

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
Denver, Colorado**

**FINANCIAL AND COMPLIANCE AUDIT
Fiscal Years Ended June 30, 2005 and 2004**

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Members of the Legislative Audit Committee:

This report contains the results of a financial and compliance audit of the College Access Network, Department of Higher Education, State of Colorado for the Fiscal Year ended June 30, 2005. The audit was conducted pursuant to Section 23-3.1-109, C.R.S., which authorizes the State Auditor to conduct an annual audit of the College Access Network, Department of Higher Education, State of Colorado. The report presents our conclusions, findings and recommendations and the responses of the College Access Network, Department of Higher Education, State of Colorado.

Clifton Gunderson LLP

Denver, Colorado
September 2, 2005, except for Note 15,
as to which the date is November 1, 2005

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**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
Fiscal Year Ended June 30, 2005**

Authority, Purpose, and Scope

This audit was conducted under Section 23-3.1-109, C.R.S., which authorizes the State Auditor to conduct an annual audit of the College Access Network, Department of Higher Education, State of Colorado, (the “Enterprise”). The State Auditor contracted with Clifton Gunderson LLP to perform this audit. The audit was conducted in accordance with auditing standards generally accepted in the United States of America as promulgated by the American Institute of Certified Public Accountants in *Statements on Auditing Standards*; the standards for financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; the Single Audit Act of 1996, as amended; and the provisions of Office of Management and Budget (“OMB”) Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*, as amended. The purpose of this report is to present the results of the financial and compliance audit of the College Access Network, Department of Higher Education, State of Colorado for the Fiscal Years ended June 30, 2005 and 2004 and to report on current year findings and on the implementation status of the prior year recommendations.

Audit Opinions and Reports

We expressed an unqualified opinion on the Enterprise’s financial statements, as of and for the Fiscal Years ended June 30, 2005 and 2004. We noted two reportable conditions related to reconciliation of the repurchase liability account and accounts related to funds collected on defaulted loans. These are described in Recommendation No. 1 and No. 2 in the “Findings and Recommendations” section of this report.

Additional Required Communications

Accounting Policies. There were no changes to the Enterprise’s accounting policies during the year ended June 30, 2005.

Management Judgments and Accounting Estimates. The Enterprise provides an allowance for loan losses of 92% of its purchased loans receivable. The allowance is determined based on historical collection experience of the related receivable. We reviewed management’s methodology for estimating this allowance and determined that the allowance was adequate. There were no other significant accounting estimates of financial data which would be particularly sensitive and require substantial judgment by management.

Additional Required Communications (continued)

Significant Audit Adjustments. There was an audit adjustment made for \$356,309 to adjust the repurchase liability account and an additional adjustment for \$64,900 to adjust another liability account for funds received on defaulted loans. There was an audit adjustment made to capitalize certain software developed in the amount of \$158,636 and record related depreciation expense of \$40,961. An adjustment was also recorded for \$326,303 to reduce the amount of depreciation taken on certain assets. There were also adjustments made that were not recorded for the Fiscal Year ended June 30, 2004 audit by the Enterprise. These adjustments are reflected on Enterprise's financial statements for the year ended June 30, 2005 and were corrected in the State's accounting system. There were no other adjustments arising from the audit that could, in our judgment, either individually or in the aggregate, have a significant effect on the Enterprise's financial reporting process.

Uncorrected Misstatements. There were four uncorrected misstatements aggregated by us during our current audit and pertain to the two periods presented in the financial statements. The first was to write down purchase loan receivable amounts and related allowance in the amount of \$63,928. The second was to properly capitalize net software license fees for \$54,167. The third was to properly record prepaid software maintenance costs in the amount of \$59,521 and the fourth was to recognize revenue relating to the prior year that was recognized this year in the amount of \$206,948. The Enterprise has determined that these uncorrected misstatements are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

Disagreements with Management. There were no disagreements with management on financial accounting and reporting matters, auditing procedures, or other matters which would be significant to the Enterprise's financial statements or our report on those financial statements.

Current Year Findings and Recommendations

The Enterprise has two current year findings and recommendations relating to maintaining proper controls and support for the repurchase liability due to the U.S. Department of Education ("DE"), and establish proper controls and accounting for funds received on defaulted loans. The Enterprise has agreed with these recommendations. A summary of the recommendations and the Enterprise's responses can be found in the Recommendation Locator.

Summary of Progress in Implementing Prior Year Recommendations

In regard to the findings and recommendations from the prior year, one was implemented and two were partially implemented.

RECOMMENDATION LOCATOR

<u>Rec. No.</u>	<u>Page No.</u>	<u>Recommendation Summary</u>	<u>Enterprise's Response</u>	<u>Implementation Date</u>
1	8	The Enterprise should continue to establish control procedures over the repurchase liability accounts.	Agree	Fiscal Year 2006
2	10	The Enterprise should establish control procedures over collection liability accounts.	Agree	Fiscal Year 2006

College Access Network, Department of Higher Education

Background

College Access Network (the “Enterprise”) was created by an act of the Colorado Legislature in June 1979. During the 2004 legislative session, House Bill 04-1350 allowed the Enterprise, formally the Colorado Student Loan Program, to change its name to Colorado College Access Network, effective July 1, 2004. It is a self-supporting enterprise and receives no State appropriation. The primary mission of the Enterprise is to assist Colorado residents with planning and financing their cost of higher education.

The Enterprise represents a partnership between lenders, schools, and the Federal government. The loan capital is provided by approximately 50 private lenders – banks, savings and loan associations, credit unions, pension funds, insurance companies, or secondary markets, plus five schools for graduate borrowers. The Enterprise administers the Federal Family Education Loan Program and guarantees the loans made to students and parents in accordance with Federal regulations established pursuant to *Title IV, Part B, of the Higher Education Act of 1965 (P.L. 89-329) as amended*, (20 U.S.C. 1071 *et seq.*). Students borrow to attend 65 participating Colorado schools, and any participating national school – colleges, universities, community colleges, career schools (proprietary), graduate and professional. The school certifies both student enrollment and financial costs.

The Enterprise insures the lender against financial loss from default, disability, death, or bankruptcy. The Enterprise also provides needed technical and training assistance to schools and lenders, and performs periodic compliance reviews to assure that both schools and lenders are performing in accordance with applicable laws, regulations, and policies. The Enterprise also performs loan-servicing functions for lenders such as loan disbursement and repayment, assists borrowers through default prevention activities, and pursues collection of defaulted loans.

The Federal government serves as the reinsurer. If the Enterprise must reimburse a lender for an uncollectible loan, it files a claim for reimbursement to the Federal government pursuant to §428(c)(1) and §682.404(a) and the Voluntary Flexible Agreement (VFA). Fiscal Year 2005 is the first year under which the VFA existed between the Enterprise and the Federal government (U.S. Department of Education). Under the VFA, claims paid by the Enterprise are reimbursed at 100%. In addition, the Enterprise is not only compensated for its collection efforts on defaulted loans, but also for its success at preventing such delinquencies and defaults. Under certain loans, the Federal government subsidizes the student’s interest payments while in school at least half-time and during authorized periods of deferment. The Federal Government also pays a special allowance to lenders for certain loans to make up for the difference between the lender’s cost of money and the interest rate they can charge the student.

Federal Family Education Loan Program

As previously mentioned, the Enterprise administers the Federal Family Education Loan Program (the “FFEL” program) for the Federal government. Since inception of the Enterprise, approximately \$10 billion has been loaned. The total loan portfolio (net loans outstanding) at June 30, 2005 is \$6.6 billion. The FFEL program consists of Stafford, PLUS, and Consolidation Loans as described below.

Federal Stafford Loans (Subsidized and Unsubsidized)

Any student, regardless of income, may receive a Federal Stafford Loan. This program makes low-interest rate loans to students enrolled at participating colleges and universities. The interest rates are variable, and they are adjusted on July 1st of each year. Subsidized Stafford Loans are those in which the Federal government pays the interest on the loan as long as the student is in school, or in grace period, or in loan deferment. If the student does not qualify financially for federal interest subsidy, the student can still borrow but will be responsible for interest payments (Unsubsidized Stafford Loan). The interest may be paid while in school, or it may accrue and be paid upon leaving school.

Since the creation of the Enterprise in 1979, Stafford loans totaling over \$4.6 billion have been made to students. Students borrowed a net total of \$433 million in Stafford Loans in Fiscal Year 2005.

Federal PLUS Loans

Parents of dependent undergraduate students are eligible to borrow under another Federal Loan Program called the Parent Loans for Undergraduate Students (PLUS). PLUS loans are not based on financial need, and have a variable interest rate that is also adjusted on July 1st of each year. The maximum amount that can be borrowed is limited only by the cost of school attendance minus any other financial aid. The school financial aid office and/or the lender make the final determination on the amount.

Since 1979, parents participating in the PLUS program have received over \$355 million in loans. In Fiscal Year 2005, the net PLUS loans totaled \$35 million.

Federal Consolidation Loans

Students attending a college or university may have more than one type of loan. The Federal Loan Consolidation Program allows student borrowers to combine their Stafford, Perkins, Federally Insured Student Loans (“FISL”), Health Professional Student Loans (“HPSL”), or Federal Supplemental Loans for Students (“SLS”) into one loan. PLUS loans made after October 17, 1986, can be consolidated by parent borrowers. Effective January 1, 1993, defaulted loans may be consolidated provided certain conditions are met. Consolidating loans may result in a lower payment, and no insurance premium is charged. In addition, the interest rate for loan consolidations is fixed for the life of the loan.

Since inception of this program, loan consolidations total \$5 billion. In Fiscal Year 2005, \$2.8 billion in net loan consolidations were generated.

Additional information regarding the services and activities of the Enterprise may be obtained from the Director's Office.

Findings and Recommendations

Reconciliation of Repurchase Liability

As previously mentioned, Colorado lenders provide loans under the Federal Family Education Loan Program (FFEL Program) through the College Access Network (the “Enterprise”) to students who want to attend college in Colorado. If a student should default on a loan, the lender files a claim for the outstanding amount of the loan with the Enterprise, which serves as the insurer on loans made under the FFEL Program. The Enterprise claims staff reviews the claim, and if all requirements are met, the Enterprise reimburses the lender for the outstanding principal balance plus accrued interest. In turn, the Enterprise files for reimbursement from the U.S. Department of Education (DE), which acts as the reinsurer on loans under the FFEL Program. The Enterprise usually receives its payment from the DE within 30 days after filing a claim for reinsurance.

In some instances, the lender may wish to repurchase the loan from the Enterprise after having been paid for its claim. For example, the lender may determine that an error was made and the loan was incorrectly identified as being in default, when, in fact, it was not. When the Enterprise sells a repurchased loan back to the lender, the Enterprise is responsible for reimbursing the DE for any reinsurance it has been paid related to the loan. When a loan is repurchased, the Enterprise records a liability to the DE to reflect reinsurance owed back to the DE.

However, if the Enterprise has not yet filed a claim or received a reinsurance payment for the repurchased loan, no amount is owed back to the DE. During our audit of the Enterprise for Fiscal Year 2004, we found that the liability account for recording reinsurance payments owed back to DE was overstated by \$1,713,493 due to instances in which the Enterprise had not previously filed for or received a reinsurance payment on repurchased loans. Therefore, no liability should have been reflected for these reinsurance payments. We recommended that the Enterprise establish control procedures to ensure that the liability account reflected only amounts related to instances in which it has filed for and received reinsurance payments on repurchased loans, and that the Enterprise review activity in the liability account and ensure that the amount is supported by underlying detail related to specific loans.

During our audit for Fiscal Year 2005, we found that the Enterprise repurchase liability account in the general ledger was overstated by \$356,309 compared to the amount supported by the underlying detail on activity in the account. An adjustment was made to decrease the liability in the general ledger from \$2,147,760 to \$1,791,451 at June 30, 2005. This adjustment was necessary because, although the Enterprise was reconciling monthly collection and payment activity to reports submitted to DE, the Enterprise was not performing a reconciliation between the detailed activity in the liability to the balance in the general ledger.

Findings and Recommendations (continued)

Recommendation No. 1

The Enterprise should continue to improve controls over repurchased loans by reconciling the amount supported by the underlying detail on individual loan activity to the liability for reinsurance payments due to DE in the general ledger.

Enterprise Response:

Agree. Beginning with July 1, 2004, College Access Network received 100% reinsurance on all claims submitted to DE. The amount of the liability that remained on the financial statements was related to claims that occurred prior to July 1, 2004. College Access Network agrees that such reconciliations should take place even if it receives 100% reinsurance. In the future, there is the possibility that College Access Network may not receive 100% reinsurance on all claims as it currently does and thus the procedure should be in place for current and future reconciliations.

College Access Network will develop a written procedure in conjunction with Nelnet, Inc. to reconcile both the monthly collection and payment activity to reports submitted to DE, as well as developing a procedure to reconcile the detailed activity in the liability to the balance in the general ledger.

Findings and Recommendations (continued)

Reconciliation of Collection Liability

The Enterprise may receive loan payments, or collections, on a defaulted loan in cases where the Enterprise has filed for and received reinsurance from DE. After a claim for reinsurance has been processed by DE and received by the Enterprise, the amounts subsequently collected on these defaulted loans by the Enterprise are due and payable to DE. The Enterprise maintains a liability account for such collections, which represents amounts owed to DE.

