

**KENTUCKY HIGHER EDUCATION ASSISTANCE AUTHORITY
KENTUCKY HIGHER EDUCATION STUDENT LOAN CORPORATION**

JUNE 30, 2017

Financial Statements

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

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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 combined 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, 2017, and the related notes to the financial statements which collectively comprise the Authority/Corporation's basic combined 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 combined 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 combined financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these combined 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 \$199,651,763 as of June 30, 2017, and an increase to fiduciary net position of \$17,242,968 for the year ended June 30, 2017. 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 combined 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 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.

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Opinions

In our opinion, based on our audit and the report of other auditors, the combined 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 aggregate remaining fund information of the Authority/Corporation as of June 30, 2017, 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 16 and the required supplemental information on pages 64 through 66 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 combined 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 combined financial statements, and other knowledge we obtained during our audit of the basic combined 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 28, 2017 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.



Louisville, Kentucky
September 28, 2017

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

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, pays lender default and other claims 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 loans directly to parents, students, and borrowers who are refinancing as part of the Kentucky Advantage loan programs, purchases and/or services eligible Federal and Kentucky Advantage student loans and performs collection activities on certain eligible student loans. The Mission of the organizations is "Helping Kentucky students and families prepare, plan, and pay for higher education." The Vision is "Connecting all Kentuckians to higher education." The Guiding Principles are "Promoting the merits of higher education and improving access, affordability, and completion." The Authority and the Corporation maintain bundled operations to maximize the efficiency of all Authority and Corporation operational and support activities. 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 critical informational 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 outreach operations are accounted for as a program benefit in a proprietary fund of the Authority/Corporation.

Student Aid – The Authority/Corporation provides some or all levels of administration of sixteen student aid programs: (1) Kentucky Tuition Grant ("KTG"), (2) College Access Program Grant ("CAP"), (3) Kentucky Educational Excellence Scholarship, (4) Teacher Scholarship, (5) Osteopathic Medicine Scholarship, (6) KHEAA Work-Study Program, (7) Kentucky Coal County College Completion Program, (8) Early Childhood Development Scholarship, (9) Go Higher Grant Program, (10) Coal County Scholarship Program for Pharmacy Students, (11) Mary Jo Young Scholarship, (12) John R. Justice Grant, (13) Kentucky National Guard Tuition Award Program, (14) Early Graduation Scholarship, (15) Minority Educator Recruitment and Retention Scholarship, and (16) Dual Credit Scholarship Program. The Mary Jo Young Scholarship program will end on June 30, 2017. A new program, the Work Ready Kentucky Scholarship, begins in fiscal year 2018.

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.

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Kentucky Higher Education Student Loan Corporation**

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College Savings Programs - The Authority/Corporation 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 higher education. 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 account owners.

An individual or entity 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 nine age bands, based on the age of the beneficiary. Each age band invests in varying percentages in the Institutional Class of the International Equity Index, Short-Term Bond, Bond Index, Inflation-Linked Bond, Equity Index, Real Estate Securities, Emerging Market Equity Index, and Guaranteed Funding Agreement of the TIAA-CREF Institutional Mutual Funds.

All allocation percentages are determined by the Authority/Corporation's Board of Directors and reviewed annually. The assets of the Guaranteed Option and a percentage of the assets of the five upper level age bands in Managed Allocation 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 Equity Options invest 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%. For fiscal year 2017, the Guaranteed investment rate was 1.30%.

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.

The Plan was established to provide families with an opportunity to save for future postsecondary education expenses. The Plan's investment policy goal is to earn rates of return that closely match or exceed anticipated tuition inflation rates and remain sufficiently liquid to meet KAPT benefit payments in a timely manner. The Plan offers certain federal and state tax advantages to purchasers.

Participants purchased annual tuition units at then current tuition levels, or tuition levels at the time of purchase 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 offered three tuition plans – the Value Plan, the Standard Plan, and the Premium Plan. In the Value Plan, participants purchased tuition units and receive benefits indexed to the tuition rate of the Kentucky Community and Technical College System.

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The Standard Plan offers tuition units and benefits indexed to the tuition rate of Kentucky's most expensive public university. The Premium Plan offered tuition units at the then 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, computers, and required 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 projected college entrance year receive the statutorily defined 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.

The Kentucky General Assembly approved certain changes to the Plan during the 2014 Legislative Session that became effective July 2014. These changes included the following: the addition of a utilization period definition; the establishment of June 30, 2028 as the closure date of the Plan; the establishment of certain limitations on the growth of a plan account beyond the utilization period; the prohibition of projected college entrance year extensions; and the clarification of provisions for transferring a plan account to another qualified tuition program.

As of June 30, 2017, the Plan maintained a present value fund deficit of \$32.9 million. This represents a \$2.9 million decrease over the previous year's deficit. Based on actuarial estimates, the Plan's assets will be exhausted in fiscal year 2023, 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 2028, actuarial estimates show the Commonwealth of Kentucky will need to transfer approximately \$47 million.

Certain costs of the Trust and the Plan are accounted for as a program benefit in a proprietary fund of the Authority/Corporation while certain other personnel, professional and administrative costs associated with administering the Trust and the Plan are accounted for in their respective Fiduciary Fund. All assets, liabilities and net position 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 position additions and deductions for the Plan are accounted for in the Kentucky Affordable Prepaid Tuition fund, a fiduciary fund of the Authority/Corporation.

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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 also 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. The Authority/Corporation also educates lenders about FFELP requirements and regulatory changes.

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 ("ED"), 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 Supplemental Student Loan Program. The Supplemental Student Loan Program is comprised of the Kentucky Advantage Education Loan ("KAEL") and Kentucky Advantage Parent Loan programs ("KAPL") for residents of the Commonwealth of Kentucky and non-residents attending a post-secondary institution or approved program in the Commonwealth of Kentucky, and the Advantage Education Loan and Advantage Parent Loan for non-residents of the Commonwealth of Kentucky. During fiscal year 2016, the Authority/Corporation introduced the Advantage Refinance Loan to help borrowers manage their education debt.

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

School Services – School service operations provide services to higher education institutions through a contractual relationship. These areas currently consist of KHEAA Verify and Cohort Default Management Services and new areas of services are continuously analyzed and evaluated based on the needs of school partners across the Commonwealth and beyond.

KHEAA Verify consists of services associated with the required verification of the Free Application for Federal Student Aid (FAFSA) information submitted by potential students at an institution. Cohort Default Management Services engages current and former students of institutions to educate them about persistence and completing their education and/or successfully repaying any educational debt while providing information about the various options available. Personnel, professional and administrative costs associated with school services are accounted for in the Agency Operating Fund ("AOF"), a proprietary fund of the Authority/Corporation and through the collection of revenues generated through service contracts with each institution.

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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, FFELP portfolios from other lenders, 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, 2017, the loan finance operation held and/or serviced approximately \$997 million 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 legacy and certain other FFELP loans with revenue bonds, internal warehouse funds, and commercial bank lines of credit. As of June 30, 2017, the Authority/Corporation maintained seven separate Indentures of Trust and related Series Resolutions for issues of revenue bonds. The indentures 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, 2017, the loan finance operation maintained \$888 million of revenue bonds outstanding and \$23.4 million of lines of credit payable.

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

Loan Servicing - The loan servicing operation performs servicing and default prevention activities on FFELP and supplemental loans held by the Authority/Corporation's loan finance operation and other lenders. Of the loans serviced, approximately \$994 million in outstanding principal of loans was held by the loan finance operation. Over 92% of these loans were pledged pursuant to the 2008 Indenture, the 2010 Indenture, the 2013-1 Indenture, the 2013-2 Indenture, the 2014 Indenture, the 2015 Indenture, and the 2016 indenture. Approximately \$3 million of FFELP Loans and other education loans were owned by another holder. For those loans, 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.

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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 \$1.75 billion of FFELP loans, continues to own \$994 million of FFELP loans and other education loans, and continues to service an additional \$3 million of FFELP and other education loans. The Authority/Corporation can no longer originate, guarantee or fund any newly originated FFELP loans; however, the Authority/Corporation does continue to look for opportunities to mitigate the impact of the runoff of the FFELP legacy loan portfolio through the acquisition of FFELP rehabilitation loans and other FFELP portfolios and through the origination of Kael loans.

The Authority/Corporation plans to leverage its experience collecting defaulted FFELP and Direct Loans to become one of the Private Collection Agencies ("PCA") selected by ED as part of future PCA Request for Proposal processes. In anticipation of future PCA selection processes, 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 ED to become a PCA. ARC was created by the Kentucky General Assembly effective July 12, 2012. ARC is attached to KHESLC for administrative and reporting purposes.

On December 26, 2013, former President Obama signed into law the Bipartisan Budget Act of 2013 (the "2013 Budget"). Section 502 of the 2013 Budget reduced the amount that the Authority/Corporation and other guaranty agencies are permitted to retain on rehabilitated defaulted student loans. Under the old rules, guaranty agencies were permitted to retain 18.5% of the principal balance of the rehabilitated loan and 100% of accrued interest, and could charge the borrower up to another 18.5% of the principal balance and accrued interest at the time of loan sale and retain such amount to defray collection costs. For rehabilitated loan sales on and after July 1, 2014, the 2013 Budget required that the guaranty agency pay ED 100% of the principal balance of the loan at the time of sale (multiplied by the reinsurance percentage in effect when payment under the guaranty agreement was made). In addition, the guaranty agency can charge to the borrower an amount not to exceed 16% of the outstanding principal and interest at the time of the loan sale in order to defray collection costs.

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 17 and 18 of this report. The combined fund financial statements can be found on pages 19 through 24 of this report.

Management's Discussion and Analysis (Unaudited)—Continued

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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 25 and 26 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, 2017 and 2016, respectively.

Management's Discussion and Analysis (Unaudited)—Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

	Governmental Fund		Proprietary Funds	
	2017	2016	2017	2016
Net Position Information				
Capital assets	\$	\$	\$ 7,553,654	\$ 8,103,643
Other assets	30,761,529	16,027,177	1,191,215,994	1,279,193,021
Total Assets	<u>30,761,529</u>	<u>16,027,177</u>	<u>1,198,769,648</u>	<u>1,287,296,664</u>
Deferred Outflows of Resources:				
Deferred pension expense			16,820,292	12,351,990
Total Assets and Deferred Outflows of Resources	<u>30,761,529</u>	<u>16,027,177</u>	<u>1,215,589,940</u>	<u>1,299,648,654</u>
Long-term liabilities			993,671,055	1,090,570,732
Other liabilities	405	75,917	37,799,836	23,376,921
Deferred pension expense			1,760,586	262,261
Deferred gain on debt retirements, net			16,413,019	18,212,949
Total Liabilities and Deferred Inflows of Resources	<u>405</u>	<u>75,917</u>	<u>1,049,644,496</u>	<u>1,132,422,863</u>
Invested in capital assets, net of expended debt proceeds			5,533,654	5,473,643
Unrestricted			(26,231,729)	
Restricted, other			98,636,457	78,413,391
Restricted for program benefits	30,761,124	15,951,260		
Restricted for student aid and related activities			88,007,062	83,338,757
Total Net Position	<u>\$ 30,761,124</u>	<u>\$ 15,951,260</u>	<u>\$ 165,945,444</u>	<u>\$ 167,225,791</u>
Activity Information				
Interest and investment income fund	\$ 445,472	\$ 744,595	\$ 700,281	\$ 1,456,282
Student aid & advancement fund revenue	234,351,769	206,702,000		
Tobacco settlement revenue	1,100,000	1,100,000		
Unclaimed lottery revenue	8,000,000	6,200,000		
Contributions from Agency Operating Fund	2,097,848	2,370,370		
Federal funds revenue	17,998	46,148		
Servicing Fees from external sources			257,675	294,159
Servicing Fees from Education Finance Funds			5,867,475	6,179,082
Conversion fees				500,000
Debt recovery commission			22,257,369	18,951,878
Early retirement of debt				
Federal fees earned			1,193,001	1,353,721
Default aversion fee income			67,130	(144,580)
Interest income on loans			15,821,497	18,686,985
Amortization of deferred gain on debt retirements			1,799,930	1,799,930
Guarantee fee			(401)	131,571
Gain on the sale of loans			(3,028)	(139,424)
Late payment penalties			1,033,829	1,185,521
School Services			628,368	615,824
Other income	711,512	699,118	159,269	127,932
Total Revenue	<u>246,724,599</u>	<u>217,862,231</u>	<u>49,782,395</u>	<u>50,998,881</u>
Kentucky Tuition Grant	28,419,433	29,093,617		
College Access Program Grant	70,494,489	70,102,359		
Early Graduation Scholarship	312,345	212,172		
Mary J Young Scholarship	175,002	583,937		
Early Childhood Development Scholarship	1,107,562	1,104,688		
Kentucky National Guard Tuition Award Program	6,093,150	6,176,935		
Kentucky Educational Excellence Scholarship	113,440,013	110,850,028		
Teacher Scholarship	874,763	820,605		
Teacher Loan Forgiveness	1,400,000	1,300,000		
Osteopathic Medicine Scholarship	593,462	624,743		
KHEAA Work-Study Program	498,282	482,692		
Go Higher Grant Program	274,430	324,950		
Coal County Scholarship Program for Pharmacy Students	285,560	249,343		
Dual Credit Scholarship	4,664,492			
Kentucky Coal County College Completion Scholarship	3,149,137	1,776,813		
John R. Justice Grant	132,615	194,612		
Loan guarantee operations			4,818,756	4,521,407
Default collections			6,724,679	5,938,223
Loan finance and servicing activities			30,852,769	29,844,606
Outreach			4,007,991	3,883,857
Student aid administration			2,053,053	1,930,370
Contribution to student aid programs			44,795	440,000
School services			2,405,205	2,216,266
Other activities			155,494	124,339
Total Expenditures	<u>231,914,735</u>	<u>223,897,494</u>	<u>51,062,742</u>	<u>48,899,068</u>
Change in Net Position	<u>\$ 14,809,864</u>	<u>\$ (6,035,263)</u>	<u>\$ (1,280,347)</u>	<u>\$ 2,099,813</u>

Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

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, 2017. 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 and deferred outflows decreased approximately \$84 million (6.5%), from \$1.30 billion to \$1.22 billion. The decrease was caused primarily by a \$77.3 million decrease in loans, a \$13.6 million decrease in cash and cash equivalents, and a \$897,000 decrease in various other assets offset by a \$3.3 million increase in the receivable from the Federal Student Loan Reserve Fund and a \$4.5 million increase to deferred outflows related to GASB 68 pension expense.
- The Authority/Corporation's proprietary fund liabilities and deferred inflows decreased \$82.8 million (7.3%), from \$1.13 billion to \$1.05 billion. The overall decrease in liabilities and deferred inflows was attributable to the net of various decreases and increases year over year. Decreases in liabilities included a \$106.4 million decrease in Bonds payable, a \$1.9 million decrease in the Payable to ED, a \$1.8 million decrease to the deferred gain on early retirement of debt, and a \$610,000 decrease to the Capital lease payable. The sum of these decreases were offset by an increase of \$15.7 million to the Line of credit payable, an increase of \$10.1 million to the Net Pension Liability, a \$1.5 million increase to deferred inflows related to GASB 68 pension expense, and a \$628,000 increase in various other liabilities.
- The Authority/Corporation's proprietary fund revenues decreased \$1.2 million (2.4%), from \$51 million to \$49.8 million. The overall decrease was attributable to a number of increases and decreases to certain revenue accounts including a \$3.3 million increase in Debt recovery commissions, a \$2.9 million decrease in interest income on loans, and \$848,000 in decreases related to servicing and conversion fees. See the condensed financial information schedule for Governmental Fund and Proprietary Funds for the remaining variances year over year.
- The Authority/Corporation's total proprietary fund expenditures increased approximately \$2.2 million (4.4%), due to the net of various fluctuations. See the condensed financial information schedule for Governmental Fund and Proprietary Funds for a detailed side by side comparison of expenditures for each business-type activity. Current year expenditures would have been significantly less than prior year if not for the additional \$7.1 million of pension expense to reflect the overall change in the Net pension liability.

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

- The Authority/Corporation's governmental fund assets increased approximately \$14.8 million (92%) due primarily to a \$13.7 million and \$1.5 million increase in Accounts receivable and Cash and cash equivalents, respectively. These increases were offset by a \$391,000 decrease to noncurrent scholarship loans and advances receivable.
- The Authority/Corporation's governmental fund liabilities decreased by less than \$76,000 over the prior year.
- The Authority/Corporation's governmental fund revenues increased approximately \$28.9 million (13.3%), resulting primarily from additional state General Funds for student aid programs.
- The Authority/Corporation's governmental fund expenditures increased \$8 million (3.6%) resulting primarily from \$4.7 million of expenditures associated with the new Dual Credit Scholarship and a \$2.6 million increase in Kentucky Educational Excellence Scholarships. See the condensed financial information schedule for Governmental Fund and Proprietary Funds for a detailed side by side comparison of Governmental Fund expenditures.

Combined Statement of Net Position – Governmental Fund and Proprietary Funds

Total governmental net position increased from \$16 million to \$30.8 million. Total proprietary fund net position decreased \$1.3 million comprised of a \$15.5 million increase from default collection operations (compared to a \$13 million increase in prior year), \$3.1 million decrease from loan guarantee operations (compared to \$2 million decrease in prior year), \$4 million contribution for outreach activities (compared to \$3.9 million contribution in prior year), \$2.1 million contribution for student aid and administration (compared to \$2.4 million in prior year), \$5.8 million loss in loan finance and servicing activities (compared to \$1 million loss in prior year), and \$1.8 million contribution for school services (compared to \$1.6 million in prior year).

Certain highlights related to the combined statement of net position as of June 30, 2017, are as follows:

- The Authority/Corporation maintained \$1.75 billion of FFELP guarantees outstanding.
- The Authority/Corporation maintained \$994 million of FFELP loans and education loans.
- The Authority/Corporation maintained \$389.9 million of defaulted loan principal in its collection portfolio.
- Unrestricted net position is presented as a negative amount reflecting the overall decrease to the Corporation's Operating Fund net position.
- Net position, restricted other, increased from \$78.4 million to \$98.6 million.
- Net position restricted for student aid and related activities increased from \$83.3 million to \$88 million.

Management's Discussion and Analysis (Unaudited)—Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Combined Statement of Revenues, Expenses and Changes in Net Position

The \$1.3 million decrease in proprietary fund net position during fiscal year 2017 was \$3.4 million less than the \$2.1 million increase during fiscal year 2016. The overall decrease in proprietary fund net position was attributable to the net of a \$4.6 million increase for the Authority and a \$5.8 million decrease for the Corporation. The Authority's increase was aided by an overall increase in Debt recovery commissions year over year of \$3.3 million while the Corporation's loss was largely due to increased pension expense and a decrease in interest income on loans. Another critical highlight related to the combined statement of revenues, expenses and changes in net position for the year ended June 30, 2017 is the \$8.8 million of program benefits provided by the Authority/Corporation. The majority of these program benefits directly benefited the citizens of the Commonwealth of Kentucky.

Management's Discussion and Analysis (Unaudited)—Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

	Federal Student Loan Reserve Fund		Kentucky's Affordable Prepaid Tuition		Kentucky Education Savings Plan Trust	
	2017	2016	2017	2016	2017	2016
Net Position Information						
Other assets	\$ 25,810,596	\$ 18,286,941	\$ 82,961,364	\$ 92,489,983	\$ 199,651,763	\$ 182,438,073
Total Assets	25,810,596	18,286,941	82,961,364	92,489,983	199,651,763	182,438,073
Total Liabilities	6,264,126	1,735,419	115,850,221	128,316,963	327,796	357,074
Restricted net position (deficit)	19,546,470	16,551,522	(32,888,857)	(35,826,980)	199,323,967	182,080,999
Total Net Position	\$ 19,546,470	\$ 16,551,522	\$ (32,888,857)	\$ (35,826,980)	\$ 199,323,967	\$ 182,080,999
Changes in Fiduciary Net Position Information						
Federal reinsurance	\$ 105,072,577	\$ 134,880,533	\$	\$	\$	\$
Contribution from Agency Operating Fund						
Fee revenue						
Contributions			187,351	208,770		
Subscriptions					189,895,506	54,196,665
Investment revenue	9,340	1,061	6,973,724	2,604,321	17,695,446	1,123,568
Other income	2,803,063	7,006,997				
Total Additions	107,884,980	141,888,591	7,161,075	2,813,091	207,590,952	55,320,233
Administrative expenses			385,356	383,759	815,619	755,235
Refunds			2,233,766	2,001,403		
Trustee expense			304,755	349,297		
Tuition benefits expense, net			1,299,075	11,851,344		
Loan claims	104,822,902	137,026,519				
Redemptions					189,532,365	52,421,202
Default aversion	67,130	(144,580)				
Total Deductions	104,890,032	136,881,939	4,222,952	14,585,803	190,347,984	53,176,437
Change in Net Position	\$ 2,994,948	\$ 5,006,652	\$ 2,938,123	\$ (11,772,712)	\$ 17,242,968	\$ 2,143,796

Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

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, 2017. 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 \$137 million in fiscal year 2016 to \$105 million in fiscal year 2017 (23% decrease).
- The Plan noted a decrease in tuition benefits payable of \$12.6 million in fiscal year 2017, due primarily to the net of several different factors including fewer participants, various gains due to favorable tuition inflation and investment experience and other changes including the projected deficit increase represented by interest on the beginning deficit amount.

Statement of Fiduciary Net Position (Deficit)

The FSLRF net position increased \$3 million over ending net position in the prior year. Assets increased nearly \$7.5 million while liabilities increased \$4.5 million. The increase in net position is primarily comprised of an elimination of the need for a reinsurance reserve. FFELP Guaranty Agencies are now reinsured at 100% of defaulted loan claim amounts (see Notes E and R).

The Plan recognized a decrease in the net deficit of \$2.9 million for fiscal year 2017 compared to an \$11.8 million increase in net deficit in the prior year. Overall, the current year decrease in net deficit from prior year is attributable to the net of various gains due to favorable tuition inflation and investment experience and other changes including the projected deficit increase represented by interest on the beginning deficit amount.

The Plan's total assets decreased \$9.5 million, from \$92.5 million as of June 30, 2016 to \$83 million as of June 30, 2017. Cash and investments decreased from \$90.8 million to \$81.8 million, a \$9 million decrease. The change in tuition and investment return assumptions, as applicable, are as follows:

- 2017-thereafter – 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 is based on the investment glide path approach for the Plan. The investments in the Plan will change over time to asset allocations that will reduce equity exposure and try to preserve investment gains. The glide path approach should better match projected payouts as the value of the Plan's assets continues to move closer to its depletion date.
- 2017-2018 academic year – tuition increase assumption was 6.25%, while actual tuition increases were 9.0% for the Value Plan and 4.0% for the Standard Plan and the Premium Plan
- 2018-thereafter – tuition increase assumption remained at 6.25%

Management's Discussion and Analysis (Unaudited)—Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

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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 \$17.2 million due primarily to \$17.7 million of investment revenues.

Statement of Changes in Fiduciary Net Position (Deficit)

The FSLRF net position increased \$3 million over ending net position in the prior year. Assets increased nearly \$7.5 million while liabilities increased \$4.5 million. The increase in net position is primarily comprised of an elimination of the need for a reinsurance reserve.

The Plan recognized a decrease in the net deficit of \$2.9 million for fiscal year 2017 compared to a \$11.8 million increase in net deficit in the prior year. Overall, the current year decrease in net deficit from prior year is attributable to the net of various gains due to favorable tuition inflation and investment experience and other changes including the projected deficit increase represented by interest on the beginning deficit amount.

