# OKLAHOMA STUDENT LOAN AUTHORITY

Management's Discussion and Analysis and
Financial Statements

June 30, 2002 and 2001

(With Independent Auditors' Report Thereon)

## Oklahoma Student Loan Authority

## Management's Discussion and Analysis

The Oklahoma Student Loan Authority (Authority) functions as a secondary market for the purchase of student loans from other lenders and as a servicer of student loans. As a servicer of student loans, the Authority services its own student loans and provides origination and pre-acquisition interim servicing for 31 other eligible lenders which are members of the OSLA Student Lending Network. The loan servicing work performed by the Authority is done under the registered tradename "OSLA Student Loan Servicing™". Each member of the OSLA Student Lending Network is required to sell its student loans to the Authority before repayment of the loans begin.

This section of the Authority's annual financial report presents a discussion and analysis of the Authority's financial performance for the fiscal year ended June 30, 2002. Please read it in conjunction with the Authority's financial statements and the notes to the financial statements, which follow this section.

### Financial Highlights

- The Authority's total assets at June 30, 2002 were approximately $583,124,000, which is an increase of approximately $97,718,000 or 20% over June 30, 2001.

- The Authority's net student loans at June 30, 2002 were approximately $475,441,000, which is an increase of approximately $79,887,000 or 20% over June 30, 2001.

- The Authority's operating revenue and interest expense for the fiscal year ended June 30, 2002 were approximately $26,790,000 and $13,928,000, respectively, resulting in a net interest margin of approximately $12,862,000. This is an increase of approximately $716,000 or 6% over the net interest margin for fiscal year ended June 30, 2001.

- The Authority's total other operating expenses for the fiscal year ended June 30, 2002 were approximately $6,646,000, which is an increase of $979,000 or 17% over the fiscal year ended June 30, 2001.

- The Authority's change in fund equity for the fiscal year ended June 30, 2002 was approximately $6,216,000, which is a decrease of approximately $263,000 or 4% over the change in fund equity for the fiscal year ended June 30, 2001.

### Overview of the Financial Statements

The Authority's financial statements are prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied on an accrual basis. Under the accrual basis of GAAP, revenues are recognized in the period in which they are earned and expenses are recognized in the period in which they are incurred. The three basic financial statements presented within the financial statements are:

<u>Balance Sheet</u> – This statement presents information regarding the Authority's assets, liabilities, and fund equity. Fund equity represents the total amount of assets less the total liabilities. The balance sheet classifies assets, liabilities, and fund equity as current, noncurrent, and restricted.

<u>Statement of Revenues, Expenses and Change in Fund Equity</u> – This statement presents the Authority's interest income, cost of funds, operating expenses, and changes in fund equity for the fiscal year.

<u>Statement of Cash Flows</u> – The Authority's statement of cash flows is presented on the direct method of reporting, which reflects cash flows from operating, non-capital financing, capital, and investing activities.

### Financial Analysis of the Authority

The Authority's total fund equity at June 30, 2002 was approximately $64,142,000, which is an increase of approximately $6,216,000 or 11% over June 30, 2001. Components of the Authority's balance sheet as of June 30, 2002 and 2001 were as follows:

| | 2002 | 2001 |
|---|---|---|
| Current assets | $ 15,757,278 | 5,282,486 |
| Capital assets | 1,489,056 | 935,431 |
| Other noncurrent assets | 10,645,766 | 16,850,841 |
| Restricted assets | 555,232,043 | 462,337,169 |
| Total Assets | $ 583,124,143 | 485,405,927 |
| Current liabilities | $ 259,075 | 246,998 |
| Current liabilities payable from restricted assets | 5,187,483 | 6,601,839 |
| Noncurrent liabilities payable from restricted assets | 513,535,551 | 420,631,147 |
| Total liabilities | 518,982,109 | 427,479,984 |
| Fund equity: | | |
| Invested in capital assets | 1,489,056 | 935,431 |
| Restricted | 34,074,320 | 29,047,172 |
| Unrestricted | 28,578,658 | 27,943,340 |
| Total Fund Equity | 64,142,034 | 57,925,943 |
| Total Liabilities and Fund Equity | $ 583,124,143 | 485,405,927 |

The growth noted above in the Authority's total assets is the continuation of a trend of significant growth in prior years. Net student loans grew from approximately $395,554,000 at June 30, 2001 to approximately $475,441,000 at June 30, 2002. The growth over the past year also relates to the issuance of the Series 2001A-2, 3, and 4 bonds and notes in December 2001 totaling $125,000,000 and Series 2002A-1 bonds and notes in February, 2002 totaling $40,625,000. Approximately $49,000,000 of Series 2001A-2, 3 and 4 and Series 2002A-1 was held as restricted assets and not yet invested in student loans at June 30, 2002.

For the fiscal year ended June 30, 2002, the Authority originated or acquired student loans with a principal balance of approximately $145,487,000. The Authority funds the origination or acquisition of student loans by periodically issuing bonds and notes.

