Tennessee Student Assistance Corporation

For the Year Ended
June 30, 2004

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STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
State Capitol
Nashville, Tennessee 37243-0260
(615) 741-2501

John G. Morgan
Comptroller

June 16, 2005

The Honorable Phil Bredesen, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
Dr. Richard G. Rhoda, Interim Executive Director
Tennessee Student Assistance Corporation
1950 Parkway Towers
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee Student Assistance Corporation for the year ended June 30, 2004. You will note from the independent auditor's report that unqualified opinions were given on the fairness of the presentation of the financial statements.

Consideration of internal control over financial reporting and tests of compliance disclosed a deficiency, which is detailed in the Results of the Audit section of this report. The corporation's management has responded to the audit finding; the response is included following the finding. The Division of State Audit will follow up the audit to examine the application of the procedures instituted because of the audit finding.

Sincerely,

John G. Morgan

John G. Morgan
Comptroller of the Treasury

JGM/cj
04/107

State of Tennessee

Audit Highlights

Comptroller of the Treasury — Division of State Audit

Financial and Compliance Audit

Tennessee Student Assistance Corporation

For the Year Ended June 30, 2004

AUDIT OBJECTIVES

The objectives of the audit were to consider the corporation's internal control over financial reporting; to determine compliance with certain provisions of laws, regulations, contracts, and grant agreements; to determine the fairness of the presentation of the financial statements; and to recommend appropriate actions to correct any deficiencies.

COMPLIANCE FINDING

The Student Loan Information Reflected in the Corporation's System Was Not Always Correct*

The Tennessee Student Assistance Corporation status of outstanding loans is not always correct in the student loan information database. The results of the current audit testwork indicated that problems with the reporting of student loan status still exist. A random sample of student loans with a status of "in-school" or "repayment" was selected from the Tennessee Student Assistance Corporation's listing of outstanding loans. For each sample loan, the lender (current holder of the loan) was contacted to confirm the status of the loan. Based on the audit procedures performed, for 6 of 40 loans (15%) tested, the loan status shown in the corporation's system did not agree with the status reported by the lender (page 11).

* This finding is repeated from the prior audit.

OPINION ON THE FINANCIAL STATEMENTS

The opinions on the financial statements are unqualified.

Audit Report
Tennessee Student Assistance Corporation
For the Year Ended June 30, 2004

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Tennessee Student Assistance Corporation
For the Year Ended June 30, 2004

INTRODUCTION

POST-AUDIT AUTHORITY

This is a report on the financial and compliance audit of the Tennessee Student Assistance Corporation. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which authorizes the Department of Audit to "perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller."

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

BACKGROUND

The Tennessee Student Assistance Corporation was chartered by the General Assembly in 1947 to aid residents of the state who desire to further their education beyond high school. The corporation is responsible for administering several student financial assistance programs supported by federal and state funds. These programs include the Federal Stafford Loan Program, Federal Parents Loans for Undergraduate Students (FPLUS) Program, Robert C. Byrd Honors Scholarship Program, Tennessee Student Assistance Award Program, Christa McAuliffe Scholarship Program, Ned McWherter Scholars Program, Minority Teaching Fellows Program, Tennessee Teaching Scholars Program, and Dependent Children's Scholarship Program.

ORGANIZATION

The corporation is governed by a board of directors, and the executive director is responsible for implementing the board's policy. The board includes the Governor, the State Treasurer, the Comptroller of the Treasury, the Commissioner of Finance and Administration, the Commissioner of Education, the Executive Director of the Tennessee Higher Education Commission, the Chancellor of the Tennessee Board of Regents, and the President of the University of Tennessee.

The corporation contracted with GuaranTec, LLP, of Jacksonville, Florida, to service its Federal Stafford Loan, FPLUS, and Consolidated Loan programs. The loan servicer is responsible for processing and approving new loans and default claims from lenders. The loan servicer also collects payments on defaulted loans from borrowers and is responsible for processing and collecting bankruptcy claims from borrowers.

An organization chart for the corporation is on the following page.

AUDIT SCOPE

The audit was limited to the period July 1, 2003, through June 30, 2004, and was conducted 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. Financial statements are presented for the year ended June 30, 2004, and for comparative purposes, the year ended June 30, 2003. The corporation has been included as a component unit in the *Tennessee Comprehensive Annual Financial Report*.

The audit covered fund 60 of the State of Tennessee Accounting and Reporting System (allotment code 332.04) and a portion of fund 25 (allotment codes 332.03, 332.05, and 332.07).

OBJECTIVES OF THE AUDIT

The objectives of the audit were

1. to consider the corporation's internal control over financial reporting to determine auditing procedures for the purpose of expressing opinions on the financial statements;

2. to determine compliance with certain provisions of laws, regulations, contracts, and grant agreements;

3. to determine the fairness of the presentation of the financial statements; and

4. to recommend appropriate actions to correct any deficiencies.

Although this audit was not intended to serve as an organization-wide audit as described in the Single Audit Act, as amended by the Single Audit Act Amendments of 1996, and Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations,* it included tests of compliance with applicable federal laws and regulations and consideration of internal control used in administering federal financial assistance programs. This audit is a segment of the organization-wide audit of the State of Tennessee, which is conducted in accordance with the Single Audit Act.

TENNESSEE STUDENT ASSISTANCE CORPORATION
ORGANIZATION CHART

PRIOR AUDIT FINDINGS

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendations in the prior audit report. A follow-up of all prior audit findings was conducted as part of the current audit.

RESOLVED AUDIT FINDING

The current audit disclosed that the Tennessee Student Assistance Corporation has corrected the previous audit finding concerning a liability owed to the Secretary of Education.

REPEATED AUDIT FINDING

The prior audit report also contained a finding concerning student loan information as reflected in the corporation's system. This finding has not been resolved and is repeated in this report.

OBSERVATIONS AND COMMENTS

FRAUD CONSIDERATIONS

Statement on Auditing Standards No. 99 promulgated by the American Institute of Certified Public Accountants requires auditors to specifically assess the risk of material misstatement of an audited entity's financial statements due to fraud. The standard also restates the obvious premise that management, and not the auditors, is primarily responsible for preventing and detecting fraud in its own entity. Management's responsibility is fulfilled in part when it takes appropriate steps to assess the risk of fraud within the entity and to implement adequate internal controls to address the results of those risk assessments.

During our audit, we discussed these responsibilities with management and how management might approach meeting them. We also increased the breadth and depth of our inquiries of management and others in the entity as we deemed appropriate. We obtained formal assurances from top management that management had reviewed the entity's policies and procedures to ensure that they are properly designed to prevent and detect fraud and that management had made changes to the policies and procedures where appropriate. Top management further assured us that all staff had been advised to promptly alert management of all allegations of fraud, suspected fraud, or detected fraud and to be totally candid in all communications with the auditors. All levels of management assured us there were no known instances or allegations of fraud that were not disclosed to us.