Combined Government-Wide Statement of Net Position

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

ASSETS	Governmental Activities	Business-Type Activities	Total
Current:			
Cash and cash equivalents	\$ 5,513,380	\$ 39,943,051	\$ 45,456,431
Accounts receivable and prepaid expenses	15,808,440	889,020	16,697,460
Accrued interest income		15,069,845	15,069,845
Investments		5,372,603	5,372,603
Teacher and Osteopathic Medicine scholarship loans Loans, net	450,000		450,000
		<u>160,658,299</u>	<u>160,658,299</u>
Total Current Assets	<u>21,771,820</u>	<u>221,932,818</u>	<u>243,704,638</u>
Noncurrent:			
Restricted cash and cash equivalents		74,680,638	74,680,638
Receivable from Federal Student Loan Reserve Fund		5,070,346	5,070,346
Investments		75,552,636	75,552,636
Fixed assets, net		7,553,654	7,553,654
Loans, net		808,324,405	808,324,405
Teacher and Osteopathic Medicine scholarship loans, net	4,287,231		4,287,231
Teacher and Osteopathic Medicine scholarship advances	4,702,478		4,702,478
Accrued interest income, net		<u>5,655,151</u>	<u>5,655,151</u>
Total Noncurrent Assets	<u>8,989,709</u>	<u>976,836,830</u>	<u>985,826,539</u>
Total Assets	<u>30,761,529</u>	<u>1,198,769,648</u>	<u>1,229,531,177</u>
Deferred Outflows of Resources:			
Deferred pension expense		<u>16,820,292</u>	<u>16,820,292</u>
Total Assets and Deferred Outflows of Resources	<u>30,761,529</u>	<u>1,215,589,940</u>	<u>1,246,351,469</u>
LIABILITIES			
Current:			
Accounts payable and accrued expenses	405	6,249,552	6,249,957
Accrued interest expense		1,632,039	1,632,039
Payable to US Department of Education		5,867,039	5,867,039
Line of credit payable		23,411,206	23,411,206
Capital lease payable		<u>640,000</u>	<u>640,000</u>
Total Current Liabilities	<u>405</u>	<u>37,799,836</u>	<u>37,800,241</u>
Noncurrent:			
Allowance for arbitrage liabilities		241,958	241,958
Net pension liability		104,038,666	104,038,666
Capital lease payable		1,380,000	1,380,000
Bonds payable		<u>888,010,431</u>	<u>888,010,431</u>
Total Noncurrent Liabilities		<u>993,671,055</u>	<u>993,671,055</u>
Total Liabilities	<u>405</u>	<u>1,031,470,891</u>	<u>1,031,471,296</u>
Deferred Inflows of Resources:			
Deferred pension expense		1,760,586	1,760,586
Deferred gain on debt retirements, net		<u>16,413,019</u>	<u>16,413,019</u>
Total Liabilities and Deferred Inflows of Resources	<u>405</u>	<u>1,049,644,496</u>	<u>1,049,644,901</u>
NET POSITION			
Invested in capital assets, net of expended debt proceeds		5,533,654	5,533,654
Unrestricted		(26,231,729)	(26,231,729)
Restricted, other		98,636,457	98,636,457
Restricted for program benefits	30,761,124		30,761,124
Restricted for student aid and related activities		<u>88,007,062</u>	<u>88,007,062</u>
Total Net Position	<u>\$ 30,761,124</u>	<u>\$ 165,945,444</u>	<u>\$ 196,706,568</u>

Combined Government-Wide Statement of Activities

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

For the Year Ending June 30, 2017

	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	\$ 28,266,022	\$ 153,411	\$	\$ 37,132,132	\$ 8,712,699	\$	\$ 8,712,699
College Access Program Grant	70,341,078	153,411		74,147,500	3,653,011		3,653,011
Early Graduation Scholarship	189,640	122,705		312,345			
Mary Jo Young Scholarship	46,234	128,768		173,663	(1,339)		(1,339)
Early Childhood Development Scholarship	971,553	136,009		1,485,326	377,764		377,764
Kentucky National Guard Tuition Award Program	5,957,141	136,009		7,042,988	949,838		949,838
Kentucky Educational Excellence Scholarship	113,286,602	153,411		113,552,018	112,005		112,005
Teacher Scholarship	721,352	153,411		2,052,091	1,177,328		1,177,328
Teacher Loan Forgiveness	1,400,000				(1,400,000)		(1,400,000)
Dual Credit Scholarship Program	4,535,746	128,746		5,128,746	464,254		464,254
Osteopathic Medicine Scholarship	457,625	135,837		693,492	100,030		100,030
KHEAA Work-Study Program	362,445	135,837		535,837	37,555		37,555
Go Higher Grant Program	146,722	127,708		299,208	24,778		24,778
Coal County Scholarship Program for Pharmacy Students	156,597	128,963		696,900	411,340		411,340
Kentucky Coal County College Completion Program	3,018,025	131,112		3,326,640	177,503		177,503
John R. Justice Grant	4,900	127,715		145,713	13,098		13,098
Total Governmental Activities	229,861,682	2,053,053		246,724,599	14,809,864		14,809,864
Business-Type Activities:							
Loan guarantee operations	4,818,756		1,732,616			(3,086,140)	(3,086,140)
Default collections	6,724,679		22,257,369			15,532,690	15,532,690
Loan finance and servicing activities	30,852,769		25,008,548			(5,844,221)	(5,844,221)
Outreach	4,007,991					(4,007,991)	(4,007,991)
Contribution to student aid programs	44,795					(44,795)	(44,795)
Student aid administration	2,053,053					(2,053,053)	(2,053,053)
School services	2,405,205		628,368			(1,776,837)	(1,776,837)
Other activities	155,494		155,494				
Total Business-Type Activities	51,062,742		49,782,395			(1,280,347)	(1,280,347)
Total Primary Government	\$ 280,924,424	\$ 2,053,053	\$ 49,782,395	\$ 246,724,599	14,809,864	(1,280,347)	13,529,517
Change in Net position					14,809,864	(1,280,347)	13,529,517
Net position, July 1, 2016					15,951,260	167,225,791	183,177,051
Net position, June 30, 2017					\$ 30,761,124	\$ 165,945,444	\$ 196,706,568

Combined Statement of Net Position - Proprietary Funds

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation

June 30, 2017

ASSETS	Authority			Corporation			Combined
	Internal Service Fund	Agency Operating Fund	Authority Total	Education Finance Funds	Operating Fund	Corporation Total	Total
Current:							
Cash and cash equivalents	\$ 2,853,425	\$ 18,233,556	\$ 21,086,981	\$	\$ 18,856,070	\$ 18,856,070	\$ 39,943,051
Investments		5,372,603	5,372,603				5,372,603
Accounts receivable and prepaid expenses		166,536	166,536		722,484	722,484	889,020
Accrued interest income		300,486	300,486	14,018,653	750,706	14,769,359	15,069,845
Loans, net				146,902,914	13,755,385	160,658,299	160,658,299
Total Current Assets	2,853,425	24,073,181	26,926,606	160,921,567	34,084,645	195,006,212	221,932,818
Noncurrent:							
Restricted cash and cash equivalents				74,680,638		74,680,638	74,680,638
Receivable from Federal Student Loan Reserve Fund		5,070,346	5,070,346				5,070,346
Investments		67,078,909	67,078,909		8,473,727	8,473,727	75,552,636
Fixed assets, net		7,045,175	7,045,175		508,479	508,479	7,553,654
Loans, net				761,235,779	47,088,626	808,324,405	808,324,405
Accrued interest income, net				5,185,340	469,811	5,655,151	5,655,151
Total Noncurrent Assets		79,194,430	79,194,430	841,101,757	56,540,643	897,642,400	976,836,830
Total Assets	2,853,425	103,267,611	106,121,036	1,002,023,324	90,625,288	1,092,648,612	1,198,769,648
Deferred Outflows of Resources:							
Deferred pension expense		1,524,801	1,524,801		15,295,491	15,295,491	16,820,292
Total Assets and Deferred Outflows of Resources	2,853,425	104,792,412	107,645,837	1,002,023,324	105,920,779	1,107,944,103	1,215,589,940
LIABILITIES							
Current:							
Accounts payable and accrued expenses	836,601	754,214	1,590,815	324,624	4,334,113	4,658,737	6,249,552
Interfund payable (receivable)	2,016,824	(1,800,844)	215,980	(1,683,764)	1,467,784	(215,980)	
Accrued interest expense		17,183	17,183	1,572,957	41,899	1,614,856	1,632,039
Payable (receivable) to U.S. Department of Education		(284,195)	(284,195)	5,719,004	432,230	6,151,234	5,867,039
Line of credit payable					23,411,206	23,411,206	23,411,206
Capital lease payable		640,000	640,000				640,000
Total Current Liabilities	2,853,425	(673,642)	2,179,783	5,932,821	29,687,232	35,620,053	37,799,836
Noncurrent:							
Capital lease payable		1,380,000	1,380,000				1,380,000
Net pension liability		10,663,495	10,663,495		93,375,171	93,375,171	104,038,666
Allowance for arbitrage liabilities				241,958		241,958	241,958
Bonds payable, net				888,010,431		888,010,431	888,010,431
Total Noncurrent Liabilities		12,043,495	12,043,495	888,252,389	93,375,171	981,627,560	993,671,055
Total Liabilities	2,853,425	11,369,853	14,223,278	894,185,210	123,062,403	1,017,247,613	1,031,470,891
Deferred Inflows of Resources:							
Deferred pension expense		390,322	390,322		1,370,264	1,370,264	1,760,586
Deferred gain on debt retirements, net				16,413,019		16,413,019	16,413,019
Total Liabilities and Deferred Inflows of Resources	2,853,425	11,760,175	14,613,600	910,598,229	124,432,667	1,035,030,896	1,049,644,496
NET POSITION							
Invested in capital assets, net		5,025,175	5,025,175		508,479	508,479	5,533,654
Unrestricted					(26,231,729)	(26,231,729)	(26,231,729)
Restricted, other				91,425,095	7,211,362	98,636,457	98,636,457
Restricted for student aid and related activities		88,007,062	88,007,062				88,007,062
Total Net Position	\$	\$ 93,032,237	\$ 93,032,237	\$ 91,425,095	\$ (18,511,888)	\$ 72,913,207	\$ 165,945,444

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 the Year Ending June 30, 2017

	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	\$	\$	\$	\$ 26,994,778	\$ 2,293,023	\$ 29,287,801	\$ 29,287,801
Interest and investment income		472,485	472,485	160,443	67,353	227,796	700,281
Amortization of deferred gain on debt retirements				1,799,930		1,799,930	1,799,930
Interest expense on bonds				(13,215,016)	(251,288)	(13,466,304)	(13,466,304)
Total net interest revenues		472,485	472,485	15,740,135	2,109,088	17,849,223	18,321,708
Financing Expenses:							
Provision for loan losses				827,728	(563,467)	264,261	264,261
Provision for arbitrage				41,939		41,939	41,939
Long-Term debt credit facility and remarketing fees				942,311	30,670	972,981	972,981
Debt issuance costs				675,963		675,963	675,963
Total financing expenses				2,487,941	(532,797)	1,955,144	1,955,144
Interest revenues net of financing expenses		472,485	472,485	13,252,194	2,641,885	15,894,079	16,366,564
Other Operating Revenues:							
Servicing fees from external sources					257,675	257,675	257,675
Servicing fees from Education Finance Funds					5,867,475	5,867,475	5,867,475
Conversion fees							
Debt recovery commission		22,257,369	22,257,369				22,257,369
Federal fees earned		1,193,001	1,193,001				1,193,001
Default aversion fee income		67,130	67,130				67,130
Guarantee fee					(401)	(401)	(401)
Gain/(loss) on sale/purchase of loans				271,419	(274,447)	(3,028)	(3,028)
Late payment penalties				993,852	39,977	1,033,829	1,033,829
School services		628,368	628,368				628,368
Other income	155,494		155,494		3,775	3,775	159,269
Total operating revenues	155,494	24,618,353	24,773,847	14,517,465	8,535,939	23,053,404	47,827,251
Operating Expenses:							
Administrative expenses	155,494	10,900,480	11,055,974		21,065,408	21,065,408	32,121,382
Servicing fees for Operating Fund				5,867,475		5,867,475	5,867,475
Depreciation and amortization		553,283	553,283		224,085	224,085	777,368
Other expenses		89,672	89,672	147,629	1,298,774	1,446,403	1,536,075
Total operating expenses	155,494	11,543,435	11,698,929	6,015,104	22,588,267	28,603,371	40,302,300
Net operating income (loss) before program benefits		13,074,918	13,074,918	8,502,361	(14,052,328)	(5,549,967)	7,524,951
Program Benefits:							
Principal and interest benefits				294,128	126	294,254	294,254
School Service		2,405,205	2,405,205				2,405,205
Outreach		4,007,991	4,007,991				4,007,991
Contribution to student aid programs		44,795	44,795				44,795
Student aid administration		2,053,053	2,053,053				2,053,053
Total program benefits		8,511,044	8,511,044	294,128	126	294,254	8,805,298
Operating income (loss) before transfers		4,563,874	4,563,874	8,208,233	(14,052,454)	(5,844,221)	(1,280,347)
Transfers (to) from other funds							
Interfund transfers				9,126,108	(9,126,108)		
Increase (decrease) in Net position after transfers		4,563,874	4,563,874	17,334,341	(23,178,562)	(5,844,221)	(1,280,347)
Net position, July 1, 2016		88,468,363	88,468,363	74,090,754	4,666,674	78,757,428	167,225,791
Net position, June 30, 2017	\$ -	\$ 93,032,237	\$ 93,032,237	\$ 91,425,095	\$ (18,511,888)	\$ 72,913,207	\$ 165,945,444

