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NORTH CAROLINA  
STATE EDUCATION ASSISTANCE AUTHORITY

Financial Statements

June 30, 2014 and 2013

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The Officers and Directors  
North Carolina State Education Assistance Authority  
Research Triangle Park, North Carolina

## INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying financial statements of the North Carolina State Education Assistance Authority, a nonmajor component unit of the State of North Carolina, as of and for the years ended June 30, 2014 and 2013, and the related notes to the financial statements, which collectively comprise the Authority's financial statements as listed in the table of contents.

### *Management's Responsibility for the Financial Statements*

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

### *Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

### *Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the North Carolina State Education Assistance Authority, as of June 30, 2014 and 2013, and the respective changes in financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

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***Adoption of GASB Statement No. 65, Items Previously Reported as Assets and Liabilities***

As discussed in Notes 1, 10, and 11 to the financial statements, the Authority adopted new accounting guidance, GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. Our opinion is not modified with respect to this matter.

***Other Matter***

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 7 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Government Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the 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 financial statements, and other knowledge we obtained during our audits of the 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.

*Koonce, Wooten & Haywood, L.L.P.*

Raleigh, North Carolina  
September 30, 2014

NORTH CAROLINA  
STATE EDUCATION ASSISTANCE AUTHORITY  
Management's Discussion and Analysis  
June 30, 2014 and 2013

The Management's Discussion and Analysis of the financial performance of the North Carolina State Education Assistance Authority (the Authority) is required supplementary information. This narrative overview and analysis of the financial activities of the Authority is for the fiscal years ended June 30, 2014 and 2013. We encourage readers to consider this information in conjunction with the Authority's financial statements which follow.

#### FINANCIAL HIGHLIGHTS

**Net Position** -- The assets of the Authority exceeded its liabilities at fiscal years ending June 30, 2014 and 2013 by approximately \$553 and \$554 million, respectively, (presented as "net position"). Of this amount, approximately \$66.5 and \$66.8 million, respectively, was reported as "unrestricted net position." Unrestricted net position represents the amount available to be used to meet the Authority's ongoing operating obligations.

**Decrease in Net Position** -- The Authority's total net position decreased by approximately \$1.4 million (.26%) in fiscal year 2014 and approximately \$9.3 million (1.66%) in fiscal year 2013. The fiscal year ending June 30, 2013 includes a restatement to net position reflecting a \$12 million decrease attributed to a change in accounting principle. See Note 11 for further detail.

#### OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the North Carolina State Education Assistance Authority's financial statements. The Authority's financial statements include four components: 1) Statements of Net Position, 2) Statements of Revenues, Expenses and Changes in Net Position, 3) Statements of Cash Flows, and 4) Notes to the Financial Statements. Per the criteria detailed in Government Accounting Standards Board Statement No. 61, the Authority is presented as a nonmajor component unit in the State of North Carolina Comprehensive Annual Financial Report (CAFR) by the State Auditor's Office and the Office of the State Controller. The financial statements contained herein report information pertaining to the Authority.

The financial statements provide a broad view of the Authority's operations in a manner similar to private-sector business. The statements provide both short-term and long-term information about the Authority's financial position, which assists in assessing the Authority's economic condition at the end of each fiscal year. These statements are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. This basically means they follow methods that are similar to those used by most businesses. They take into account all revenues and expenses connected with the fiscal years even if cash involved has not been received or paid.

The statements of net position present all of the Authority's assets and liabilities, with the difference between the two reported as "net position." Over time, increases or decreases in the Authority's net position may serve as a useful indicator of whether the financial position of the Authority is improving or deteriorating.

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The statements of revenues, expenses, and changes in net position present information showing how the Authority's net position changed during the most recent fiscal years. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in these statements for some items that will not result in cash flows until future fiscal periods.

The statements of cash flows present a reconciliation of cash and cash equivalents between the beginning of a year and the end of a year. These statements assist in assessing the Authority's ability to generate future net cash flows, ability to meet obligations as they come due, reasons for differences in operating income and cash flows from operations, and the effect of noncash transactions.

## FINANCIAL ANALYSIS

### Net Position

As noted earlier, net position may serve over time as a useful indicator of an entity's financial position. The Authority's net position totaled approximately \$553 million as of June 30, 2014, compared to approximately \$554 million as of June 30, 2013.

NORTH CAROLINA  
STATE EDUCATION ASSISTANCE AUTHORITY'S  
Condensed Statements of Net Position

	<u>2014</u>	<u>2013</u>
Current Assets	\$ 657,370,419	\$ 789,846,590
Noncurrent Assets	3,758,711,046	3,548,652,861
Capital Assets	<u>5,071,142</u>	<u>5,321,543</u>
Total Assets	<u>\$ 4,421,152,607</u>	<u>\$ 4,343,820,994</u>
Current Liabilities	\$ 376,602,974	\$ 346,204,195
Noncurrent Liabilities	<u>3,395,409,190</u>	<u>3,383,007,309</u>
Total Liabilities	<u>3,772,012,164</u>	<u>3,729,211,504</u>
Deferred Inflows of Resources	<u>95,865,459</u>	<u>59,859,562</u>
Net Investment in Capital Assets	5,071,142	5,321,544
Restricted for Educational Assistance Programs	481,611,200	482,578,652
Unrestricted	<u>66,592,642</u>	<u>66,849,732</u>
Total Net Position	<u>553,274,984</u>	<u>554,749,928</u>
Total Liabilities and Net Position	<u>\$ 4,421,152,607</u>	<u>\$ 4,343,820,994</u>

The largest portion of the Authority's net position (87% at June 30, 2014 and June 30, 2013) represents resources that are subject to external restrictions on how they may be used. An additional portion (.92% at June 30, 2014 and .96% at June 30, 2013) reflects the Authority's investment in capital assets such as equipment, data processing systems, and intangible assets. The Authority uses these capital assets to provide educational assistance services; consequently, these assets are not available for future spending. The remaining balance of unrestricted net position may be used to meet the Authority's ongoing operating obligations. Internally imposed designations of resources are not presented as restricted net position.

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At the end of the current fiscal year, the Authority is able to report positive balances in all three categories of net position. The same situation held true for the prior fiscal year.

Changes in Net Position

The Authority's net position decreased by approximately \$1.4 million or .26% during the year ended June 30, 2014, and decreased by approximately \$9.3 million or 1.66% during the year ended June 30, 2013.

	2014	2013
REVENUES:		
Operating Revenues:		
Interest Earnings on Loans	\$ 52,834,384	\$ 56,563,982
Miscellaneous	<u>10,221,600</u>	<u>8,202,216</u>
Total Operating Revenues	<u>63,055,984</u>	<u>64,766,198</u>
Nonoperating Revenues:		
State Aid	105,481,975	110,614,929
Grants	75,047,258	94,257,925
Investment Earnings	<u>4,059,699</u>	<u>1,251,485</u>
Total Nonoperating Revenues	<u>184,588,932</u>	<u>206,124,339</u>
Total Revenues	<u>247,644,916</u>	<u>270,890,537</u>
EXPENSES:		
Operating Expenses:		
Services	41,953,703	48,900,321
Interest	30,239,512	34,819,265
Student Loan Service Cancellations	14,572,765	17,678,285
Depreciation	250,402	352,803
Other Expenses	<u>4,007,505</u>	<u>3,881,291</u>
Total Operating Expenses	<u>91,023,887</u>	<u>105,631,965</u>
Nonoperating Expenses:		
Grants, Aid and Subsidies	<u>158,095,973</u>	<u>174,650,205</u>
Total Nonoperating Expenses	<u>158,095,973</u>	<u>174,650,205</u>
Total Expenses	<u>249,119,860</u>	<u>280,282,170</u>
CHANGES IN NET POSITION	(1,474,944)	(9,391,633)
NET POSITION--Beginning of Year, as Restated	<u>554,749,928</u>	<u>564,141,561</u>
NET POSITION--End of Year	<u>\$ 553,274,984</u>	<u>\$ 554,749,928</u>

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Approximately 25.5% of the Authority's total revenues came from interest earnings and other miscellaneous revenue on resources invested in student loans under various education programs originated by or assigned to the Authority. An additional 30.3% resulted from grants that include federal and state aid and state designated funds for student assistance. Approximately 42.6% of total revenues came from the State of North Carolina Education Lottery and interest earnings on and corpus from escheated monies held by the State. These funds were distributed to the Authority pursuant to State law for the purpose of providing grants to North Carolina residents enrolled at certain institutions of higher education in North Carolina. Lastly, an additional 1.6% resulted from investment earnings on cash, cash equivalents, and short-term and long-term investments during the fiscal year.