During our audit procedures for Fiscal Year 2005, we noted that this liability account in the general ledger had not been reconciled to the underlying activity in the account, and as a result, the general ledger was overstated by \$64,900 for a balance of \$1,143,104. Therefore, an adjustment was made to reflect the correct general ledger balance of \$1,078,204 at June 30, 2005. The adjustment was made to reduce the liability balance at June 30, 2005 to the same balance for this liability at June 30, 2004.

The Enterprise stated that the liability represents an accumulation of excess collections on defaulted loans over several years not yet remitted to DE. The liability was computed each year based on an annual analysis of what was reported to DE as that entity's share of collections and what was actually paid to DE for each fiscal year. The liability was adjusted each year based on this analysis.

Furthermore, the Enterprise stated that with the implementation of the Voluntary Flexible Agreement ("VFA") on July 1, 2004, the calculation of this excess collection revenue was no longer required. Therefore, since no payments on the liability were made to DE during Fiscal Year 2005 on this liability, there was no change in the liability balance from June 30, 2004 to June 30, 2005. In addition, the staff stated that under the new VFA the Enterprise may no longer be liable to DE for the \$1,078,204 liability related to collections on defaulted loans received prior to July 1, 2004. However, the staff of the Enterprise did not provide specific correspondence from DE or other documentation to support this or that these collections were no longer required to be remitted to DE.

The Enterprise has the responsibility to ensure that collections on defaulted loans and the related liabilities to DE are properly reconciled to supporting detail on a timely basis and that the general ledger balance for this liability is adjusted accordingly. If the excess collections were due to DE prior to July 1, 2004 and, under the new VFA, all subsequent excess collections are not a liability to DE, the Enterprise is still responsible for properly stating any remaining liability from the period prior to the new agreement. Additionally, the Enterprise should consult with DE to determine whether the liability of \$1,078,024 from the period prior to the new agreement is still owed to DE under the current VFA.

Findings and Recommendations (continued)

Recommendation No. 2

The Enterprise should establish control procedures over collections on defaulted loans in instances where reinsurance has been received from DE and collections on loans are owed to DE. The procedures should include monitoring collections received on these loans and reconciling the collections due to DE, supported by the underlying detailed activity, to the liability balance in the general ledger of the appropriate fund on a monthly basis. The Enterprise should also consult with DE on the treatment of the outstanding liability of \$1,078,024 and the treatment of collections on these types of loans received on or after July 1, 2004.

Enterprise Response:

Agree. Over the past years, College Access Network reviewed the amount of revenue received from collections against the amount sent to the DE. Beginning at the end of Fiscal Year 2004, the accounting staff recognized that this liability continued to grow each year with no resolution to transferring the amount due to the DE. Research conducted during Fiscal Year 2005 indicated that this amount was due to DE.

Beginning in September 2004, College Access Network implemented a new Form 2000 reporting process which alleviated this annual differential. For Fiscal Year 2005, the amount of difference between collections and amount sent to the DE was \$0.

On October 14, 2005 for the fiscal period ending September 30, 2005, the agency transferred to the Federal Reserve Fund an amount of \$1,078,204 reducing the liability to \$0.

For Fiscal Year 2006, the agency will develop a written formal review policy and a financial reconciliation procedure in conjunction with Nelnet, Inc. to be completed on a monthly basis to make sure that the revenue received from collections is then appropriately sent to the DE.

Disposition of Prior Year Audit Findings

The following is a summary of audit recommendations made as part of the financial audit for the year ended June 30, 2004 and the current disposition of these recommendations.

Recommendation No. 1

The Enterprise should establish control procedures over the repurchase liability accounts.

Disposition

Partially implemented. See current year recommendation No. 1.

Recommendation No. 2

The Enterprise should ensure adequate controls are in place over default aversion fees (“DAF”).

Disposition

Implemented.

Recommendation No. 3

The Enterprise should properly capitalize assets and record costs incurred relating to capital assets.

Disposition

Partially implemented. The Enterprise did not capitalize all software costs during Fiscal Year 2005. Implementation date July 1, 2005.

FINANCIAL SECTION

Independent Auditor's Report

Members of the Legislative Audit Committee:

We have audited the accompanying combined statement of net assets of the College Access Network, Department of Higher Education, State of Colorado (the "Enterprise") as of June 30, 2005 and 2004 and the combined statements of revenues, expenses and changes in net assets and cash flows for the years then ended, which collectively comprise the Enterprise's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Enterprise's management. 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 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 audits 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 opinion.

As discussed in Note 1, the financial statements of the Enterprise are intended to present the financial position, and results of operations and cash flows for only that portion of the financial reporting entity, the State of Colorado, that is attributable to the transactions of the Enterprise. They do not purport to, and do not present fairly, the financial position of the State of Colorado as of June 30, 2005 and 2004 and the changes in its financial position and its cash flows, where applicable, for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Enterprise as of June 30, 2005 and 2004 and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 2, 2005, except for Note 15, as to which the date is November 1, 2005, on our consideration of the Enterprise'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 considered in assessing the results of our audit.

The Management's Discussion and Analysis (MD&A) is not a required part of the basic financial statements but is supplemental 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 this supplemental 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 financial statements that collectively comprise the Enterprise's basic financial statements. The accompanying supplemental information 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 audit of the basic financial statements, and, in our opinion, is presented fairly, in all material respects, in relation to the basic financial statements taken as whole.

Clifton Gunderson LLP

Denver, Colorado
September 2, 2005, except for Note 15
as to which the date is November 1, 2005

MANAGEMENT'S DISCUSSION AND ANALYSIS

The Management's Discussion and Analysis (MD & A) is required by Governmental Accounting Standards. It was prepared by the Enterprise's management and is designed to provide an analysis of the Enterprise's financial condition and operating results for the fiscal years ended June 30, 2005 and 2004. The MD & A also informs the reader of the financial issues and activities related to the Enterprise. It should be read in conjunction with the Enterprise's financial statements, which begin on page 30. College Access Network, formerly the Colorado Student Loan Program, is a state agency that provides origination, servicing and collection services on behalf of private and non-profit lenders participating in the Federal Family Education Loan Program ("FFEL") pursuant to the *Higher Education Act of 1965*.

Basic Financial Statements

The financial report includes the report of independent auditors, the management's discussion and analysis, and the basic financial statements. The financial statements are interrelated and represent the financial status of the Enterprise.

The Balance Sheet is now referred to as the Statement of Net Assets, which includes the assets, liabilities and net assets at the end of the fiscal year. Over time, increases or decreases in the net assets continue to serve as a useful indicator of whether the financial position of the Enterprise is improving or deteriorating.

The Statement of Revenues, Expenses and Changes in Net Assets presents the revenues earned and expenses incurred during the fiscal year. Revenues and expenses are reported on the accrual basis. Thus, revenues and expenses are reported in the statement for some items that will result in cash flows in future fiscal periods.

The Statement of Cash Flows presents information related to cash inflows and outflows summarized by operating, noncapital, investing and capital and related financing activities. Operating activities represent the day-to-day activities of the Enterprise. Noncapital activities represent transfers to other agencies. Capital and related financing activities represent acquisitions of capital assets and payments on capital debt and capitalized leases. Investing activities represent investment earnings on temporary cash investments.

Financial Overview

The Enterprise is an Enterprise Fund of the State of Colorado. The Enterprise's activities are accounted for in three separate funds residing with the State Treasurer – the Agency Operating Fund, the Loan Servicing Fund, and the Federal Reserve Fund. The following condensed financial statements do not distinguish between the Agency Operating and Loan Servicing Funds (operating funds for the guarantor and lender servicing functions of the Enterprise), but do make a distinction between these operating funds and the Federal Reserve Fund. The Federal Reserve Fund is designated only for paying lender claims and/or returning funds owed to the United States Department of Education ("DE"), respectively. The Federal Reserve Fund is the property of the federal government.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Management Highlights

During the 2004 legislative session, House Bill 04-1350 allowed the Enterprise, formally the Colorado Student Loan Program, to change its name to *Colorado College Access Network, d.b.a College Access Network*, effective July 1, 2004. The name change positions the Enterprise to capitalize on new markets internal and external to Colorado.

The Enterprise's largest source of revenue in the Federal Reserve Fund is reinsurance from the DE on claims paid to lenders on defaulted loans. The Enterprise receives reinsurance from DE for 95% to 100% of the amount of lender claims paid. For fiscal year 2005, the Enterprise claims were generally reimbursed at 100% reflecting the Voluntary Flexible Agreement (VFA) entered into between the Enterprise and DE, effective July 1, 2004. For fiscal year 2005, this represented \$65,263,224 of the \$71,047,303 in revenue for the Federal Reserve Fund. For fiscal year 2004, revenue from reinsurance was \$50,492,123. Total claims paid to lenders for the fiscal year 2005 from Federal Fund were \$64,740,853, an increase of 25% from fiscal year 2004. For fiscal year 2005, the Enterprise also re-implemented on July 1, 2004 a Guarantee Fee – a 1% fee paid by students or lenders on the disbursed principal of a loan for the purpose of sustaining the Federal Reserve Fund. Guarantee fee revenue earned by the fund in fiscal year 2005 totaled \$4,131,024, an increase of 2,347% over fee income to the fund of \$168,808 in the previous fiscal year. The fee amount in 2004 reflects the timing of the reintroduction of the fee by the Enterprise, which had suspended charging the fee in 1999 to borrowers. The total Federal Reserve Fund assets increased 70% between Fiscal Years 2004 and 2005.

On February 17, 2005, the Enterprise and DE finalized an agreement to allow for the Enterprise to purchase the Loan Servicing assets owned by DE for a total of \$1,451,606. This purchase of federal assets allowed the Enterprise to fully realize funds earned by Loan Servicing to remain in the Enterprise's Agency Operating Fund rather than maintaining a separate Loan Servicing Fund.

The Enterprise is in the business of guaranteeing student loans and should a loan default, continuing collection efforts on these loans. During Fiscal Year 2005, the new gross loan volume guaranteed totaled \$3,581,286,904. The gross new loan volume guaranteed in Fiscal Year 2004 was \$1,719,333,597. The difference, \$1,861,953,307, represents a 108% increase in new loans guaranteed.

A large portion of this increase resulted from consolidation loan volume. Consolidation volume is created when borrowers combine all outstanding loans into a single loan that is often repaid over a longer term. In Fiscal Year 2005, new consolidation loans guaranteed totaled \$3,060,751,345, compared to \$1,233,639,550 in consolidation loan guarantees in Fiscal Year 2004. The growth rate of new consolidations guaranteed in Fiscal Year 2005 over Fiscal Year 2004 was 148%. Consolidation loans from many lenders increased in the fiscal year as students took advantage of historic low interest rates. Interest rates, which change annually for the Stafford program on July 1, reflect overall interest rate hikes. DE for the first time concluded students already in school could take advantage of consolidation options for existing loans, which added to the consolidation loan volume as lenders and schools encouraged students to consolidate outstanding debt at the lower rates.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

The Enterprise's total loan portfolio (net outstanding loans guaranteed) on June 30, 2005, was \$6,642,558,385. The net outstanding loans are computed by subtracting loan cancellations from gross loan volume. The total loan portfolio increased 82% or \$3,009,919,930 in Fiscal Year 2005. The Fiscal Year 2004 net outstanding loans was \$3,632,638,455.

The Enterprise, entered into a new funding agreement with the DE effective July 1, 2004. The Voluntary Flexible Agreement (VFA) allowed the Enterprise to receive compensation performance incentives based on its success at preventing student loan defaults. Instead of receiving a majority of its fees for collecting on defaulted loans, fees are also earned by implementing strategies to prevent defaults. The Enterprise is required to prove to the DE that the VFA benefits student borrowers, is cost effective to Federal taxpayers, and saves the U.S. of Department of Education resources.

Operating for the first full fiscal year under its VFA with DE, the Enterprise's revenue streams changed significantly in Fiscal Year 2005. The Enterprise continued to reduce expenditures in key areas, including salaries and benefits, the largest portion of the Enterprise expense budget.

The net increase in net assets for the Agency Operating and Loan Servicing Fund, fueled by significant revenue increases in multiple revenue sources, grew by 62% -- from \$20,095,310 in Fiscal Year 2004 to \$32,572,766 in Fiscal Year 2005. Revenue changes for all Funds, including the Federal Reserve Fund, resulting from the VFA included:

- Reinsurance from DE to the Enterprise for claim payments to lenders at 100%, rather than at 95-98% as in past years. Claims are paid from the Agency Operating Fund and the dollar-for-dollar reimbursement offsets those payments.
- Collections reimbursement at a variable rate rather than a fixed rate of 23%. The VFA's emphasis is on preventing defaults, not on collecting on accounts in default.
- Payment of the Default Aversion Fee at a variable rate with 1.01% being the floor and rising to 1.10%. Formerly the rate was a flat 1% on all eligible default aversion requests. In addition, the Enterprise may re-bill DE for diversion requests on eligible loans that are older than 12 months. Default Aversion payments also are made directly to the Enterprise by DE rather than as a transfer from the Federal Reserve Fund.
- Account Maintenance Fee and Loan Processing Issuance Fee are invoiced to DE monthly rather than quarterly as in the past.
- A new Delinquency Prevention fee is based on how successful the Enterprise is in preventing delinquencies. This fee is also invoiced to DE on a monthly basis.
- The Enterprise is now allowed to rehabilitate a loan based on a borrower making nine consecutive payments rather than 12 as has been done in the past. The Enterprise benefits from rehabilitating student loans, a process that allows student borrowers to rehabilitate their credit rating and bring their loans out of default.
- Effective July 1, 2004, the Federal Reserve Fund is escrowed and the .25% reserve requirement is waived under the agreement.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Historically, the Enterprise revenue growth relied heavily on default collections. Under the VFA, that revenue source decreased as a portion of total revenue comprising 29.1% of total revenues for Fiscal Year 2005 compared to 50.1% in 2004. The revenue sources of the Enterprise were more balanced under the VFA with growth in both Default Aversion fee revenue and the Delinquency Prevention fee revenues accounting for larger shares in total revenue. The Enterprise collected \$19,180,313 and \$11,106,343 on defaulted loans and bankruptcies in Fiscal Years 2005 and 2004, respectively. This represented 60.0% and 50.1% of the total operating revenues for Fiscal Years 2005 and 2004, respectively.