The Authority's change in fund equity for the fiscal year ended June 30, 2002 was approximately $6,216,000 which is a decrease of approximately $263,000 or 4% over the change in fund equity for the fiscal year ended June 30, 2001. Components of the statement of revenues, expenses and changes in fund equity for the fiscal years ending June 30, 2002 and 2001 are as follows:

| | | 2002 | 2001 |
|---|---|---|---|
| Loan interest income | $ | 24,996,023 | 28,640,905 |
| Investment interest income | | 1,793,685 | 2,864,212 |
| Total operating revenue | | 26,789,708 | 31,505,117 |
| Interest expense | | 13,927,536 | 19,358,782 |
| Other operating expenses | | | |
| General administration | | 3,542,235 | 2,937,662 |
| External loan servicing | | 657,658 | 735,322 |
| Professional fees | | 404,070 | 302,244 |
| Consolidation rebate fees | | 905,118 | 741,319 |
| Provision for loan losses | | 1,137,000 | 950,500 |
| Total other operating expenses | | 6,646,081 | 5,667,047 |
| Total operating expenses | | 20,573,617 | 25,025,829 |
| Change in fund equity | $ | 6,216,091 | 6,479,288 |

The growth noted above in the Authority's fund equity is the continuation of a trend of significant growth in prior years. The change in fund equity of approximately $6,216,000 for the year ended June 30, 2002 relates to both the Authority's debt service funds (which serve as collateral on outstanding bonds and notes) and to the Authority's general funds as both experienced increased fund equity.

The decrease noted above in loan interest income for the fiscal year ended June 30, 2002 is related to decreases in the variable interest rates on the student loans, which was partially offset by the increase in student loans. The variable interest rates on student loans are reset annually on July 1st. The rates for the fiscal year ended June 30, 2002 varied from 5.39% to 6.79%, and the rates for the fiscal year ended June 30, 2001 varied from 7.59% to 8.99%.

The Authority's net interest margin, as calculated below, for the fiscal year ended June 30, 2002, was approximately $12,862,000. This is an increase of approximately $716,000 or 6% over the net interest margin for the fiscal year ended June 30, 2001.

| | | 2002 | 2001 |
|---|---|---|---|
| Operating revenue | $ | 26,790,000 | 31,505,000 |
| Interest expense | | 13,928,000 | 19,359,000 |
| Net interest margin | $ | 12,862,000 | 12,146,000 |

The decrease noted above in interest expense for the fiscal year ended June 30, 2002 is related to lower interest rates for the fiscal year ended June 30, 2002 in which the majority of the Authority's bonds and notes are variable. The decrease is partially offset by the increase in bonds and notes for the fiscal year ended June 30, 2002.

As noted above, the Authority's other operating expenses for the fiscal year ended June 30, 2002 grew by 17% over the previous fiscal year. The increase in other operating expenses was related to additional personnel costs to accommodate the Authority's growth; increased depreciation and amortization of fixed assets and deferred costs, increased consolidation rebate fee expense and increased provision for loan losses. The Authority prepares an annual operating budget that is used as a management tool for tracking the various operating expenses. There were no significant variances between the budget and actual operating expenses for the fiscal year ended June 30, 2002.

**Debt Administration**

The Authority funds student loan notes receivable by issuing tax-exempt and taxable bonds and notes. The bonds and notes must be approved by the State of Oklahoma bond oversight process prior to being issued. Tax-exempt bonds or notes also must receive an allocation of the State of Oklahoma private activity volume ceiling or "cap". In addition, the issues must comply with federal statutes and with the rules and regulations of the United States Treasury Department and the United States Securities and Exchange Commission.

At June 30, 2002, the Authority had $515,930,000 principal amount of bonds and notes payable outstanding, an increase of 22% from the $423,085,000 principal amount outstanding at June 30, 2001. Detailed information on the Authority's debt is presented in note 5 to the financial statements.

$514,530,000 of Authority debt is publicly held and has long term credit ratings assigned by Moody's Investors Service (Moody's) and Standard and Poor's (S&P) based on the type of security as shown in the table below. The credit ratings have been maintained and periodically the ratings have been confirmed in connection with new parity debt issues or extensions of recycling periods.

| Credit Ratings(s) | Principal Amount | Type of Security |
|---|---|---|
| Aaa Moody's /AAA S&P | $ 429,475,000 | Senior Lien or Insured |
| Aaa Moody's | $ 41,870,000 | Over Collateralized |
| A2 Moody's/A S&P | $ 43,185,000 | Subordinate Bonds |

$160,250,000 of the Authority debt listed above bears a Weekly Rate and, in addition to the long-term ratings, also has short-term ratings by Moody's (VMIG-1) and S&P (A-1+ or A-1).

The Authority meets its temporary requirements for funding student loan notes receivable through a taxable, revolving warehouse line of credit provided by commercial banks. The commitment amount of the line of credit is $125,000,000, of which $1,400,000 principal amount was outstanding at June 30, 2002. The line of credit is not rated by a credit rating agency.

## Oklahoma Student Loan Authority

## Management's Discussion and Analysis

### Conditions Affecting Financial Position

At June 30, 2002, the Authority was servicing and committed to purchase student loans from members of the OSLA Student Lending Network with a principal balance of approximately $71,064,000. The total portfolio of gross student loans that the Authority owns or services for members of the OSLA Student Lending Network was approximately $543,857,000 at June 30, 2002. This is an increase of approximately $90,000,000 or 20% over this total as of June 30, 2001.

The Authority has experienced significant growth in all aspects of its operations. With the growth in the volume of student loan applications being processed and the conversion of the Authority's loan servicing to an in-house system, the Authority's fiscal year 2003 budget reflects continued growth. The Authority's budgeted administrative expenses for fiscal year 2003 reflect the additional costs to be incurred as a result of the Authority's growth and the operation of the in-house loan servicing system.

Lower market interest rates mean that student loan interest rates on outstanding student loans will be reduced in the fiscal year ending June 30, 2003, causing a reduction in the average yield for the total student loan portfolio. The variable student loan rates for the fiscal year ending June 30, 2003 vary from 3.46% to 4.86% compared to 5.39% to 6.79% for the fiscal year ended June 30, 2002.