The Authority's expenses cover a range of services. Approximately 16.8% of the Authority's total expenses were for personnel costs, fees paid to others in exchange for administration of education assistance programs, collection costs related to student loans, and fees for professional and specialized services incurred by the Authority to maintain and enhance its information dissemination program on planning, applying, and paying for higher education. Approximately 12.1% of expenses were for interest incurred on bonds issued by the Authority in order to fund student loans, 63.5% were for grants and aid distributed for education assistance, and 5.8% were for student loan service cancellations related to certain state sponsored loan programs.

The decrease in net position for the year ended June 30, 2014 is primarily attributable to decreased revenue flows in the Student Loan Finance Program as a result of obligations associated with the U.S. Department of Education's authority over the Federal Family Education Loan Program.

## CAPITAL ASSETS AND DEBT ADMINISTRATION

### Capital Assets

The Authority's investment in capital assets as of June 30, 2014 amounts to approximately \$18.8 million, net of accumulated depreciation of approximately \$13.7 million, leaving a net book value of approximately \$5.1 million. The Authority's investment in capital assets as of June 30, 2013 amounts to approximately \$18.8 million, net of accumulated depreciation of approximately \$13.5 million, leaving a net book value of approximately \$5.3 million. This investment in capital assets includes office furniture and equipment, data processing systems, other equipment, and intangible assets.

There was no change in the Authority's gross investment in capital assets for the fiscal year 2014. The total gross increase in the Authority's investment in capital assets for the fiscal year 2013 was approximately \$.01 million.

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Bonds Payable

All long-term indebtedness represents special obligations of the Authority and does not constitute a debt, liability, or obligation of the State of North Carolina. The 2008-1 Series Bonds are secured by certain non-federal loans of the Authority which are not insured by the federal government. All other indebtedness is secured by federally insured student loans of the Authority.

The Authority's total debt decreased by approximately \$280 million (11.3%) and approximately \$402 million (14%) during the fiscal years 2014 and 2013, respectively. The majority of the 2014 decrease was attributable to the Authority's repayment of debt.

Additional information on the Authority's debt obligations can be found in Note 6 of the notes to the financial statements of this report.

**ECONOMIC FACTORS**

The primary economic factors affecting the Authority result from economic trends coupled with the effects of decisions of the federal government related to student loans. The low interest rate environment continued to compress returns on the Authority's student loan portfolio over the past year. At the same time, certain decisions of the U.S. Department of Education in administering the federal student loan programs pursuant to changes in federal law along with budgetary actions of the Congress have operated to decrease the flow of federal revenue to guaranty agencies and holders of student loans. While the value of the Authority's student loan portfolio has not increased due to new guaranteed student loan originations, and the existing portfolio is maturing through repayment, the revenues and obligations associated with the Authority's portfolio of financed student loans and loans under guaranty remain relatively constant for the immediate and intermediate future. The Authority anticipates that as economic trends produce higher interest rates, the strain on the student loan portfolio due to changes in fees charged by the Department of Education will be ameliorated.

In direct response to the changes in federal law, the Authority, in collaboration with College Foundation, Inc., has developed and launched new services for colleges and universities, including the verification of student financial aid application data and a series of financial education and default prevention services. In addition, and at the behest of the North Carolina General Assembly, the Authority is working with the University of North Carolina, as well as the other principal sectors of higher education, to create operational efficiencies in determining residency for tuition purposes. The Authority expects these new services to generate net revenue in the years ahead, and although there is growth in demand for the services, verification is particular, the actual collective impact of these new endeavors is difficult to quantify.

STATEMENTS OF NET POSITION

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STATE EDUCATION ASSISTANCE AUTHORITY  
Statements of Net Position  
June 30, 2014 and 2013

ASSETS

	2014	2013
<b>CURRENT ASSETS:</b>		
Cash and Cash Equivalents	\$ 47,071,628	\$ 55,237,464
Restricted Cash and Cash Equivalents	202,000,547	291,547,686
Restricted Investments	114,268,092	94,896,575
Receivables:		
Accounts Receivable	7,086,197	8,474,253
Intergovernmental Receivables	1,753,032	1,359,461
Interest Receivable	35,478,686	42,279,812
Due From Component Unit	2,508,080	2,906,852
Notes Receivable	247,151,395	293,075,240
Prepaid Items	52,762	69,247
Total Current Assets	657,370,419	789,846,590
<b>NONCURRENT ASSETS:</b>		
Restricted Cash and Cash Equivalents	181,707,591	42,516,504
Restricted Investments	1,439,446,926	1,143,429,256
Notes Receivable	2,137,556,529	2,362,707,101
Total Noncurrent Assets	3,758,711,046	3,548,652,861
<b>CAPITAL ASSETS:</b>		
Office Furniture and Equipment	175,641	175,641
Data Processing Systems	13,286,816	13,286,816
Other Equipment	311,009	311,009
Intangible Assets	5,000,000	5,000,000
Accumulated Depreciation	(13,702,324)	(13,451,923)
Net Capital Assets	5,071,142	5,321,543
 Total Assets	 \$ 4,421,152,607	 \$ 4,343,820,994

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

## LIABILITIES AND NET POSITION

	<u>2014</u>	<u>2013</u>
<b>CURRENT LIABILITIES:</b>		
Accounts Payable and Accrued Liabilities:		
Accounts Payable	\$ 22,048,657	\$ 21,791,617
Accrued Payroll	107,130	82,328
Interest Payable	2,745,809	3,077,507
Due to IRC Section 529 Plan Participants	121,424,872	86,237,694
Bonds Payable	230,263,593	235,009,792
Accrued Vacation Leave	12,913	5,257
Total Current Liabilities	<u>376,602,974</u>	<u>346,204,195</u>
<b>NONCURRENT LIABILITIES:</b>		
Due to IRC Section 529 Plan Participants	1,427,737,374	1,139,830,465
Bonds Payable	1,967,303,359	2,242,835,699
Accrued Vacation Leave	368,457	341,145
Total Noncurrent Liabilities	<u>3,395,409,190</u>	<u>3,383,007,309</u>
Total Liabilities	<u>3,772,012,164</u>	<u>3,729,211,504</u>
<b>DEFERRED INFLOWS OF RESOURCES</b>		
Deferred Inflows-Nonexchange Transactions	<u>95,865,459</u>	<u>59,859,562</u>
<b>NET POSITION:</b>		
Net Investment in Capital Assets	5,071,142	5,321,544
Restricted for Educational Assistance Programs	481,611,200	482,578,652
Unrestricted	66,592,642	66,849,732
Total Net Position	<u>553,274,984</u>	<u>554,749,928</u>
Total Liabilities and Net Position	<u>\$ 4,421,152,607</u>	<u>\$ 4,343,820,994</u>

NORTH CAROLINA  
STATE EDUCATION ASSISTANCE AUTHORITY  
Statements of Revenues, Expenses and Changes in Net Position  
For the Years Ended June 30, 2014 and 2013