See accompanying notes

Combined Statement of Cash Flows - Proprietary Funds

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

For the Year Ending June 30, 2017

	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	\$	\$	\$	\$ 170,202,475	\$ 11,072,188	\$ 181,274,663	\$ 181,274,663
Interest received on loans				31,310,268	2,223,327	33,533,595	33,533,595
Special allowance paid				(19,242,101)	(1,100,940)	(20,343,041)	(20,343,041)
Servicing fees received, internal sources	(155,494)	74,511	(80,983)	(5,867,475)	5,867,475		(80,983)
School services fees received		628,368	628,368				628,368
Servicing fees received, external sources					236,978	236,978	236,978
Debt recovery commission received		22,257,369	22,257,369				22,257,369
Federal fees received		1,193,001	1,193,001				1,193,001
Default aversion fees received		67,130	67,130				67,130
Outreach		(4,007,991)	(4,007,991)				(4,007,991)
School services		(2,405,205)	(2,405,205)				(2,405,205)
Internal activity-payments to other funds	628,636	(628,636)		759,225	(759,225)		
Loans originated, including costs				8,358	(13,846,252)	(13,837,894)	(13,837,894)
Administrative expenses paid		(11,382,954)	(11,382,954)	(3,780,006)	(14,096,911)	(17,876,917)	(29,259,871)
Credit facility fees paid				(942,311)	(29,755)	(972,066)	(972,066)
Loans purchased, including premiums				(1,948,211)	(69,322,367)	(71,270,578)	(71,270,578)
Contribution to student aid programs		(44,795)	(44,795)				(44,795)
Student aid administration		(2,053,053)	(2,053,053)				(2,053,053)
Interfund loan sales and purchases				(38,612,751)	38,612,751		
Client loan receipts					1,020,411	1,020,411	1,020,411
Loan receipts remitted to clients					(1,160,084)	(1,160,084)	(1,160,084)
Net Cash Provided by (Used in) Operating Activities	<u>473,142</u>	<u>3,697,745</u>	<u>4,170,887</u>	<u>131,887,471</u>	<u>(41,282,404)</u>	<u>90,605,067</u>	<u>94,775,954</u>
Cash Paid from Noncapital Financing Activities:							
Proceeds from debt issued				41,090,361	20,412,939	61,503,300	61,503,300
Debt principal payments				(147,506,510)	(4,727,204)	(152,233,714)	(152,233,714)
Interest on debt				(12,631,787)	(261,712)	(12,893,499)	(12,893,499)
Debt issuance costs				(675,963)		(675,963)	(675,963)
Interfund transfers				9,126,108	(9,126,108)		
Increase in Federal Student Loan Reserve receivable		(3,338,173)	(3,338,173)				(3,338,173)
Net Cash Provided by (Used in) Noncapital Financing Activities		<u>(3,338,173)</u>	<u>(3,338,173)</u>	<u>(110,597,791)</u>	<u>6,297,915</u>	<u>(104,299,876)</u>	<u>(107,638,049)</u>
Cash Flows From Capital and Related Financing Activities:							
Capital expenditures		(206,106)	(206,106)		(437,218)	(437,218)	(643,324)
Interest paid on capital lease		(5,239)	(5,239)				(5,239)
Bond principal payments		(610,000)	(610,000)				(610,000)
Net Cash Used in Capital and Related Financing Activities		<u>(821,345)</u>	<u>(821,345)</u>		<u>(437,218)</u>	<u>(437,218)</u>	<u>(1,258,563)</u>
Cash Flows From Investing Activities:							
Proceeds from sales/maturities of investments		54,262,291	54,262,291		7,247,705	7,247,705	61,509,996
Purchases of investments		(54,285,374)	(54,285,374)		(7,331,441)	(7,331,441)	(61,616,815)
Investment income		345,675	345,675	132,771	129,259	262,030	607,705
Net Cash Provided by Investing Activities		<u>322,592</u>	<u>322,592</u>	<u>132,771</u>	<u>45,523</u>	<u>178,294</u>	<u>500,886</u>
Net Increases (Decrease) in Cash and Cash Equivalents	<u>473,142</u>	<u>(139,181)</u>	<u>333,961</u>	<u>21,422,451</u>	<u>(35,376,184)</u>	<u>(13,953,733)</u>	<u>(13,619,772)</u>
Cash and Cash Equivalents, July 1, 2016	<u>2,380,283</u>	<u>18,372,737</u>	<u>20,753,020</u>	<u>53,258,187</u>	<u>54,232,254</u>	<u>107,490,441</u>	<u>128,243,461</u>
Cash and Cash Equivalents, June 30, 2017	<u>\$ 2,853,425</u>	<u>\$ 18,233,556</u>	<u>\$ 21,086,981</u>	<u>\$ 74,680,638</u>	<u>\$ 18,856,070</u>	<u>\$ 93,536,708</u>	<u>\$ 114,623,689</u>

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

For the Year Ending June 30, 2017

	Authority			Corporation			Combined
	Internal Service Fund	Agency Operating Fund	Authority Total	Education Finance Funds	Operating Fund	Corporation Total	Total
Reconciliation of Operating Income to Net Cash Provided by (Used in) Operating Activities							
Operating income (loss) before transfers	\$	\$ 4,563,874	\$ 4,563,874	\$ 8,208,233	\$ (14,052,454)	\$ (5,844,221)	\$ (1,280,347)
Adjustments to reconcile operating income to net cash provided by (used in) operating activities:							
Investment income				(132,771)	(52,093)	(184,864)	(184,864)
Depreciation and amortization		920,538	920,538		224,085	224,085	1,144,623
Amortization of deferred gain on debt retirements				(1,799,930)		(1,799,930)	(1,799,930)
Amortization, expense and write-off of debt issuance costs				675,963		675,963	675,963
Interest expense		5,239	5,239	13,215,016	251,288	13,466,304	13,471,543
Provision for loan losses				827,728	(563,467)	264,261	264,261
Borrower interest converted to principal				(18,574,054)	(802,345)	(19,376,399)	(19,376,399)
Loan forgiveness				294,128		294,128	294,128
Gain or loss on equipment disposal					48,692	48,692	48,692
Pension expense		500,596	500,596		6,598,333	6,598,333	7,098,929
(Increases) decreases in assets:							
Accounts receivables and prepaid expenses		39,384	39,384		(72,245)	(72,245)	(32,861)
Accrued interest receivable		35,127	35,127	561,502	(495,740)	65,762	100,889
Principal received on loans				170,202,475	11,072,188	181,274,663	181,274,663
Loans purchased, including premiums				(1,948,211)	(69,322,367)	(71,270,578)	(71,270,578)
Loans originated, including costs				8,358	(13,846,252)	(13,837,894)	(13,837,894)
Interfund loan sales and purchases				(38,612,751)	38,612,751		
Increases (decreases) in liabilities:							
Accounts payable and accrued expenses	(164,837)	26,823	(138,014)	(35,244)	237,877	202,633	64,619
Payable to U.S. Department of Education				(1,804,135)	(112,048)	(1,916,183)	(1,916,183)
Interfund receivable/payable	637,979	(2,388,597)	(1,750,618)	759,225	991,393	1,750,618	
Accrued interest payable		(5,239)	(5,239)				(5,239)
Allowance for arbitrage liabilities				41,939		41,939	41,939
Net Cash Provided by (Used in) Operating Activities	<u>\$ 473,142</u>	<u>\$ 3,697,745</u>	<u>\$ 4,170,887</u>	<u>\$ 131,887,471</u>	<u>\$ (41,282,404)</u>	<u>\$ 90,605,067</u>	<u>\$ 94,775,954</u>

Balance Sheet - Governmental Fund

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

ASSETS	Governmental Fund Student Aid
Current:	
Cash and cash equivalents	\$ 5,513,380
Accounts receivable	15,808,440
Teacher and Osteopathic Medicine scholarship loans	<u>450,000</u>
Total Current Assets	<u>21,771,820</u>
Noncurrent:	
Teacher and Osteopathic Medicine scholarship loans, net of allowance of \$3,690,000	4,287,231
Teacher and Osteopathic Medicine scholarship advances	<u>4,702,478</u>
Total Noncurrent Assets	<u>8,989,709</u>
Total Assets	<u>30,761,529</u>
LIABILITIES	
Current:	
Accounts payable	<u>405</u>
Total Liabilities	<u>405</u>
FUND BALANCE	
Restricted for program benefits	<u>\$ 30,761,124</u>

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

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

For the Year Ending June 30, 2017

	Governmental Fund Student Aid
Revenues:	
Interest and investment income fund	\$ 445,472
Tobacco settlement revenue	1,100,000
Unclaimed lottery revenue	8,000,000
State General Fund revenue	234,351,769
Federal funds revenue	17,998
Other income	711,512
Contribution from Agency Operating Fund	<u>2,097,848</u>
Total Revenues	<u>246,724,599</u>
Expenditures:	
Kentucky Tuition Grant	28,419,433
College Access Program Grant	70,494,489
Early Graduation Scholarship	312,345
Mary Jo Young Scholarship	175,002
Early Childhood Development Scholarship	1,107,562
Kentucky National Guard Tuition Award Program	6,093,150
Kentucky Educational Excellence Scholarship	113,440,013
Teacher Scholarship	874,763
Teacher Loan Forgiveness	1,400,000
Osteopathic Medicine Scholarship	593,462
Coal County Scholarship Program for Pharmacy Students	285,560
KHEAA Work-Study Program	498,282
Go Higher Grant Program	274,430
Dual Credit Scholarship Program	4,664,492
Kentucky Coal County College Completion Program	3,149,137
John R. Justice Grant	<u>132,615</u>
Total Expenditures	<u>231,914,735</u>
Net Change in Fund Balance	14,809,864
Fund Balance, July 1, 2016	<u>15,951,260</u>
Fund Balance, June 30, 2017	<u>\$ 30,761,124</u>

Statement of Fiduciary Net Position (Deficit)

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

ASSETS	Federal Student Loan Reserve Fund	Kentucky's Affordable Prepaid Tuition	Kentucky Education Savings Plan Trust
Current:			
Cash and cash equivalents	\$ 25,775,692	\$ 1,873,985	\$
Contributions receivable		404,789	
Fees receivable		195,816	
Investments		79,927,735	199,470,254
Other current assets	34,904		181,509
Total Current Assets	25,810,596	82,402,325	199,651,763
Noncurrent:			
Contributions receivable		559,039	
Total Assets	25,810,596	82,961,364	199,651,763
LIABILITIES			
Current:			
Accounts payable	841,802	221,162	183,001
Accrued expenses			144,795
Payable to U.S. Department of Education	351,978		
Total Current Liabilities	1,193,780	221,162	327,796
Noncurrent:			
Payable to Agency Operating Fund	5,070,346		
Tuition benefits payable		115,629,059	
Total Liabilities	6,264,126	115,850,221	327,796
NET POSITION (DEFICIT)			
Restricted for program benefits		(32,888,857)	199,323,967
Restricted for other purposes	19,546,470		
Total Net Position (Deficit)	\$ 19,546,470	\$ (32,888,857)	\$ 199,323,967

Statement of Changes in Fiduciary Net Position (Deficit)

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

For the Year Ending June 30, 2017

	Federal Student Loan Reserve Fund	Kentucky's Affordable Prepaid Tuition	Kentucky Education Savings Plan Trust
Additions:			
Federal reinsurance	\$ 105,072,577	\$	\$
Contract income, net		187,351	
Subscriptions			189,895,506
Investment Revenues:			
Net unrealized gain on investments		2,043,866	16,347,983
Interest and investment income	9,340	4,929,858	1,347,463
Other income	2,803,063		
Total Additions	107,884,980	7,161,075	207,590,952
Deductions:			
Program benefits:			
Loan claims	104,822,902		
Default aversion fee expense	67,130		
Redemptions			189,532,365
Administrative expenses		45,876	815,619
Personnel and professional expenses		339,480	
Refunds		2,233,766	
Trustee fee expense		304,755	
Tuition benefits expense, net		1,299,075	
Total Deductions	104,890,032	4,222,952	190,347,984
Change in Net Position	2,994,948	2,938,123	17,242,968
Net Position (Deficit), July 1, 2016	16,551,522	(35,826,980)	182,080,999
Net Position (Deficit), June 30, 2017	\$ 19,546,470	\$ (32,888,857)	\$ 199,323,967

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note A--Description of 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 existing Federal Family Education Loan Program ("FFELP") loans, performs default aversion activities, pays lender default and other claims 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 loans directly to parents, students, and borrowers who are refinancing as part of the Kentucky Advantage loan programs, purchases and/or services eligible Federal and Kentucky Advantage student loans and performs collection activities on certain eligible student loans. The Mission of the organizations is "Helping Kentucky students and families prepare, plan, and pay for higher education. The Vision is "Connecting all Kentuckians to higher education." The Guiding Principles are "Promoting the merits of higher education and improving access, affordability, and completion. The Authority and the Corporation maintain bundled operations to maximize the efficiency of all Authority and Corporation operational and support activities. 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 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 newly-originated FFELP loans. However, the Authority/Corporation continues to operate under existing FFELP regulations for loans originated and guaranteed prior to July 1, 2010.