The Federal Balanced Budget Act of 1997 and the 1998 Reauthorization of the Higher Education Act required the Enterprise to return funds to the Federal Government. In Fiscal Year 2003, two payments were made. One payment of \$23,268,032 and a second payment of \$1,577,957 were made from the Federal Reserve Fund for a total of \$24,845,989. Two additional recall payments of \$1,531,547 and \$1,531,546 will be paid to DE in Fiscal Year 2007 and Fiscal Year 2008, respectively, from the Federal Reserve Fund.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

CONDENSED SCHEDULE OF NET ASSETS

Years Ended June 30,	Agency Operating and Loan Servicing Funds		Percent Change	Federal Reserve and Drawdown Funds		Percent Change
	2005	2004		2005	2004	
ASSETS						
Current Assets	\$ 35,072,926	\$ 24,090,034	46%	\$ -	\$ -	
Restricted Assets	-	-		13,041,957	7,690,188	70%
Capital Assets	1,243,933	732,502	70%	-	-	
Total Assets	<u>\$ 36,316,859</u>	<u>\$ 24,822,536</u>	46%	<u>\$ 13,041,957</u>	<u>\$ 7,690,188</u>	70%
LIABILITIES						
Current Liabilities	\$ 3,422,838	\$ 3,640,500	-6%	\$ -	\$ -	
Noncurrent Liabilities	321,255	1,086,726	-70%	-	-	
Liabilities Payable from Restricted Assets	-	-		4,221,993	4,541,600	
Total Liabilities	<u>\$ 3,744,093</u>	<u>\$ 4,727,226</u>	-21%	<u>\$ 4,221,993</u>	<u>\$ 4,541,600</u>	-7%
NET ASSETS						
Invested in Capital Assets, Net of Related Debt	\$ 1,029,741	\$ 386,451	166%	\$ -	\$ -	
Restricted	-	-		8,819,964	3,148,588	180%
Unrestricted	31,543,025	19,708,859	60%	-	-	
Total Net Assets	<u>\$ 32,572,766</u>	<u>\$ 20,095,310</u>	62%	<u>\$ 8,819,964</u>	<u>\$ 3,148,588</u>	180%

Years Ended June 30,	Agency Operating and Loan Servicing Funds		Percent Change	Federal Reserve and Drawdown Funds		Percent Change
	2004	2003		2004	2003	
ASSETS						
Current Assets	\$ 24,090,034	\$ 22,383,796	8%	\$ -	\$ -	
Restricted Assets	-	-		7,690,188	10,475,596	-27%
Capital Assets	732,502	643,182	14%	-	-	
Total Assets	<u>\$ 24,822,536</u>	<u>\$ 23,026,978</u>	8%	<u>\$ 7,690,188</u>	<u>\$ 10,475,596</u>	-27%
LIABILITIES						
Current Liabilities	\$ 3,640,500	\$ 3,870,189	-6%	\$ -	\$ -	
Noncurrent Liabilities	1,086,726	891,401	22%	-	-	
Liabilities Payable from Restricted Assets	-	-		4,541,600	4,772,553	
Total Liabilities	<u>\$ 4,727,226</u>	<u>\$ 4,761,590</u>	-1%	<u>\$ 4,541,600</u>	<u>\$ 4,772,553</u>	-5%
NET ASSETS						
Invested in Capital Assets, Net of Related Debt	\$ 386,451	\$ 416,447	-7%	\$ -	\$ -	
Restricted	-	-		3,148,588	5,703,043	-45%
Unrestricted	19,708,859	17,848,941	10%	-	-	
Total Net Assets	<u>\$ 20,095,310</u>	<u>\$ 18,265,388</u>	10%	<u>\$ 3,148,588</u>	<u>\$ 5,703,043</u>	-45%

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Agency Operating and Loan Servicing Funds – Fiscal Year 2005

Unrestricted Net Assets of the Agency Operating and Loan Servicing Funds increased from \$19,708,859 to \$31,543,025 or 60% in Fiscal Year 2005 due to the monthly direct billing of default aversion and account maintenance fees and the additional revenue from the default prevention fee. New originations and consolidation volume increased the Enterprise's overall loan portfolio, impacting Enterprise revenues as well. (See Condensed Statement of Revenues and Condensed Statement of Expenses on the following pages.) Total liabilities decreased 21% because of a significant reduction in the amount owed to vendors compounded by a reduction in accrued salaries and benefits. A 70% reduction in noncurrent liabilities resulted from the payout of accrued leave to a number of long-time Enterprise employees who chose to exercise an employee buy-out offered to classified employees in Fiscal Year 2005.

Agency Operating and Loan Servicing Funds – Fiscal Year 2004

Unrestricted Net Assets of the Agency Operating and Loan Servicing Funds increased from \$17,848,941 to \$19,708,859 or \$1,859,918 (10%) in Fiscal Year 2004 due to the transfer of default aversion and account maintenance fees for the fiscal year to the Agency Operating Fund from the Federal Reserve Fund. Current liabilities decreased 6% from \$3,870,189 to \$3,640,500 or a reduction of \$229,689 in Fiscal Year 2004. The most significant change occurred in accounts payable and accrued liabilities, which resulted from a decrease in accounts payable. The reduction in accounts payable was due to an accrual that was recorded for \$379,000 payable to Raytheon Corporation for fees related to the Quester Debt Management Collection System in Fiscal Year 2003 which was subsequently paid in Fiscal Year 2004. The Quester system is designed to provide electronic accounting and collection services for outstanding student loans.

Federal Reserve Fund – Fiscal Year 2005

Total assets increased in Fiscal Year 2005 by 70% reflecting several changes. First, the fund grew due to a constant revenue stream from guarantee fees paid by borrowers with new loans beginning July 1, 2004. Second, the fund was not depleted monthly by payment of the default aversion fee to the Agency Operating Fund or a transfer of revenue to accommodate a DE shortfall to pay Enterprise's earned account maintenance fees. Finally, the VFA provides for escrowing the Federal Fund and direct payment of claims at 100%, a provision that further reduced the expenditures from this fund compared to previous years.

The total change in net assets was an increase of \$5,671,376 (180%) from \$3,148,588 to \$8,819,964. The total increase reflects a transfer of \$1,202,608 made from Agency Operating Fund to Federal Reserve Fund in February 2005 to resolve ownership of the Enterprise loan servicing division with DE. The payment, authorized by the federal legislature several years ago, resulted from agreement between the Enterprise and DE as to the value of the federal interest in the operation. (See Economic Facts and Conditions for the Future for a discussion on insurance premium fee to be charged.)

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Federal Reserve Fund – Fiscal Year 2004

Total assets decreased in Fiscal Year 2004 from \$10,475,596 to \$7,690,188 or \$2,785,408 (27%). The decrease resulted from a reduction in the amount of Federal Reinsurance due to the Enterprise at the end of the fiscal year. This reduction was caused by a reduction in the amount of claim reimbursement due from the federal government.

The total change in net assets was a decrease of \$2,554,455 (44.8%) from 5,703,043 to \$3,148,588. This decrease resulted from interfund transfers totaling \$2,098,662. The transfer amount is related to the payment of the Agency Operating Fund for default aversion and account maintenance fees due as allowed by the Higher Education Act. The decrease also reflects the difference between the guarantee claims paid to lending institutions and federal reinsurance received on those claims.

The Federal Reserve Fund's beginning net assets balance was adjusted to correct an overstatement of repurchase obligations due to the Federal Government prior to June 30, 2002. The beginning net assets were increased by \$1,567,094 and the liability was decreased by the same amount. The cash payments for these amounts were appropriately paid to the Federal Government. However, the adjustment reflecting the payments was not appropriately recorded on the financials. Measures have been taken to prevent this oversight from reoccurring. The following summarizes the restatement to beginning net assets:

Net Assets June 30, 2003	\$4,135,949
Adjustment	<u>\$1,567,094</u>
Restated Net Assets June 30, 2003	<u>\$5,703,043</u>

CONDENSED SCHEDULE OF CHANGES IN NET ASSETS

Years Ended June 30,	Agency Operating and Loan Servicing Funds		Percent Change	Federal Reserve and Drawdown Funds		Percent Change
	2005	2004		2005	2004	
Operating Revenues	\$ 31,103,550	\$ 20,946,214	48%	\$ 71,047,303	\$ 51,275,215	39%
Operating Expenses	20,040,311	21,061,620	-5%	64,740,853	51,760,586	25%
Operating Income or (Loss)	<u>11,063,239</u>	<u>(115,406)</u>	9686%	6,306,450	(485,371)	1399%
Earnings on Investments	534,385	44,052	1113%	346,953	29,578	1073%
Loss on Sale of Equipment	-	(49,944)	-100%	-	-	-
Total Transfers In/(Out)	879,832	1,951,220	-55%	(982,027)	(2,098,662)	-53%
NET INCREASE/(DECREASE) IN NET ASSETS	<u>12,477,456</u>	<u>1,829,922</u>	582%	5,671,376	(2,554,455)	322%
NET ASSETS, BEGINNING	<u>20,095,310</u>	<u>18,265,388</u>	10%	<u>3,148,588</u>	<u>5,703,043</u>	-45%
NET ASSETS, ENDING	<u>\$ 32,572,766</u>	<u>\$ 20,095,310</u>	62%	<u>\$ 8,819,964</u>	<u>\$ 3,148,588</u>	180%

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

CONDENSED SCHEDULE OF CHANGES IN NET ASSETS (continued)

Years Ended June 30,	Agency Operating and Loan Servicing Funds		Percent Change	Federal Reserve and Drawdown Funds		Percent Change
	2004	2003		2004	2003	
Operating Revenues	\$ 20,946,214	\$ 19,844,513	6%	\$ 51,275,215	\$ 57,240,585	-10%
Operating Expenses	21,061,620	21,174,047	-1%	51,760,586	58,571,486	-12%
Operating Income or (Loss)	<u>(115,406)</u>	<u>(1,329,534)</u>	91%	<u>(485,371)</u>	<u>(1,330,901)</u>	64%
Earnings on Investments	44,052	984,752	-96%	29,578	(1,644)	1899%
Loss on Sale of Equipment	(49,944)	-		-	-	
Total Transfers In/(Out)	1,951,220	3,478,979	-44%	(2,098,662)	(3,604,800)	-42%
NET INCREASE/(DECREASE) IN NET ASSETS	<u>1,829,922</u>	<u>3,134,197</u>	-42%	<u>(2,554,455)</u>	<u>(4,937,345)</u>	48%
NET ASSETS, BEGINNING	<u>18,265,388</u>	<u>15,131,191</u>	21%	<u>5,703,043</u>	<u>10,640,388</u>	-46%
NET ASSETS, ENDING	<u>\$ 20,095,310</u>	<u>\$ 18,265,388</u>	10%	<u>\$ 3,148,588</u>	<u>\$ 5,703,043</u>	-45%

CONDENSED SCHEDULE OF REVENUES

Years Ended June 30,	Agency Operating and Loan Servicing Funds		Percent Change	Federal Reserve and Drawdown Funds		Percent Change
	2005	2004		2005	2004	
OPERATING REVENUES						
Federal Grants and Contracts	\$ 25,155,493	\$ 15,277,292	65%	\$ 65,642,773	\$ 51,106,407	28%
Charges for Goods and Services	5,667,484	5,217,078	9%	4,131,024	168,808	2347%
Interest on Purchased Loans	259,891	414,475	-37%	-	-	
Other	20,682	37,369	-45%	1,273,506	-	
Total Operating Revenues	<u>\$ 31,103,550</u>	<u>\$ 20,946,214</u>	48%	<u>\$ 71,047,303</u>	<u>\$ 51,275,215</u>	39%
NONOPERATING REVENUES	<u>\$ 534,385</u>	<u>\$ 44,052</u>	1113%	<u>\$ 346,953</u>	<u>\$ 29,578</u>	1073%
TOTAL REVENUES	<u>\$ 31,637,935</u>	<u>\$ 20,990,266</u>	51%	<u>\$ 71,394,256</u>	<u>\$ 51,304,793</u>	39%

Years Ended June 30,	Agency Operating and Loan Servicing Funds		Percent Change	Federal Reserve and Drawdown Funds		Percent Change
	2004	2003		2004	2003	
OPERATING REVENUES						
Federal Grants and Contracts	\$ 15,277,292	\$ 14,334,462	7%	\$ 51,106,407	\$ 57,240,585	-11%
Charges for Goods and Services	5,217,078	4,701,986	11%	168,808	-	
Interest on Purchased Loans	414,475	488,257	-15%	-	-	
Other	37,369	319,808	-88%	-	-	
Total Operating Revenues	<u>\$ 20,946,214</u>	<u>\$ 19,844,513</u>	6%	<u>\$ 51,275,215</u>	<u>\$ 57,240,585</u>	-10%
NONOPERATING REVENUES	<u>\$ 44,052</u>	<u>\$ 984,752</u>	-96%	<u>\$ 29,578</u>	<u>\$ (1,644)</u>	1899%
TOTAL REVENUES	<u>\$ 20,990,266</u>	<u>\$ 20,829,265</u>	1%	<u>\$ 51,304,793</u>	<u>\$ 57,238,941</u>	-10%

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Agency Operating and Loan Servicing Funds – Fiscal Year 2005

Federal Grants and Contracts increased in Fiscal Year 2005 from \$15,277,292 to \$25,155,493 or 65% in the Agency Operating and Loan Servicing Funds. As previously discussed, most changes in guarantee-related revenue resulted from increased revenue due to overall portfolio growth, the growth in consolidation loans guaranteed and changes in the billing resulting from the VFA with DE. The Enterprise cash flow improved due to monthly invoicing of fees due from DE compared to previous quarterly payment of those revenues. Collections revenue actually declined from previous years under the VFA as the Enterprise refocused its efforts on rehabilitating – returning loans to good standing and repairing borrowers' credit histories – under the terms of the VFA and preventing borrowers with delinquent loans from entering default. Total operating revenues increased 48%, while loan-servicing revenues, charges for servicing loans for various lenders, increased 9% in fiscal year 2005.