	2014	2013
<b>OPERATING REVENUES:</b>		
Interest Earnings on Loans	\$ 52,834,384	\$ 56,563,982
Miscellaneous	10,221,600	8,202,216
Total Operating Revenues	63,055,984	64,766,198
<b>OPERATING EXPENSES:</b>		
Personal Services	3,679,048	3,434,920
Supplies and Materials	43,013	54,433
Services	38,274,655	45,465,401
Interest	30,239,512	34,819,265
Depreciation	250,402	352,803
Student Loan Service Cancellations	14,572,765	17,678,285
Other Expenses	3,964,492	3,826,858
Total Operating Expenses	91,023,887	105,631,965
Operating Loss	(27,967,903)	(40,865,767)
<b>NONOPERATING REVENUES (EXPENSES):</b>		
State Aid	105,481,975	110,614,929
Noncapital Grants	73,356,483	92,425,100
Federal Grants	1,690,775	1,832,825
Investment Earnings	4,059,699	1,251,485
Grants, Aid and Subsidies	(158,095,973)	(174,650,205)
Total Nonoperating Revenues (Expenses)	26,492,959	31,474,134
Changes in Net Position	(1,474,944)	(9,391,633)
NET POSITION--Beginning of Year, as Restated	554,749,928	564,141,561
NET POSITION--End of Year	\$ 553,274,984	\$ 554,749,928

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

NORTH CAROLINA  
STATE EDUCATION ASSISTANCE AUTHORITY  
Statements of Cash Flows  
For the Years Ended June 30, 2014 and 2013

	2014	2013
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Receipts from Customers	\$ 377,463,253	\$ 278,423,667
Collection of Loans from Students	405,098,977	553,263,846
Payments to Employees and Fringe Benefits	(3,619,278)	(3,429,815)
Payments to Vendors and Suppliers	(41,270,250)	(52,640,123)
Loans Issued to Students	(96,833,024)	(131,444,075)
Payments of Operating Interest Expense	(27,846,608)	(32,436,126)
Net Cash Provided by Operating Activities	612,993,070	611,737,374
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>		
Proceeds from Sale of Bonds and Notes		1,139,143,780
Repayment of Bond Principal	(282,671,443)	(1,539,950,367)
State Aid	105,481,975	110,614,929
Noncapital Grants	73,356,483	92,425,100
Federal Grants	1,690,775	1,832,825
Grants, Aid and Subsidies	(158,095,973)	(174,650,205)
Net Cash Used by Noncapital Financing Activities	(260,238,183)	(370,583,938)
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>		
Acquisition of Capital Assets		(16,955)
Net Cash Used by Capital and Related Financing Activities		(16,955)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Proceeds from the Sale and Maturities of Non-State Treasurer Investments	834,311,703	2,755,289,943
Investment Earnings	1,681,807	1,703,766
Purchase of Non-State Treasurer Investments	(1,147,270,285)	(2,899,650,474)
Net Cash Used by Investing Activities	(311,276,775)	(142,656,765)
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	41,478,112	98,479,716
<b>CASH AND CASH EQUIVALENTS--Beginning of Year</b>	389,301,654	290,821,938
<b>CASH AND CASH EQUIVALENTS--End of Year</b>	\$ 430,779,766	\$ 389,301,654

NORTH CAROLINA  
STATE EDUCATION ASSISTANCE AUTHORITY  
Statements of Cash Flows  
For the Years Ended June 30, 2014 and 2013

	2014	2013
RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating Loss	\$ (27,967,903)	\$ (40,865,767)
Adjustments to Reconcile Operating Loss to Net Cash Provided by Operating Activities:		
Depreciation	250,402	352,803
Original Issue Discount Expensed	2,392,904	2,383,139
Student Loan Principal Repayments	337,441,844	478,853,626
Student Loans Issued	(32,395,278)	(79,839,875)
Student Loan Cancellations and Write-offs	13,333,748	14,056,238
Allowances and Uncollectible Accounts	1,489,000	3,790,000
Capitalized Interest and Other	(48,794,897)	(34,326,641)
(Increase) Decrease in Assets:		
Accounts Receivable	1,388,056	(50,912)
Intergovernmental Receivables	(393,571)	2,842,655
Investment Earnings Receivable	6,748,413	13,773,919
Due from Component Units	398,772	(265,114)
Prepaid Expense	16,484	(24,967)
Increase (Decrease) in Liabilities:		
Accounts Payable	(74,658)	(2,867,738)
Accrued Payroll	24,802	(4,681)
Due to IRC Section 529 Plan Participants	323,094,087	253,920,903
Accrued Vacation Leave	34,968	9,786
Increase in Deferred Inflows	36,005,897	
Net Cash Provided by Operating Activities	\$ 612,993,070	\$ 611,737,374
 SUPPLEMENTAL DISCLOSURE OF CASH FLOWS INFORMATION:		
Cash Paid During the Year for Interest	\$ 28,178,306	\$ 33,901,686
 NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES:		
Noncash Distributions from State Treasurer		
Long-Term Investment Pool	\$ 1,940,654	\$ 2,025,672
Write-Up (Down) of Investments to Fair Market Value	\$ 489,950	\$ (2,473,532)

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

NORTH CAROLINA  
STATE EDUCATION ASSISTANCE AUTHORITY  
Notes to Financial Statements  
June 30, 2014 and 2013

1. Summary of Significant Accounting Policies

A. Organization and Reporting Entity:

Governmental Accounting Standards Board (GASB) Statement No. 61, *The Financial Reporting Entity: Omnibus – An Amendment of GASB Statements No. 14 and No. 34*, clarifies the types of relationships that affect the determination of major component units in the financial reporting entity. As a result of GASB No. 61, the North Carolina State Education Assistance Authority is presented as a nonmajor component unit in the State of North Carolina Comprehensive Annual Financial Reports (CAFR) by the State Auditor's Office and the Office of the State Controller.

The State Education Assistance Authority is a legally separate authority created to provide a system of financial assistance, consisting of grants, loans, work-study or other employment, and other aids, to qualified students to obtain an education. The Authority is governed by a nine-member board of directors, seven of whom are appointed by the Governor and two of whom shall be ex officio. The state provides program subsidies to the Authority.

The accompanying financial statements present all funds subject to the direct administrative authority and responsibility of the Authority. These funds are as follows:

1. Student Aid Funds
2. North Carolina Student Loan Fund
3. Guaranteed Student Loan Revenue Bond Fund and Conduit Funding Program
4. UNC Need-Based Grant Program
5. Principal Fellows Program
6. Paul Douglas Teacher Scholarship Loan Program
7. Golden LEAF Scholars Program
8. North Carolina National College Savings Program
9. Guaranty Reserve Funds
10. Education Lottery Scholarship Fund
11. John B. McLendon Scholarship Fund
12. Child Welfare Postsecondary Support Program
13. National Board for Professional Teaching Standards Loan Program
14. Forgivable Education Loans for Service Program
  - Comprised of the following programs combined in 2013:
    - Student Loan Program for Health, Science and Mathematics
    - North Carolina Nurse Scholarship Loan Program
    - North Carolina Maters Nurse Scholarship Loan Program
    - North Carolina Nurse Education Scholarship Loan Program
    - Social Workers Scholarship Loan Program
    - Millennium Teacher Scholarship Loan Program
    - Future Teachers of North Carolina Scholarship Loan Program
    - Physical Education/Coaching Scholarship Loan Program
    - Prospective Teacher/Teacher Assistant Scholarship Loan Program
    - Board of Governor's Dental Scholarship Loan Program
    - Board of Governor/s Medical Scholarship Loan Program
    - Graduate Nurse Scholarship Loan Program
    - Optometry Scholarship Loan Program

A special restricted trust fund, maintained in State budget code 66010, is used to insure loans to students by eligible lenders according to the provisions of the Higher Education Act of 1965, as amended.

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STATE EDUCATION ASSISTANCE AUTHORITY  
Notes to Financial Statements  
June 30, 2014 and 2013

1. Summary of Significant Accounting Policies (Continued)

B. Basis of Presentation:

The accompanying financial statements are presented in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

During the year ended June 30, 2014, the Authority implemented GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This Statement amends the financial statement element classification of certain items previously reported as assets and liabilities. As a result, debt issuance costs are no longer capitalized and amortized over the life of the debt but rather recognized as an expense in the period incurred.

During the year ended June 30, 2014, the Authority implemented GASB Statement No. 66, *Technical Corrections - 2012 - An Amendment of GASB Statements No. 10 and No. 62*. The objective of this is to improve accounting and financial reporting by resolving conflicting guidance that resulted from the issuance of GASB Statements No. 54 and No. 62.