AUDIT COMMITTEE RECOMMENDED

As a result of the fraud-related business failures of companies such as Enron and WorldCom in recent years, Congress and the accounting profession have taken aggressive measures to try to detect and prevent future failures related to fraud. These measures have included the signing of the *Sarbanes-Oxley Act of 2002* by the President of the United States and the issuance of Statement on Auditing Standards No. 99 by the American Institute of Certified Public Accountants. This new fraud auditing standard has not only changed the way auditors perform audits but has also provided guidance to management and boards of directors on creating antifraud programs and controls. This guidance has included the need for an independent audit committee.

As a result of these developments, we are recommending that agencies with boards establish audit committees. The specific activities of any audit committee will depend on, among other things, the mission, nature, structure, and size of each agency. In establishing the audit committee and creating its charter, each board should examine its agency's particular circumstances. Anti-fraud literature notes that there are two categories of fraud: fraudulent financial reporting and misappropriation of assets. The audit committee should consider the risks of fraud in its agency in general as well as the history of its particular agency with regard to prior audit findings, previously disclosed weaknesses in internal control, and compliance issues. The audit committee should consider both the risk of fraudulent financial reporting and the risk of fraud due to misappropriation or abuse of agency assets. Also, the board and the audit committee should keep in mind that agencies receiving public funding should have a lower threshold of materiality than private sector entities with regard to fraud risks.

Boards should exercise professional judgment in establishing the duties, responsibilities, and authority of their audit committee. The factors noted below are not intended to be an exhaustive listing of those matters to be considered. The committee should not limit its scope to reacting to a preconceived set of issues and actions but rather should be proactive in its oversight of the corporation as it concentrates on the internal control and audit-related activities of the entity. In fact, this individualized approach is one of the main benefits derived from an audit committee.

At a minimum, audit committees should:

1. Develop a written charter that addresses the audit committee's purpose and mission, which should be, at a minimum, to assist the board in its oversight of the corporation.

2. Formally reiterate, on a regular basis, to the board, agency management, and staff their responsibilities for preventing, detecting, and reporting fraud, waste, and abuse.

3. Serve as a facilitator of any audits or investigations of the corporation, including advising auditors and investigators of any information they may receive or otherwise note regarding risks of fraud or weaknesses in the agency's internal controls; reviewing with the auditors any findings or other matters noted by the auditors during audit engagements; working with the corporation management and staff to ensure implementation of audit recommendations; and assisting in the resolution of any problems the auditors may have with cooperation from corporation management or staff.

4. Develop a formal process for assessing the risk of fraud at the corporation, including documentation of the results of the assessments and assuring that internal controls are in place to adequately mitigate those risks.

5. Develop and communicate to staff of the corporation their responsibilities to report allegations of fraud, waste, or abuse at the corporation to the committee and the Comptroller of the Treasury's office as well as a process for immediately reporting such information.

6. Immediately inform the Comptroller's office when fraud is detected.

7. Develop and communicate to the board, corporation management, and staff a written code of conduct reminding those individuals of the public nature of the agency and the need for all to maintain the highest level of integrity with regard to the financial operations and any related financial reporting responsibilities of the corporation; to avoid preparing or issuing fraudulent or misleading financial reports or other information; to protect corporation assets from fraud, waste, and abuse; to comply with all relevant laws, rules, policies, and procedures; and to avoid engaging in activities which would otherwise bring dishonor to the corporation.

The charter of the audit committee should include, at a minimum, the following provisions:

1. The audit committee should be a standing committee of the board.

2. The audit committee should be composed of at least three members. The chair of the audit committee should preferably have some accounting or financial management background. Each member of the audit committee should have an adequate background and education to allow a reasonable understanding of the information presented in the financial reports of the agency and the comments of auditors with regard to internal control and compliance findings and other issues.

3. The members of the audit committee must be independent from any appearances of other interests that are in conflict with their duties as members of the audit committee.

4. An express recognition that the board, the audit committee, and the management and staff of the corporation are responsible for taking all reasonable steps to prevent, detect, and report fraud, waste, and abuse.

5. The audit committee should meet regularly throughout the year. The audit committee can meet by telephone, if that is permissible for other committees. However, the audit committee is strongly urged to meet at least once a year in person. Members of the audit committee may be members of other standing committees of the board, but the audit committee meetings should be separate from the meetings of other committees of the board.

6. The audit committee should record minutes of its meetings.

The Division of State Audit will be available to discuss with the board any questions it might have about the creation of its particular audit committee. There are also other audit committees which have already been established at other state agencies that the board may wish to contact for advice and further information.

TITLE VI OF THE CIVIL RIGHTS ACT OF 1964

Section 4-21-901, *Tennessee Code Annotated*, requires each state governmental entity subject to the requirements of Title VI of the Civil Rights Act of 1964 to submit an annual Title VI compliance report and implementation plan to the Department of Audit by June 30 each year. The Tennessee Student Assistance Corporation filed its compliance report and implementation plan on June 30, 2004.

Title VI of the Civil Rights Act of 1964 is a federal law. The act requires all state agencies receiving federal money to develop and implement plans to ensure that no person shall, on the grounds of race, color, or origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving federal funds. The Tennessee Title VI Compliance Commission is responsible for monitoring and enforcement of Title VI. A summary of the dates state agencies filed their annual Title VI compliance reports and implementation plans is presented in the special report *Submission of Title VI Implementation Plans*, issued annually by the Comptroller of the Treasury.

RESULTS OF THE AUDIT

AUDIT CONCLUSIONS

Internal Control

As part of the audit of the corporation's financial statements for the year ended June 30, 2004, we considered internal control over financial reporting to determine auditing procedures for the purpose of expressing opinions on the financial statements, as required by 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. Consideration of internal control over financial reporting disclosed no material weaknesses.

Compliance and Other Matters

The results of our audit tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. An immaterial instance of noncompliance, along with the recommendation and management's response, is detailed in the finding and recommendation.

Fairness of Financial Statement Presentation

The Division of State Audit has rendered unqualified opinions on the corporation's financial statements.

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Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

December 3, 2004

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have audited the financial statements of the Tennessee Student Assistance Corporation, a component unit of the State of Tennessee, as of and for the year ended June 30, 2004, and have issued our report thereon dated December 3, 2004. 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.