The Authority's budgets for funding the growth of student loans are based on a larger proportion of taxable debt, with correspondingly higher interest rates than tax-exempt debt, in the Authority's outstanding bonds and notes. This increase in taxable debt in proportion to tax-exempt debt will cause an increase to the overall average rate paid for interest expense.

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**Independent Auditors' Report**

Trustees
Oklahoma Student Loan Authority:

We have audited the balance sheets of the Oklahoma Student Loan Authority (the Authority), a component unit of the State of Oklahoma, as of June 30, 2002 and 2001, and the related statements of revenues, expenses and changes in fund equity and cash flows for the years then ended. These financial statements are the responsibility of the management of the Authority. 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 the *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Oklahoma Student Loan Authority as of June 30, 2002 and 2001, and the results of its operations and its 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 a report dated August 23, 2002 on our consideration of the Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audits.

The Management's Discussion and Analysis on pages 1 through 5 is not a required part of the basic financial statements but is supplementary information required by the accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

August 23, 2002

## OKLAHOMA STUDENT LOAN AUTHORITY

Balance Sheets

June 30, 2002 and 2001

| Assets | | 2002 | 2001 |
|---|---|---|---|
| Current assets: | | | |
| Cash | $ | 14,531 | 10,409 |
| Investments | | 15,548,887 | 5,005,481 |
| Interest receivable | | 193,860 | 266,596 |
| Total current assets | | 15,757,278 | 5,282,486 |
| Noncurrent assets: | | | |
| Loans, net of allowance for loan losses | | 10,459,367 | 16,749,617 |
| Capital assets, net of accumulated depreciation | | 1,489,056 | 935,431 |
| Other noncurrent assets | | 186,399 | 101,224 |
| Total noncurrent assets | | 12,134,822 | 17,786,272 |
| Restricted assets: | | | |
| Cash | | 783,681 | 75,139 |
| Investments | | 71,788,018 | 68,042,684 |
| Interest receivable | | 13,876,797 | 11,669,310 |
| Loans, net of allowance for loan losses | | 464,982,058 | 378,804,133 |
| Other restricted assets | | 3,801,489 | 3,745,903 |
| Total restricted assets | | 555,232,043 | 462,337,169 |
| | $ | 583,124,143 | 485,405,927 |
| **Liabilities and Fund Equity** | | | |
| Current liabilities: | | | |
| Accounts payable and other accrued expenses | $ | 259,075 | 246,998 |
| Current liabilities payable from restricted assets: | | | |
| Accounts payable and other accrued expenses | | 815,844 | 848,371 |
| Accrued interest payable | | 1,441,639 | 2,408,468 |
| Current portion of bonds payable | | 2,930,000 | 3,345,000 |
| Total current liabilities payable from restricted assets | | 5,187,483 | 6,601,839 |
| Noncurrent liabilities payable from restricted assets: | | | |
| Arbitrage rebate payable | | 535,551 | 891,147 |
| Notes payable | | 80,000,000 | 99,435,000 |
| Bonds payable | | 433,000,000 | 320,305,000 |
| Total noncurrent liabilities payable from restricted assets | | 513,535,551 | 420,631,147 |
| Total liabilities | | 518,982,109 | 427,479,984 |
| Fund equity: | | | |
| Invested in capital assets | | 1,489,056 | 935,431 |
| Restricted | | 34,074,320 | 29,047,172 |
| Unrestricted | | 28,578,658 | 27,943,340 |
| Total fund equity | | 64,142,034 | 57,925,943 |
| Commitments and contingencies, (note 7) | | — | — |
| Total liabilities and fund equity | $ | 583,124,143 | 485,405,927 |

See accompanying notes to financial statements.

**OKLAHOMA STUDENT LOAN AUTHORITY**

Statements of Revenues, Expenses and Changes in Fund Equity

Years ended June 30, 2002 and 2001

| | 2002 | 2001 |
|---|---|---|
| Operating revenues: | | |
| Loan interest income | | |
| From borrowers | $ 18,033,914 | 20,033,511 |
| From U.S. Department of Education (USDE) | 6,962,109 | 8,607,394 |
| Investment interest income | 1,793,685 | 2,864,212 |
| Total operating revenues | 26,789,708 | 31,505,117 |
| Operating expenses: | | |
| Interest expense | 13,927,536 | 19,358,782 |
| General administration | 3,542,235 | 2,937,662 |
| External loan servicing fees | 657,658 | 735,322 |
| Professional fees | 404,070 | 302,244 |
| Consolidation rebate fees | 905,118 | 741,319 |
| Provision for loan losses | 1,137,000 | 950,500 |
| Total operating expenses | 20,573,617 | 25,025,829 |
| Change in fund equity | 6,216,091 | 6,479,288 |
| Fund equity, beginning of year | 57,925,943 | 51,446,655 |
| Fund equity, end of year | $ 64,142,034 | 57,925,943 |

See accompanying notes to financial statements.