During the year ended June 30, 2013, the Authority implemented GASB Statement No. 61, *The Financial Reporting Entity: Omnibus – An Amendment of GASB Statements No. 14 and No. 34*. As a result, the Authority is presented as a nonmajor component unit in the State of North Carolina Comprehensive Annual Financial Reports (CAFR).

During the year ended June 30, 2013, the Authority implemented GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. This statement incorporates into the GASB authoritative literature certain accounting and financial reporting guidance included in Financial Accounting Standards Board (FASB) and American Institute of Certified Public Accountants' (AICPA) pronouncements issued on or before November 30, 1989.

During the year ended June 30, 2013, the Authority implemented GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*. This Statement amends the net asset reporting requirements in previous standards by incorporating deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position.

C. Basis of Accounting:

The financial statements of the Authority have been prepared on the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred, regardless of the timing of the cash flows.

Nonexchange transactions, in which the Authority receives (or gives) value without directly giving (or receiving) equal value in exchange includes state appropriations and certain grants. Revenues are recognized as soon as all eligibility requirements imposed by the provider have been met.

The Authority is a sub-agency of the University of North Carolina - General Administration (UNC-GA). As a sub-agency, its records are maintained on the UNC-GA accounting system under the National Association of Colleges and University Business Offices fund structure.

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1. Summary of Significant Accounting Policies (Continued)

Accounting records for funds with state appropriated budgets are maintained on the cash basis of accounting. The cash basis records are adjusted as of the end of the fiscal year in order to prepare accrual basis financial statements.

The Statements of Net Position include a self-balancing set of assets, liabilities, deferred inflows of resources, and net position that report the financial position of the Authority at the end of the fiscal years ended June 30, 2014 and 2013. The Statements of Revenues, Expenses and Changes in Net Position include the one accounting fund group and identify activities which changed net position balances during the fiscal years.

D. Cash and Cash Equivalents:

This classification includes deposits held by the State Treasurer in the short-term investment fund, as well as cash on deposit with trustees/custodians. The short-term investment fund maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty. Additional information regarding cash and cash equivalents is provided in Note 2.

E. Investments:

This classification includes deposits held by the State Treasurer in certain long-term investment funds, as well as investments with trustees/custodians. Investments generally are reported at fair value, as determined by quoted market prices. The net increase (decrease) in the fair value of investments is recognized as a component of investment earnings. Additional information regarding investments is provided in Note 2.

F. Receivables:

Provision for expenses and losses on receivables is made in amounts required to maintain an adequate allowance to cover receivables paid through service cancellations and bad debts. At year end, the allowance is adjusted by management based on review of the receivables.

G. Capital Assets:

Capital assets are stated at cost at date of acquisition or fair value at date of donation in the case of gifts. The Authority capitalizes assets that have a value or cost of \$5,000 or greater at the date of acquisition and an estimated useful life of more than one year except for internally generated software which is capitalized when the value or cost is \$1,000,000 or greater and other intangible assets which are capitalized when the value or cost is \$100,000 or greater. Depreciation is computed using the straight-line method over the estimated useful lives of the assets as follows: Office furniture and equipment, data processing systems, and other equipment--5 to 8 years.

H. Restricted Assets:

Restricted assets represent assets whose use is restricted by external parties, by law through constitutional provisions, or by enabling legislation of other governments.

I. Noncurrent Long-Term Liabilities:

Noncurrent long-term liabilities include amounts due to participants in the IRC Section 529 savings plan, principal amounts of bonds and notes payable, and compensated absences that will not be paid within the next fiscal year.

Original issue discounts are deferred and amortized over the life of the debt using the straight-line method.

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1. Summary of Significant Accounting Policies (Continued)

J. Compensated Absences:

The Authority's policy is to record the cost of vacation leave when earned. The policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1<sup>st</sup> or for which an employee can be paid upon termination of employment. When classifying compensated absences into current and noncurrent, leave is considered taken using a last in, first out (LIFO) method. Also, any accumulated vacation leave in excess of 30 days at year-end is converted to sick leave. Under this policy, the accumulated vacation leave for each employee at June 30<sup>th</sup> equals the leave carried forward at the previous December 31<sup>st</sup>, plus the leave earned, less the leave taken between January 1<sup>st</sup> and June 30<sup>th</sup>.

In addition to the vacation leave described above, compensated absences include the accumulated unused portion of the special annual leave bonuses awarded by the North Carolina General Assembly. The bonus leave balance on December 31<sup>st</sup> is retained by employees and transferred into the next calendar year. It is not subject to the limitation on annual leave carried forward described above and is not subject to conversion to sick leave.

There is no liability for unpaid accumulated sick leave because the Authority has no obligation to pay sick leave upon termination or retirement. However, additional service credit for retirement pension benefits is given for accumulated sick leave upon retirement.

K. Net Position:

The Authority's net position is classified as follows:

**Net Investment in Capital Assets:** This represents the Authority's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of net investment in capital assets.

**Restricted Net Position--Nonexpendable:** Nonexpendable restricted net position includes endowments and similar type assets whose use is limited by donors or other outside sources, and, as a condition of the gift, the principal is to be maintained in perpetuity. The Authority currently has no nonexpendable restricted net position.

**Restricted Net Position--Expendable:** Expendable restricted net position includes resources for which the Authority is legally or contractually obligated to spend in accordance with restrictions imposed by external parties.

**Unrestricted Net Position:** Unrestricted net position includes resources derived from noncapital state grants and related state-supported loan programs.

Restricted and unrestricted resources are tracked using a fund accounting system and are spent in accordance with established fund authorities. Fund authorities provide rules for the fund activity and are separately established for restricted and unrestricted activities. Resources are applied on a transactional basis with unrestricted resources applied to expenses of a general unrestricted nature and to expenses of a restricted nature when restricted resources are unavailable. Restricted resources, when available, are applied to appropriate restricted expenses. Both restricted and unrestricted net position include consideration of deferred inflows and outflows of resources.

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1. Summary of Significant Accounting Policies (Concluded)

L. Revenue and Expense Recognition:

The Authority classifies its revenues and expenses as operating or nonoperating in the accompanying Statements of Revenues, Expenses, and Changes in Net Position. Operating revenues and expenses generally result from providing services in connection with the Authority's principal ongoing operations. Operating revenues include activities that have characteristics of exchange transactions, such as (1) interest earned on loans and (2) borrower recoveries and fees. Operating expenses are all expense transactions incurred other than those related to capital and noncapital financing or investing activities.

Nonoperating revenues include activities that have the characteristics of nonexchange transactions. Revenues from nonexchange transactions and State appropriations that represent subsidies to the Authority, as well as investment income, are considered nonoperating since these are either investing, capital or noncapital financing activities.

M. Income Taxes:

The Authority is a political subdivision of the State of North Carolina. Accordingly, exemption from state and local taxation is provided by Chapter 116, Article 23 of the North Carolina General Statutes. Internal Revenue Code Section 115 provides exemption from federal income taxes.

N. Accounting Estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of allowance for service cancellations and doubtful accounts, and the calculation of current and noncurrent notes receivable, due to IRC Section 529 plan participants, and bonds payable.

2. Deposits and Investments

A. Deposits:

Unless specifically exempt, the Authority is required by North Carolina General Statute 147-77 to deposit moneys received with the State Treasurer or with a depository institution in the name of the State Treasurer. In addition, General Statute 116-36.1 requires the Authority to deposit its institutional trust funds with the State Treasurer.