<u>Internal Control Over Financial Reporting</u>

In planning and performing our audit, we considered the corporation’s internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of The performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

However, we noted certain matters involving the internal control over financial reporting, which we have reported to the corporation's management in a separate letter.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the corporation's financial statements are free of material misstatement, we performed tests of the corporation's compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We did, however, note an immaterial instance of noncompliance that we have included in the Finding and Recommendation section of this report. We also noted certain other less significant matters, which we have reported to the corporation's management in a separate letter.

This report is intended solely for the information and use of the General Assembly of the State of Tennessee, board of directors, and management and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record.

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

AAH/cj

FINDING AND RECOMMENDATION

<u>The student loan information reflected in the corporation's system was not always correct</u>

Finding

As stated in the prior audit, the Tennessee Student Assistance Corporation (TSAC) has not ensured that the status of outstanding loans is correct in the student loan information database. Management concurred with the prior finding and stated:

> Status changes that have been rejected [and sent] back to the lender or lender servicer for additional information will be closely monitored by the Loan Division at TSAC. This issue will also be addressed at TSAC's Annual Lender Conference in April. The Loan Division at TSAC will also begin a systematic review of older loans in the portfolio to identify those loans with incorrect status information.

However, results of the current audit indicate that problems with the reporting of student loan status still exist.

A random sample of student loans with a status of "in-school" or "repayment" was selected from the TSAC's listing of outstanding loans. For each sample loan, the school or lender (current holder of the loan) was contacted to confirm the authenticity and status of the loan. Based on the audit procedures performed, for 6 of 40 loans (15%) tested, the student status shown in the corporation's system did not agree with the status reported by the lender. Last year, for 7 of 40 loans (18%) tested, the student status shown in the corporation's system did not agree with the status reported by the lender.

The amount of loans in repayment status is used in the calculation for determining the reinsurance rate that the U.S. Department of Education (ED) pays to the corporation. The information on the National Student Loan Data System (NSLDS) is used by ED to calculate the amount of loans in repayment. If loans are not correctly shown in a repayment status in the corporation's system, then the amount reflected on NSLDS may be in error, and the amount paid to TSAC for reinsurance may be incorrect.

TSAC's procedures for ensuring the correct status include periodic counseling sessions with lenders to discuss the various loan program requirements, including the reporting of changes in student status. TSAC also provides a Loan Status Update Form, and lenders can submit status change data via hardcopy, tape, e*CLIPS (the loan servicer's Internet application and transaction processing tool), and Common Line 4 format via FTP server. When a lender submits status change information to the loan servicer, the loan servicer's system first determines that the loan is in a status compatible with the change before the change will be accepted. For example, if a loan is currently in an in-school status, a new status of deferment would not be accepted. If the change is rejected, the lender is informed as to the reason and asked for additional information to resolve the rejection. However, it should be noted that section *A.4.a* of the corporation's contract with the loan servicer requires that all loan maintenance activities either electronically or manually received be processed, returned for correction, or rejected within a maximum turn-around time of five business days, measured from the servicer's initial receipt of the loan maintenance activity to the posting of the activity on the corporation's database.

TSAC did have a system in place to encourage and provide for the reporting of changes in loan status by the lenders and procedures to properly record loans paid in full when the lenders report them. However, as noted above, the testwork indicated that there were problems with lenders reporting status changes. Three of the exceptions noted were due to the lenders not submitting loan status updates when status changes occurred. The fact that the lenders have not been held formally accountable for reporting "paid-in-full" status to TSAC through the system limits the effectiveness of TSAC's procedures. Furthermore, TSAC has not adequately reviewed status changes rejected by the system and has not ensured that the corrections needed for system acceptance are made by the lenders. The other three exceptions noted were where lenders had submitted status updates which were rejected by the system and the discrepancy was never resolved by TSAC and the lenders. Subsequent updates were never resubmitted on two of the loans, and one update was resubmitted and rejected two additional times. TSAC did not satisfactorily follow up, obtain the correct loan status, and correct the status in its system on any of the items until they were brought to TSAC's attention.

For lenders that are in substantial noncompliance with requirements for student status reporting, TSAC could refuse to guarantee loans, per its enforcement authority under the *Code of Federal Regulations*, Title 34, Part 682, Section 410. Exercised appropriately, this authority could effectively prompt lenders to comply.

Recommendation

The director and program administrator should consult the U.S. Department of Education and the corporation's loan servicer to determine what further procedures can be established to ensure that updated student loan information is maintained in the corporation's system. TSAC should analyze its status change error reports, determine the causes of rejections of the status changes, and contact the lenders to determine the necessary corrective action for processing. The interaction with the lender should be much more proactive and continue until the system accepts and processes the status change. Appropriate actions should be initiated with respect to lenders with recurring errors, up to and including refusal to guarantee loans until lenders properly report student information.

Management's Comment

TSAC concurs. TSAC's Loan Program Administrator has taken several steps to ensure that the updated student loan information is correctly maintained by TSAC's contracted servicer, GuaranTec. These steps include:

- Personal meetings with senior management at participating lenders and GuaranTec to determine the cause and a solution to the problem;

- Designation of a TSAC Loan Staff employee to work closely with the lenders and GuarenTec to correct the information on the database;
- Develop and implement a policy and procedures for lenders and GuaranTec concerning loan status error reports;
- Develop and implement a "Limit, Suspend, and Terminate" policy and procedures for lenders who fail to comply with required loan maintenance updates;
- Provide regular informational updates and guidance to lenders on common reject scenarios and their solutions;
- TSAC senior management will perform periodic review of steps to ensure compliance; and
- Employment of an Internal Auditor.

STATE OF TENNESSEE
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Independent Auditor's Report

December 3, 2004

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have audited the accompanying financial statements of the governmental activities, general fund, and the Federal Family Education Loan Trust Fund of the Tennessee Student Assistance Corporation, a component unit of the State of Tennessee, as of and for the years ended June 30, 2004, and June 30, 2003, which collectively comprise the corporation's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the corporation's management. Our responsibility is to express opinions on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of directors of Tennessee Student Assistance Corporation, a component unit of the State of Tennessee; approving accounting policies of the state as prepared by the state's Department of Finance and Administration; approving certain state contracts; and participating in the negotiation and procurement of services for the state.

In our opinion, the financial statements of the governmental activities, general fund, and the Federal Family Education Loan Trust Fund present fairly, in all material respects, the financial position of the corporation as of June 30, 2004, and June 30, 2003, and the respective changes in financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 16 through 23 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming opinions on the basic financial statements that collectively comprise the corporation's basic financial statements. The accompanying financial information on page 37 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 3, 2004, on our consideration of the 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

Arthur A. Hayes, Jr.