## OKLAHOMA STUDENT LOAN AUTHORITY

Statements of Cash Flows

Years ended June 30, 2002 and 2001

| | 2002 | 2001 |
|---|---|---|
| Cash flows from operating activities: | | |
| Receipts of interest income from USDE | $ 7,251,383 | 9,124,653 |
| Receipts of interest income from borrowers | 17,695,951 | 18,790,803 |
| Receipts of interest on investments | 2,188,077 | 2,810,717 |
| Payments for interest on notes and bonds payable | (14,287,981) | (19,693,359) |
| Payments to Internal Revenue Service for arbitrage rebate | (711,575) | (116,815) |
| Payments to employees and suppliers | (5,232,034) | (3,700,644) |
| Net cash provided by operating activities | 6,903,821 | 7,215,355 |
| Cash flows from non-capital financing activities: | | |
| Advances on notes payable | 50,000,000 | 49,065,000 |
| Proceeds from issuance of bonds | 115,625,000 | 161,570,000 |
| Payments of debt financing costs | (831,905) | (979,853) |
| Payments on notes payable | (69,435,000) | (85,455,000) |
| Payments on bonds payable | (3,345,000) | (3,665,000) |
| Net cash provided by non-capital financing activities | 92,013,095 | 120,535,147 |
| Cash flows from investing activities: | | |
| Proceeds from maturity of investments | 341,393,846 | 279,014,665 |
| Receipts of loan principal payments | 74,088,016 | 54,232,694 |
| Purchases of investments | (355,682,586) | (332,699,668) |
| Disbursements of loan funds | (157,173,899) | (127,549,608) |
| Net cash used in investing activities | (97,374,623) | (127,001,917) |
| Cash flows from capital activities: | | |
| Purchases of capital assets | (829,629) | (741,909) |
| Net increase in cash | 712,664 | 6,676 |
| Cash at beginning of year (including $75,139 and $53,630 for 2002 and 2001, respectively, reported in restricted assets) | 85,548 | 78,872 |
| Cash at end of year (including $783,681 and $75,139 for 2002 and 2001, respectively, reported in restricted assets) | $ 798,212 | 85,548 |

See accompanying notes to financial statements.



(Continued)

**OKLAHOMA STUDENT LOAN AUTHORITY**

Statements of Cash Flows

Years ended June 30, 2002 and 2001

| | | 2002 | 2001 |
|---|---|---|---|
| Reconciliation of change in fund equity to net cash provided by operating activities: | | | |
| Change in fund equity | $ | 6,216,091 | 6,479,288 |
| Adjustments to reconcile change in fund equity to net cash provided by operating activities: | | | |
| Depreciation and amortization | | 3,006,864 | 1,987,690 |
| Provision for loan losses | | 1,137,000 | 950,500 |
| (Increase) decrease in assets: | | | |
| Interest receivable | | (2,134,751) | (2,253,371) |
| Other assets | | 21,492 | 97,818 |
| Increase (decrease) in liabilities: | | | |
| Accounts payable and other accrued expenses | | (20,450) | 766,523 |
| Accrued interest payable | | (966,829) | (777,300) |
| Arbitrage rebate payable | | (355,596) | (35,793) |
| Net cash provided by operating activities | $ | 6,903,821 | 7,215,355 |

See accompanying notes to financial statements.

## (1) Reporting Entity and Nature of the Program

The Oklahoma Student Loan Authority (the Authority) was created as an express trust under applicable Oklahoma statutes and a Trust Indenture dated August 2, 1972, with the State of Oklahoma (the State) accepting the beneficial interest therein. The Authority is a component unit of the State and is included in the financial statements of the State as a part of the Enterprise Fund. Enterprise funds are used to account for the operations and financial position of governmental entities that are financed and operated in a manner similar to private enterprise.

The purpose of the Authority is to provide loan funds to qualified persons at participating post secondary educational institutions. The Authority also performs origination and interim status servicing for other Federal Family Education Loan (FFEL) Program lenders in addition to providing a secondary market for FFEL Program loans for participating financial institutions. The student loans held by the Authority under the federal Higher Education Act of 1965, as amended, include Federal Stafford Loans (Stafford), Unsubsidized Stafford Loans for Middle Income Borrowers (Unsubsidized Stafford), Federal Supplemental Loans for Students (SLS), Federal Parent Loans for Undergraduate Students (PLUS), and Federal Consolidation Loans (Consolidation).

These FFEL Program loans are 98% guaranteed with certain exceptions (100% guaranteed for loans first disbursed before October 1, 1993) by the Oklahoma State Regents for Higher Education Guaranteed Student Loan Program (State Guarantee Agency), which is reinsured by the United States Department of Education (USDE), or guaranteed by other guarantors approved by the USDE (Guarantee Agencies).

As of June 30, 2002 and 2001, the Authority serviced approximately $71,064,000 and $60,400,000, respectively, in FFEL Program loans for other financial institutions. As a servicer of FFEL Program loans, the Authority collects student loan remittances and subsequently disburses these remittances to the appropriate lending entities.

## (2) Summary of Significant Accounting Policies

The financial statements of the Authority included herein reflect the combined assets, liabilities, fund equity, and changes therein for the Authority.

### *(a) Basis of Accounting*

The Authority accounts for its operation as an enterprise fund. Enterprise funds are accounted for on the flow of economic resources measurement focus and use the accrual basis of accounting, similar to private business enterprises. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when incurred. In accordance with the provisions of Governmental Accounting Standards Board (GASB) Statement No. 20, the Authority utilizes all Financial Accounting Standards Board statements as the Authority's accounting principles, unless such statements are in direct conflict with statements issued by the GASB.

The preparation of the 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 at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

***(b) Accounts of the Authority***

The accounts of the Authority are organized on the basis of individual funds as prescribed by the "Oklahoma Student Loan Act" (Act) and terms of various debt obligations. The various accounts assigned to each fund could include any of the following depending upon the terms of the related debt obligation: Principal Account, Interest Account, Student Loan Account, Repayment Account, Debt Service Reserve Account, Investment Earnings Account, Rebate Account and General Investment Account.

***(c) Cash***

The Authority only considers cash in demand deposit accounts, which are entirely insured by federal deposit insurance, to be cash for purposes of the statement of cash flows.

***(d) Investments***

Investments consist of repurchase agreements, certain government obligations, and mutual funds. Applicable Oklahoma statutes authorize certain types of investments the Authority can utilize. As of June 30, 2002 and 2001, the Authority was in compliance with these investment requirements.