At June 30, 2014 and 2013, the amounts shown on the Statements of Net Position as cash and cash equivalents include \$365,403,832 and \$335,525,662, respectively, which represent the Authority's equity position in the State Treasurer's Short-Term Investment Fund. The Short-Term Investment Fund (a portfolio within the State Treasurer's Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating) had a weighted average maturity of 1.3 years and 1.6 years as of June 30, 2014 and 2013, respectively. Assets and shares of the Short-Term Investment Fund are valued at amortized cost, which approximates fair value. Deposit and investment risks associated with the State Treasurer's Investment Pool (which includes the State Treasurer's Short-Term Investment Fund) are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Reports," or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

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2. Deposits and Investments (Continued)

Cash on hand at June 30, 2014 and 2013 was \$430,779,766 and \$389,301,654, respectively. The carrying amount and bank balance of the Authority's deposits not with the State Treasurer at June 30, 2014 was \$65,375,934. The carrying amount and bank balance of the Authority's deposits not with the State Treasurer at June 30, 2013 was \$53,775,992. Custodial credit risk is the risk that in the event of a bank failure, the Authority's deposits may not be returned to it. The Authority has a deposit policy for custodial credit risk. As of June 30, 2014 and 2013, none of the Authority's bank balance was exposed to custodial credit risk.

**B. Investments:**

North Carolina General Statutes 147-69.1(c) and 147-69.2, which are applicable to the Authority, authorize the State Treasurer to invest in the following: obligations of or fully guaranteed by the United States; obligations of certain federal agencies; repurchase agreements; obligations of the State of North Carolina; time deposits of specified institutions; prime quality commercial paper, and asset-backed securities with specified ratings. Also, General Statute 147-69.1(c) authorizes the following: specified bills of exchange or time drafts and corporate bonds and notes with specified ratings. General Statute 147-69.2 authorizes the following: general obligations of other states; general obligations of North Carolina local governments; and obligations of certain entities with specified ratings.

Investments totaled \$1,553,715,018 at June 30, 2014 and \$1,238,325,831 at June 30, 2013. The Authority's portion of the State Treasurer's Long-Term Investment Fund at June 30, 2014 and 2013 was \$42,579,737 and \$40,149,133, respectively. The Authority's investments not with the State Treasurer as of June 30, 2014 and 2013 totaled \$1,511,135,281 and \$1,198,176,698, respectively.

In accordance with bond resolutions, bond proceeds and debt service funds are invested in obligations that will by their terms mature on or before the date funds are expected to be required for expenditure or withdrawal.

**Non-Pooled Investments:**

*Interest Rate Risk:* Interest rate risk is the risk the Authority may face should interest rate variances affect the fair value of investments. The Authority does not have a formal investment policy that addresses interest rate risk.

The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2014, for the Authority's non-pooled investments:

	Total	Investment Maturities (in Years)			
		Less Than 1	1 to 5	6 to 10	More Than 10
Investments Subject to Interest Rate Risk:					
Debt Mutual Funds	\$ 529,346,187	\$ 529,346,187	\$	\$	\$
Money Market Mutual Funds	143,451,315	143,451,315			
Total Investments Subject to Interest Rate Risk	<u>672,797,502</u>	<u>\$ 672,797,502</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>
Investments Not Subject to Interest Rate Risk:					
Other Mutual Funds	838,337,779				
Total Non-Pooled Investments	<u>\$ 1,511,135,281</u>				

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2. Deposits and Investments (Continued)

The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2013, for the Authority's non-pooled investments:

	Total	Investment Maturities (in Years)			
		Less Than 1	1 to 5	6 to 10	More Than 10
Investments Subject to Interest Rate Risk:					
Debt Mutual Funds	\$ 439,286,688	\$ 439,286,688	\$	\$	\$
Money Market Mutual Funds	<u>138,659,364</u>	<u>138,659,364</u>			
Total Investments Subject to Interest Rate Risk	<u>577,946,052</u>	<u>\$ 577,946,052</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>
Investments Not Subject to Interest Rate Risk:					
Other Mutual Funds	<u>620,230,646</u>				
Total Non-Pooled Investments	<u>\$ 1,198,176,698</u>				

*Credit Risk:* Credit Risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Authority has formally adopted investment policies for credit risk stating that certain investment obligations shall bear one of the two highest ratings by nationally recognized rating services.

As of June 30, 2014, the Authority's non-pooled investments had the following credit quality distribution for securities with credit exposure:

	Fair Value	AAA Aaa	AA Aa	A	BBB Baa	BB/Ba and Below	Unrated
Debt Mutual Funds	\$ 529,346,187	\$	\$	\$	\$	\$	\$ 529,346,187
Money Market Mutual Funds	<u>143,451,315</u>						<u>143,451,315</u>
Total	<u>\$ 672,797,502</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$ 672,797,502</u>

As of June 30, 2013, the Authority's non-pooled investments had the following credit quality distribution for securities with credit exposure:

	Fair Value	AAA Aaa	AA Aa	A	BBB Baa	BB/Ba and Below	Unrated
Debt Mutual Funds	\$ 439,286,688	\$	\$	\$	\$	\$	\$ 439,286,688
Money Market Mutual Funds	<u>138,659,364</u>						<u>138,659,364</u>
Total	<u>\$ 577,946,052</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$ 577,946,052</u>

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2. Deposits and Investments (Continued)

*Custodial Credit Risk:* Custodial credit risk is the risk that, in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Authority does not have a formal policy that addresses custodial credit risk.

At June 30, 2014, the Authority's non-pooled investments were exposed to custodial credit risk as follows:

Investments Not Categorized:	
Debt Mutual Funds	\$ 529,346,187
Money Market Mutual Funds	143,451,315
Other Mutual Funds	<u>838,337,779</u>
 Total Non-Pooled Investments	 \$ <u>1,511,135,281</u>

At June 30, 2013, the Authority's non-pooled investments were exposed to custodial credit risk as follows:

Investments Not Categorized:	
Debt Mutual Funds	\$ 439,286,688
Money Market Mutual Funds	138,659,364
Other Mutual Funds	<u>620,230,646</u>
 Total Non-Pooled Investments	 \$ <u>1,198,176,698</u>

*Concentration of Credit Risk:* Concentration of credit risk is the risk of loss attributable to the magnitude of an investment in a single issuer. The Authority does not have a formal policy that addresses concentration of credit risk. The Authority places no limit on the amount that may be invested in any one issuer. As of June 30, 2014 and 2013, the Authority had no non-pooled investments in any one issuer that equaled more than 5% of the Authority's total non-pooled investments.

*Foreign Currency Risk:* Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The Authority has formally adopted investment policies for foreign currency risk stating that foreign investments must be denominated in U.S. dollars or the securities must be traded solely on an exchange based in the United States. The Authority's non-pooled investments exposed to foreign currency risk are comprised entirely of amounts invested in International Mutual Funds. As of June 30, 2014, there was \$221,450,838 invested in International Mutual Funds. As of June 30, 2013, there was \$164,294,407 invested in International Mutual Funds.

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2. Deposits and Investments (Continued)

**Total Non-Pooled Investments:**

The following table presents the fair value of the Authority's total investments not with the State Treasurer at June 30, 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Debt Securities:		
Debt Mutual Funds	\$ 529,346,187	\$ 439,286,688
Money Market Mutual Funds	<u>143,451,315</u>	<u>138,659,364</u>
Total Debt Securities	<u>672,797,502</u>	<u>577,946,052</u>
Other Securities:		
Other Mutual Funds	<u>838,337,779</u>	<u>620,230,646</u>
Total Other Securities	<u>838,337,779</u>	<u>620,230,646</u>
 Total Non-Pooled Investments	 \$ <u>1,511,135,281</u>	 \$ <u>1,198,176,698</u>

**Reconciliation of Deposits and Investments:**

A reconciliation of deposits and investments for the Authority at June 30, 2014 and 2013 is as follows:

	<u>2014</u>	<u>2013</u>
Amount of Deposits with Private Financial Institutions	\$ 65,375,934	\$ 53,775,992
Deposits in the Short Term Investment Fund	365,403,832	335,525,662
Long-Term Investment Fund	42,579,737	40,149,133
Non-Pooled Investments	<u>1,511,135,281</u>	<u>1,198,176,698</u>
 Total Deposits and Investments	 \$ <u>1,984,494,784</u>	 \$ <u>1,627,627,485</u>
Deposits		
Current:		
Cash and Cash Equivalents	\$ 47,071,628	\$ 55,237,464
Restricted Cash and Cash Equivalents	202,000,547	291,547,686
Noncurrent:		
Restricted Cash and Cash Equivalents	<u>181,707,591</u>	<u>42,516,504</u>
 Total Deposits	 <u>430,779,766</u>	 <u>389,301,654</u>
Investments		
Current:		
Restricted Short-Term Investments	114,268,092	94,896,575
Noncurrent:		
Restricted Long-Term Investments	<u>1,439,446,926</u>	<u>1,143,429,256</u>
 Total Investments	 <u>1,553,715,018</u>	 <u>1,238,325,831</u>
 Total Deposits and Investments	 \$ <u>1,984,494,784</u>	 \$ <u>1,627,627,485</u>