Non-operating revenues in the Agency Operating and Loan Servicing Funds consist of earnings on temporary cash investments. Investment earnings increased from \$44,052 in Fiscal Year 2004 to \$534,385 (1113%) in Fiscal Year 2005 – a reflection of larger cash flow available on a monthly basis in the Enterprise funds invested by the State Treasurer and somewhat higher interest rates.

Agency Operating and Loan Servicing Funds – Fiscal Year 2004

Federal Grants and Contracts increased in Fiscal Year 2004 from \$14,334,462 to \$15,277,292 or \$942,830 (7%) in the Agency Operating and Loan Servicing Funds primarily due to increased defaulted loan collections and an increase in the account maintenance and loan processing and issuance fee. The Enterprise is allowed to retain 23% of all borrower payments collected on defaulted loans. Purchased Loan interest decreased by \$73,782 from \$488,257 to \$414,475 in fiscal year 2004. This decrease reflected a slight decrease in the number of loans repurchased by lenders.

During Fiscal Year 2004, \$13,800 was received by the Enterprise on behalf of the ColoradoMentor program compared to the previous year when \$309,900 in donations was received for a media campaign to promote the website. The amount received in Fiscal Year 2004 was used primarily for maintenance of data from participants who entered the program after the initial year. These amounts were recorded as Gifts and Donations and reported on the "Other" line under the Condensed Statement of Revenues for Fiscal Years 2003 and 2004.

Non-operating revenues in the Agency Operating and Loan Servicing Funds consist of earnings on temporary cash investments. Investment earnings decreased from \$984,752 to \$44,052 in fiscal year 2004 or \$940,700 (96%) due to a smaller amount of cash available on a monthly basis for investment, lower interest rates and a market adjustment to the state's pool investments at the end of the Fiscal Year 2004.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Federal Reserve Fund – Fiscal Year 2005

Federal Grants and Contracts increased in Fiscal Year 2005 by 28%, from \$51,106,407 in 2004 to \$65,642,773 in 2005. The increase reflects both an increase in the number of default claims paid to lenders and a slight increase in the size of some individual lender claims. The latter results from borrowers with larger-balance consolidation loans entering default. Reimbursement of claims by DE at 100% also impacted the increase in this revenue element. The revenue from guarantee fees paid is reflected in the Charges for Goods and Services in this fund (\$4,131,024) while Other reflects the amount of the transfer for the purchase of Loan Servicing from DE. Again, interest accrued on higher cash balances is reflected in a significant growth in the Nonoperating Revenues for this fund.

Federal Reserve Fund – Fiscal Year 2004

Federal Grants and Contracts decreased in Fiscal Year 2004 from \$57,240,585 to \$51,106,407 or \$6,134,178 (11%) in the Federal Reserve Fund. This decrease was caused mainly by a reduction in the amount of claims purchased from lenders. The Enterprise receives from 95% to 100% reinsurance on all claims paid to lending institutions. Claim payments decreased, resulting in a corresponding reinsurance decrease. Non-operating revenues (earnings on temporary cash investments) increased from (\$1,644) to \$29,578 in Fiscal Year 2004 or \$31,222 (+1899%) in the Federal Reserve Fund. The main reason for the difference is the investment market adjustment on the State Treasury pooled investments as of June 30, 2004.

CONDENSED SCHEDULE OF EXPENSES

Years Ended June 30,	Agency Operating and Loan Servicing Funds		Percent Change	Federal Reserve and Drawdown Funds		Percent Change
	2005	2004		2005	2004	
OPERATING EXPENSES						
Guarantee Claims Paid to Lending Institutions				\$ 64,740,853	\$ 51,760,586	25%
Salaries and Fringe Benefits	\$ 11,855,407	\$ 12,722,611	-7%	-	-	
Contracted Collection Costs	1,470,786	2,548,645	-42%	-	-	
Other Operating and Travel	6,342,322	5,376,354	18%	-	-	
Depreciation	371,796	414,010	-10%	-	-	
Total Operating Expenses	<u>\$ 20,040,311</u>	<u>\$ 21,061,620</u>	-5%	<u>\$ 64,740,853</u>	<u>\$ 51,760,586</u>	25%
NON OPERATING EXPENSES	102,195	147,442	-31%	-	-	
TOTAL EXPENSES	<u>\$ 20,142,506</u>	<u>\$ 21,209,062</u>	-5%	<u>\$ 64,740,853</u>	<u>\$ 51,760,586</u>	25%
Years Ended June 30,	Agency Operating and Loan Servicing Funds		Percent Change	Federal Reserve and Drawdown Funds		Percent Change
	2004	2003		2004	2003	
OPERATING EXPENSES						
Guarantee Claims Paid to Lending Institutions				\$ 51,760,586	\$ 58,570,453	-12%
Salaries and Fringe Benefits	\$ 12,722,611	\$ 13,520,461	-6%	-	-	
Contracted Collection Costs	2,548,645	1,706,541	49%	-	-	
Other Operating and Travel	5,376,354	5,423,057	-1%	-	1,033	-100%
Depreciation	414,010	523,988	-21%	-	-	
Total Operating Expenses	<u>\$ 21,061,620</u>	<u>\$ 21,174,047</u>	-1%	<u>\$ 51,760,586</u>	<u>\$ 58,571,486</u>	-12%
NON OPERATING EXPENSES	147,442	125,821	17%	-	-	
TOTAL EXPENSES	<u>\$ 21,209,062</u>	<u>\$ 21,299,868</u>	0%	<u>\$ 51,760,586</u>	<u>\$ 58,571,486</u>	-12%

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Agency Operating and Loan Servicing Funds – Fiscal Year 2005

Salaries and Fringe Benefits decreased from \$12,722,611 to \$11,855,407 or (7%) in fiscal year 2005. The reduction resulted from savings to the Enterprise in not filling vacancies in several areas. The Enterprise offered classified employees an opportunity to exercise voluntary separation agreements in the fiscal year and reduced both classified and non-classified staff positions in an agency-wide reorganization. Contracted Collection Costs decreased 42% from \$2,548,645 in fiscal year 2004 to \$1,470,786 in Fiscal Year 2005 due to a reduction in the number of outside collection agencies under contract with the Enterprise. Other Operating and Travel increased from \$5,376,354 to \$6,342,322 (18%) due in large part to the purchase of Loan Servicing from DE. Non-operating transfers to other agencies decreased from \$147,442 to \$102,195 or \$45,247 (31% in Fiscal Year 2005 due to a decrease in the statewide indirect cost allocation of expenses to the Enterprise.

Agency Operating and Loan Servicing Funds – Fiscal Year 2004

Salaries and Fringe Benefits decreased from \$13,520,461 to \$12,722,611 or \$797,850 (6%) in Fiscal Year 2004. The majority of the reduction was due to an effort by CSLP to reduce staff throughout the Enterprise to more appropriate levels for the work being accomplished within the Enterprise. Contracted Collection Costs increased from \$1,706,541 to \$2,548,645 or \$842,104 (49%) in fiscal year 2004 due to a large increase in consolidation collections by the outside collection agencies. Other Operating and Travel decreased slightly from \$5,423,057 to \$5,376,354 or \$46,703 (1%) due in large part to management efforts to decrease costs of doing business. Non-operating transfers to other agencies increased from \$125,821 to \$147,442 or \$21,621 (17%) in Fiscal Year 2004 due to an increase in the statewide indirect cost allocation of expenses to Colorado Student Loan Program.

Federal Reserve Fund – Fiscal Year 2005

Guarantee Claims Paid to Lending Institutions increased from \$51,760,586 in Fiscal Year 2004 to \$64,740,853 in Fiscal Year 2005 (25%) due to factors noted under the revenue analysis above.

Federal Reserve Fund – Fiscal Year 2004

Guarantee Claims Paid to Lending Institutions decreased from \$58,570,453 to \$51,760,586 or \$6,809,867 (12%) in Fiscal Year 2004 as noted under the revenue analysis above.

Budget versus Actual

The Enterprise prepares an annual budget, based on fiscal year projected revenues and expenses that is reviewed and approved by its Board of Directors (created by the Legislature in 2004) and by the Executive Director of the Department of Higher Education.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

During the preparation of the annual budget, the Agency Operating Fund and the Loan Servicing Fund are budgeted as separate funds. For financial presentation purposes, both the audit report and MD & A combine these presentations into one fund entitled Agency Operating and Loan Servicing Funds. On February 17, 2005, the Enterprise completed the purchase of the Loan Servicing Fund from DE. Therefore, beginning with the Fiscal Year 2005 audit the Loan Servicing Fund and the Agency Operating Fund will now be one fund and reported as the Agency Operating Fund.

Agency Operating and Loan Servicing Funds – Fiscal Year 2005

There was no budgeted change in net assets for the Agency Operating and Loan Servicing Funds between Fiscal Year 2004 and Fiscal Year 2005. The actual change in net assets was \$12,477,456. The change was caused by two major factors. These factors were an increase in revenues of \$10,157,336 and a reduction of anticipated expenditures of \$1,021,309 with the remaining difference of \$3,341,429 coming from changes in earnings on investments and interfund transfers.

Of the nearly \$10 million in increased revenues, the majority of the change was in the amount received by the Enterprise from payments made by DE for VFA revenue items including the new revenue stream entitled the Delinquency Prevention Fee. Approximately \$3.7 million of the increased revenues were related to the DPF and nearly \$4.2 million was related to increased Default Prevention Fees.

The reduction in expenditures came mainly from reduced personnel costs. In March 2005, nearly 25 classified employees voluntarily separated from the Enterprise. This saved nearly ¼ of their annual salary and benefits. In addition to the classified staff, six non-classified management and professional staff also took advantage of the voluntary separation package.

The change in net assets also includes non-operating revenue of \$982,027 in interfund transfers (see definition of interfund transfers and detail of transfers in section Interfund Transfers) from the Federal Reserve Fund to the Agency Operating Fund.

Agency Operating and Loan Servicing Funds – Fiscal Year 2004

The original budgeted change in net assets for the Agency Operating and Loan Servicing Funds was \$549,527. The budget for change in net assets was later revised upward to \$960,479. The actual change in net assets was \$1,829,922. The actual changes exceeded the budgeted amount because actual operating expenses were lower than budgeted.

Items that were in the original budget but not expended were as follows:

- Quester Debt Collection System hosting and travel \$1,238,321, was carried forward into the current year because the project was not completed;
- Administrative Shared expenditures. \$113,397, for travel, dues and fees and memberships was not expended. Most of these funds were used to offset the excess cost in outside collection agency fees;

MANAGEMENT’S DISCUSSION AND ANALYSIS (continued)

- Replacement positions were not filled in Business Research unit, \$83,608. This unit was later merged with other units within the Enterprise.
 - Reduction in purchased property services, mainly maintenance contracts, within Information Technology, \$88,898.
 - Partnership Initiatives did not hire additional staff as proposed, \$82,669.

The change in net assets also includes non-operating revenue of \$2,098,662 in interfund transfers (see definition of interfund transfers and detail of transfers in section Interfund Transfers) from the Federal Reserve Fund to the Agency Operating Fund.

Federal Reserve Fund – Fiscal Year 2005

The original budgeted net gain for the Federal Reserve Fund was \$4,606,303.00. The actual change in net assets was an increase of \$5,671,376. The majority of the increase was caused by the additional revenue, \$4.1 million, received by the implementation of a guarantee fee.

Federal Reserve Fund – Fiscal Year 2004

The original budgeted net gain for the Federal Reserve Fund was \$308,505. The budget was later revised to a loss of \$292,823. The actual change in net assets was a decrease of \$2,554,455. This decrease was caused by interfund transfers of \$2,098,662, which consists primarily of account maintenance and default aversion fees owed to the Agency Operating Fund. A portion of the decrease also resulted from the difference between claims paid by the Enterprise and reinsurance it received on those claims.