Investments are stated at fair value, based on quoted prices for debt and equity securities and at cost for repurchase agreements, with changes in fair value included in the statements of revenues, expenses and changes in fund equity.

***(e) Loans and Allowance for Loan Losses***

Loans are stated at cost, net of an allowance for loan losses. The Authority includes as the cost of a loan any premium paid on student loans purchased. Premiums are amortized over the estimated life of the loan as an adjustment to interest income.

All of the loans made or acquired by the Authority are guaranteed as noted above. There is still risk to the Authority if the loans should lose their guarantee. The Authority has established cure and recovery procedures to be applied to loans that have lost their guarantee. If the cure and recovery procedures are not successful within a maximum of three years, the loan will be written-off as uncollectible. Additionally, the Authority is at risk for 2% of the loans with first disbursement on or after October 1, 1993.



(Continued)

As of June 30, 2002 approximately $459,384,000 of the Authority's loans were guaranteed at the 98% level. The allowance for loan losses was established by the management of the Authority to provide for these two types of losses. Student loans are written off when they are deemed uncollectible and charged against the allowance upon such determination. Any subsequent collection or recovery on an account written off as uncollectible is credited to the allowance.

### *(f) Capital Assets*

The Authority capitalizes expenditures for equipment, system development, and leasehold improvements. Depreciation and amortization is calculated primarily on a straight-line basis of five to ten years. Accumulated depreciation and amortization on capital assets at June 30, 2002 and 2001, was approximately $1,042,000 and $786,000, respectively. Maintenance of equipment and other assets is expensed as incurred.

### *(g) Restricted Fund Equity*

Certain assets of the Authority are restricted by the applicable bond and note covenants for the purpose of providing collateral for the outstanding debt obligations and paying debt interest and principal payments that are due (see note 5).

### *(h) Operating Revenues and Expenses*

Balances classified as operating revenues and expenses are those which comprise the Authority's principle ongoing operations. Since the Authority's operations are similar to those of any other finance company, all revenues and expenses are considered operating.

### *(i) Interest Income*

Interest is earned from the borrowers on the various types of student loans, the USDE and from investments. The USDE makes two types of interest payments to the Authority. One is for the interest on Stafford loans when the borrower is not currently required to make principal and interest payments under the terms of the loan. Interest income from USDE for the years ended June 30, 2002 and 2001 was approximately $5,732,000 and $6,878,000, respectively. The other type of interest payment from the USDE is "Special Allowance Payments." The rates for Special Allowance Payments are based on quarterly formulas that differ according to the type of loan, the date the loan was first disbursed, the interest rate and the type of funds used to finance such loans (tax-exempt or taxable). These rates are based upon the average rate established in the auctions of 91-day U.S. Treasury bills during such quarter or the quotes of 3-month commercial paper (financial) in effect for each of the days in such quarter. Special allowance payments from USDE for the years ended June 30, 2002 and 2001 were approximately $1,230,000 and $1,729,000, respectively.

***(j) Arbitrage Rebate***

The proceeds from the Authority's tax exempt debt issues are subject to arbitrage rebate laws under the Internal Revenue Code. This arbitrage rebate limits the earnings on investment of tax exempt proceeds in non-purpose investments. The Authority has calculated and made provisions for the estimated cumulative rebatable arbitrage that must be remitted to the Internal Revenue Service for the excess earnings on non-purpose investments.

***(k) Income Taxes***

As a State beneficiary trust, the income of the Authority earned in the exercise of its essential function is exempt from state and federal income taxes.

***(l) Reclassifications***

Certain reclassifications have been made to the 2001 balances in order to conform to the 2002 presentation.

## (3) Investments

The Authority invests its idle cash in collateralized repurchase agreements, U.S. Treasury securities and U.S. Government securities based mutual funds. The Authority's investments would generally be categorized into one of three separate credit risk categories. Category 1 includes investments that are insured or registered, or are held by the Authority or its agent in the Authority's name. The Authority's Category 1 restricted investments totaled $3,351,622 and $4,023,925 at June 30, 2002 and 2001, respectively. Category 2 includes uninsured and unregistered investments which are held by the counterparty's trust department or agent in the Authority's name. The Authority did not have any Category 2 investments at June 30, 2002 or 2001. Category 3 includes uninsured and unregistered investments, held by the counterparty, or by its trust department or agent, but not in the Authority's name. The Authority's Category 3 restricted investments totaled $780,900 at June 30, 2002 and 2001. One of the Authority's repurchase agreements is classified as Category 3 because the securities underlying the repurchase agreement are held by an independent custodian in the name of the seller of the purchased securities.

The U.S. Government securities based mutual funds are not subject to classification in categories of credit risk because they are not evidenced by securities that exist in physical or book entry form. The Authority's restricted investment in U.S. Government securities based mutual funds totaled $67,542,259 and $63,237,859 at June 30, 2002 and 2001, respectively. The Authority's unrestricted investment in U.S. Government securities based mutual funds totaled $15,548,887 and $5,005,481 at June 30, 2002 and 2001, respectively.