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3. Receivables

The gross receivables and related allowances for service cancellations and doubtful accounts on student loans at June 30, 2014 were:

	<u>Total</u>	<u>Current</u>	<u>Noncurrent</u>
Note Receivable--XAP Corporation	\$ 1,624,219	\$ 541,406	\$ 1,082,813
Gross Student Loan Receivables	2,469,910,705	333,436,989	2,136,473,716
Less: Allowance for Service Cancellations and Doubtful Accounts	<u>86,827,000</u>	<u>86,827,000</u>	<u>                    </u>
Net Receivables	<u>\$ 2,384,707,924</u>	<u>\$ 247,151,395</u>	<u>\$ 2,137,556,529</u>

The gross receivables and related allowances for service cancellations and doubtful accounts on student loans at June 30, 2013 were:

	<u>Total</u>	<u>Current</u>	<u>Noncurrent</u>
Note Receivable--XAP Corporation	\$ 2,165,625	\$ 541,406	\$ 1,624,219
Gross Student Loan Receivables	2,738,954,716	377,871,834	2,361,082,882
Less: Allowance for Service Cancellations and Doubtful Accounts	<u>85,338,000</u>	<u>85,338,000</u>	<u>                    </u>
Net Receivables	<u>\$ 2,655,782,341</u>	<u>\$ 293,075,240</u>	<u>\$ 2,362,707,101</u>

4. Capital Assets

A summary of changes in capital assets for the year ended June 30, 2013 is presented as follows:

	<u>Balance July 1, 2013</u>	<u>Increases</u>	<u>Balance June 30, 2014</u>
Capital Assets Not Being Depreciated:			
Intangible Assets	\$ 5,000,000	\$	\$ 5,000,000
Capital Assets Being Depreciated:			
Office Furniture and Equipment	175,641		175,641
Data Processing Systems	13,286,817		13,286,817
Other Equipment	<u>311,009</u>		<u>311,009</u>
Total Capital Assets	<u>18,773,467</u>		<u>18,773,467</u>
Less Accumulated Depreciation for:			
Office Furniture and Equipment	169,306		169,306
Data Processing Systems	13,017,671	231,154	13,248,825
Other Equipment	<u>264,946</u>	<u>19,248</u>	<u>284,194</u>
Total Accumulated Depreciation	<u>13,451,923</u>	<u>250,402</u>	<u>13,702,325</u>
Net Capital Assets	<u>\$ 5,321,544</u>	<u>\$ 250,402</u>	<u>\$ 5,071,142</u>

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4. Capital Assets (Continued)

A summary of changes in capital assets for the year ended June 30, 2013 is presented as follows:

	Balance July 1, 2012	Increases	Decreases	Balance June 30, 2013
Capital Assets Not Being Depreciated:				
Intangible Assets	\$ 5,000,000	\$	\$	\$ 5,000,000
Capital Assets Being Depreciated:				
Office Furniture and Equipment	175,641			175,641
Data Processing Systems	13,286,452	8,589	8,224	13,286,817
Other Equipment	<u>302,643</u>	<u>8,366</u>		<u>311,009</u>
Total Capital Assets	<u>18,764,736</u>	<u>16,955</u>	<u>8,224</u>	<u>18,773,467</u>
Less Accumulated Depreciation for:				
Office Furniture and Equipment	161,200	8,106		169,306
Data Processing Systems	12,706,393	319,502	8,224	13,017,671
Other Equipment	<u>239,751</u>	<u>25,195</u>		<u>264,946</u>
Total Accumulated Depreciation	<u>13,107,344</u>	<u>352,803</u>	<u>8,224</u>	<u>13,451,923</u>
Net Capital Assets	\$ <u>5,657,392</u>	\$ <u>(335,848)</u>	\$ <u>0</u>	\$ <u>5,321,544</u>

5. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities at June 30, 2014 and 2013 were as follows:

	2014	2013
Accounts Payable	\$ 22,048,657	\$ 21,791,617
Accrued Payroll	<u>107,130</u>	<u>82,328</u>
	\$ <u>22,155,787</u>	\$ <u>21,873,945</u>

6. Noncurrent Liabilities

A. Changes in Noncurrent Liabilities:

A summary of changes in noncurrent liabilities for the year ended June 30, 2014 is presented as follows:

	Balance July 1, 2013	Additions	Reductions	Balance June 30, 2014	Current Portion
Bonds Payable	\$ 2,477,845,491	\$	\$ 280,278,539	\$ 2,197,566,952	\$ 230,263,593
Accrued Vacation Leave	346,402	34,968		381,370	12,913
Due to IRC Section 529					
Plan Participants	<u>1,226,068,159</u>	<u>420,551,640</u>	<u>97,457,553</u>	<u>1,549,162,246</u>	<u>121,424,872</u>
Total Noncurrent Liabilities	\$ <u>3,704,260,052</u>	\$ <u>420,586,608</u>	\$ <u>377,736,092</u>	\$ <u>3,747,110,568</u>	\$ <u>351,701,378</u>



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6. Noncurrent Liabilities (Continued)

	<u>Balance</u> <u>July 1, 2013</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>June 30, 2014</u>
Taxable Student Loan Backed Notes				
Student Loan Backed Notes,				
2011-1 Series:				
LIBOR Indexed:				
Tranche A-1 (Sold at 99.9%)				
Due 7/25/21 (Variable Rate)	\$ 18,716,370		\$ 18,716,370	0
Tranche A-2 (Sold at 99.1%)				
Due 1/26/26 (Variable Rate)	127,000,000		9,539,938	117,460,062
Tranche A-3 (Sold at 93.9%)				
Due 10/25/41 (Variable Rate)	220,000,000			220,000,000
Original Issue Discount	<u>(12,871,430)</u>		<u>(758,631)</u>	<u>(12,112,799)</u>
	<u>352,844,940</u>		<u>27,497,677</u>	<u>325,347,263</u>
Taxable Student Loan Backed Notes				
Student Loan Backed Notes,				
2011-2 Series:				
LIBOR Indexed:				
Tranche A-1 (Sold at 99.8%)				
Due 10/26/20 (Variable Rate)	97,436,726		44,195,281	53,241,445
Tranche A-2 (Sold at 97.5%)				
Due 7/25/25 (Variable Rate)	186,000,000			186,000,000
Tranche A-3 (Sold at 94.1%)				
Due 7/25/36 (Variable Rate)	113,000,000			113,000,000
Original Issue Discount	<u>(10,097,693)</u>		<u>(787,856)</u>	<u>(9,309,837)</u>
	<u>386,339,033</u>		<u>43,407,425</u>	<u>342,931,608</u>
Taxable Student Loan Backed Notes				
Student Loan Backed Notes,				
2012-1 Series:				
LIBOR Indexed:				
Due 7/25/39 (Variable Rate)	535,498,362		66,424,926	469,073,436
Original Issue Discount	<u>(1,298,800)</u>		<u>(117,185)</u>	<u>(1,181,615)</u>
	<u>534,199,562</u>		<u>66,307,741</u>	<u>467,891,821</u>
Taxable Student Loan Backed Notes				
Student Loan Backed Notes,				
2013-1 Series:				
LIBOR Indexed:				
Due 12/26/39 (Variable Rate)	<u>518,387,224</u>		<u>66,853,235</u>	<u>451,533,989</u>
Total	\$ <u>2,477,845,491</u>	\$ _____	\$ <u>280,278,539</u>	\$ <u>2,197,566,952</u>

The Authority participated in the Asset-Backed Commercial Paper (ABCP) Conduit Program established by the U.S. Department of Education, with the cooperation of the Department of Treasury and the Office of Management and Budget and pursuant to federal law, as a temporary financing facility to ensure the continued availability of FFELP loans in the academic years immediately following the credit crisis.