Interfund Transfers – Fiscal Year 2005

Interfund transfers are made to reclassify revenues and expenditures that have been classified to a particular fund during the fiscal year and are now owed to another fund. In Fiscal Year 2004, the Enterprise made an interfund transfer from the Agency Operating Fund to the Federal Fund to satisfy its Federal Fund Reserve requirement. In addition, for a number of years, DE has required the Enterprise to pay itself the Account Maintenance Fee from the Federal Fund in the fourth quarter of the federal fiscal year. The Enterprise was required to do so this past fiscal year. The Enterprise also settled an audit finding from a prior Office of Inspector General (OIG) audit. At the time the interest associated with this finding was calculated by OIG to be \$451,824. The Enterprise appealed and subsequently prevailed in its appeal and reduced the interest cost to \$244,249.

The Enterprise made the following transfers during Fiscal Year 2005:

Transfers from Federal Fund to Agency Operating Fund:	
Account Maintenance Fee Shortfall	\$1,226,276
Transfers from Agency Operating Fund to Federal Fund:	
DE Audit Finding	<u>\$ (244,249)</u>
Net Transfers from the Federal Fund to the Agency Operating Fund	<u>\$ 982,027</u>

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Interfund Transfers – Fiscal Year 2004

Interfund transfers are made to reclassify revenues and expenditures that have been classified to a particular fund during the fiscal year and are now owed to another fund. The Enterprise made an interfund transfer from the Agency Operating Fund to the Federal Fund to satisfy its Federal Fund Reserve requirement. In addition, for a number of years, DE has required the Enterprise to pay itself the Account Maintenance Fee from the Federal Fund in the fourth quarter of the federal fiscal year. The Enterprise was required to do so this past fiscal year.

The Enterprise made the following transfers during fiscal year 2004:

Transfers from Federal Fund to Agency Operating Fund:	
Default Aversion Fee	\$ 3,536,751
Account Maintenance Fee Shortfall	521,328
Default Aversion Settlement due DE	(257,231)
Transfers from Agency Operating Fund to Federal Fund:	
Transfer to Federal Reserve Fund for Reserve Requirement	(1,700,000)
DE Audit Finding (Overpayment of Account Maintenance Fee)	<u>(2,186)</u>
Net Transfers from the federal Fund to the Agency Operating Fund	<u>\$ 2,098,662</u>

Capital Assets – Fiscal Year 2005

The Enterprise spent \$1,087,860 for purchasing, installation, and upgrade of the phone equipment during Fiscal Year 2005. The Enterprise also capitalized \$454,107 in software development costs. These transactions were the only significant changes in capital outlay items in Fiscal Year 2005.

Capital Assets – Fiscal Year 2004

The Enterprise spent \$407,962 for a new mainframe and imaging equipment during Fiscal Year 2004. This transaction was the only significant change in capital outlay items in Fiscal Year 2004.

Economic Facts and Conditions for the Future

Effective July 1, 2004, the U.S. Department of Education granted the Enterprise a three-year contract with the DE known as a Voluntary Flexible Agreement (VFA). Provisions within the contract entitle either the DE or the Enterprise to rescind the agreement with 90 days notice.

The VFA has a number of provisions that impact the revenue of the Enterprise, many of which have been reviewed in the revenue sections of this Management Discussion and Analysis.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

The Enterprise was notified by DE that it would need to renegotiate the terms of its VFA in March 2005 along with the four other agencies that are operating under separate VFAs. Agencies with applications pending also were notified by DE that it would not consider applications where the department paid 100% reimbursement to an agency for its claims. Similarly, agencies were informed that despite past waivers, no agency would be exempt from maintaining a .25% reserve ratio in its federal fund, waivers that had allowed agencies to waive guarantee fees on loans originated by new borrowers.

The Enterprise submitted changes to its current VFA to DE in May 2005. Action on the revised VFA proposal is pending at this submission and the Enterprise continues in the interim to operate under the terms of the original VFA agreement.

Also pending is the Reauthorization of the Higher Education Act in Congress. Although the programs were extended through December 2005 by Congress, action on many student loan program changes was pending in both the Senate and House at the writing of this analysis.

The Enterprise began assessing a 1% insurance premium for loans disbursed after July 1, 2004, a factor that increased the health of the fund during Fiscal Year 2005. Pending congressional action to require all guarantee agencies to collect the guarantee fee, the Enterprise's Advisory Board approved the suspension of the fee for the 2005-2006 academic year for loans guaranteed on or after July 1, 2005. The Board motion included a recommendation to revisit the fee issue after Congressional action or in the third quarter of Fiscal Year 2006 if no legislative action has mandated charging the fee.

Effective in Fiscal Year 2005, the Enterprise has a statutorily created Board of Directors whose members are appointed by the Governor to advise it on financial matters and policy issues. The Board chairman named a three-member audit committee. The Board reviews quarterly financials, contracts exceeding \$250,000, the Enterprise budget, Enterprise audits and financial operating procedures.

Financial Contact

If you have any questions about this report, please contact:

College Access Network
999 18th Street, Suite 425
Denver, CO 80202
Attention: Director of Accounting and Human Resources

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
COMBINED STATEMENTS OF NET ASSETS
June 30, 2005 and 2004**

ASSETS

	<u>2005</u>	<u>2004</u>
CURRENT ASSETS		
Cash and pooled cash investments	\$ 31,690,010	\$ 21,769,042
Due from other governments		
Federal account maintenance fee	553,457	676,034
Federal loan processing and issuance fee	66,852	479,701
Other federal receivables	1,572,610	89,103
Other receivables, net	1,059,935	837,027
Supplies inventory	68,555	75,592
Prepaid expenses	61,507	163,535
Total current assets	<u>35,072,926</u>	<u>24,090,034</u>
RESTRICTED ASSETS		
Restricted cash and pooled cash investments	13,019,526	4,310,075
Federal reinsurance receivable	14,682	3,372,364
Other receivables, net	7,749	7,749
Total restricted assets	<u>13,041,957</u>	<u>7,690,188</u>
CAPITAL ASSETS		
Office furniture and equipment	2,038,877	951,017
Computer hardware and software	3,444,200	2,990,093
Property held under capital lease	329,144	987,884
Leasehold improvements	97,946	97,946
	<u>5,910,167</u>	<u>5,026,940</u>
Less accumulated depreciation	<u>(4,666,234)</u>	<u>(4,294,438)</u>
Capital assets, net	<u>1,243,933</u>	<u>732,502</u>
 TOTAL ASSETS	 <u><u>\$ 49,358,816</u></u>	 <u><u>\$ 32,512,724</u></u>

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
COMBINED STATEMENTS OF NET ASSETS
June 30, 2005 and 2004**

LIABILITIES AND NET ASSETS

	2005	2004
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	\$ 1,041,172	\$ 1,668,964
Payable to the U.S. Department of Education:		
Loan collections and other liabilities due to federal government	1,078,204	1,078,204
Accrued compensated absences	419,969	-
Other current liabilities		
Current portion of obligation under capital lease	111,325	131,859
Other	760,999	291,077
Interfund payable - other agencies	11,169	347,841
Deferred revenue	-	122,555
Total current liabilities	3,422,838	3,640,500
LIABILITIES PAYABLE FROM RESTRICTED ASSETS		
Recall reserves due to DE	3,063,093	3,063,093
Accounts payable and accrued liabilities	-	9,016
Loan collections and other liabilities due to federal government	1,158,900	1,469,491
Total liabilities payable from restricted assets	4,221,993	4,541,600
NONCURRENT LIABILITIES		
Accrued compensated absences	218,388	872,534
Obligation under capital leases, net of current portion	102,867	214,192
Total noncurrent liabilities	321,255	1,086,726
Total liabilities	7,966,086	9,268,826
NET ASSETS		
Invested in capital assets, net of related debt	1,029,741	386,451
Restricted	8,819,964	3,148,588
Unrestricted	31,543,025	19,708,859
Total net assets	41,392,730	23,243,898
TOTAL LIABILITIES AND NET ASSETS	\$ 49,358,816	\$ 32,512,724

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

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
COMBINED STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN NET ASSETS
For the Years Ended June 30, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
OPERATING REVENUES		
Federal grants and contracts		
Division's share of collections on loans and bankruptcies	\$ 19,180,313	\$ 11,106,343
Federal account maintenance fee	4,847,234	2,338,103
Federal loan processing and issuance fee	1,507,495	2,447,130
Federal reinsurance	65,263,224	50,492,123
Charges for goods and services		
Contractual service fees	5,667,484	5,217,078
Guarantee fees	4,131,024	168,808
Interest on purchased loans and other	259,891	414,475
Gifts and donations	5,000	13,800
Other revenue	1,289,188	23,569
	<u>102,150,853</u>	<u>72,221,429</u>
OPERATING EXPENSES		
Guarantee claims paid to lending institutions	64,740,853	51,760,586
Salaries and fringe benefits	11,855,407	12,722,611
Operating and travel		
Contracted collection costs	1,470,786	2,548,645
Other operating and travel	6,342,322	5,376,354
Depreciation	371,796	414,010
	<u>84,781,164</u>	<u>72,822,206</u>
OPERATING INCOME (LOSS)	<u>17,369,689</u>	<u>(600,777)</u>
NONOPERATING REVENUES (EXPENSES)		
Earnings on temporary cash investments	881,338	73,630
Loss on sale of equipment	-	(49,944)
	<u>18,251,027</u>	<u>(577,091)</u>
Income (loss) before operating transfer		
Operating transfers to other agencies	(102,195)	(147,442)
CHANGE IN NET ASSETS	<u>18,148,832</u>	<u>(724,533)</u>
NET ASSETS, BEGINNING OF YEAR	<u>23,243,898</u>	<u>23,968,431</u>
NET ASSETS, END OF YEAR	<u>\$ 41,392,730</u>	<u>\$ 23,243,898</u>

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

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
COMBINED STATEMENTS OF CASH FLOWS
For the Years Ended June 30, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from:		
Fees for service	\$ 9,453,045	\$ 5,456,930
Federal grants and contracts	92,897,276	68,965,119
Interest on purchased loans and other	259,891	414,475
Gifts and donations	5,000	13,800
Other sources	1,289,188	23,569
	<u>103,904,400</u>	<u>74,873,893</u>
Cash disbursed for:		
Guarantee claims paid to lending institutions	(64,749,869)	(51,758,873)
Employees	(12,089,584)	(12,724,491)
Suppliers	(6,727,799)	(5,504,005)
Contracted collection costs	(1,470,786)	(2,548,645)
	<u>(85,038,038)</u>	<u>(72,536,014)</u>
Net cash provided by operating activities	<u>18,866,362</u>	<u>2,337,879</u>
CASH FLOW FROM NONCAPITAL FINANCING ACTIVITIES		
Transfers - out	(102,195)	(147,442)
Net cash used in noncapital activities	<u>(102,195)</u>	<u>(147,442)</u>
CASH FLOW FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from capital leases	-	329,144
Acquisition of capital assets	(883,227)	(578,545)
Capital lease payments	(131,859)	(184,557)
Net cash used in capital and related financing activities	<u>(1,015,086)</u>	<u>(433,958)</u>
CASH FLOW FROM INVESTING ACTIVITIES		
Earnings on temporary cash investments	881,338	73,630
NET INCREASE IN CASH AND TEMPORARY CASH INVESTMENTS		
	18,630,419	1,830,109
CASH AND TEMPORARY CASH INVESTMENTS, BEGINNING OF YEAR		
	<u>26,079,117</u>	<u>24,249,008</u>
CASH AND TEMPORARY CASH INVESTMENTS, END OF YEAR		
	<u>\$ 44,709,536</u>	<u>\$ 26,079,117</u>

	<u>2005</u>	<u>2004</u>
RECONCILIATION OF NET OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Net operating income (loss)	\$ 17,369,689	\$ (600,777)
Adjustments to reconcile net operating income (loss) to net cash provided by operating activities:		
Depreciation	371,796	414,010
Effects of changes in net assets and liabilities:		
Receivables	2,186,693	2,707,861
Supplies inventory	7,037	24,569
Prepaid expenses	102,028	176,849
Accounts payable and accrued liabilities	(636,808)	(360,822)
Other current liabilities	469,922	53,850
Loan collections and other liabilities due to federal government	(310,591)	(177,952)
Accrued compensated absences	(234,177)	(1,880)
Interfund payable other agencies	(336,672)	(20,384)
Deferred revenue	(122,555)	122,555
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 18,866,362</u>	<u>\$ 2,337,879</u>

During the year ended June 30, 2004, there was a non-cash reduction to a capital lease obligation in the amount of \$25,271.

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

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

College Access Network (the “Enterprise”) is a self-supporting business of the State of Colorado. It was established as an entity of the Colorado Department of Higher Education pursuant to *Title 23, Article 3.1, Part 1, Colorado Revised Statutes, 1973*, as amended, and was created July 1, 1979. It was formerly called the Colorado Student Loan Program until July 1, 2004. The Enterprise administers the Federal Family Education Loan Program (“FFEL”), which consists of Stafford, Parent Loans for Undergraduate Students (“PLUS”), Supplemental Loans for Students (“SLS”), and Consolidation Loans Programs. The Enterprise guarantees loans by lending institutions to students attending post-secondary schools, in compliance with operating agreements (the “Agreements”) with the U.S. Department of Education (the “DE”), pursuant to *Section 428 of the Higher Education Act of 1965* (the “Act”). In addition, the Enterprise must comply with provisions of the *1998 Reauthorization of Higher Education Act*.

The financial statements of the Enterprise include all integral parts of its operations. There are no other legally separate entities or organizations for which the officers of the Enterprise are financially accountable.