Outreach Programs

The Authority/Corporation offers college planning and student financial aid guidance to students and families, school counselors, adult education providers and other community contacts. Programs and services include regional field counselors, a mobile college-planning classroom, a one-stop Web portal, near-peer college coaches and targeted publications for students of all ages. Initiatives include Kentucky College Application Campaign, which provides participating seniors with hands-on assistance in applying to college or technical school; Close the Deal, which connects students with community leaders and business representatives to set and meet goals for college and future careers; *Surviving College*, workshops and publications designed to ease the transition to college for traditional students and adult learners, increasing retention; and the Kentucky College Coaches Program, in which recent college graduates serve as coaches to students in schools with predominantly first-generation, low-income students.

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note A--Description of Business--Continued

Student Aid Programs

Student Aid – The Authority/Corporation provides some or all levels of administration of sixteen student aid programs: (1) Kentucky Tuition Grant (“KTG”), (2) College Access Program Grant (“CAP”), (3) Kentucky Educational Excellence Scholarship, (4) Teacher Scholarship, (5) Osteopathic Medicine Scholarship, (6) KHEAA Work-Study Program, (7) Kentucky Coal County College Completion Program, (8) Early Childhood Development Scholarship, (9) Go Higher Grant Program, (10) Coal County Scholarship Program for Pharmacy Students, (11) Mary Jo Young Scholarship, (12) John R. Justice Grant, (13) Kentucky National Guard Tuition Award Program, (14) Early Graduation Scholarship, (15) Minority Educator Recruitment and Retention Scholarship, and (16) Dual Credit Scholarship Program. The Mary Jo Young Scholarship program will end on June 30, 2017. A new program, the Work Ready Kentucky Scholarship, begins in fiscal year 2018.

Kentucky Educational Savings Plan Trust

The Trust was formed on July 15, 1988 by Kentucky law, to help families save for the costs of higher education. 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. The Trust offers certain federal and state tax advantages to account owners.

An individual or entity 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 nine age bands, based on the age of the beneficiary. Each age band invests in varying percentages in the Institutional Class of the International Equity Index, Short-Term Bond, Bond Index, Inflation-Linked Bond, Equity Index, Real Estate Securities, Emerging Market Equity Index, and Guaranteed Funding Agreement of the TIAA-CREF Institutional Mutual Funds.

The Equity Option 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%. For fiscal year 2017, the Guaranteed investment rate was 1.30%.

All allocation percentages are determined by the Authority/Corporation’s Board of Directors and are subject to change. The assets of the Guaranteed Option and a percentage of the assets of the five upper level age bands in Managed Allocation 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.

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note A--Description of Business--Continued

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 policy goal is to earn rates of return that closely match tuition inflation rates and remain sufficiently liquid to meet KAPT benefit payments in a timely manner. 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 \$32.9 million.

Participants purchased annual tuition units at then current tuition levels, or 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 offered three tuition plans – the Value Plan, the Standard Plan and the Premium Plan. In the Value Plan, participants bought 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 then 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, computers, and required 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 projected college entrance year receive the statutorily defined 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.

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note A--Description of Business--Continued

The Kentucky General Assembly approved certain changes to the Plan during the 2014 Legislative Session that became effective July 2014. These changes included the following: the addition of a utilization period definition; the establishment of June 30, 2028 as the closure date of the Plan; the establishment of certain limitations on the growth of a plan account beyond the utilization period; the prohibition of projected college entrance year extensions; and the clarification of provisions for transferring a plan account to another qualified tuition program.

As of June 30, 2017, the Plan maintained a present value fund deficit of \$32.9 million. This represents a \$2.9 million decrease over the previous year's deficit. Based on actuarial estimates, the Plan's assets will be exhausted in fiscal year 2023, 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 2028, actuarial estimates show the Commonwealth of Kentucky will need to transfer approximately \$47 million.

Loan Guarantee Operations

The Authority/Corporation's loan guarantee operations guarantee 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 guaranteed student loans. FFELP was established by Congress and is administered by ED as a pre-HCERA 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, reporting loan information to the National Student Loan Data System ("NSLDS") paying lender claims for loans in default, paying lender specialty claims such as 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.

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%. The maximum reinsurance rate was amended to 100% effective for default claims paid on or after December 1, 2015 (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. FSLRF assets and all earnings on those assets are the property of the Federal government.

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note A--Description of Business—Continued

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 primarily 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 are restricted for financial aid related activities including guaranty agency activities.

Sources of funds to the AOF include investment income, agency retention on collections of defaulted loans, default aversion fees, account maintenance fees, and school services revenue. Expenditures from the AOF include personnel, professional and other administrative expenses directly related to the loan program operations, outreach program activities, school services, and other operating activities. The AOF also provides funding to the governmental fund to pay administration costs for sixteen student aid programs, administrative costs for the Trust, and direct benefits for the Mary Jo Young Scholarship program. Both the FSLRF and AOF are subject to federal oversight.

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 or who have attended eligible post-secondary institutions. In addition, the Corporation services and collects education loans and issues 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, KAEL, certain federal and other education loans; and (iv) the collection of FFELP, KAEL, certain federal 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 guaranty agency. 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

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Note A--Description of Business—Continued

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. KAEL loans do not have the same insurance as the FFELP loans originated under the federal program; however, upon default, ownership of the loans remain with the Authority/Corporation and debt recovery efforts continue.

The Authority/Corporation's indentures and separate series resolutions for issuance of revenue bonds 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. In addition, the Authority/Corporation's lines of credit also provide for certain collateral account and proceeds restrictions.

As of June 30, 2017 the Authority/Corporation held and/or serviced approximately \$997 million outstanding principal amount of FFELP and other education loans. \$915 million of loans were pledged pursuant to the 2008 Indenture, the 2010 Indenture, the 2013-1 Indenture, the 2013-2 Indenture, the 2014 Indenture, the 2015 Indenture, and the 2016 Indenture. The remaining \$79 million of loans were funded by the Corporation's Operating Fund. Also, the Authority/Corporation services approximately \$3 million of FFELP and other education loans on behalf of other holders. 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.

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 position 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, loan finance and servicing, outreach program activities, student aid administration and contributions, school services and other activities.

**Kentucky Higher Education Assistance Authority
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Note B--Summary of Significant Accounting Policies—Continued

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 governmental 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, loan finance and servicing, outreach program activities, student aid administration and contributions, school services 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.

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 in fiduciary 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. FSLRF assets and all earnings on those assets are the property of the Federal government and are used primarily to facilitate FFELP claim payments. 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.

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.

**Kentucky Higher Education Assistance Authority
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Note B--Summary of Significant Accounting Policies--Continued

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

Large Cap U.S. stocks	30%
Mid Cap U.S. stocks	5%
Small Cap U.S. stocks	4%
Non-U.S. stocks	9%
	<hr/>
Total Equity	48%
	<hr/> <hr/>
Inflation indexed bonds	7%
Domestic fixed income	44%
Cash	1%
	<hr/>
Total Fixed Income	52%
	<hr/> <hr/>

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 & Poor's;
- 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

**Kentucky Higher Education Assistance Authority
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Note B--Summary of Significant Accounting Policies--Continued

Income Option, the Balanced Option, the Equity Index Option, the Active Equity Option and the Guaranteed Option.

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.

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 applicable 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 position.

Allowance for Uncollectible Loans - As discussed in Note A, most FFELP loans held by the Authority/Corporation are insured by guarantee agencies and the ED. Management of the Authority/Corporation believes that all of its respective guaranty agencies and the ED 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 \$6.6 million for loan principal and \$601,000 for accrued interest as of June 30, 2017. Furthermore, the Authority/Corporation is required to purchase loans owned by third party customers with certain loan servicing violations. As of June 30, 2017, the allowance for third party servicing loan losses for loans that have been purchased was \$1.4 million for loan principal and \$655,000 for accrued interest. In July 2015, the Authority/Corporation purchased an uninsured loan portfolio at a substantial discount. As of June 30, 2017, the allowance for the loans purchased at a discount was \$15.7 million for loan principal and \$4.2 million 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, 2016, the allowance for advances converted to loans was \$3.7 million.

Pensions - For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Kentucky Employees Retirement System (KERS) and additions to/deductions from KERS' fiduciary net position have been determined on the same basis as they are reported by KERS. For this purpose, benefit payments (including refunds of employee

**Kentucky Higher Education Assistance Authority
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June 30, 2017

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

contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Interest Income on Loans - The Authority/Corporation earns interest income on loans from the following three sources: (1) subsidized interest from ED earned while certain students are in school, in grace or in deferment status; (2) special allowance from ED (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 and net of any negative special allowance owed to ED (discussed in Note G).

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.

Debt Issuance Costs - Debt issuance costs are expensed when incurred.

Deferred Gain on Early Retirement of Debt - In accordance with GASB No. 23, *Accounting and Financial Reporting of Debt Reported by Proprietary Activities*, and in accordance with GASB No. 63, *Financial Reporting of Deferred Outflows or Resources, Deferred Inflows of Resources and Net Position*, 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 are also not subject to federal or state income taxes.

Use of Estimates - Accounting principles generally accepted in the United States of America require 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 position. 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,

**Kentucky Higher Education Assistance Authority
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June 30, 2017

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

default collection, interest income from the corporate loan finance and servicing activities, school services, 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.

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. As of June 30, 2017, the Authority/Corporation's unrestricted net position is (\$26, 231,729).

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.

**Kentucky Higher Education Assistance Authority
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June 30, 2017

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, agency mortgage-backed securities, asset-backed commercial paper, banker's 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. 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.

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, 2017, the Authority/Corporation's Proprietary Funds, Governmental Fund and Fiduciary Funds maintained cash on deposit as follows:

Of the \$115.4 million of cash and cash equivalents maintained in the Proprietary Funds, \$21.4 million was held for guarantee operations and the remaining \$94 million was held for loan finance and servicing activities.

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note C--Cash and Investments--Continued

Of the \$27.6 million of cash and cash equivalents maintained in the Fiduciary Funds, \$25.8 million was related to the FSLRF and the remaining \$1.8 million was associated with the Plan.

	Governmental Fund Bank Balance	Proprietary Fund Bank Balance	Fiduciary Fund Bank Balance
FDIC Insured	\$	\$ 551,916	\$ 521,476
Uninsured			
Collateralized by securities held by the pledging financial institution		7,908,890	21,442,236
Money market demand deposits			
Money market securities		104,104,662	5,644,057
Cash deposited with Kentucky State Treasurer	5,513,380	2,853,425	27,827
	<u>\$ 5,513,380</u>	<u>\$ 115,418,893</u>	<u>\$ 27,635,596</u>

As of June 30, 2017, all Proprietary Fund investments were registered in the Authority/Corporation's name and maintained by an external trustee or investment manager, as applicable. The investment balances as of June 30, 2017 are summarized as follows:

	Fair Value	Weighted Average Maturity (in years)
Corporate bonds	\$ 44,750,003	2.61
U.S. Treasury and government agency securities	27,633,239	2.06
Collateralized mortgage obligations	8,541,997	12.10
	<u>\$ 80,925,239</u>	

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note C--Cash and Investments--Continued

As of June 30, 2017, Trust investments of \$199.5 million comprised entirely of TIAA mutual funds.