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6. Noncurrent Liabilities (Continued)

The conduit, "Straight-A Funding LLC," issued short-term promissory notes and lent the proceeds to eligible lenders and holders by taking FFELP loans as collateral. The short-term notes had variable maturities of no longer than 90 days. As previously issued notes matured, proceeds from newly issued notes were used to satisfy investors holding earlier maturities. To ensure repayment of the short-term notes at maturity, the Federal Financing Bank provided a back-up liquidity facility. The Department of Education also had a put agreement in place to purchase loans from the conduit to enable the conduit to repay investors, if necessary. The Straight-A Conduit provided an advance of 97% of the student loan value for loans in the program; during the year ended June 30, 2010, the Authority financed \$1.57 billion in FFELP loans through the program.

During the year ended June 30, 2013, the Authority was able to obtain stable, permanent financing for its loans pledged to the Straight-A Conduit, and thereby retire its obligation to the conduit in full. Without such permanent financing, upon expiration of its agreement under the conduit program in January of 2014, the Authority would have lost the collateral value of the loans and the right to continue servicing the loans, which would have resulted in a disruption of service to the student and parent borrowers. The Authority chose to refinance while investor demand was sufficient and bond market rates were favorable. Student Loan Backed Notes were issued for the 2012-1 Series on August 23, 2012, in the amount of \$600,000,000 with interest at a rate of 1-month LIBOR plus .8% and for the 2013-1 Series on January 24, 2013, in the amount of \$540,550,000 with interest at a rate of 1-month LIBOR plus .5%.

C. Pledged Revenues:

The Agency has collateralized \$2,314,020,163 in student loans receivable and \$14,953,934 in reserves to repay \$2,232,626,663 bonds payable at June 30, 2014. These taxable guaranteed student loan revenue bonds were issued between fiscal years June 30, 2006 through June 30, 2013. Proceeds from the bonds issued were utilized to finance student loans. The bonds are payable through fiscal year 2033 and are paid down from cash collections on student loans receivable, interest earnings on loans and investments, and unexpended bond proceeds. In addition to cash collections on student loans receivable, all net available revenues are expected to be pledged to meet annual principal and interest payments on the bonds. For the current fiscal year, principal and interest paid and total net available revenues were \$310,737,514 and \$308,857,053, respectively. The total principal and interest remaining to be paid on the bonds is \$2,469,466,937.

D. Annual Requirements:

The annual requirements to pay principal and interest on bonds outstanding at June 30, 2014 are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>
2015	\$ 230,263,593	\$ 25,183,037
2016	246,311,681	23,187,290
2017	242,469,199	21,063,756
2018	229,203,290	18,977,213
2019	211,588,176	17,001,637
2020-2024	698,131,800	61,250,484
2025-2029	166,038,577	41,411,918
2030-2034	<u>208,620,347</u>	<u>28,764,939</u>
Total Requirements	\$ <u>2,232,626,663</u>	\$ <u>236,840,274</u>

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6. Noncurrent Liabilities (Concluded)

The Taxable Guaranteed Student Loan Revenue Bonds, 2005 Series P are LIBOR indexed debt instruments due June 1, 2020. The Taxable Guaranteed Student Loan Revenue Private Placement Bonds, 2008-1 Series are LIBOR indexed debt instruments due June 1, 2033. The Taxable Guaranteed Student Loan Revenue Private Placement Bonds, 2008-4 Series are LIBOR indexed debt instruments due December 1, 2033. The Taxable Student Loan Backed Notes 2010-1 Series are LIBOR indexed debt instruments due July 25, 2041. The Taxable Student Loan Backed Notes 2011-1 Series are LIBOR indexed debt instruments due October, 25, 2041. The Taxable Student Loan Backed Notes 2011-2 are LIBOR indexed debt instruments due July, 25, 2036. The Taxable Student Loan Backed Notes 2012-1 are LIBOR indexed debt instruments due July 25, 2039. The Taxable Student Loan Backed Notes 2013-1 are LIBOR indexed debt instruments due December 26, 2039. All of the above series have a variable interest rate that changes either monthly or quarterly. The annual interest requirements in the schedule above were calculated using the rates in effect on June 30, 2014. Therefore, the debt service interest requirements on the aforementioned series will change on a monthly/quarterly basis throughout the life of the bonds.

7. Pension Plans

A. Retirement Plans:

Each permanent full-time employee, as a condition of employment, is a member of either the Teachers' and State Employees' Retirement System or the Optional Retirement Program. Eligible employees can elect to participate in the Optional Retirement Program at the time of employment; otherwise they are automatically enrolled in the Teachers' and State Employees' Retirement System.

The Teachers' and State Employees' Retirement System (TSERS) is a cost sharing multiple-employer defined benefit pension plan established by the State to provide pension benefits for employees of the State, its component units, and local boards of education. TSERS is administered by a 14-member Board of Trustees, with the State Treasurer serving as Chairman of the Board.

Benefit and contribution provisions for the TSERS are established by North Carolina General Statutes 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 2014, these rates were set at 8.69% of covered payroll for employers and 6% of covered payroll for members. Required employer contribution rates for the years ended June 30, 2013 and 2012 were 8.33% and 7.44%, respectively, while employee contributions were 6% each year. The Authority made 100% of its annual required contributions for the years ended June 30, 2014, 2013, and 2012.

The Teachers' and State Employees' Retirement System's financial information is included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Reports," or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

The Optional Retirement Program (Program) is a defined contribution retirement plan that provides retirement benefits with options for payments to beneficiaries in the event of the participant's death. Administrators of the Authority may join the Program instead of the TSERS. The Board of Governors of The University of North Carolina is responsible for the administration of the Program and designates the companies authorized to offer investment products or the trustee responsible for the investment of contributions under the Program and approves the form and contents of the contracts and trust agreements.

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7. Pension Plans (Continued)

Participants in the Program are immediately vested in the value of employee contributions. The value of employer contributions is vested after five years of participation in the Program. Participants become eligible to receive distributions when they terminate employment or retire.

Participant eligibility and contributory requirements are established by General Statute 135-5.1. Employer and member contribution rates are set each year by the North Carolina General Assembly. For the years ended June 30, 2014 and 2013, these rates were set at 6.84% of covered payroll for employers and 6% of covered payroll for members. The Authority assumes no liability other than its contribution.

For the years ended June 30, 2014 and 2013, the Authority had a total payroll of \$2,704,087 and \$2,555,439, respectively, of which \$2,308,847 and \$2,209,421 was covered under the Teachers' and State Employees' Retirement System and \$495,240 and \$346,018 was covered under the Optional Retirement Program. Total employee contributions for pension benefits under the Teachers' and State Employees' Retirement System for the years ended June 30, 2014 and 2013 were \$132,531 and \$132,565, respectively. Total employee contributions under the Optional Retirement Program for the years ended June 30, 2014 and 2013 were \$29,714 and \$20,761, respectively. Total employer contributions for pension benefits under the Teachers' and State Employees' Retirement System for the years ended June 30, 2014, 2013, and 2012 were \$191,949, \$184,045, and \$138,421, respectively. Total employer contributions under the Optional Retirement Program for the years ended June 30, 2014, 2013, and 2012 were \$33,874, \$23,667, and \$20,297, respectively.

B. Deferred Compensation and Supplemental Retirement Income Plans:

IRC Section 457 Plan - The State of North Carolina offers its permanent employers a deferred compensation plan created in accordance with Internal Revenue Code Section 457 through the North Carolina Public Employee Deferred Compensation Plan (the Plan). The Plan permits each participating employee to defer a portion of his or her salary until future years. The deferred compensation is available to employees upon separation from service, death, disability, retirement or financial hardships if approved by the Board of Trustees of the Plan. The Board, a part of the North Carolina Department of Administration, maintains a separate fund for the exclusive benefit of the participating employees and their beneficiaries, *the North Carolina Public Employee Deferred Compensation Trust Fund*. The Board also contracts with an external third party to perform certain administrative requirements and to manage the trust fund's assets. All costs of administering and funding the Plan are the responsibility of the Plan participants. No costs are incurred by the Authority. The voluntary contributions by employees amounted to \$44,736 and \$44,609 for the years ended June 30, 2014 and 2013, respectively.