Arthur A. Hayes, Jr., CPA
Director

Tennessee Student Assistance Corporation
Management's Discussion and Analysis
For the Year Ended June 30, 2004, and June 30, 2003

This section of the Tennessee Student Assistance Corporation's annual financial report presents a discussion and analysis of the financial performance of the corporation during the fiscal years ended June 30, 2004, and June 30, 2003. This discussion has been prepared by management along with the financial statements and related note disclosures and should be read in conjunction with the financial statements and notes. The financial statements, notes, and this discussion are the responsibility of management.

Using This Annual Report

This annual report consists of a series of financial statements. The Statements of Net Assets and the Statements of Activities provide information about the activities of the corporation as a whole. The Balance Sheets and the Statements of Revenues, Expenditures, and Changes in Fund Balances provide financial information about the activities of the corporation's general fund. The Statements of Fiduciary Net Assets and the Statements of Changes in Fiduciary Net Assets provide financial information about the activities for which the corporation acts solely as a trustee for the benefit of those outside the corporation.

Statements of Net Assets

The Statements of Net Assets present the financial position of those programs included in the state's Education Fund as administered by the corporation at the end of the fiscal year. They include all assets and liabilities, measured in current values, of the corporation. The difference between total assets and total liabilities—net assets—is an indicator of the corporation's current financial condition.

Statements of Net Assets

	6/30/2004	6/30/2003	6/30/2002
Current assets	$ 8,886,766	$ 7,399,445	$ 7,586,231
Capital assets, net	-	-	-
Total Assets	8,886,766	7,399,445	7,586,231
Current liabilities	2,717,852	1,948,034	1,881,688
Long-term liabilities	60,302	45,010	52,272
Total Liabilities	2,778,154	1,993,044	1,933,960
Total Net Assets-unrestricted	$ 6,108,612	$ 5,406,401	$ 5,652,271

Some highlights of material assets and liabilities on the Statements of Net Assets are as follows:

- The notes and interest receivables include notes and interest due the corporation from students having participated in one of the teaching loan/scholarship programs administered by the corporation. Under these programs, students agree to meet certain program conditions upon graduation. If those conditions are met, the loans are forgiven based on a previously agreed upon schedule; at any time the conditions are not met, the loan then becomes due and payable.

- Accrued liabilities include amounts due to the corporation's loan servicer. Due to the federal government and advance from the federal government include funds received from the Paul Douglas Teacher Scholarship Program that are held in trust and administered by the corporation.

Unrestricted net assets are available to the corporation for any lawful purpose of the corporation.

FY 2004 to FY 2003

The corporation's total net assets increased from $5,406,401 to $6,108,612. The increase resulted primarily from an increase in cash related to additional services and related charges. See notes for additional details.

FY 2003 to FY 2002

The corporation's total net assets decreased $245,870 from $5,652,271 at June 30, 2002, to $5,406,401 at June 30, 2003. This decrease resulted primarily from a reduction in notes receivable from Loan/Scholarship recipients. See description of notes and interest receivables above, for additional information.

Statements of Activities

The Statements of Activities present the activities occurring in those programs included in the state's Education Fund as administered by the corporation for the fiscal year.

Statements of Activities

	6/30/2004	6/30/2003	6/30/2002
Expenses for education	$ 60,981,724	$ 49,323,566	$ 39,923,314
Program revenues:			
Charges for services	13,018,841	785,625	739,163
Operating grants and contributions	6,630,325	1,888,451	1,173,895
Total program revenues	19,649,166	2,674,076	1,913,058
Net program expenses	41,332,558	46,649,490	38,010,256
General revenues:			
Payments from primary government	42,034,769	46,403,620	38,503,401
Increase (Decrease) in net assets	702,211	(245,870)	493,145
Net assets, beginning of year	5,406,401	5,652,271	5,159,126
Net assets, end of year	$ 6,108,612	$ 5,406,401	$ 5,652,271

Some highlights of the Statements of Activities are as follows:

- Expenses for education included grants made in the Tennessee Student Assistance Awards and other education programs, costs incurred by the corporation in administering the programs, and loans and interest cancelled for those students participating in the loan/scholarship programs who met the requirement of those programs.

- Revenues include state appropriations for programs administered by the corporation, the collection of loan and interest payments, and refunds from those programs.

FY 2004 to FY 2003

The increase is attributable to a 25% increase in collection costs, a 50% increase in TSAC staff for the Lottery and an increase in Bank Claims of 8%.

FY 2003 to FY 2002

Expenses for education increased due to additional funding that was provided to the Tennessee Student Assistance Award Program by the State Legislature for FY 2003 and for the increased grant award amounts which were received from the U.S. Department of Education. The increased award amounts allowed additional loan/scholarships which are reflected as additional expenses.

Balance Sheets - General Fund

The Balance Sheets present the current financial condition of those programs included in the state's Education Fund as administered by the corporation at the end of the fiscal year. They include all assets, liabilities, and fund balances, measured in current values, of the corporation.

Some highlights of the General Fund Balance Sheets are as follows:

- The notes and interest receivables include notes and interest due the corporation from students having participated in one of the teaching loan/scholarship programs administered by the corporation. Under these programs, students agree to meet certain program conditions upon graduation. If those conditions are met, the loans are forgiven based on a previously agreed upon schedule; at any time the conditions are not met, the loan then becomes due and payable.

- Accrued liabilities include amounts due to the corporation's loan servicer. Due to the federal government and advance from the federal government include funds received for the Paul Douglas Teacher Scholarship Program that are held in trust and administered by the corporation.

- Fund balances include reserves for the loan/scholarship outstanding loans and continuing appropriations for projects begun in the fiscal year but continuing into the next fiscal year.

At June 30, 2004; June 30, 2003; and June 30, 2002, the general fund had total fund balances of $6,224,880, $5,492,498, and $5,754,765, respectively. Reconciliations of the total fund balances with the total net assets presented on the Statements of Net Assets are shown at the bottom of the Balance Sheets.

<u>FY 2004 to FY 2003</u>

The total fund balance increase is indicative of the growth in the programs that occurred during the fiscal year and is directly attributable to the Lottery.

<u>FY 2003 to FY 2002</u>

Total fund balance decreased primarily due to a reduction in notes receivable from Loan/Scholarship recipients due to an annual timing differences.

Statements of Revenues, Expenditures, and Changes in Fund Balances-General Fund

The Statements of Revenues, Expenditures, and Changes in Fund Balances present the results of operations for those programs included in the state's Education Fund as administered by the corporation for the fiscal years.

Some highlights of the General Fund Statements of Revenues, Expenditures, and Changes in Fund Balances are as follows:

- Revenues include state and federal appropriations for programs administered by the corporation, the collection of loan interest and payments, and refunds from those programs.