As of June 30, 2017, Plan investments of \$79.9 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 & Poor's / Moody's rating (as applicable) for all corporate bonds held by the Authority/Corporation's Proprietary Funds as of June 30, 2017:

<u>Rating</u>	<u>Fair Value</u>
AAA / Aaa	\$ 16,593,619
AA / Aa	3,378,312
A / A	9,969,209
BAA / Baa	<u>14,808,863</u>
	<u>\$ 44,750,003</u>

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 & Poor's or Prime 1 by Moody's. As previously noted, at June 30, 2017 the Plan primarily invested in mutual funds.

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
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June 30, 2017

Note C--Cash and Investments--Continued

Fair Value Measurement

In accordance with GASB 72, *Fair Value Measurement and Application*, the Authority/Corporation categorizes its fair value measurements within the fair value hierarchy established by accounting principles generally accepted in the United States of America. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets, Level 2 inputs are significant other observable inputs; and Level 3 are significant unobservable inputs.

Level 1: Quoted prices (unadjusted) of identical assets or liabilities in active markets that an entity has the ability to access as of the measurement date, or observable inputs.

Level 2: Significant other observable inputs other than Level 1 prices, such as quoted prices for similar assets and liabilities, quoted prices in markets that are not active, and other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect an entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Fair Value on a Recurring Basis

The Authority/Corporation has the following recurring fair value measurements as of June 30, 2017:

Money Market Securities of \$104,104,662 are valued using quoted market prices. (Level 1 Inputs).

Corporate bonds, U.S. Treasury and government agency securities, and collateralized mortgage obligations of \$80,925,239 were based on Level 2 inputs.

As of June 30, 2017, 100% of the value of the Trust and Plan investments was based on Level 1 inputs.

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note D--Fixed Assets

A summary of fixed assets follows:

	Beginning Balance July 1, 2016	Additions	Disposals	Ending Balance June 30, 2017
Proprietary fund:				
Furniture and equipment	\$ 14,826,228	\$ 643,324	\$ 1,259,548	\$ 14,210,004
Building	12,075,049			12,075,049
System development	55,955			55,955
Student loan servicing	541,131			541,131
Debt recovery system	81,047			81,047
Accumulated depreciation and amortization	<u>(19,475,767)</u>	<u>(1,144,623)</u>	<u>(1,210,858)</u>	<u>(19,409,532)</u>
	<u>\$ 8,103,643</u>	<u>\$ (501,299)</u>	<u>\$ 48,690</u>	<u>\$ 7,553,654</u>
Fiduciary Fund:				
Furniture and equipment	\$ 67,688	\$	\$	\$ 67,688
Accumulated depreciation	<u>(67,688)</u>			<u>(67,688)</u>
	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>

Depreciation and amortization expense totaled \$1,144,623 for the year ended June 30, 2017, of which \$1,008,495 was allocated to business-type activities, \$129,588 allocated to governmental activities, and \$6,540 allocated to the fiduciary activities.

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

	TOTAL
Loan guarantee operations	\$ 406,016
Outreach	182,381
School services	48,746
Default collections	147,267
Loan finance and servicing	<u>224,085</u>
	<u>\$ 1,008,495</u>

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note D--Fixed Assets--Continued

The Authority/Corporation has assets under capital lease agreements, as described in Note I, of \$12,075,049 with related accumulated amortization of \$5,694,772. 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 \$402,502 for the year ended June 30, 2017.

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

Pursuant to FFELP, the loan guarantee operating unit of the 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, 2017, the outstanding balance of aggregate insured student loans was approximately \$1.75 billion.

Loans insured by the Authority/Corporation are reinsured under FFELP by the federal government. Death, disability, bankruptcy, lender of last resort, closed school, false certification, and ineligible borrower 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. On December 18, 2015, the Consolidated Appropriations Act, 2016, was signed into law and amended the maximum reinsurance rate within Section 428(c)(1) of the Higher Education Act by striking 95% and inserting 100%. Therefore, the Authority/Corporation has not recorded a reserve at June 30, 2017 for losses on federal reinsurance. See Footnote R.

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 was entitled to retain 18.5% of principal and all accrued interest for rehabilitated loans, plus 18.5% of collection costs through June 30, 2014. Effective July 1, 2014, 100% of principal is paid to ED and the Authority/Corporation is entitled to retain all accrued interest for rehabilitated loans plus 16% 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 ED).

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

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

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

at the time lenders request default aversion assistance. DAF 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 are recorded monthly and are recognized as a deduction in the FSLRF and as revenue in the AOF. DAF are remitted back to the FSLRF for loans that default.

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 generally ten years with most FFELP consolidation loans and many KAEL refinance loans having longer repayment terms. 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 1.9% to 12% for the fiscal year ended June 30, 2017 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.

Loans consist of the following at June 30, 2017:

Stafford - Subsidized	\$ 263,012,902
Stafford - Unsubsidized	300,752,976
PLUS/SLS	18,629,777
Consolidation	356,655,372
Supplemental	44,110,032
Other	<u>11,322,407</u>
Total gross loans	994,483,466
Allowance for loan losses	(23,650,944)
Loan rebate due to borrowers	(41,436)
Unamortized discount on purchase of loans	<u>(1,808,382)</u>
Loans, net	968,982,704
Less amount shown as current assets	<u>160,658,299</u>
Noncurrent loans, net	<u><u>\$ 808,324,405</u></u>

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

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

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. In July 2015, the Authority/Corporation purchased an uninsured loan portfolio at a substantial discount. As of June 30, 2017, the allowance for the loan principal purchased at a discount was \$15.7 million. In addition, \$2,268,120 of student loan principal was no longer insured due to violations of due diligence requirements.

All student loans in the Education Finance Funds and some student loans of the Corporation Operating Fund are pledged as collateral for certain bonds and lines of credit payable.

Note G--Special Allowance

The Higher Education Act of 1965 provides for quarterly Special Allowance Payments to be made by ED 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 2017, the Authority/Corporation forgave approximately \$1.7 million in loan principal and accrued interest for teachers funded by ED, and an additional \$1.4 million in loan forgiveness for teachers funded by the Commonwealth of Kentucky. Also, during fiscal year 2017, the Authority/Corporation provided additional loan forgiveness of \$294,254.

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.

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note I--Capital Lease Payable--Continued

The scheduled payments of principal and interest on the bonds are guaranteed under an insurance policy.

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, 2018.

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, 2018.

A summary of the activity for the capital lease for the year ended June 30, 2017 is as follows:

	<u>June 30, 2016</u>	<u>Additions</u>	<u>Payments</u>	<u>June 30, 2017</u>
Capital Lease Payable	<u>\$ 2,630,000</u>	<u>\$</u>	<u>\$ 610,000</u>	<u>\$ 2,020,000</u>

Debt service requirements for the final four fiscal years are as follows:

Year Ending June 30,	<u>Principal</u>	<u>Interest</u>
2018	\$ 640,000	\$ 103,663
2019	670,000	72,013
2020	710,000	37,275
	<u>\$ 2,020,000</u>	<u>\$ 212,951</u>

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note J--Revenue Bonds and Notes Payable

The balance of revenue bonds and notes payable at June 30, 2017 and the related activity for the year ended June 30, 2017 is as follows:

<u>Series</u>	<u>Scheduled Maturity</u>	<u>Interest</u>	<u>Beginning Balance July 1, 2016</u>	<u>Bond Maturities Refundings</u>	<u>New Issues</u>	<u>Amortization of Premium / (Discount) June 30, 2017</u>	<u>Ending Balance June 30, 2017</u>
<u>2008 Indenture</u>							
2008 A-1	* June 1, 2037	Weekly	\$ 71,420,000	\$	\$	\$	\$ 71,420,000
2008 A-2	* June 1, 2038	Weekly	51,325,000				51,325,000
			<u>122,745,000</u>	<u></u>	<u></u>	<u></u>	<u>122,745,000</u>
<u>2010 Indenture</u>							
2010 A-2	* May 1, 2034	Quarterly	106,540,000	(12,350,000)			94,190,000
			<u>106,540,000</u>	<u>(12,350,000)</u>	<u></u>	<u></u>	<u>94,190,000</u>
<u>2013-1 Indenture</u>							
2013-1	June 1, 2026	Monthly	303,365,000	(56,180,000)			247,185,000
<u>2013-2 Indenture</u>							
2013-2	June 1, 2028	Monthly	245,399,555	(43,655,000)		174,612	201,919,167
<u>2014 Indenture</u>							
2014 A	* June 1, 2031	Fixed	18,446,398	(3,045,000)		(114,779)	15,286,619
2017 A	* June 1, 2034	Fixed			41,090,361	(14,206)	41,076,155
			<u>18,446,398</u>	<u>(3,045,000)</u>	<u>41,090,361</u>	<u>(128,985)</u>	<u>56,362,774</u>
<u>2015-1 Indenture</u>							
2015-1	December 1, 2031	Monthly	108,385,000	(21,240,000)			87,145,000
<u>2016-1 Indenture</u>							
2016-1-1-A & B	* June 1, 2026	Monthly	51,250,000	(5,893,820)			45,356,180
2016-1-2-A & B	June 1, 2026	Monthly	38,250,000	(5,142,690)			33,107,310
			<u>89,500,000</u>	<u>(11,036,510)</u>	<u></u>	<u></u>	<u>78,463,490</u>
			<u>\$ 994,380,953</u>	<u>\$ (147,506,510)</u>	<u>\$ 41,090,361</u>	<u>\$ 45,627</u>	<u>\$ 888,010,431</u>

* This bond series is tax exempt

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

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

The Authority/Corporation's revenue bonds include fixed and variable rates of interest based on various index rates. Those fixed rates and variable index rates ranged from 0.70% to 5.0% as of June 30, 2017.

Debt service requirements to maturity or redemption date, assuming interest rates based on fixed rates and variable index rates at June 30, 2017, are as follows:

	Principal Repayment Amount (Thousands)							Total
	2008	2010	2013-1	2013-2	2014	2015-1	2016-1	
Year Ending June 30, 2018					\$ 1,200			\$ 1,200
2 Years Ending June 30, 2020					5,300			5,300
5 Years Ending June 30, 2025					13,780			13,780
5 Years Ending June 30, 2030			\$ 247,185	\$ 203,869	22,290		\$ 78,463	551,807
5 Years Ending June 30, 2035		\$ 94,190			12,465	\$ 87,145		193,800
3 Years Ending June 30, 2038	\$ 122,745							122,745
	<u>\$ 122,745</u>	<u>\$ 94,190</u>	<u>\$ 247,185</u>	<u>\$ 203,869</u>	<u>\$ 55,035</u>	<u>\$ 87,145</u>	<u>\$ 78,463</u>	<u>\$ 888,632</u>
	Interest Repayment Amount (Thousands)							
	2008	2010	2013-1	2013-2	2014	2015-1	2016-1	Total
Year Ending June 30, 2018	\$ 1,166	\$ 2,232	\$ 3,833	\$ 3,365	\$ 2,254	\$ 1,569	\$ 1,646	\$ 16,065
Year Ending June 30, 2019	1,166	2,232	3,833	3,365	2,194	1,569	1,646	16,005
Year Ending June 30, 2020	1,166	2,232	3,833	3,365	2,087	1,569	1,646	15,898
Year Ending June 30, 2021	1,166	2,232	3,833	3,365	1,953	1,569	1,646	15,764
Year Ending June 30, 2022	1,166	2,232	3,833	3,365	1,813	1,569	1,646	15,624
5 Years Ending June 30, 2027	5,830	11,159	15,328	16,824	6,920	7,846	6,587	70,494
5 Years Ending June 30, 2032	5,830	11,159		3,364	3,161	6,276		29,790
5 Years Ending June 30, 2037	5,830	4,464			430			10,724
1 Years Ending June 30, 2038	489							489
	<u>\$ 23,809</u>	<u>\$ 37,942</u>	<u>\$ 34,493</u>	<u>\$ 37,013</u>	<u>\$ 20,812</u>	<u>\$ 21,967</u>	<u>\$ 14,817</u>	<u>\$ 190,853</u>

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

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 then outstanding principal (\$131,845,000) and accrued interest (\$10,215,278) calculated as described above. At June 30, 2017, there was no balance nor has there been activity on the LOC.