IRC Section 401(k) Plan - All members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program are eligible to enroll in the Supplemental Retirement Income Plan, a defined contribution plan, created under Internal Revenue Code Section 401(k). All costs of administering the Plan are the responsibility of the Plan participants. No costs are incurred by the Authority. The voluntary contributions by employees amounted to \$52,197 and \$69,847 for the years ended June 30, 2014 and 2013, respectively.

IRC Section 403(b) and 403(b)(7) Plans - Eligible Authority employees can participate in tax sheltered annuity plans created under Internal Revenue Code Sections 403(b) and 403(b)(7). The employee's eligible contributions, made through salary reduction agreements, are exempt from federal and State income taxes until the annuity is received or the contributions are withdrawn. These plans are exclusively for employees of universities and certain charitable and other nonprofit institutions. All costs of administering

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8. Other Postemployment Benefits

and funding these plans are the responsibility of the Plan participants. No costs are incurred by the Authority. The voluntary contributions by employees amounted to \$3,453 at June 30, 2014 and \$22,922 for June 30, 2013.

A. Health Benefits:

The Authority participates in the Comprehensive Major Medical Plan (the Plan), a cost sharing, multiple-employer defined benefit health care plan that provides postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System or the Optional Retirement Program. Coverage eligibility varies depending on years of contributory membership service in their retirement system prior to disability or retirement.

The Plan benefit and contribution provisions are established by the State Treasurer and the Board of Trustees of the State Health Plan for Teachers and State Employees as authorized by Chapter 135, Article 3B, of the General Statutes. The Plan does not provide for automatic post-retirement benefit increases.

By General Statute, a Retiree Health Benefit Fund (the Fund) has been established as a fund in which accumulated contributions from employers and any earnings on those contributions shall be used to provide health benefits to retired and disabled employees and applicable beneficiaries. By statute, the Fund is administered by the Board of Trustees of the Teachers' and State Employees' Retirement System and contributions to the Fund are irrevocable. Also by law, Fund assets are dedicated to providing benefits to retired and disabled employees and applicable beneficiaries and are not subject to the claims of creditors of the employers making contributions to the Fund. Contribution rates to the Fund, which are intended to finance benefits and administrative expenses on a pay-as-you-go basis, are determined by the State Treasurer and the Board of Trustees of the State Health Plan for Teachers and State Employees.

For the current fiscal year, the Authority contributed 5.4% of the covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the Fund. Required contribution rate for the years ended June 30, 2013 and 2012 was 5.3% and 5.0%, respectively. The Authority made 100% of its annual required contributions to the Plan for the years ended June 30, 2014, 2013, and 2012, which were \$146,021, \$135,438, and \$155,223, respectively. The Authority assumes no liability for retiree health care benefits provided by the programs other than its required contribution.

Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Reports," or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

B. Disability Income:

The Authority participates in the Disability Income Plan of North Carolina (DIPNC), a cost-sharing, multiple-employer defined benefit plan, to provide short-term and long-term disability benefits to eligible members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program. Benefit and contribution provisions are established by Chapter 135, Article 6 of the General Statutes, and may be amended only by the North Carolina General Assembly. The plan does not provide for automatic post-retirement benefit increases.

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8. Other Postemployment Benefits (Continued)

Disability income benefits are funded by actuarially determined employer contributions that are established by the General Assembly. For the fiscal year ended June 30, 2014, the Authority made a statutory contribution of .44% of covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the DIPNC. The required contribution rate for the years ended June 30, 2013 and 2012 was .44% and .52%, respectively. The Authority made 100% of its annual required contributions to the DIPNC for the years ended June 30, 2014, 2013, and 2012, which were \$11,898, \$11,244, and \$16,143, respectively. The Authority assumes no liability for long-term disability benefits under the DIPNC other than its contribution.

Additional detailed information about the DIPNC is disclosed in the State of North Carolina's *Comprehensive Annual Financial Report*.

9. Insurance

Physical plant and equipment used by the Authority and reported on the statement of net assets are owned by the State of North Carolina. To provide financial protection for this ownership equity in assets, the State maintains a State Property Fire Insurance Fund as self-insurance against losses which might occur to state-owned property. This fund is administered by the North Carolina Department of Insurance and is maintained without direct cost to individual State agencies. Extended coverage insurance is available at a cost to electing agencies.

Additional details on the state-administered risk management programs are disclosed in the State of North Carolina's *Comprehensive Annual Financial Report*, issued by the Office of the State Controller.

10. Adoption of New Accounting Standards

For the fiscal year ended June 30, 2014, the Authority implemented the following pronouncements issued by Governmental Accounting Standards Board (GASB):

GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*.

GASB Statement No. 66, *Technical Corrections - 2012 - An Amendment of GASB Statements No. 10 and No. 62*.

GASB Statement No. 65 establishes accounting and financial reporting standards that reclassify certain items that were previously reported as assets and liabilities as deferred outflows of resources or deferred inflows of resources, and recognizes certain items that were previously reported as assets and liabilities as expenses/expenditures or revenues. Refer to Note 11, Change in Accounting Principle and Net Position Restatement, for information on how the adoption of this Statement affected the financial statements.

GASB Statement No. 66 resolves conflicting accounting and financial reporting guidance that resulted from the issuance of new pronouncements. The adoption of this statement had no impact on the financial statements.

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10. Adoption of New Accounting Standards (Continued)

For the fiscal year ended June 30, 2013, the Authority implemented the following pronouncements issued by Governmental Accounting Standards Board (GASB):

GASB Statement No. 61, *The Financial Reporting Entity: Omnibus – An Amendment of GASB Statements No. 14 and No. 34.*

GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements.*

GASB Statement No. 63, *Financing Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position.*

GASB Statement No. 61 sets forth additional requirements for identifying component units, blending identified component units, presenting condensed combining information for blended component units, and accounting for certain equity interests. The adoption of this statement resulted in the Authority being presented as a nonmajor component unit in the State of North Carolina Comprehensive Annual Financial Reports (CAFR).

GASB Statements No. 62 does not propose any new guidance. The purpose of this statement is to incorporate into the GASB's authoritative literature certain guidance from Pre-November 1989 FASB Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins from the AICPA Committee on Accounting Procedure. The adoption of this statement had no impact on the financial statements.

GASB Statement No. 63 provides guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position and related disclosures. The adoption of this statement impacted the names and titles of certain items presented in the financial statements.

11. Change in Accounting Principle and Net Position Restatement

As discussed previously, the Authority adopted GASB Statement No. 65 during the year ended June 30, 2014. Under this Statement, bond issuance costs are to be expensed in the period in which they are incurred, rather than deferred and amortized over the life of the related debt as was prescribed under previous standards. This change is to be applied retroactively by restating the financial statements for all prior periods presented. As a result, any previously unamortized bond issuance costs have been removed from the statements of net position of the Authority. In addition, costs of issuance associated with newly issued debt are presented as expenses in the statement of revenues, expenses, and changes in net position in the year the related debt was issued.

As of July 1, 2012, net position as previously reported was restated as follows:

July 1, 2012 Net Position, as Previously Reported	\$ 576,227,396
Restatements: Expense previously amortized bond issuance costs pursuant to GASB Statement No. 65 requirements	<u>(12,085,835)</u>
July 1, 2012 Net Position, as Restated	\$ <u>564,141,561</u>

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12. Reclassifications

Certain reclassifications have been made to the 2013 financial statements to conform with the 2014 presentation. Such reclassifications have no effect on the changes in financial position or cash flows as previously reported.

13. Subsequent Events

Subsequent events have been evaluated through September 30, 2014, which is the date the financial statements were available to be issued.