- Expenditures include grants made in the Tennessee Student Assistance Awards and other education program awards made to students, administrative costs incurred by the corporation, and loans and interest cancelled for those students participating in the loan/scholarship programs.

The general fund had an excess of revenues over expenditures of $732,382 for the fiscal year ended June 30, 2004. The general fund had a deficiency of revenues under expenditures of ($262,268) for the fiscal year ended June 30, 2003. The general fund also had an excess of revenues over expenditures of $504,858 for the fiscal year ended June 30, 2002. Reconciliations of excess (deficiency) of revenues over (under) expenditures with increase (decrease) in net assets presented on the Statements of Activities are shown at the bottom of the Statements of Revenues, Expenditures, and Changes in Fund Balances.

<u>FY 2004 to FY 2003</u>

- Grant revenue from primary government was increased for the Tennessee Student Assistance Awards program for FY 2004. As a reflection of this increase, grant expenditures were correspondingly larger.

- Federal grant award amounts received in FY 2004 were substantially higher than the previous year, which also increased grant expenditures. Federal grant awards were higher due to supplemental monies received from the U.S. Department of Education's Leverage Educational Assistance Partnership and Special Leverage Educational Assistance Partnership Programs.

FY 2003 to FY 2002

- Grant revenue from primary government was increased for the Tennessee Student Assistance Awards Program for FY 2003. As a reflection of this increase, grants expenditures were correspondingly larger.

- Federal Grant award amounts received in FY 2003 were substantially higher than the previous year, which also increased grant expenditures. Federal grant awards were higher due to higher than anticipated supplemental monies received from the U.S. Department of Education's Leverage Educational Assistance Partnership and Special Leverage Educational Assistance Partnership Programs received as additional appropriations.

- Loan cancellations for FY 2003 were larger due to more Loan/Scholarship recipients fulfilling program requirements. However, this resulted in decreased revenues in current services when compared to FY 2002.

Statements of Fiduciary Net Assets-
Federal Family Education Loan Trust Fund

The Statements of Fiduciary Net Assets present the assets and liabilities of the Federal Family Education Loan (FFEL) Trust Fund as administered by the corporation as the Federal Guaranty Agency for Tennessee.

Some highlights of the Statements of Fiduciary Net Assets are as follows:

- Assets include cash reserves of the corporation for the FFEL Program and receivables consisting of reinsurance claims pending and not yet made.

- Liabilities include cash reserves due to the United States Department of Education under sections 422(h) and 422(i) of the Higher Education Act of 1965, as amended (HEA) and as required by the Balanced Budget Act of 1997 (Pub. L.105-33).

The trust fund had net assets held in trust for student loan activities of $78,758,191 at June 30, 2004; $72,835,674 at June 30, 2003; and $71,997,352 at June 30, 2002.

FY 2004 to FY 2003

Net assets increased by $5,922,517 from June 30, 2003, to June 30, 2004. This was due to an increased loan volume which resulted in higher collection costs received and additional servicing costs received.

FY 2003 to FY 2002

In accordance with increased activity in the corporation's FFEL Program, the net assets increased by $838,322 from FY 2002 to FY 2003 due to an increase in student loan volume.

Statements of Changes in Fiduciary Net Assets-
Federal Family Education Loan Trust Fund

The Statements of Changes in Fiduciary Net Assets present the additions to and deductions from the Federal Family Education Loan Trust Fund for the fiscal year as administered by the corporation as the Federal Guaranty Agency for Tennessee.

Some highlights of the Statements of Changes in Fiduciary Net Assets are as follows:

- Additions include federal revenues in the form of fees and allowances earned by the corporation in administration of the Federal Family Education Loan Program as the Federal Guaranty Agency, interest earned on program reserves held by the corporation, and contributions from the state into the state sponsored Tennessee Student Loan Program reserves.

- Deductions include expenses incurred by the corporation in the administration of the Federal Family Education Loan Program and the Tennessee Student Loan Program and the return of reserve funds.

FY 2004 to FY 2003

- Federal Revenue additions are subject to loan volume and payment receipt fluctuations. A multi-year analysis of the Federal Education Loan Fund better reflects the Federal revenue of this fund.

FY 2003 to FY 2002

- Federal Revenue additions are subject to loan volume and payment receipt fluctuations. A multi-year analysis of the Federal Education Loan Trust Fund better reflects the Federal revenue activity of this fund.

- FY 2003 reflects reserves returned by the corporation to the U.S. Department of Education as required by the Reauthorization of the Higher Education Act of 1965. This principle reduction, combined with a lower rate of available investment return, resulted in lower additions in interest income and a reduced amount in total deductions for FY 2003.

Economic Factors Affecting the Corporation's Future Financial Condition

The upcoming Reauthorization of The Higher Education Act of 1965 will affect Guarantor Agencies such as the corporation. It is premature to speculate what these changes will be, and therefore their effect on the corporation is unknown at this time. Previous actions, such as the recall of Federal Reserve Funds, required Tennessee to return $24.9 million. Currently, the corporation is scheduled to return an additional $2.6 million of Federal Reserve Funds in two payments during fiscal years 2006 and 2007 as its remaining share.

The Corporation will begin issuance of Tennessee Education Lottery Scholarship Program payments during Fiscal Year 2005 as the first eligible recipients start school in the fall of 2004. At that time, this program will become the Corporation's largest scholarship program.

Although Tennessee State Government revenue growth improved during FY 2004, the Corporation continues to operate under budget restrictions. In FY 2005 the Corporation has been requested to reduce expenditures in the Tennessee Student Assistance Awards Program by approximately $1,500,000 in order for these funds to be reverted into the General Fund.

Exhibit A

Tennessee Student Assistance Corporation
Statements of Net Assets
June 30, 2004, and June 30, 2003

	June 30, 2004	June 30, 2003
Assets:		
Cash (Note 2)	$ 2,665,632.08	$ 1,422,267.73
Receivables:		
Notes receivable	5,903,799.21	5,246,771.44
Interest receivable	314,088.34	561,227.13
Due from the federal government		169,134.00
Accounts receivable	3,245.98	44.55
Total assets	8,886,765.61	7,399,444.85
Liabilities:		
Accounts payable	795,018.78	25,304.61
Accrued liabilities	1,246,198.24	819,436.22
Payroll related accruals	56,296.86	37,098.85
Due to the primary government	14,015.58	9,075.19
Deferred revenue	127,104.00	98,422.43
Due to the federal government		468,854.79
Advance from the federal government	423,252.19	448,755.11
Compensated absences:		
Payable within one year	55,965.95	41,086.26
Payable after one year	60,302.40	45,010.04
Total liabilities	2,778,154.00	1,993,043.50
Net assets:		
Unrestricted	$ 6,108,611.61	$ 5,406,401.35

The notes to the financial statements are an integral part of this statement.