During the 2004, legislative session, House Bill 04-1350 allowed the Enterprise, formally the Colorado Student Loan Program, to change its name to Colorado College Access Network, d.b.a. College Access Network, effective July 1, 2004. The name change positions College Access Network to capitalize on new markets internal and external to Colorado.

The Enterprise entered into a new funding agreement with the DE effective July 1, 2004. The Voluntary Flexible Agreement (“VFA”) allowed the Enterprise to receive compensation performance incentives based on its success at preventing student loan defaults. Instead of receiving a majority of its fees for collecting on defaulted loans, fees are also earned by implementing strategies to prevent defaults. The Enterprise is required to prove to the DE that the VFA benefits student borrowers, is cost effective to Federal taxpayers, and saves the U.S. Department of Education resources.

The Enterprise was notified by DE in March 2005 that it would need to renegotiate the terms of its original VFA. Agencies, including the Enterprise with applications pending, also were notified by DE that it would not consider applications where the department paid 100% reimbursement to an agency for its claims. Similarly, agencies were informed that despite past waivers, no agency would be exempt from maintaining a .25% reserve ratio in its Federal Fund (see Note 6).

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The Enterprise submitted changes to its current VFA to DE in May 2005. Action on the revised VFA proposal is currently pending. The Enterprise continues to operate under the terms of the original VFA agreement that was effective July 1, 2004.

Basis of Accounting and Presentation

The Enterprise uses the accrual basis of accounting to summarize its activities. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when an obligation is incurred.

The financial statements of the Enterprise have been prepared in accordance with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB), Financial Accounting Standards Board (FASB) and other applicable guidelines or pronouncements. The Enterprise uses self-balancing accounting funds to record its financial accounting transactions. However, GASB reporting guidelines require the Enterprise to report its assets, liabilities, net assets, revenues, expenses, changes in net assets and cash flows from an entity-wide perspective, rather than by accounting fund. The guidelines further require that intra-fund accounting transactions be eliminated. The Enterprise has the option to apply all FASB pronouncements issued after November 30, 1989, unless those pronouncements conflict with GASB standards. The Enterprise has elected not to apply FASB pronouncements after the applicable date.

Use of Estimates in Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 periods. Actual results could differ from those estimates.

Cash and Pooled Cash Investments

Cash and pooled cash investments consist of cash on deposit with the State Treasurer, cash on hand, and cash on deposit with financial institutions. For purposes of the statement of cash flows, cash and temporary cash investments are defined as instruments with maturities of three months

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

or less at date of acquisition, and pooled cash held by the Colorado State Treasurer. Cash and pooled cash investments that are restricted in nature are distinguished as such in the financial statements.

Receivables

Amounts owed from the DE are reported as due from other governments. Loans purchased from lenders are reported as other receivables. Other receivables are reported net of the estimated allowance for uncollectible accounts. Receivables that are restricted in nature are reported as such in the financials.

Supplies Inventory

Supply commodities are carried in an inventory account at cost, which approximates market and are subsequently charged to expense when consumed.

Capital Assets

Depreciable capital assets are recorded at cost on the date of acquisition, or fair market value on the date of donation, in the case of gifts. The Enterprise's capitalization policy is \$5,000 or more, per individual piece of equipment, with an estimated useful life of greater than one year. Renovation cost to leased property in excess of \$5,000 is also capitalized. Cost to renovated leased property is reported as leasehold improvements.

Depreciation is charged using a straight-line method over the estimated useful lives of the assets. Generally, furniture, equipment, and software are depreciated over 3 to 10 years. Leasehold improvements are depreciated over the lesser of 5 years, or the life of the lease in which the renovation was made.

Liabilities

Amounts due to suppliers and others within one year are reported as current liabilities. Amounts owed after one year are reported as noncurrent liabilities. Noncurrent liabilities include capital lease obligations and compensated absences. The principal amount due in the next accounting period for capital leases is reported as a current liability. The balance of this obligation is shown as a noncurrent liability. Liabilities restricted in nature are distinguished as such in the financial statements.

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Compensated Absences

Employees of the Enterprise are entitled to paid vacations, sick days, and personal days off, depending on job classification, length of service, and other factors. The Enterprise has recorded the amount of compensation for future absences as an accrued liability in the accompanying financial statements. The estimated liability is based on hours earned up to assigned maximums. Unused vacation days are paid to employees leaving the Enterprise. One-fourth of unused sick days may be paid to employees upon retirement or death.

Deferred Revenues

Deferred revenues represent amounts received prior to the end of the fiscal year, but the revenue will not be reported as earned until the subsequent accounting period.

Loan Processing and Issuance Fee

Under the *1998 Reauthorization of the Higher Education Act*, the U.S. Department of Education pays the Enterprise a quarterly loan processing and issuance fee of .40% on net loans guaranteed by the Enterprise, effective October 1, 2003. Prior to October 1, 2003, the fee was .65%.

Account Maintenance Fee

Under the *1998 Reauthorization of the Higher Education Act*, the U.S. Department of Education pays the Enterprise a quarterly account maintenance fee of .10% of the original principal amount of outstanding loans.

Net Assets

The net assets of the Enterprise are classified as follows:

Invested in capital assets, net of related debt: This amount represents the Enterprise's total investment in capital assets, net outstanding debt obligations related to those capital assets. Debt incurred but not yet expended for capital assets is not included as a component of this category.

Restricted net assets: Restricted net assets represent resources in which the Enterprise is contractually obligated to spend or reserve in accordance with restrictions imposed by external parties.

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Unrestricted net assets: Unrestricted net assets represent resources derived from services provided to borrowers, lenders, and collection activities. These resources are used to pay the operating cost of the Enterprise. Although they are reported as unrestricted, the officers of the Enterprise internally designated these funds.

Classification of Revenues and Expenses

The Enterprise has classified its revenues and expenses as either operating or nonoperating. Operating revenues and expenses generally result from providing services or incurring expenses in connection with the Enterprise's principal activities. Nonoperating revenues and expenses include transactions such as interest revenue earned on deposits and interest expense on capital debt.

Loan Defaults

Student Loans guaranteed by the Enterprise that subsequently fall into default status are purchased by the Enterprise. This occurs after a claim is paid to the lending institution. Once a claim is paid to a lender, the Enterprise becomes the holder of the loan and seeks to collect on the loan. Although claim payments are made on defaults, deaths, disabilities and bankruptcies, only loans in default and loans included under Chapter 7 and Chapter 13 bankruptcies are collectible by The Enterprise. It is the Enterprise's policy under the Voluntary Flexible Agreement to retain from 17% to 25% of subsequent loan collections to cover the costs associated with collection efforts. The balance (83% to 75%) is remitted to the U.S. Department of Education.

Defaulted Loans

The Enterprise subrogates or assigns loans that meet certain criteria to the U.S. Department of Education. In addition, the Enterprise uses the U.S. Treasurer's Offset Program to pursue collections of defaulted loans. Under this program, Federal Income Tax refunds are applied or offset against student loans in default.

Federal Reinsurance

Under the agreement with the U.S. Department of Education ("DE"), in accordance with Section 428 of the Act, the Enterprise is reimbursed by the DE for 100% of claims under the Voluntary Flexible Agreement. Federal reinsurance on defaulted loans is paid according to the following schedule:

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

<u>Rate of Annual Losses (Defaults)</u>	<u>Federal Reinsurance on Loans Made Prior to October 1, 1993</u>	<u>Federal Reinsurance on Loans Made October 1, 1993 Through September 30, 1998</u>	<u>Federal Reinsurance on Loans Made October 1, 1998 Through June 30, 2004 and after July 1, 2004 (VFA)</u>
0% to 5%	100%	98%	95%
More than 5% but less than or equal to 9%	90%	88%	85%
Over 9%	80%	78%	75%

The rate of annual losses (defaults) for purposes of the application for Federal reinsurance is a result of the year-to-date incurred losses divided by the original amount of guaranteed loans in repayment status at the beginning of the year. The annual rate of default for the Federal years ended September 30, 2005 and September 30, 2004 did not exceed 5% in either period.

Budgets and Budgetary Accounting

The Enterprise prepares an annual operating budget. By statute, the Enterprise is continuously funded through user service charges. Therefore, the budget is not legislatively adopted and a Budget to Actual Statement of Revenues and Expenses is not a required part of these financial statements. However, the operating budget and revisions thereto are reviewed by members of the Governing Board, and approved by the Colorado Commission on Higher Education.

In summary, the total estimated revenues of the Enterprise were \$92.3 million as compared with actual revenues of \$103.0 million for the fiscal year ended June 30, 2005. The total budgeted expenses for the fiscal year ended June 30, 2005 were \$92.3 million compared to actual expenses of \$84.7 million.

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 2 – CASH AND INVESTMENTS

The Enterprise deposits cash with the Colorado State Treasurer as required by the Colorado Revised Statutes (CRS). The State Treasurer pools these deposits and invests them in securities approved by CRS 24-75-601.1. The Enterprise reports its share of the Treasurer’s unrealized gains and losses based on its participation in the State Treasurer’s pooled cash investments. All of the investments are reported at fair value, which is determined based on quoted market prices at June 30, 2005 and 2004. The State Treasurer will not invest pooled resources in external investments, and there is no assignment of income related to participation in the pool. Detailed information on the State Treasurer’s pooled cash and investments is available from that office. It may also be obtained in the State of Colorado’s Comprehensive Annual Financial Report.

Including restricted amounts, the Enterprise had \$43,773,714 and \$25,239,975 on deposit with the State Treasurer at June 30, 2005 and 2004, respectively. Cash on hand, including petty cash funds at June 30, 2005 and 2004, was \$12,570 and \$3,876, respectively.

At June 30, 2005 and 2004, the Enterprise had cash deposited in banks with a book or carrying value of \$923,252 and \$835,266 respectively. However, at June 30, 2005 and 2004, the bank balances of this cash is \$2,504,691 and \$1,820,718 respectively. These amounts are federally insured deposits, or deposits fully collateralized with securities held by the State, or the banks’ trust department or its agent, in the name of the Enterprise. The Enterprise had no uninsured or uncollateralized deposits in the bank. The following summarizes cash and investments:

	<u>2005</u>	<u>2004</u>
Cash on deposit with State Treasurer	\$ 43,893,970	\$ 25,084,780
State Treasurer pooled cash investments – unrealized gain/(loss)	(120,256)	155,195
Cash on hand in transit to bank	12,370	3,676
Petty cash	200	200
Cash on deposit with banks	<u>923,252</u>	<u>835,266</u>
Total	<u>\$ 44,709,536</u>	<u>\$ 26,079,117</u>

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 2 – CASH AND INVESTMENTS (CONTINUED)

Cash and temporary cash investments are presented in the accompanying statement of net assets as follows:

	<u>2005</u>	<u>2004</u>
Cash and pooled cash investments	\$ 31,690,010	\$ 21,769,042
Restricted cash and pooled cash investments	<u>13,019,526</u>	<u>4,310,075</u>
Total	<u>\$ 44,709,536</u>	<u>\$ 26,079,117</u>

The Colorado Public Deposit Protection Act (PDPA) requires that all units of local government deposit cash in eligible public depositories. Eligibility is determined by state regulations. Amounts on deposit in excess of federal insurance levels must be collateralized by eligible collateral determined by the PDPA. The institution is allowed to create a single collateral pool for all public funds held. The pool is maintained by another institution or held in trust for all the uninsured public deposits as a group. The fair value of the collateral must be at least equal to 102% of the uninsured deposits.

NOTE 3 – OTHER RECEIVABLES – NET

Other receivables – net, includes purchased student loans. Purchased student loans represent loan balances not reinsured by the DE that are the property of the Enterprise. Since the loans are purchased by the Enterprise and become an asset of the Enterprise, they do not fall within the scope of reinsurance from the DE. An allowance for the uncollectible loans equal to 92% of the purchased loan receivable has been recorded at June 30, 2005 and 2004. These rates are based on historical collection activity for purchased student loans. The net purchased loans receivable included in Other receivables – net at June 30, 2005 and 2004 is \$99,058 and \$88,474, respectively. Other receivables included in Other receivables – net include billed receivables to certain financial institutions for loan servicing activities.

NOTE 4 – ACCRUED PAYROLL

Prior to Fiscal Year 2003, salaries and wages earned through the end of the fiscal year were paid to employees on June 30. Under Senate Bill 03-197, salaries and wages for June 2005 and 2004 that were normally paid at the end of the month were paid at the beginning of July. This created an accrued liability at June 30, 2005 and 2004 of \$801,338 and \$938,747, respectively, for incurred but unpaid salaries and wages which is included in accounts payable and accrued liabilities on the accompanying combined statements of net assets.

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 4 – CAPITAL ASSETS

A summary of changes in capital assets is as follows for the years ended June 30, 2005 and 2004:

	Balance July 1, 2004	Additions	Transfers	Balance June 30, 2005
Office furniture and equipment	\$ 951,017	\$ 429,120	\$ 658,740	\$ 2,038,877
Computer hardware	2,990,093	454,107	-	3,444,200
Property held under capital lease	987,884	-	(658,740)	329,144
Leasehold improvements	97,946	-	-	97,946
Total	5,026,940	883,227	-	5,910,167
Less accumulated depreciation	(4,294,438)	(371,796)	-	(4,666,234)
Capital assets, net	\$ 732,502	\$ 511,431	\$ -	\$ 1,243,933

	Balance July 1, 2003	Additions	Deletions	Balance June 30, 2004
Office furniture and equipment	\$ 907,098	\$ 43,919	\$ -	\$ 951,017
Computer hardware and software	2,784,610	205,483	-	2,990,093
Property held under capital lease	829,472	329,144	(170,732)	987,884
Leasehold improvements	97,946	-	-	97,946
Total	4,619,126	578,546	(170,732)	5,026,940
Less accumulated depreciation	(3,975,944)	(414,010)	95,516	(4,294,438)
Capital assets, net	\$ 643,182	\$ 164,536	\$ (75,216)	\$ 732,502

There were no capital asset deletions for the year ended June 30, 2005.