All assets of the 2008 Indenture, the 2010 Indenture, the 2013-1 Indenture, the 2013-2 Indenture, the 2014 Indenture, the 2015 Indenture, and the 2016 Indenture are pledged for repayment of the specific bond or note issues under each resolution or program.

Note K--Line of Credit

The Authority/Corporation maintains two line of credit agreements with a commercial bank (the "Bank"). One line of credit is a revolving line of credit ("Revolver") with cash and marketable securities of the Operating Funds of the Authority/Corporation pledged as collateral against any outstanding balance on this \$30,000,000 line of credit. The Revolver had an outstanding balance of \$21.3 million as of June 30, 2017 and was scheduled to expire on September 17, 2017. The other line of credit is a multi-draw term loan ("Credit Facility") with a 12-month period for advances on the Credit Facility followed by a one-year term loan. The Credit Facility is restricted to the acquisition of loans made through FFELP and is collateralized by the loans financed with funds advanced by the Bank. The Credit Facility had an outstanding balance of \$2.1 million as of June 30, 2017 and expires on September 17, 2017. In addition, both Lines of Credit are cross-collateralized. See subsequent events footnote for applicable updates regarding these lines of credit subsequent to June 30, 2017.

Note L--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, may be satisfied in three ways (1) yield adjustment payments with respect to (a) non-purpose obligations allocated to bonds issued on a variable rate basis, and (b) purpose obligations that were acquired after July 18, 2016 or that were acquired prior to such date if allocated to tax exempt bonds bearing interest on a variable rate basis or to tax exempt bonds issued primarily to finance Federal Family Education Loan Program loans, (2) loan forgiveness, and (3) arbitrage rebate. At June 30, 2017, the Authority/Corporation is reporting a liability for excess yield on acquired purpose investments of \$241,958.

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note L--Allowance for Arbitrage Liabilities--Continued

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.

Yield adjustment payments, which also relate to yield restriction on acquired purpose investments, are applicable to all tax exempt bonds with respect to such investments that were acquired after July 18, 2016 and also apply to such investments that were acquired prior to such date if allocated to tax exempt bonds bearing interest on variable rate basis or to tax exempt bonds issued primarily to finance Federal Family Education Loan Program loans. 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 75% of the excess yield to the US treasury at least once every five years subsequent to the 10th anniversary date of the issuance and the full amount 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 Corporation 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"). The VCA modified the application of the foregoing excess yield discussion with respect to the Subject Bond Issues. The determination of excess yield on acquired purpose investments is no longer applicable for 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 M--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. In addition in fiscal year 2014, the Authority/Corporation purchased \$358.65 million of its own auction rate securities and retired the debt. This resulted in an additional \$7.2 million of gain which was deferred and is being amortized over the remaining life of the old debt. The Authority/Corporation recognized a gain of \$1.8 million for the year ended June 30, 2017. As of June 30, 2017 there is \$16.4 million of gain remaining to be amortized.

Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note N--Retirement Plans

Plan Description. Employees of the Authority/Corporation participate in Kentucky Employees Retirement systems (KERS), a cost-sharing multiple-employer defined benefit pension plan administered by Kentucky Retirement Systems (KRS). KRS is governed by Kentucky Revised Statutes 61.510 through 61.705 and can only be modified by the state legislature.

Benefits Provided. KERS provides retirement, disability, and death benefits. Benefit provisions are established by state statute and can only be modified by the state legislature.

All regular full-time employees of the Authority/Corporation are covered by KERS. A regular full-time employee is an employee that averages one hundred or more hours per month over a calendar or fiscal year. KERS consist of three tiers:

- Tier 1: Participation prior to September 1, 2008
- Tier 2: Participation on or after September 1, 2008 to December 31, 2013
- Tier 3: Participation on or after January 1, 2014

For Tiers 1 and 2, the benefit paid is based on the following formula: Final Compensation X Benefit Factor X Years of Service = Annual Benefit. For Tier 3, the benefit paid is based on the member's accumulated account balance at the time of retirement.

In 2013, all Cost of Living Adjustments (COLA's) were eliminated unless the State Legislature so authorizes on a biennial basis and either (1) the system is over 100% funded or (2) the Legislature appropriates sufficient funds to prepay the increased liability for the COLA.

Contributions. Kentucky statutes set the rates for employer and employee contributions. Contributions rates can only be modified by the state legislature.

The employer and each employee contribute a percentage of the employee's creditable compensation. Creditable compensation consists of all wages includable on the employee's Federal Form W-2, Wage and Tax statement, under the heading "Wages, Tips, and Other Compensation". There are two exceptions of payment of wages not included in creditable compensation: (1) the lump-sum compensatory leave payments to employees in Tier 2 and 3 and (2) vacation payout at termination. The employer total contribution rate for FY17 was 48.59% comprised of 40.24% for pension contributions and 8.35% for insurance contributions and FY16 was 38.77% comprised of 30.84% for pension contributions and 7.93% for insurance contributions. The employee's contribution rates are as follows: Tier 1 - 5%, Tier 2 and 3 - 6%.

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note N--Retirement Plans--Continued

The contributions for the employer and employee are as follows:

	<u>FY17</u>	<u>FY16</u>
Authority: Employer	\$ 542,195	\$ 467,558
Authority: Employee	65,425	75,449
	<u>607,620</u>	<u>543,007</u>
Corporation: Employer	5,177,378	4,186,642
Corporation: Employee	680,160	698,419
	<u>5,857,538</u>	<u>4,885,061</u>
Total: Employer	5,719,573	4,654,200
Total: Employee	745,585	773,868
	<u>\$ 6,465,158</u>	<u>\$ 5,428,068</u>

The employer is responsible for additional contributions if pension spiking occurs. Pension spiking may be deemed to have occurred for certain large compensation increases in the five years immediately preceding retirement. Kentucky Revised Statute 61.598 requires the last participating employer, for employees retiring on or after January 1, 2014, to pay for any additional actuarial costs resulting from annual increases in an employee's creditable compensation greater than ten percent over the employee's last five fiscal years of employment that are not a direct result of a bona fide promotion or career advancement.

Pension Costs. At June 30, 2017, the Authority/Corporation reported a net pension liability of \$104,038,666 for its proportionate share of the KERS's net pension liability. The Authority's portion is \$10,663,495 and the Corporation's is \$93,375,171. The net pension liability was measured as of June 30, 2016, and the total pension liability used to calculate the net pension liability was determined by the actuarial valuation as of that date. The Authority/Corporation's estimated proportionate share of the collective net pension liability was based on a projection of the Authority/Corporation's long-term share of contributions to the pension plan relative to the projected contributions of all employer participants, as actuarially determined. The Authority's contributions during the measurement period as provided by KRS were \$479,957 with a proportionate share percentage of .093544%. The Corporation's contributions during the measurement period as provided by KRS were \$4,202,759 with a proportionate share percentage of .819117%.

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note N--Retirement Plans--Continued

For the year ended June 30, 2017, the Authority/Corporation recognized pension expense of \$12,818,502 for its proportionate share of KERS's pension expense. The Authority's portion was \$1,042,791 and the Corporation's was \$11,775,711.

At June 30, 2017, the Authority reported its proportionate share of KERS's deferred outflows of resources and deferred inflows of resources, and its contributions subsequent to the measurement date, from the following sources:

<u>Authority</u>	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Difference between expected and actual experience	\$ 11,138	\$
Net difference between projected and actual investment earnings on pension plan investments	163,728	
Changes in assumptions	807,740	
Changes in proportion and differences between employer contributions and proportionate share of contributions		390,322
Authority's contributions to KERS subsequent to the measurement date	542,195	
	<u>\$ 1,524,801</u>	<u>\$ 390,322</u>

Continued

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note N--Retirement Plans--Continued

\$542,195 reported as deferred outflows of resources related to pensions resulting from the Authority's contributions to KERS subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2018. Other amounts reported as deferred outflows and inflows of resources related to KERS pensions will be recognized in pension expense as follows:

Authority Deferred Outflows of Resources

Original Deferral Year	Original Deferral Amount	2017	2018	2019	2020	2020
2015	\$ 515,941	(128,985)	(128,985)	(128,985)	(128,986)	
2016	595,650		(148,913)	(148,913)	(148,913)	(148,911)
	<u>\$ 1,111,591</u>	<u>\$ (128,985)</u>	<u>\$ (277,898)</u>	<u>\$ (277,898)</u>	<u>\$ (277,899)</u>	<u>\$ (148,911)</u>
Amortization 2017						<u>\$ 128,985</u>
Unamortized Amount 2017						<u>\$ 982,606</u>

Authority Deferred Inflows of Resources

Original Deferral Year	Original Deferral Amount	2016	2017	2018	2019	2020	2021
2014	\$ 117,000	(29,250)	(29,250)	(29,250)	(29,250)		
2015	174,511		(43,628)	(43,628)	(43,628)	(43,627)	
2016	200,939			(50,325)	(50,325)	(50,325)	(50,325)
	<u>\$ 492,450</u>	<u>\$ (29,250)</u>	<u>\$ (72,878)</u>	<u>\$ (123,203)</u>	<u>\$ (123,203)</u>	<u>\$ (93,952)</u>	<u>\$ (50,325)</u>
Amortization 2017							<u>\$ (72,878)</u>
Unamortized Amount 2017							<u>\$ 390,322</u>

Continued

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note N--Retirement Plans--Continued

At June 30, 2017, the Corporation reported its proportionate share of KERS's deferred outflows of resources and deferred inflows of resources, and its contributions subsequent to the measurement date, from the following sources:

<u>Corporation</u>	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Difference between expected and actual experience	\$ 97,531	\$
Net difference between projected and actual investment earnings on pension plan investments	1,433,687	
Changes in assumptions	7,072,998	
Changes in proportion and differences between employer contributions and proportionate share of contributions	1,513,897	1,370,264
Authority's contributions to KERS subsequent to the measurement date	5,177,378	
	<u>\$ 15,295,491</u>	<u>\$ 1,370,264</u>

Continued

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note N--Retirement Plans--Continued

\$5,177,378 reported as deferred outflows of resources related to pensions resulting from the Corporation's contributions to KERS subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2018. Other amounts reported as deferred outflows and inflows of resources related to KERS pensions will be recognized in pension expense as follows:

Corporation Deferred Outflows of Resources

Original Deferral Year	Original Deferral Amount	2017	2018	2019	2020	2021
2015	\$ 7,181,849	(1,795,462)	(1,795,462)	(1,795,462)	(1,795,463)	
2016	4,731,726		(1,182,932)	(1,182,932)	(1,182,932)	(1,182,930)
	<u>\$ 11,913,575</u>	<u>\$(1,795,462)</u>	<u>\$(2,978,394)</u>	<u>\$(2,978,394)</u>	<u>\$(2,978,395)</u>	<u>\$ (1,182,930)</u>
Amortization 2017						<u>\$ 1,795,462</u>
Unamortized Amount 2017						<u>\$ 10,118,113</u>

Corporation Deferred Inflows of Resources

Original Deferral Year	Original Deferral Amount	2016	2017	2018	2019	2020	2020
2014	\$ 918,000	(229,500)	(229,500)	(229,500)	(229,500)		
2015	(688,500)		172,125	172,125	172,125	172,125	
2016	1,427,639			(356,910)	(356,910)	(356,910)	(356,909)
	<u>\$ 1,657,139</u>	<u>\$(229,500)</u>	<u>\$(57,375)</u>	<u>\$(414,285)</u>	<u>\$(414,285)</u>	<u>\$(184,785)</u>	<u>\$ (356,909)</u>
Amortization 2017							<u>\$ (57,375)</u>
Unamortized Amount 2017							<u>\$ 1,370,264</u>

Continued

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note N--Retirement Plans--Continued

Actuarial Assumptions. The total pension liability was determined by an actuarial valuation as of June 30, 2016, using the entry age normal actuarial cost method and the following actuarial assumptions:

<u>Assumptions</u>	<u>Percentage</u>
Inflation	3.25% per year
Active Member Payroll Growth	4.00% per year
Investment Rate of Return	6.75% per year

Salary increases were based on a service-related table.