Exhibit B

Tennessee Student Assistance Corporation
Statements of Activities
For the Years Ended June 30, 2004, and June 30, 2003

	Year Ended June 30, 2004	Year Ended June 30, 2003
Expenses for education:		
Grants expenses	$ 58,362,356.95	$ 46,649,229.63
Administrative expenses	2,177,595.98	952,671.66
Loan cancellations	441,771.29	1,721,664.68
Total program expenses	60,981,724.22	49,323,565.97
Program revenues:		
Charges for services	13,018,841.20	785,625.00
Operating grant and contributions	6,630,324.86	1,888,450.66
Total program revenues	19,649,166.06	2,674,075.66
Net program expenses	41,332,558.16	46,649,490.31
General revenues:		
Payments from primary government	42,034,768.42	46,403,620.68
Increase (decrease) in net assets	702,210.26	(245,869.63)
Net assets, beginning of year	5,406,401.35	5,652,270.98
Net assets, end of year	$ 6,108,611.61	$ 5,406,401.35

The notes to the financial statements are an integral part of this statement.

Exhibit C

Tennessee Student Assistance Corporation
Balance Sheets
General Fund
June 30, 2004, and June 30, 2003

	June 30, 2004	June 30, 2003
Assets:		
Cash (Note 2)	$ 2,665,632.08	$ 1,422,267.73
Receivables:		
Notes receivable	5,903,799.21	5,246,771.44
Interest receivable	314,088.34	561,227.13
Due from federal government		169,134.00
Accounts receivable	3,245.98	44.55
Total assets	$ 8,886,765.61	$ 7,399,444.85
Liabilities and fund balances:		
Liabilities:		
Accounts payable	$ 795,018.78	$ 25,304.61
Accrued liabilities	1,246,198.24	819,436.22
Payroll related accruals	56,296.86	37,098.85
Due to primary government	14,015.58	9,075.19
Deferred revenue	127,104.00	98,422.43
Due to federal government		468,854.79
Advance from federal government	423,252.19	448,755.11
Total liabilities	2,661,885.65	1,906,947.20
Fund balances (Note 4):		
Reserved for related assets	5,903,799.21	5,246,771.44
Reserved for other specific purposes	95,962.93	15,726.21
Reserved for continuing appropriations	225,117.82	230,000.00
Total fund balances	6,224,879.96	5,492,497.65
Total liabilities and fund balances	$ 8,886,765.61	$ 7,399,444.85

Reconciliation to Statement of Net Assets

Total fund balances	$ 6,224,879.96	$ 5,492,497.65
Compensated absences liability not reported in the fund	(116,268.35)	(86,096.30)
Total net assets	$ 6,108,611.61	$ 5,406,401.35

The notes to the financial statements are an integral part of this statement.

Exhibit D

Tennessee Student Assistance Corporation
Statements of Revenues, Expenditures, and Changes in Fund Balances
General Fund
For the Years Ended June 30, 2004, and June 30, 2003

	Year Ended June 30, 2004	Year Ended June 30, 2003
Revenues:		
Grant revenue from primary government	$ 42,034,768.42	$ 46,403,620.68
Departmental services revenue	13,018,841.20	785,625.00
Federal revenue	6,642,379.00	1,731,552.00
Interest income	(12,054.14)	156,898.66
Total revenues	61,683,934.48	49,077,696.34
Expenditures:		
Grants expenditures	58,362,356.95	46,649,229.63
Administrative expenditures	2,147,423.93	969,069.79
Loan cancellations	441,771.29	1,721,664.68
Total expenditures	60,951,552.17	49,339,964.10
Excess (deficiency) of revenues over (under) expenditures	732,382.31	(262,267.76)
Fund balance, beginning of year	5,492,497.65	5,754,765.41
Fund balance, end of year	$ 6,224,879.96	$ 5,492,497.65

Reconciliation to Statement of Activities

	Year Ended June 30, 2004	Year Ended June 30, 2003
Excess (deficiency) of revenues over (under) expenditures	$ 732,382.31	$ (262,267.76)
Compensated absences expense not reported as an expenditure in the fund	(30,172.05)	16,398.13
Increase (decrease) in net assets	$ 702,210.26	$ (245,869.63)

The notes to the financial statements are an integral part of this statement.

Exhibit E

Tennessee Student Assistance Corporation
Statements of Fiduciary Net Assets
Federal Family Education Loan Trust Fund
June 30, 2004, and June 30, 2003

	June 30, 2004	June 30, 2003
Assets:		
Cash (Note 2)	$ 62,936,631.23	$ 55,892,989.73
Receivables:		
Due from the federal government	1,236,344.00	761,581.00
Claims receivable	16,712,722.71	16,254,543.03
Total assets	80,885,697.94	72,909,113.76
Liabilities:		
Accounts payable	2,127,507.86	73,440.24
Total liabilities	2,127,507.86	73,440.24
Net assets:		
Held in trust for student loans (Note 5)	$ 78,758,190.08	$ 72,835,673.52

The notes to the financial statements are an integral part of this statement.

Exhibit F

Tennessee Student Assistance Corporation
Statements of Changes in Fiduciary Net Assets
Federal Family Education Loan Trust Fund
For the Years Ended June 30, 2004, and June 30, 2003

	Year Ended June 30, 2004	Year Ended June 30, 2003
Additions:		
Federal revenue	$ 22,472,961.76	$ 14,861,501.91
Interest income	619,965.30	867,668.11
Contribution from primary government	1,895,708.44	207,192.00
Miscellaneous	23,603.06	80,378.86
Total additions	25,012,238.56	16,016,740.88
Deductions:		
Administrative expenses	7,102,267.48	5,975,730.54
Collection expense	11,987,454.52	9,202,689.21
Total deductions	19,089,722.00	15,178,419.75
Increase (decrease) in net assets	5,922,516.56	838,321.13
Net assets, beginning of year	72,835,673.52	71,997,352.39
Net assets, end of year	$ 78,758,190.08	$ 72,835,673.52

The notes to the financial statements are an integral part of this statement.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The corporation is responsible for guaranteeing student loans under federal programs and administering federal and state grants/loans to students. The corporation is a component unit of the State of Tennessee. Although it is a separate legal entity, the majority of its board members are either appointed by the Governor or are state officials, and the corporation's budget is approved by the state. The corporation is discretely presented in the *Tennessee Comprehensive Annual Financial Report.*

Basis of Presentation

The financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). In June 1999, the GASB issued Statement 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*. The financial statements required by that statement provide a government-wide perspective of the corporation's assets, liabilities, net assets, revenues, expenses, and changes in net assets, in addition to the fund perspective previously required.

