for an estimated amount of mandatory repurchases of loans subject to bankruptcy claims.

e. **Student Aid Funds:** The Student Aid net assets are restricted for the Student Aid Programs.

f. **The Trust:** Net assets are restricted for use by trust participants.

Note P--Operating Leases

The Authority/Corporation leases office space and equipment under agreements expiring through 2022. Rental expense was $1,916,822 for the year ended June 30, 2013. Minimum future rental payments for real estate and equipment, including common area maintenance commitments, at June 30, 2013 are as follows:

Year Ending June 30,	
2014	$ 1,510,507
2015	721,386
2016	655,686
2017	594,184
2018	636,170
Five Years Ending June 30,	
2019 - 2023	2,486,191
	$ 6,604,124

Note Q--Commitments and Contingencies

The FSLRF is contingently liable for loans made by financial institutions that qualify for guarantee. The default ratio for loans guaranteed by the Authority/Corporation's loan guarantee operations is below 5% for the fiscal year ended June 30, 2013. The federal government's reinsurance rate for defaults for the fiscal year ending September 30, 2012, is 100% for loans made prior to October 1, 1993, 98% for loans made on or after October 1993 to September 30, 1998, and 95% for loans made after September 30, 1998. In the event of future adverse default experience, the FSLRF could be liable for up to 25% of defaulted loans. At the beginning of each fiscal year, the reinsurance rate returns to baseline (100%, 98% or 95%); management does not expect that all guaranteed loans could default in one year.

While management believes the FSLRF's expected maximum contingent liability is less than 25% of outstanding guaranteed loans, the maximum contingent liability at June 30, 2013 is calculated as follows:

Amount of guaranteed student loans outstanding at lenders	$ 2,868,564,104
Less minimum federal government share - 75%	2,151,423,078
	$ 717,141,026

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation

June 30, 2013

Note R--Subsequent Events

On July 8, 2013, the Authority/Corporation entered into an agreement with an existing eligible not-for-profit servicer (the "servicer") with the intention to add the Authority/Corporation as a Key Subcontractor to the servicer's contract with (USDE). USDE approval was received on July 17, 2013 to initiate phase I of the agreement and transfer the Corporation's portfolio to the servicer. The Corporation and the servicer are actively pursuing phase II of the agreement that would provide for the Corporation to perform certain servicing activities associated with the loan portfolio.

On August 14, 2013 the Letter of Credit and Reimbursement Agreement associated with the Series 2008 Bonds (see Note J) was extended from September 13, 2013 to November 12, 2013.

On September 30, 2013, the Authority/Corporation executed a Line of Credit Agreement with a commercial bank (the "Bank"). The agreement provides for a commitment amount not to exceed $30,000,000 or the cash and marketable securities maintained at the Bank, adjusted for asset class factors. Cash and marketable securities of the Operating Funds of the Authority/Corporation are pledged as collateral against outstanding balances. The agreement expires on September 30, 2016.

Note S--Implementation of GASB 63

In June 2012, the GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. GASB Statement No. 63 provides financial reporting guidance relative to deferred outflows of resources, a consumption of net assets by the entity that is applicable to a future reporting period, a deferred inflow of resources, and acquisition of net assets by the entity that is applicable to a future reporting period. GASB Statement No. 63 incorporates deferred outflows and inflows of resources into the definitions of the required components of the residual measure, renaming such measure as net position, rather than net assets. The provisions of GASB Statement No. 63 are effective for fiscal periods beginning after December 15, 2012 (the fiscal year ended June 30, 2013 for the Authority/Corporation). The Authority/Corporation adopted GASB 63 for the year ended June 30, 2013. The adoption of this standard did not have an impact on the Authority/Corporation's financial position, results of operations, and/or cash flows.

Note T--Early Adoption of GASB 65

In March 2012, the GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities.* GASB Statement No. 65 establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities.

Concepts Statement No. 4, *Elements of Financial Statements,* introduced and defined the elements included in financial statements, including deferred outflows of resources and deferred inflows of resources. In addition, Concepts Statement 4 provides that reporting a deferred outflow of resources or a deferred inflow of resources should be limited to those instances identified by the Board in

Note T--Early Adoption of GASB 65--continued

authoritative pronouncements that are established after applicable due process. Prior to the issuance of this Statement, only two such pronouncements have been issued. Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments,* requires the reporting of a deferred outflow of resources or a deferred inflow of resources for the changes in fair value of hedging derivative instruments, and Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, requires a deferred inflow of resources to be reported by a transferor government in a qualifying service concession arrangement. This Statement amends the financial statement element classification of certain items previously reported as assets and liabilities to be consistent with the definitions in Concepts Statement 4.

This Statement also provides other financial reporting guidance related to the impact of the financial statement elements deferred outflows of resources and deferred inflows of resources, such as changes in the determination of the major fund calculations and limiting the use of the term *deferred* in financial statement presentations.

The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012. The Authority/Corporation elected to early implement the statement. The net result for the Authority was a decrease of net position in the amount of $67,813 due to the elimination of debt issuance costs. The net result for the Corporation was a decrease of net position in the amount of $14,123,370 due to the elimination of debt issuance costs, lender origination costs, and front end borrower benefit costs.