NOTE 5 – LEASES

The Enterprise has capital lease agreements for equipment with an original cost of \$329,144 and \$987,884 at June 30, 2005 and 2004, respectively. For these same periods, accumulated depreciation of \$74,125 and \$623,934, respectively is recorded for these items. Existing capital leases at June 30, 2005 expire in Fiscal Year 2007.

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 5 – LEASES (CONTINUED)

The Enterprise also leases its office space and various other office equipment under operating leases that expire in Fiscal Year 2006.

Future minimum rentals under capital leases and noncancellable operating leases are as follows:

<u>Year Ending June 30,</u>	<u>Capital Leases</u>	<u>Operating Leases</u>
2006	\$ 129,948	\$ 679,410
2007	108,289	-
Total	238,237	<u>\$ 679,410</u>
Less interest	(24,045)	
	214,192	
Less current portion	(111,325)	
Long-term portion	<u>\$ 102,867</u>	

Total rent expense for the years ended June 30, 2005 and 2004 was \$713,820 and \$703,735, respectively.

During the Fiscal Years ended June 30, 2005 and 2004, the following changes occurred with long-term debt.

	<u>Balance July 1, 2004</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance June 30, 2005</u>	<u>Amounts Due Within One Year</u>
Capital lease obligations	\$ 346,051	\$ -	\$ (131,859)	\$ 214,192	\$ 111,325
Accrued compensated Absences	<u>872,534</u>	<u>211,232</u>	<u>(445,409)</u>	<u>638,357</u>	<u>419,969</u>
Total	<u>\$ 1,218,585</u>	<u>\$ 211,232</u>	<u>\$ (577,268)</u>	<u>\$ 852,549</u>	<u>\$ 531,294</u>

	<u>Balance July 1, 2003</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance June 30, 2004</u>	<u>Amounts Due Within One Year</u>
Capital lease obligations	\$ 226,735	\$ 329,144	\$ (209,828)	\$ 346,051	\$ 131,859
Accrued compensated absences	<u>874,414</u>	<u>117,007</u>	<u>(118,887)</u>	<u>872,534</u>	<u>-</u>
Total	<u>\$ 1,101,149</u>	<u>\$ 446,151</u>	<u>\$ (328,715)</u>	<u>\$ 1,218,585</u>	<u>\$ 131,859</u>

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 5 – LEASES (CONTINUED)

The Enterprise had determined that accrued compensation absences due within one year at June 30, 2004 were not considered material to the financial statements.

NOTE 6 – COMMITMENTS

Statutory Guarantee Fund Requirements

The Enterprise was required by Federal and State statute to maintain a minimum reserve of .25% of the unpaid balance of outstanding loans. In conjunction with the Enterprise's funding agreement (VFA) with DE effective July 1, 2004, the reserve requirement was initially waived. However, as discussed in Note 1, the Enterprise was notified by DE in March 2005 that it would need to renegotiate the terms of the original VFA. Agencies including the Enterprise were informed that waivers would not be granted exemption from maintaining a .25% reserve ratio in its Federal Fund. The Enterprise believes it will continue to meet the reserve requirement. DE assesses the required reserve amount at September 30 of each year.

The required Federal reserve balance at June 30, 2005 and 2004 based on the outstanding loan balances is \$16,606,396 and \$9,081,596, respectively. The Federal reserve balance consisting of restricted current assets minus restricted current liabilities at June 30, 2005 and 2004 is \$11,883,057 and \$6,211,681, respectively. Noncurrent liabilities including recall reserves payable to DE are allowed to be excluded from the reserve requirement calculation.

NOTE 7 – CONTINGENCIES

Loan Guarantees

The outstanding principal balances of student loans guaranteed by the Enterprise through June 30, 2005 is approximately \$6.6 billion. As disclosed in Note 1, the Federal government reinsures new loans guaranteed at a Voluntary Flexible Agreement minimum rate of 100% until the Enterprise's rate of annual losses (defaults) exceeds 5%. If the Enterprise exceeds the 5% threshold (the trigger rate), it may be liable for up to a maximum 25% of the outstanding balance of loans in repayment at the beginning of each year. The Enterprise did not exceed its trigger rate for the period ended June 30, 2005, or prior years.

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 8 – EMPLOYEE PENSION PLAN

Plan Description

Virtually all of the Enterprise's employees participate in a Defined Benefit Pension Plan. The purpose of the Defined Benefit Pension Plan is to provide income to members and their families at retirement or in case of death or disability. This Plan is a cost-sharing multiple-employer deferred benefit plan administered by the Public Employees Retirement Association (PERA). PERA was established by State statute in 1931. Responsibility for the organization and administration of the Plan is placed with the Board of Trustees of PERA. Changes to the Plan require legislation by the General Assembly. The State Plan, as well as the other division's plans, are included in PERA's financial statements which may be obtained by writing PERA at 1300 Logan Street, Denver, Colorado 80203, by calling PERA at 303-832-9550 or 1-800-729-PERA (7372), or by visiting www.copera.org.

Plan members vest after five years of service and most are eligible for retirement benefits at age 50 with 30 years of service, age 60 with 20 years of service, or at age 65 with 5 years of service. Members are also eligible for retirement benefits without a reduction for early retirement if they are at least 55 and have a minimum of 5 years of service credit and their age plus years of service equals 80 or more. State troopers and judges comprise a small percentage of Plan members but have higher contribution rates and are eligible for retirement benefits at different ages and years of service. Monthly benefits are calculated as a percentage of highest average salary (HAS). HAS is one-twelfth of the average of the highest salaries on which contributions were paid, associated with three periods of 12 consecutive months of service credit.

Members disabled, who have five or more years of service credit, six months of which has been earned since the most recent period of membership, may receive retirement benefits if determined to be permanently disabled. If a member dies before retirement, their spouse or their eligible children under the age of 18 (23 if a full time student) are entitled to monthly benefit payments. If there is no eligible spouse, financially dependent parents will receive a survivor's benefit.

Funding Policy

Most employees contribute 8.0 percent (10.0 percent for State troopers) of their gross covered wages to an individual account in the retirement program. During Fiscal Year 2004 – 2005, the State contributed 10.15 percent (12.85 percent for State troopers and 13.66 percent for the Judicial Branch) of the employee's gross covered wages. Effective January 1, 2004, 1.02% of the total contribution was allocated to the Health Care Trust Program (see Note 10).

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 8 – EMPLOYEE PENSION PLAN (CONTINUED)

Salary subject to PERA contribution is the gross earnings less any reduction in pay to offset employer contributions to the State sponsored IRC 125 Plan established under Section 125 of the Internal Revenue Code. The contribution requirements of Plan members and their employers are established, and may be amended, by the General Assembly.

The Enterprise's contributions to the retirement and health care programs for the Fiscal Years ending June 30, 2005, 2004, and 2003 were \$898,919, \$982,767, and \$962,226, respectively. These contributions met the funding requirements for each year.

NOTE 9 – VOLUNTARY TAX-DEFERRED RETIREMENT PLANS

PERA offers a voluntary 401k plan entirely separate from the defined benefit pension plan. The State offers a 457 deferred compensation plan and certain agencies and institutions of the State offer 403(b) or 401(a) plans. Members who contribute to any of these plans also receive the State match, when available.

In January 2001, the Matchmaker Program established a State match for PERA member's voluntary contributions to tax-deferred retirement plans. The PERA Board sets the level of the match annually based on actuarial funding of the defined benefit pension plan. The match is only available when the actuarial value of the defined benefit plan's assets is 110 percent of actuarial accrued plan liabilities. This condition was not met during Fiscal Year 2004-05.

NOTE 10 – POSTRETIREMENT HEALTH CARE AND LIFE INSURANCE BENEFITS

Health Care Program

PERACare (formerly known as the PERA Health Care Program) began covering benefit recipients and qualified dependents on July 1, 1986. This benefit was developed after legislation in 1985 established the program and the Health Care Trust Fund. Under this program, PERA subsidizes a portion of the monthly premium for health care coverage. The benefit recipient pays any remaining amount of that premium through an automatic deduction from the monthly retirement benefit. During Fiscal Year 2004-05, the premium subsidy was \$115 for those with 20 years of service credit (\$230 for members under age 65), and it was reduced by 5 percent for each year of service fewer than 20.

The Health Care Trust Fund is maintained by a contribution as discussed above in Note 8.

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

**NOTE 10 – POSTRETIREMENT HEALTH CARE AND LIFE INSURANCE BENEFITS
(CONTINUED)**

Monthly premium costs for participants depend on the health care plan selected, the number of persons being covered, Medicare eligibility, and the number of years of retiree service credit. PERA contracts with a major medical indemnity carrier to administer claims for self-insured plans and with health maintenance organizations to provide services within Colorado. As of December 31, 2004, there were 39,668 enrollees in the Plan.

Life Insurance Program

During Fiscal Year 2004-2005, PERA provided its members access to two group decreasing term life insurance plans offered by Prudential Insurance Company and Anthem Life. Effective April 1, 2005, PERA consolidated the two plans, and UnumProvident became the administrator. Members who transition to the new plan may continue coverage into retirement. Premiums are collected monthly by payroll deduction or other means.

NOTE 11 – LITIGATION

The Enterprise was involved in various legal proceedings primarily for personnel related actions. These matters were settled during the year ended June 30, 2005 with no material impact on the financial condition of the Enterprise.

NOTE 12 – FEDERAL LEGISLATIVE IMPACTS ON THE ENTERPRISE

Balanced Budget Act of 1997

As a result of the Balanced Budget Act of 1997, guarantee agencies were required to transfer approximately \$1 billion of guarantor reserves to the Federal Treasury in Federal Fiscal Year 2002. Beginning in Fiscal Year 1998, each guarantee agency was required to establish a restricted account in which each agency will be required make an annual transfer of funds. The principal amount in the restricted accounts will not be available for use; however, interest earnings will be utilized for default reduction activities. The Enterprise transferred \$23,268,032 million to its recall fund at June 30, 2002. In September 2002, the Division paid \$23,268,032 to DE for this recall.

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 12 – FEDERAL LEGISLATIVE IMPACTS ON THE ENTERPRISE (CONTINUED)

1998 Reauthorization of Higher Education Act

In October 1998, legislation was passed re-authorizing the Higher Education Act. One of the provisions of reauthorization requires the guarantee agencies to pay back reserves to the Federal Treasury of \$250 million by September 30, 2007. The Enterprise's share of this recall is \$4,641,050. The Enterprise paid DE \$1,577,957 in Fiscal Year 2003, and will pay DE \$1,531,547 in Fiscal Year 2007 and \$1,531,546 in Fiscal Year 2008. The combined recall reserve due in Fiscal Year 2007 and Fiscal Year 2008 is recorded as restricted liabilities.

The legislation also required the Enterprise to set up an Agency Operating Fund and a Federal Reserve/Escrow Fund. These accounting funds are maintained on the accounting system, and are combined for financial reporting purposes.

NOTE 13 – RISK MANAGEMENT

The State of Colorado currently self-insures its agencies, officials, and employees for the risks of losses to which they are exposed. That includes general liability, motor vehicle liability, worker's compensation, and medical claims. Property claims are not self-insured; rather the State has purchased insurance.

The Enterprise participates in the Risk Management Fund of the State of Colorado. Agency premiums are based on an assessment of risk exposure and historical experience. Liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities include an amount of claims that have been incurred but not reported. Because actual claims liabilities depend on such complex factors as inflation, changes in legal doctrines and damage awards, the process used in computing claims liability does not necessarily result in an exact amount. Claims liabilities are re-evaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and social factors.

There were no significant reductions or changes in insurance coverage from the prior year in any of the above mentioned risk management arrangements. Settlements did not exceed insurance coverage in any of the past three fiscal years.

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
June 30, 2005 and 2004**

NOTE 14 – TAX, SPENDING AND DEBT LIMITATIONS

Colorado voters passed an amendment to the State Constitution, Article X, Section 20, which has several limitations, including revenue raising, spending abilities, and other specific requirements of state and local governments. The amendment excludes from its provision Enterprise Operations. Enterprises are defined as government-owned businesses authorized to issue revenue bonds, which receive less than 10% of their annual revenue in grants from all state and local governments combined. The Enterprise qualifies as an Enterprise pursuant to *Title 23, Article 3.1, Part 103.5, Colorado Revised Statutes, 1998*, as amended.

NOTE 15 – SUBSEQUENT EVENT

On November 1, 2005, the Enterprise announced an agreement to expand its existing relationship with its current servicing vendor, Nelnet. Under this expanded agreement, Nelnet will operate all aspects of the loan and guarantee servicing operations for the agency. This represents the majority of the agency's business operations. In exchange for the right to provide these services, Nelnet paid the State of Colorado an upfront fee of \$41,200,000. This money has been deposited in the Enterprise's operating fund and will be used to expand an internal reserve fund and increase financial aid support for students.