Measurement Focus and Basis of Accounting – Government-wide Statements

The government-wide financial statements include the statement of net assets and the statement of activities and report information about the corporation as a whole, except for the fiduciary fund. The government-wide financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The corporation has the option of following private-sector guidance issued subsequent to November 30, 1989, subject to the above limitation. The corporation elected not to follow private-sector guidance issued subsequent to November 30, 1989.

Measurement Focus and Basis of Accounting – General Fund Statements

The general fund is used to account for all financial transactions not required to be accounted for in another fund. The fund financial statements for the general fund include the balance sheet and the statement of revenues, expenditures, and changes in fund balances. The general fund financial statements have been prepared using the current financial resources measurement focus and the modified accrual basis of accounting. With this measurement focus, only current assets and current liabilities are generally included on the balance sheet. Under the modified accrual basis, revenues are recognized when they become susceptible to accrual, that is, when they become both measurable and available to finance expenditures of the current period. The corporation considers receivables collected within 60 days after year-end to be available and recognizes them as revenues of the current year. Expenditures are recorded at the time fund liabilities are incurred.

Measurement Focus and Basis of Accounting – Fiduciary Fund Statements

The Federal Family Education Loan Trust Fund is a private-purpose trust fund, which is used to account for the activities of a trust whose principal and income may be used for the purpose of the trust. The fund financial statements for the Federal Family Education Loan Trust Fund include the statement of fiduciary net assets and the statement of changes in fiduciary net assets. The fiduciary fund financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting except that (1) interest is not accrued on notes purchased under the provisions of the Federal Family Education Loan Program, as explained below; and (2) student loan guaranty fees are recorded as income in the year received rather than being amortized over the life of the student loans guaranteed.

Compensated Absences

It is the corporation’s policy to permit employees to accumulate earned but unused vacation and sick pay benefits. There is no liability for unpaid accumulated sick leave since the corporation’s policy is to pay this only if the employee is sick or upon death. All vacation pay is accrued when earned in the government-wide financial statements.

Accrual of Interest

Since the beginning of the federal loan program in 1963, the corporation has purchased insured loans whenever the student has defaulted, been declared bankrupt, died, or become totally and permanently disabled. Subsequent transactions with the U.S. Department of Education reduce the corporation's equity in these loans. Since it is anticipated that a large number of these loans are uncollectible, the corporation does not accrue interest on them but does attempt to collect interest on each one if repayment terms can be established with the borrower.

NOTE 2. CASH

This classification includes demand deposits and a $100.00 amount of petty cash on hand. The demand deposits are in the State Treasurer's Pooled Investment Fund. The Pooled Investment Fund's investment policy and custodial credit risk are presented in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Eighth Avenue North, Nashville, Tennessee 37243-0298, or by calling (615) 741-2140.

NOTE 3. COMPENSATED ABSENCES

Long-term liability activity for the year ended June 30, 2004, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amount Due Within One Year
Compensated absences	$86,096.30	$112,893.35	$82,721.30	$116,268.35	$55,965.95

Long-term liability activity for the year ended June 30, 2003, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amount Due Within One Year
Compensated absences	$102,494.43	$64,125.17	$80,523.30	$86,096.30	$41,086.26

NOTE 4. FUND BALANCE RESERVES

The fund balance reserves represent those portions of fund balance (1) not appropriable for expenditure—reserved for related assets—or (2) legally segregated for a specific future use—reserved for other specific purposes and reserved for continuing appropriations.

NOTE 5. NET ASSETS HELD IN TRUST FOR STUDENT LOANS

The corporation is required by state law to maintain a reserve equal to .25 percent of all outstanding loans that it has insured. The corporation has an agreement with the U.S. Department of Education whereby the federal government reinsures all loans insured by the corporation for at least 80 percent of the principal amount for loans made prior to October 1, 1993; 78 percent for loans made from October 1, 1993, through September 30, 1998; and 75 percent for loans made after October 1, 1998. Therefore, the corporation maintains a cash reserve equal to at least 2 percent of the outstanding loans that it has insured. The statutory reserve is invested by the Treasurer of Tennessee along with idle cash of the state, and a pro rata share of the monthly interest is paid to the corporation. By agreement, the corporation is free to withdraw from this investment pool such amounts as may be needed to honor its commitments under loan insurance agreements with commercial lenders. At June 30, 2004, the corporation had insured loans outstanding of $4,712,536,071.00 and the Treasurer of Tennessee held short-term investments of cash belonging to the loan program in the amount of $62,045,467.37. At June 30, 2003, the corporation had insured loans outstanding of $3,325,912,198.40, and the Treasurer of Tennessee held short-term investments of cash belonging to the loan program reserve in the amount of $56,581,130.49.

NOTE 6. DEFINED BENEFIT PENSION PLAN

Plan Description - The corporation contributes to the State Employees, Teachers, and Higher Education Employees Pension Plan (SETHEEPP), a cost-sharing multiple-employer defined benefit pension plan administered by the Tennessee Consolidated Retirement System (TCRS). TCRS provides retirement, death, and disability benefits as well as annual cost-of-living adjustments to plan members and their beneficiaries. Title 8, Chapters 34-37, *Tennessee Code Annotated*, establishes benefit provisions. State statutes are amended by the Tennessee General Assembly.

The TCRS issues a publicly available financial report that includes financial statements and required supplementary information for SETHEEPP. That report may be obtained by writing to the Tennessee Department of the Treasury, Consolidated Retirement System, 10th Floor Andrew Jackson Building, Nashville, Tennessee 37243-0230, or by calling (615) 741-8202.

Funding Policy - Plan members are noncontributory. The corporation is required to contribute an actuarially determined rate. The current rate is 7.29% of annual covered payroll. Contribution requirements for the corporation are established and may be amended by the TCRS' Board of Trustees. The corporation's contributions to TCRS for the years ended June 30, 2004, 2003, and 2002, were $91,151.60, $68,698.98, and $59,512.24. Contributions met the requirements for each year.

NOTE 7. OTHER POST-EMPLOYMENT BENEFITS

The State of Tennessee administers a group health insurance program which provides post-employment health insurance benefits to eligible corporation retirees. This benefit is provided and administered by the State of Tennessee. The corporation assumes no liability for retiree health care programs. Information related to this plan is available at the statewide level in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Eighth Avenue North, Nashville, Tennessee 37243-0298, or by calling (615) 741-2140.