(Continued)

Investments at fair value consist of the following at June 30, 2002 and 2001:

| | 2002 | 2001 |
|---|---|---|
| U.S. Government securities based mutual funds: | | |
| Restricted | $ 67,542,259 | 63,237,859 |
| U.S. Treasury securities: | | |
| Restricted | 113,000 | 113,000 |
| Repurchase agreements: | | |
| Restricted | 4,132,759 | 4,691,825 |
| Total restricted investment | 71,788,018 | 68,042,684 |
| U.S. Government securities based mutual funds: | | |
| Unrestricted | 15,548,887 | 5,005,481 |
| Total investment | $ 87,336,905 | 73,048,165 |

## (4) Loans

The Authority originates, purchases and holds various types of student loans as described in note 1. The terms of these loans, which vary on an individual basis depending upon loan type and the date the loan was originated, generally provide for repayment in monthly installments of principal and interest over a period of up to thirty years for Consolidation loans and generally up to ten years for other loans. The repayment period begins after a grace period of six months following graduation or loss of qualified student status for the Subsidized and Unsubsidized Stafford loans. The repayment period for Consolidation, SLS, and PLUS loans begins within 60 days from the date the loan is fully disbursed. Interest rates on student loans ranged from 4.16% to 11.00% for the fiscal year ended June 30, 2002 depending upon the type and date of origination of the individual loan.

Loans consist of the following at June 30, 2002 and 2001:

| | 2002 | 2001 |
|---|---|---|
| Stafford – Subsidized | $ 213,713,718 | 182,632,820 |
| Stafford – Unsubsidized | 137,619,699 | 108,574,760 |
| PLUS/SLS | 27,847,383 | 24,046,655 |
| Consolidation | 92,239,335 | 77,745,806 |
| Other | 1,373,148 | 394,670 |
| Total gross loans | 472,793,283 | 393,394,711 |
| Net deferred premium and loan cost | 6,507,067 | 5,154,909 |
| Allowance for loan losses | (3,858,925) | (2,995,870) |
| Net loans | $ 475,441,425 | 395,553,750 |

All FFEL Program student loans are guaranteed as to principal and accrued interest. The Guarantee Agencies are entitled to charge fees for these services, which may be withheld from the loan disbursements to the borrower and remitted to the Guarantee Agencies. The Authority pays the guarantee fees on all loans disbursed when the guarantee agency does not waive those fees. Guarantee fees are capitalized when the loan is made and are amortized, using the interest method, over the estimated economic life of the loan. The capitalized guarantee fees, net of accumulated amortization, at June 30, 2002 and 2001 were approximately $2,176,000 and $2,360,000, respectively. In order for the loans to be or remain guaranteed, certain due diligence requirements in loan servicing must be met. As of June 30, 2002 and 2001, respectively, approximately $199,000 and $151,000 of loans were no longer considered as being guaranteed.

The Authority also withholds certain origination fees from the loan disbursements on FFEL Program loans to the borrowers and remits these fees to USDE. The amount of the origination fees is a certain percentage of the gross loan amount.

The Authority is also required to pay to USDE certain lender and rebate fees. The amount of the lender fees includes a certain percentage of the gross loan amount on all FFEL Program loans originated after October 1, 1993 and a certain percentage of the carrying value of the Consolidation loans.

Loan origination costs are capitalized when the loan is made and are amortized, using the interest method, over the estimated economic life of the loan. The capitalized loan origination costs, net of accumulated amortization, at June 30, 2002 and 2001 were approximately $1,128,000 and $977,000, respectively.

Generally, student loans of the Authority are pledged as collateral for the various obligations of the Authority. The promissory notes for the pledged student loans are in the custody of Bank of Oklahoma, N.A. in its capacity as custodian for the Authority.

**(5) Notes and Bonds Payable**

The Authority periodically issues bonds and notes for the purpose of funding student loans. All notes and bonds payable are primarily secured by the student loans, related accrued interest, and by the amounts on deposit in the accounts established under the respective bond resolution or financing agreement as maintained by the corporate trustees. The accompanying financial information on pages 22 and 23 summarize the General Funds and pledged assets and liabilities related to the Authority's debt obligation trust estates as of June 30, 2002 and 2001. The Authority is in compliance with all significant financing agreement requirements and bond covenants.

Notes payable at June 30, 2002 and 2001 consist of the following:

$125,000,000 Taxable Variable Rate Revenue Note (line of credit), Series 1993L (1993L), dated May 2, 2002, as modified, payable to Bank One, Oklahoma, N.A. The interest rate is adjusted weekly based on the 91-day U.S. Treasury bill auction rate plus 1%. The interest rates were 2.71% and 4.45% as of June 30, 2002 and 2001, respectively. The principal is due at maturity on November 30, 2003. Advances and payments can be made under the provisions of the note, provided that the amount outstanding does not exceed the note amount.

$21,600,000 Senior Notes, Series 1995A-1 (1995A-1) dated November 9, 1995. The interest rate is based on a 35-day auction period with rates of 1.45% and 3.00% as of June 30, 2002 and 2001, respectively. The principal is due at maturity on September 1, 2025.

$7,000,000 Senior Notes, Series 1995A-2 (1995A-2) dated November 9, 1995. The interest rate is based on a one-year auction period with rates of 1.9% and 3.05% as of June 30, 2002 and 2001, respectively. The principal is due at maturity on September 1, 2025.

$10,455,000 1999A-1 Tax Exempt Promissory Note (1999A-1) dated August 25, 1999. The interest rate was a fixed rate of 4.92%. This issue was redeemed by the 2000A-4 Bonds issued August 31, 2000.

$5,770,000 1999A-2 Tax Exempt Promissory Note (1999A-2) modified July 25, 2000. The interest rate adjusted to 80% of LIBOR at the first of each month with a rate of 3.25% as of June 30, 2001. The 2001A-1 Bonds provided for the redemption of this note in July 2001.

$3,665,000 2000N Tax Exempt Revenue Note (2000N) dated July 25, 2000. The interest rate adjusted to 80% of LIBOR at the first of each month with a rate of 3.25% as of June 30, 2001. The 2001A-1 Bonds provided for the redemption of this note in July 2001.