The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (setback one year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (setback four years for males) is used for the period after disability retirement.

The actuarial assumptions used in the June 30, 2016, valuation were based on the results of an actuarial experience study for the period July 1, 2008 - June 30, 2013. The Kentucky Retirement systems Board of Directors lowered the three actuarial assumptions in May 2017. The inflation rate was lowered from 3.25% to 2.3%, the active member payroll growth was lowered from 4% to 0%, and the investment rate of return was lowered from 6.75% to 5.25%. These assumption changes will become effective for the actuarial valuation as of the June 30, 2017 measurement date.

The long-term expected rate of return on pension plan investments is reviewed as part of the regular experience studies prepared every five years. Several factors are considered in evaluating the long-term rate of return assumption including long-term historical data, estimates inherent in current market data, and a log-normal distribution analysis in which best estimate ranges of expected future real rates of return were developed by the investment consultant for each major asset class. These ranges were combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and then adding expected inflation.

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note N--Retirement Plans--Continued

The target asset allocation and arithmetic real rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Long Term Expected Real Rate of Return</u>	<u>Target Allocation</u>
Combined Equity	5.30%	50.00%
Intermediate Duration Fixed Income	1.00%	11.00%
Custom KRS Fixed Income	3.33%	11.00%
Core Real Estate	4.25%	5.00%
Diversified Hedge Funds	4.00%	10.00%
Private Equity	8.00%	2.00%
Diversified Inflation Strategy	3.15%	8.00%
Cash Equivalent	-0.25%	3.00%
Total		<u>100.00%</u>

The long-term expected rate of return on plan assets is 6.75%, which was established by the Board of Trustees of the Kentucky Retirement Systems based on a blending of the factors described above.

Discount Rate. The discount rate used to measure the total pension liability was 6.75%. The projection of cash flows used to determine the discount rate assumed employers would contribute the actuarially determined contribution rate of projected compensation over the remaining 27 year amortization period of the unfunded actuarial accrued liability.

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note N--Retirement Plans--Continued

Pension Liability Sensitivity. The following table presents the Authority/Corporation's proportionate share of the net pension liability in KRS, calculated using the discount rate disclosed in the preceding paragraph, as well as what the Authority/Corporation's proportionate share of the net pension liability would be if it were calculated using a discount rate 1 percentage point lower or 1 percentage point higher than the current discount rate:

	<u>1% Decrease in Discount Rate</u>	<u>Discount Rate</u>	<u>1% Increase in Discount Rate</u>
KRS Discount Rate	5.75%	6.75%	7.75%
Authority's proportionate share of net pension liability	\$ 12,013,495	\$ 10,663,495	\$ 9,529,495
Corporation's proportionate share of net pension liability	\$ 105,194,171	\$ 93,375,171	\$ 83,442,171

Pension Plan Fiduciary Net Position. Detailed information about KERS's fiduciary net position is available in a KRS financial report. That report may be obtained on the Internet at www.kyret.ky.gov; by writing to Kentucky Retirement Systems at Perimeter Park West, 1260 Louisville Road, Frankfort, KY 40601; or by calling 1-800-928-4646.

Note O--Tuition Benefit Payable

The following assumptions provided by management were used in the actuarial valuation of tuition benefits payable as of June 30, 2017. These assumptions are based on national and state specific economic data, contractual provisions, previous program actuarial valuation reports, historical state general fund appropriations to the University of Kentucky and KCTCS, actual tuition increases from previous years (2002-2016) and other state prepaid tuition programs' annual tuition inflation assumptions.

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 is based on the investment glide path approach for the Plan. The investments in the Plan will change over time to asset allocations that will reduce equity exposure and try to preserve investment gains. The glide path approach should better match projected payouts as the value of the Plan's assets continues to move closer to its depletion date.

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

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note O--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 2002-2003 academic year were 32.4% for the Value Plan and 6.4% for the Standard Plan and the Premium Plan.
- 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 24.3% 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.
- The tuition increases for the 2013-2014 academic year were 2.9% for the Value Plan and 3.0% for the Standard Plan and the Premium Plan.
- The tuition increases for the 2014-2015 academic year were 2.1% for the Value Plan and 5.0% for the Standard Plan and the Premium Plan.

Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note O--Tuition Benefit Payable--Continued

- The tuition increases for the 2015-2016 academic year were 2.0% for the Value Plan and 3.0% for the Standard Plan and the Premium Plan.
- The tuition increases for the 2016-2017 academic year were 4.0% for the Value Plan and 5.0% for the Standard Plan and the Premium Plan.
- As of June 30, 2017, the tuition increases for the 2017-2018 academic year were 9.0% for the Value Plan and 4.0% for the Standard Plan and the Premium Plan. The tuition increase assumption was 6.25% for the 2017-2018 academic year and 6.25% for each year thereafter.

For the period from inception to June 30, 2017, 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 and Premium Plans, which represents 95.4% of the Plan's enrollments, has been 7.7%. 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, 2017, has been 9%.

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 P--Restricted Net Position

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

- a. **Federal Student Loan Reserve Fund:** Net position is restricted for certain FFELP activities, primarily the payments of claims.
- b. **Agency Operating Fund:** Net position is restricted for certain FFELP activities and other student aid activities.
- c. **Education Finance Funds:** Net position is restricted as required by the 2008 Indenture, the 2010 Indenture, the 2013-1 Indenture, the 2013-2 Indenture, the 2014 Indenture, the 2015 Indenture, and the 2016 Indenture.
- d. **Corporation Operating Fund:** Net position is primarily restricted for an estimated amount of mandatory repurchases of loans subject to bankruptcy claims.
- e. **Student Aid Funds:** The Student Aid fund balance is restricted for the Student Aid Programs.
- f. **The Trust:** Net position is restricted for use by trust participants.

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note Q--Operating Leases

The Authority/Corporation leases office space and equipment under agreements through 2022. Rental and space utilization expense was \$1,392,616 for the year ended June 30, 2017. Minimum future rental payments for real estate and equipment, including common area maintenance commitments, at June 30, 2017 are as follows:

Year Ending June 30,	
2018	\$ 1,365,983
2019	755,560
2020	663,580
2021	651,644
2022	595,244
	<hr/>
	\$ 4,032,011
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Note R--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, 2017. Prior to December 1, 2015, the federal government's reinsurance rate for defaults was 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. Effective December 1, 2015, the maximum reinsurance rate was amended from 95% to 100%. In the event of future adverse default experience, the FSLRF could be liable for 25% of defaulted loans for a default ratio in excess of 9%. The liability for a default ratio over 5% and up to 9% is 15%. At the beginning of each fiscal year, the reinsurance rate returns to applicable baseline; 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, 2017 is calculated as follows:

Amount of guaranteed student loans outstanding at lenders	\$ 1,750,393,959
Less minimum federal government share - 75%	<hr/> 1,312,795,469
	<hr/>
	\$ 437,598,490
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Notes to Financial Statements--Continued

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation**

June 30, 2017

Note S--Subsequent Events

On September 12, 2017, the Authority/Corporation executed a new Warehouse Loan and Security Agreement and Amendment to Loan Documents with a commercial bank (the "Bank") to provide up to \$45,000,000 for each of the two Lines of Credit for a total of \$90,000,000. One Line of Credit is a revolving Line of Credit with a three-year term period. Cash and marketable securities of the Operating Funds of the Authority/Corporation are pledged as collateral against any outstanding balance on the \$45,000,000 Line of Credit. The second \$45,000,000 Line of Credit is a multi-draw term loan ("Credit Facility") with an 18-month period for advances on the Credit Facility followed by a one-year term loan. The Credit Facility is restricted to the acquisition of loans made through FFELP and is collateralized by the loans financed with funds advanced by the Bank. In addition, both Lines of Credit will also be cross-collateralized.

Note T--Recent Pronouncements

In June 2015, the GASB issued Statement No. 75, *Accounting and Reporting for Postemployment Other Than Pensions*. The provisions of this statement are effective for fiscal years beginning after June 15, 2017.

This statement establishes new accounting and financial reporting requirements for OPEB plans. The scope of this Statement addresses accounting and financial reporting for OPEB that is provided to the employees of state and local governmental employers. This Statement establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. For defined benefit OPEB, this Statement identifies the methods and assumptions that are required to be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Note disclosure and required supplementary information requirements about defined benefit OPEB also are addressed.

The Authority/Corporation is currently evaluating the impact that will result from adopting GASB No. 75 and is therefore unable to disclose the impact that adopting these Standards will have on the Authority/Corporation's financial position and the results of its operations when the Statement is adopted.

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation
Schedule of Proportionate Share of the Net Pension Liability and Related Ratios
June 30, 2016

	<u>FY 2016</u>	<u>FY 2015</u>	<u>FY 2014</u>
Authority's proportion of the net pension liability	0.093544%	0.097187%	0.101355%
Authority's proportionate share of the net pension liability	\$ 10,663,495	\$ 9,749,658	\$ 9,093,000
Authority's covered-employee payroll	\$ 1,556,281	\$ 1,628,998	\$ 1,740,891
Authority's proportionate share of the net pension liability as a percentage of its covered-employee payroll	685.19%	598.51%	522.32%
Plan fiduciary net position as a percentage of the total pension liability	14.87%	18.83%	22.32%
	<u>FY 2016</u>	<u>FY 2015</u>	<u>FY 2014</u>
Corporation's proportion of the net pension liability	0.819117%	0.839524%	0.796208%
Corporation's proportionate share of the net pension liability	\$ 93,375,171	\$ 84,220,102	\$ 71,434,000
Corporation's covered-employee payroll	\$ 13,627,623	\$ 14,071,702	\$ 13,672,643
Corporation's proportionate share of the net pension liability as a percentage of its covered-employee payroll	685.19%	598.51%	522.46%
Plan fiduciary net position as a percentage of the total pension liability	14.87%	18.83%	22.32%
Total collective net pension liability for the Kentucky Employees Retirement System (KERS) non-hazardous employees	\$ 11,399,489,047	\$ 10,031,891,000	\$ 8,971,820,000
KERS' non-hazardous employees total fiduciary net position	\$ 1,980,292,118	\$ 2,327,782,000	\$ 2,578,290,000
KERS' non-hazardous employees total pension liability	\$ 13,379,781,165	\$ 12,359,673,000	\$ 11,550,110,000

Note: Schedule is intended to show information for 10 years. Additional years will be displayed as they become available

See accompanying auditor's report and note to the required supplemental information.

Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation
Schedule of Required Contributions
June 30, 2016

	<u>FY 2016</u>	<u>FY 2015</u>	<u>FY 2014</u>
Authority's contractually required contribution	\$ 479,957	\$ 502,383	\$ 567,008
Authority's contributions in relation to the contractually required contribution	(479,957)	(502,383)	(301,000)
Authority's contribution deficiency	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 266,008</u>
Authority's covered-employee payroll	1,556,281	1,628,998	1,740,891
Authority's contributions as a percentage of covered-employee payroll	30.84%	30.84%	17.29%
	<u>FY 2016</u>	<u>FY 2015</u>	<u>FY 2014</u>
Corporation's contractually required contribution	\$ 4,202,759	\$ 4,339,713	\$ 4,453,180
Corporation's contributions in relation to the contractually required contribution	(4,202,759)	(4,339,713)	(2,364,000)
Corporation's contribution deficiency	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,089,180</u>
Corporation's covered-employee payroll	13,627,623	14,071,702	13,672,643
Corporation's contributions as a percentage of covered-employee payroll	30.84%	30.84%	17.29%

Note: Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.

See accompanying auditor's report and note to the required supplemental information.

**Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation
Note to the Required Supplemental Information
June 30, 2016**

Actuarial valuation date	June 30, 2016
Actuarial cost method	Entry age
Amortization method	Level of percentage of payroll, closed
Remaining amortization period	27 years
Asset valuation method	5 year smoothed market
Inflation	3.25%
Projected salary increases	4.00%, average, including inflation
Investment rate of return	6.75%, net of investment expense, including inflation

See accompanying independent auditor's report.