NOTE 8. RISK MANAGEMENT

It is the policy of the state not to purchase commercial insurance for the risks of casualty losses for general liability, automobile liability, professional malpractice, and workers' compensation. The state's management believes it is more economical to manage these risks internally and set aside assets for claim settlement in its internal service fund, the Risk Management Fund. The state purchases commercial insurance for real property, flood, earthquake, and builder's risk losses and surety bond coverage on the state's officials and employees. The Risk Management Fund is also responsible for claims for damages to state owned property up to the amount of the property insurance aggregate deductible amount. The insurance policy deductibles vary from $25,000 per occurrence, depending on the type of coverage, to an aggregate of $7.5 million. The corporation participates in the Risk Management Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the corporation based on a percentage of the corporation's expected loss costs, which include both experience and exposures. This charge considers recent trends in actual claims experience of the state as a whole. An actuarial valuation is performed as of the fiscal year-end to determine the fund liability and premium allocation. The corporation is subject to the liability limitations under the provisions of the Tennessee Claims Commission Act, *Tennessee Code Annotated*, Section 9-8-101 et seq. Liability for negligence of the corporation for bodily injury and property damage is limited to $300,000 per person and $1,000,000 per occurrence. The limits of liability under workers' compensation are set forth in *Tennessee Code Annotated*, Section 50-6-101 et seq. Claims are paid through the state's Risk Management Fund. At June 30, 2004, the Risk Management Fund held $101.1 million in cash designated for payment of claims. In FY 2003, the state incurred 13 property claims which exceeded the per occurrence deductible. The gross amount of claims for the period was approximately $7.2 million, of which the state's property insurance carrier will ultimately assume approximately $2.2 million.

The state has also set aside assets in the Employee Group Insurance Fund, an internal service fund, to provide a program of health insurance coverage for the employees of the state with the risk retained by the state. The corporation participates in the Employee Group Insurance Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the corporation based on estimates of the ultimate cost of claims that have been reported but not settled and of claims that have been incurred but not reported. Employees and providers have 13 months to file medical claims.

NOTE 9. COMMITMENTS AND CONTINGENCIES

Sick Leave - The corporation records the cost of sick leave when paid. Generally, since sick leave (earned one day per month with unlimited accumulation) is paid only when an employee dies or is absent because of illness, injury, or related family death, there is no liability for sick leave at June 30. The dollar amount of unused sick leave was $403,969.13 at June 30, 2004, and $260,915.03 at June 30, 2003.

Operating Lease - The corporation has entered into an operating lease for office space. This lease will likely continue to be required. Expenditures under the operating lease were $204,012 for the year ended June 30, 2004, and $164,442 for the year ended June 30, 2003. The operating lease is cancelable at the lessee's option.

Schedule 1

SUPPLEMENTARY INFORMATION
TENNESSEE STUDENT ASSISTANCE CORPORATION
BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEARS ENDED JUNE 30, 2004 AND JUNE 30, 2003

	FOR THE YEAR ENDED JUNE 30, 2004				FOR THE YEAR ENDED JUNE 30, 2003			
	Budgeted Amounts			Variance with Final Budget	Budgeted Amounts			Variance with Final Budget
	Original	Final	Actual Amounts (Budgetary Basis)1	Positive (Negative)	Original	Final	Actual Amounts (Budgetary Basis)	Positive (Negative)
Budgetary fund balance, July 1	$ 5,492,497.65	$ 5,492,497.65	$ 5,492,497.65	$ -	$ 5,754,765.41	$ 5,754,765.41	$ 5,754,765.41	$ -
Resources (inflows):								
Grant revenue from primary government	43,667,200.00	43,667,200.00	42,034,768.42	(1,632,431.58)	55,358,700.00	47,978,900.00	46,403,620.68	(1,575,279.32)
Departmental services revenue	-	-	13,018,841.20	13,018,841.20	932,500.00	932,500.00	785,625.00	(146,875.00)
Federal revenue	1,562,400.00	1,562,400.00	6,642,379.00	5,079,979.00	1,562,400.00	1,562,400.00	1,731,552.00	169,152.00
Interest income	-	-	(12,054.14)	(12,054.14)	-	-	156,898.66	156,898.66
Amounts available for appropriation	50,722,097.65	50,722,097.65	67,176,432.13	16,454,334.48	63,608,365.41	56,228,565.41	54,832,461.75	(1,396,103.66)
Charges to appropriations (outflows):								
Personal services	584,400.00	584,400.00	472,215.74	112,184.26	542,400.00	542,400.00	490,605.54	51,794.46
Employee benefits	189,020.00	189,020.00	160,308.65	28,711.35	146,380.00	146,380.00	142,512.40	3,867.60
Travel	17,900.00	17,900.00	51,727.54	(33,827.54)	43,000.00	43,000.00	9,635.84	33,364.16
Printing, duplicating, and film processing	10,000.00	10,000.00	11,733.84	(1,733.84)	16,500.00	16,500.00	17,011.82	(511.82)
Communication and shipping cost	41,000.00	41,000.00	14,705.28	26,294.72	110,000.00	110,000.00	81,957.22	28,042.78
Maintenance, repairs, and services	1,700.00	1,700.00	1,054.40	645.60	1,700.00	1,700.00	495.00	1,205.00
Professional and administrative services	12,849,880.00	15,049,880.00	14,693,148.64	356,731.36	174,020.00	174,020.00	19,148.81	154,871.19
Supplies	79,700.00	79,700.00	16,504.48	63,195.52	42,600.00	42,600.00	13,706.45	28,893.55
Rentals and insurance	87,900.00	87,900.00	16,883.39	71,016.61	66,800.00	66,800.00	84,289.55	(17,489.55)
Awards and indemnities	1,050.00	1,050.00	138.30	911.70	1,050.00	1,050.00	0.00	1,050.00
Grants and subsidies	45,413,350.00	45,413,350.00	45,425,010.11	(11,660.11)	49,118,850.00	49,118,850.00	48,372,587.94	746,262.06
Professional services	28,600.00	28,600.00	88,121.80	(59,521.80)	210,500.00	210,500.00	108,013.53	102,486.47
Total charges to appropriations	59,304,500.00	61,504,500.00	60,951,552.17	552,947.83	50,473,800.00	50,473,800.00	49,339,964.10	1,133,835.90
Budgetary fund balance, June 30	$ (8,582,402.35)	$ (10,782,402.35)	$ 6,224,879.96	$ 17,007,282.31	$ 13,134,565.41	$ 5,754,765.41	$ 5,492,497.65	$ (262,267.76)

1 GAAP (i.e.,modified accrual) serves as the budgetary basis of accounting.