$50,000,000 Senior Notes, Series 2001A-4 (2001A-4) dated December 20, 2001. The interest rate is adjusted quarterly to the federal Commercial Paper Rate with a rate of 1.84% as of June 30, 2002. The principal is due at maturity on December 1, 2011.

The following schedules summarize the notes payable outstanding as of June 30, 2002 and 2001:

| 2002 | | Beginning balance | Additions | Retired | Ending balance |
|---|---|---|---|---|---|
| 1993L | $ | 61,400,000 | — | 60,000,000 | 1,400,000 |
| 1995A-1 | | 21,600,000 | — | — | 21,600,000 |
| 1995A-2 | | 7,000,000 | — | — | 7,000,0000 |
| 1999A-2 | | 5,770,000 | — | 5,770,000 | — |
| 2000N | | 3,665,000 | — | 3,665,000 | — |
| 2001A-4 | | — | 50,000,000 | — | 50,000,000 |
| | $ | 99,435,000 | 50,000,000 | 69,435,000 | 80,000,000 |

| 2001 | | Beginning balance | Additions | Retired | Ending balance |
|---|---|---|---|---|---|
| 1993L | $ | 91,000,000 | 45,400,000 | (75,000,000) | 61,400,000 |
| 1995A-1 | | 21,600,000 | — | — | 21,600,000 |
| 1995A-2 | | 7,000,000 | — | — | 7,000,000 |
| 1999A-1 | | 10,455,000 | — | (10,455,000) | — |
| 1999A-2 | | 5,770,000 | — | — | 5,770,000 |
| 2000N | | — | 3,665,000 | — | 3,665,000 |
| Total | $ | 135,825,000 | 49,065,000 | (85,455,000) | 99,435,000 |

 (Continued)

The following schedules summarize the bonds payable outstanding as of June 30, 2002 and 2001:

| 2002 | | Beginning balance | Additions | Retired | Ending balance |
|---|---|---|---|---|---|
| 6.40% - 6.70% Series 1992A, due serially through 9-1-05 | $ | 13,015,000 | — | (3,345,000) | 9,670,000 |
| Variable rate Series 1994A-1, due 9-1-20 | | 25,200,000 | — | — | 25,200,000 |
| Variable rate Series 1994A-2, due 9-1-15 | | 7,000,000 | — | — | 7,000,000 |
| 5.80% Series 1995B-1 Subordinate, due 9-1-08 | | 2,000,000 | — | — | 2,000,000 |
| 6.35% Series 1995B-2 Subordinate, due 9-1-25 | | 3,980,000 | — | — | 3,980,000 |
| Variable rate demand obligations Series 1996A, due 6-1-26 | | 32,580,000 | — | — | 32,580,000 |
| 4.80% Series 1996B-1 Subordinate, due 8-1-04 | | 5,975,000 | — | — | 5,975,000 |
| 5.10% Series 1996B-2 Subordinate, due 8-1-08 | | 6,230,000 | — | — | 6,230,000 |
| Variable rate demand obligations Series 1997A, due 12-1-26 | | 33,000,000 | — | — | 33,000,000 |
| Variable rate demand obligations Series 1998A, due 6-1-28 | | 33,100,000 | — | — | 33,100,000 |
| Variable rate Series 2000A-1, 2000A-2, and 2000A-3 due 6-1-30, 2000A-4 (demand obligation) due 6-1-29 | | 120,945,000 | — | — | 120,945,000 |
| 5.625% Senior Series 2001A-1, due 6-1-31 | | 15,625,000 | — | — | 15,625,000 |
| Variable rate Series 2001B-1 Subordinate, due 6-1-31 | | 25,000,000 | — | — | 25,000,000 |
| Variable rate Series 2001A-2 and 2001A-3, due 12-1-31 | | — | 75,000,000 | — | 75,000,000 |
| Variable rate Series 2002A-1, due 12-1-31 | | — | 40,625,000 | — | 40,625,000 |
| Total | $ | 323,650,000 | 115,625,000 | (3,345,000) | 435,930,000 |

| 2001 | | Beginning balance | Additions | Retired | Ending balance |
|---|---|---|---|---|---|
| 6.30% - 6.70% Series 1992A, due serially through 9-1-05 | $ | 16,680,000 | — | (3,665,000) | 13,015,000 |
| Variable rate Series 1994A-1, due 9-1-20 | | 25,200,000 | — | — | 25,200,000 |
| Variable rate Series 1994A-2, due 9-1-15 | | 7,000,000 | — | — | 7,000,000 |
| 5.80% Series 1995B-1 Subordinate, due 9-1-08 | | 2,000,000 | — | — | 2,000,000 |
| 6.35% Series 1995B-2 Subordinate, due 9-1-25 | | 3,980,000 | — | — | 3,980,000 |
| Variable rate demand obligations Series 1996A, due 6-1-26 | | 32,580,000 | — | — | 32,580,000 |
| 4.80% Series 1996B-1 Subordinate, due 8-1-04 | | 5,975,000 | — | — | 5,975,000 |
| 5.10% Series 1996B-2 Subordinate, due 8-1-08 | | 6,230,000 | — | — | 6,230,000 |
| Variable rate demand obligations Series 1997A, due 12-1-26 | | 33,000,000 | — | — | 33,000,000 |
| Variable rate demand obligations Series 1998A, due 6-1-28 | | 33,100,000 | — | — | 33,100,000 |
| Variable rate Series 2000A-1, 2000A-2, and 2000A-3 due 6-1-30, 2000A-4 (demand obligation) due 6-1-29 | | — | 120,945,000 | — | 120,945,000 |
| 5.625% Senior Series 2001A-1, due 6-1-31 | | — | 15,625,000 | — | 15,625,000 |
| Variable rate Series 2001B-1 Subordinate, due 6-1-31 | | — | 25,000,000 | — | 25,000,000 |
| Total | $ | 165,745,000 | 161,570,000 | (3,665,000) | 323,650,000 |

The variable interest rates on the 1994A Bonds are based on periodic auctions of these bonds. The Series 1994A-1 Bonds are based on a 35-day auction period with a rate of 1.39% and 2.80% as of June 30, 2002 and 2001, respectively. The Series 1994A-2 Bonds are based on a one year auction period with a rate of 1.97% and 2.95% as of June 30, 2002 and 2001, respectively.