The agreement requires that Nelnet be responsible for all operating expenses associated with this expanded servicing contract. This includes, but is not limited to, personnel, operating, rent, and other expenses normally associated with running a government agency. Nelnet will receive seventy percent of the agency's operating revenues under the expanded agreement to pay for these operating expenses. The Enterprise itself retains thirty percent of the revenues to pay for contract monitoring and related activities under the agreement.

The term of the contract is for ten years, cancelable after seven by the agency if revenues or expenses change, and can be renewed for a second ten year term if both parties agree.

This information is an integral part of the accompanying financial statements.

**Independent Auditor's 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**

Members of the Legislative Audit Committee:

We have audited the basic financial statements of the College Access Network, Department of Higher Education, State of Colorado (the "Enterprise") as of and for the year ended June 30, 2005, which collectively comprise the Enterprise's basic financial statements and have issued our report thereon dated September 2, 2005, except for Note 15 as to which the date is November 1, 2005. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Enterprise's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Enterprise's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in Finding and Recommendation No. 1 and No. 2 and relate to repurchase liabilities and collections on defaulted loans.

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 performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all

reportable conditions that are also considered to be material weaknesses. However, we believe none of the reportable conditions described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Enterprise's financial statements are free of material misstatement, we performed tests of its 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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the findings and recommendations.

This report is intended solely for the information and use of the Legislative Audit Committee 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 and its distribution is not limited.

Clifton Gunderson LLP

Denver, Colorado
September 2, 2005, except for Note 15
as to which the date is November 1, 2005

SUPPLEMENTAL INFORMATION

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
COMBINING SCHEDULES OF NET ASSETS
June 30, 2005
(With Comparative Totals for June 30, 2004)**

ASSETS

	Agency Operating and Loan Servicing Funds	Federal Reserve and Drawdown Funds	Totals	
			2005	2004
CURRENT ASSETS				
Cash and pooled cash investments	\$ 31,690,010	\$ -	\$ 31,690,010	\$ 21,769,042
Due from other governments				
Federal account maintenance fee	553,457	-	553,457	676,034
Federal loan processing and issuance fee	66,852	-	66,852	479,701
Other federal receivables	1,572,610	-	1,572,610	89,103
Other receivables, net	1,059,935	-	1,059,935	837,027
Due from other funds	-	-	-	-
Supplies inventory	68,555	-	68,555	75,592
Prepaid expenses	61,507	-	61,507	163,535
Total current assets	<u>35,072,926</u>	<u>-</u>	<u>35,072,926</u>	<u>24,090,034</u>
RESTRICTED ASSETS				
Restricted cash and pooled cash investments	-	13,019,526	13,019,526	4,310,075
Federal reinsurance receivable	-	14,682	14,682	3,372,364
Other receivables, net	-	7,749	7,749	7,749
Total restricted assets	<u>-</u>	<u>13,041,957</u>	<u>13,041,957</u>	<u>7,690,188</u>
CAPITAL ASSETS				
Office furniture and equipment	2,038,877	-	2,038,877	951,017
Computer hardware and software	3,444,200	-	3,444,200	2,990,093
Property held under capital lease	329,144	-	329,144	987,884
Leasehold improvements	97,946	-	97,946	97,946
	5,910,167	-	5,910,167	5,026,940
Less accumulated depreciation	<u>(4,666,234)</u>	<u>-</u>	<u>(4,666,234)</u>	<u>(4,294,438)</u>
Capital assets, net	<u>1,243,933</u>	<u>-</u>	<u>1,243,933</u>	<u>732,502</u>
TOTAL ASSETS	<u>\$ 36,316,859</u>	<u>\$ 13,041,957</u>	<u>\$ 49,358,816</u>	<u>\$ 32,512,724</u>

LIABILITIES AND NET ASSETS

	Agency Operating and Loan Servicing Funds	Federal Reserve and Drawdown Funds	Totals	
			2005	2004
CURRENT LIABILITIES				
Accounts payable and accrued liabilities	\$ 1,041,172	\$ -	\$ 1,041,172	\$ 1,668,964
Payable to the U.S. Department of Education:				
Loan collections and other liabilities due to federal government	1,078,204	-	1,078,204	1,078,204
Accrued compensated absences	419,969	-	419,969	-
Other current liabilities:				
Current portion of obligation under capital lease	111,325	-	111,325	131,859
Other	760,999	-	760,999	291,077
Interfund payable - other agencies	11,169	-	11,169	347,841
Deferred revenue	-	-	-	122,555
Total current liabilities	<u>3,422,838</u>	<u>-</u>	<u>3,422,838</u>	<u>3,640,500</u>
LIABILITIES PAYABLE FROM RESTRICTED ASSETS				
Recall reserves due to DE	-	3,063,093	3,063,093	3,063,093
Accounts payable and accrued liabilities	-	-	-	9,016
Loan collections and other liabilities due to federal government	-	1,158,900	1,158,900	1,469,491
Total liabilities payable from restricted assets	<u>-</u>	<u>4,221,993</u>	<u>4,221,993</u>	<u>4,541,600</u>
NONCURRENT LIABILITIES				
Accrued compensated absences	218,388	-	218,388	872,534
Obligation under capital leases, net of current portion	102,867	-	102,867	214,192
Total noncurrent liabilities	<u>321,255</u>	<u>-</u>	<u>321,255</u>	<u>1,086,726</u>
Total liabilities	<u>3,744,093</u>	<u>4,221,993</u>	<u>7,966,086</u>	<u>9,268,826</u>
NET ASSETS				
Invested in capital assets, net of related debt	1,029,741	-	1,029,741	386,451
Restricted	-	8,819,964	8,819,964	3,148,588
Unrestricted	31,543,025	-	31,543,025	19,708,859
Total net assets	<u>32,572,766</u>	<u>8,819,964</u>	<u>41,392,730</u>	<u>23,243,898</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 36,316,859</u>	<u>\$ 13,041,957</u>	<u>\$ 49,358,816</u>	<u>\$ 32,512,724</u>

See accompanying independent auditor's report.

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
COMBINING SCHEDULES OF REVENUES, EXPENSES, AND
CHANGES IN NET ASSETS
For the Year Ended June 30, 2005
(With Comparative Totals for the Year Ended June 30, 2004)**

	Agency Operating and Loan Servicing Funds	Federal Reserve and Drawdown Funds	Totals	
			2005	2004
OPERATING REVENUES				
Federal grants and contracts				
Division's share of collections on				
loans and bankruptcies	\$ 18,800,764	\$ 379,549	\$ 19,180,313	\$ 11,106,343
Federal account maintenance fee	4,847,234	-	4,847,234	2,338,103
Federal loan processing and issuance fee	1,507,495	-	1,507,495	2,447,130
Federal reinsurance	-	65,263,224	65,263,224	50,492,123
Charges for goods and services				
Contractual service fees	5,667,484	-	5,667,484	5,217,078
Guarantee fees	-	4,131,024	4,131,024	168,808
Interest on purchased loans and other	259,891	-	259,891	414,475
Gifts and donations	5,000	-	5,000	13,800
Other revenue	15,682	1,273,506	1,289,188	23,569
Total operating revenues	<u>31,103,550</u>	<u>71,047,303</u>	<u>102,150,853</u>	<u>72,221,429</u>
OPERATING EXPENSES				
Guarantee claims paid to lending institutions	-	64,740,853	64,740,853	51,760,586
Salaries and fringe benefits	11,855,407	-	11,855,407	12,722,611
Operating and travel				
Contracted collection costs	1,470,786	-	1,470,786	2,548,645
Other operating and travel	6,342,322	-	6,342,322	5,376,354
Depreciation	371,796	-	371,796	414,010
Total operating expenses	<u>20,040,311</u>	<u>64,740,853</u>	<u>84,781,164</u>	<u>72,822,206</u>
OPERATING INCOME (LOSS)	<u>11,063,239</u>	<u>6,306,450</u>	<u>17,369,689</u>	<u>(600,777)</u>
NONOPERATING REVENUES (EXPENSES)				
Earnings (loss) on temporary cash investments	534,385	346,953	881,338	73,630
Loss on sale of equipment	-	-	-	(49,944)
Income (loss) before operating transfers	<u>11,597,624</u>	<u>6,653,403</u>	<u>18,251,027</u>	<u>(577,091)</u>
Operating transfers to other agencies	(102,195)	-	(102,195)	(147,442)
Interfund transfers in/(out)	982,027	(982,027)	-	-
Total transfers	<u>879,832</u>	<u>(982,027)</u>	<u>(102,195)</u>	<u>(147,442)</u>
CHANGE IN NET ASSETS	<u>12,477,456</u>	<u>5,671,376</u>	<u>18,148,832</u>	<u>(724,533)</u>
NET ASSETS, BEGINNING OF YEAR	<u>20,095,310</u>	<u>3,148,588</u>	<u>23,243,898</u>	<u>23,968,431</u>
NET ASSETS, END OF YEAR	<u>\$ 32,572,766</u>	<u>\$ 8,819,964</u>	<u>\$ 41,392,730</u>	<u>\$ 23,243,898</u>

See accompanying independent auditor's report.

**COLLEGE ACCESS NETWORK
DEPARTMENT OF HIGHER EDUCATION
STATE OF COLORADO
COMBINING SCHEDULES OF CASH FLOWS
For the Year Ended June 30, 2005
(With Comparative Totals for the Year Ended June 30, 2004)**

	Agency Operating and Loan Servicing Funds	Federal Reserve and Drawdown Funds	Totals	
			2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES				
Cash received from:				
Fees for service	\$ 5,322,021	\$ 4,131,024	\$ 9,453,045	\$ 5,456,930
Federal grants and contracts	24,207,412	68,689,864	92,897,276	68,965,119
Interest on purchased loans and other	259,891	-	259,891	414,475
Gifts and donations	5,000	-	5,000	13,800
Other sources	15,682	1,273,506	1,289,188	23,569
	<u>29,810,006</u>	<u>74,094,394</u>	<u>103,904,400</u>	<u>74,873,893</u>
Cash disbursed for:				
Guarantee claims paid to lending institutions	-	(64,749,869)	(64,749,869)	(51,758,873)
Employees	(12,089,584)	-	(12,089,584)	(12,724,491)
Suppliers	(6,727,799)	-	(6,727,799)	(5,504,005)
Contracted collection costs	(1,470,786)	-	(1,470,786)	(2,548,645)
Recall reserves paid to DE	-	-	-	-
	<u>(20,288,169)</u>	<u>(64,749,869)</u>	<u>(85,038,038)</u>	<u>(72,536,014)</u>
Net cash provided by operating activities	<u>9,521,837</u>	<u>9,344,525</u>	<u>18,866,362</u>	<u>2,337,879</u>
CASH FLOW FROM NONCAPITAL ACTIVITIES				
Transfers - out	(102,195)	-	(102,195)	(147,442)
Net cash used in noncapital activities	<u>(102,195)</u>	<u>-</u>	<u>(102,195)</u>	<u>(147,442)</u>
INTERFUND TRANSFERS	982,027	(982,027)	-	-
CASH FLOW FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
Proceeds from capital leases	-	-	-	329,144
Acquisition of capital assets	(883,227)	-	(883,227)	(578,545)
Capital lease payments	(131,859)	-	(131,859)	(184,557)
Net cash used in capital and related financing activities	<u>(1,015,086)</u>	<u>-</u>	<u>(1,015,086)</u>	<u>(433,958)</u>
CASH FLOW FROM INVESTING ACTIVITIES				
Interest on temporary cash investments	534,385	346,953	881,338	73,630
NET INCREASE IN CASH AND TEMPORARY CASH INVESTMENTS	9,920,968	8,709,451	18,630,419	1,830,109
CASH AND TEMPORARY CASH INVESTMENTS, BEGINNING OF YEAR	<u>21,769,042</u>	<u>4,310,075</u>	<u>26,079,117</u>	<u>24,249,008</u>
CASH AND TEMPORARY CASH INVESTMENTS, END OF YEAR	<u>\$ 31,690,010</u>	<u>\$ 13,019,526</u>	<u>\$ 44,709,536</u>	<u>\$ 26,079,117</u>

	Agency Operating and Loan Servicing Funds	Federal Reserve and Drawdown Funds	Totals	
			2005	2004
RECONCILIATION OF NET OPERATING INCOME (LOSS)				
TO NET CASH PROVIDED BY IN OPERATING ACTIVITIES				
Net operating income (loss)	\$ 11,063,239	\$ 6,306,450	\$ 17,369,689	\$ (600,777)
Adjustments to reconcile net operating income (loss)				
to net cash provided by operating activities:				
Depreciation	371,796	-	371,796	414,010
Effects of changes in net assets and liabilities:				
Receivables	(1,170,989)	3,357,682	2,186,693	2,707,861
Supplies inventory	7,037	-	7,037	24,569
Prepaid expenses	102,028	-	102,028	176,849
Accounts payable and accrued liabilities	(627,792)	(9,016)	(636,808)	(360,822)
Other current liabilities	469,922	-	469,922	53,850
Loan collections and other liabilities				
due to federal government	-	(310,591)	(310,591)	(177,952)
Accrued compensated absences	(234,177)	-	(234,177)	(1,880)
Interfund payable other agencies	(336,672)	-	(336,672)	(20,384)
Deferred revenue	(122,555)	-	(122,555)	122,555
NET CASH PROVIDED BY OPERATING ACTIVITIES	\$ 9,521,837	\$ 9,344,525	\$ 18,866,362	\$ 2,337,879

See accompanying independent auditors report.

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