The variable rates on the 1996A bonds are set on a weekly basis by the Remarketing Agent, with a rate of 1.30% and 2.75% as of June 30, 2002 and 2001, respectively.

The variable rates of the 1997A bonds are set on a weekly basis by the Remarketing Agent, with a rate of 1.30% and 2.75% as of June 30, 2002 and 2001, respectively.

The variable rates on the 1998A bonds are set on a weekly basis by the Remarketing Agent, with a rate of 1.30% and 2.75% as of June 30, 2002 and 2001, respectively.

The variable interest rates on the 2000A Bonds are based on periodic resets of these bonds. The Series 2000A-1, 2000A-2, and 2000A-3 Bonds are based on a 28-day auction period with rates of 1.99% 1.95%, and 1.88% as of June 30, 2002 and 4.08%, 3.90%, and 4.07% as of June 30, 2001. The Series 2000A-4 Bonds are set on a weekly basis by the Remarketing Agent, with a rate of 1.30% and 2.75% as of June 30, 2002 and 2001, respectively.

The Subordinate Auction Rate Obligations, Series 2001B-1 (2001B-1) are dated June 7, 2001. The interest rate is based on a 35-day auction period with a rate of 1.60% and 3.00% as of June 30, 2002 and 2001, respectively. The principal is due at maturity on June 1, 2031.

The Senior Taxable Auction Rate Bonds, Series 2001A-2 (2001A-2) and Series 2001A-3 (2001A-3) are dated December 20, 2001. The interest rates are based on a 28-day auction rate with rates of 1.97% and 1.94% as of June 30, 2002 for the Series 2001A-2 and 2001A-3 bonds, respectively.

The Variable Rate Demand Obligations, Series 2002A-1 (2002A-1) are dated January 31, 2002. The interest rate is set on a weekly basis by the Remarketing Agent, with a rate of 1.33% as of June 30, 2002.

Fiscal year debt service requirements to maturity or redemption date, assuming interest rates on variable rate debt remains at June 30, 2002 levels, are as follows:

| Year ending June 30 | Principal | Interest | Total |
|---|---|---|---|
| 2003 | $ 2,930,000 | 10,151,191 | 13,081,191 |
| 2004 | 3,640,000 | 9,973,938 | 13,613,938 |
| 2005 | 7,875,000 | 9,566,304 | 17,441,304 |
| 2006 | 2,600,000 | 9,375,231 | 11,975,231 |
| 2007 | — | 9,345,184 | 9,345,184 |
| 2008 – 2012 | 58,230,000 | 44,507,633 | 102,737,633 |
| 2013 – 2017 | 7,000,000 | 39,704,971 | 46,704,971 |
| 2018 – 2022 | 25,200,000 | 38,627,866 | 63,827,866 |
| 2023 – 2027 | 98,160,000 | 35,534,253 | 133,694,253 |
| 2028 – 2032 | 310,295,000 | 20,560,257 | 330,855,257 |
| | $ 515,930,000 | 227,346,828 | 743,276,828 |

## (6) Retirement Plan

The Authority contributes to the Teachers Retirement System of Oklahoma (TRS), a cost-sharing multiple-employer public employee retirement system which is self-administered. TRS provides retirement, disability, and death benefits to plan members and beneficiaries. The benefit provisions are established and may be amended by the legislature of the State of Oklahoma. Title 70 of the Oklahoma Statutes, Sections 17-101 through 116.9, as amended, assigns the authority for management and operation of the Plan to the Board of Trustees of TRS. TRS issues a publicly available annual financial report that includes financial statements and required supplementary information for TRS. That annual report may be obtained by writing to the TRS, P.O. 53524, Oklahoma City, OK 73152 or by calling at 1-405-521-2387.

Employees of the Authority, as TRS members, are required to contribute to the Plan at a rate set by statute. The contribution rate for system members is based on 7% of their covered salary. The Authority made the system members' required contribution on behalf of its employees in 2002 and 2001.

The Authority itself is required to contribute a legislated rate on regular annual compensation for administration of the Plan. In 2002 and 2001, the contribution rate for the Authority was 11.5% of regular annual compensation. As provided by State statute, the amount of the Authority's contribution each fiscal year shall be reduced by the estimated revenue due to TRS from the dedicated natural and casinghead gas tax, which is considered an on behalf payment made by the State of Oklahoma for the Authority's employees. In 2002 and 2001, the actual net contribution rate due from the Authority was 6.8% and 5.8%, respectively.

The Authority's contributions to TRS were approximately $297,000, $215,000, and $189,000 for the years ended June 30, 2002, 2001, and 2000, respectively. These contributions equaled the required contributions for system members and plan administration each period.

## (7) Commitments and Contingencies

The Authority conducts certain programs subject to audit by various federal and state agencies. Amounts questioned as a result of audits, if any, may result in refunds to these governmental agencies.

As part of its lender network activities for FFEL Program loans, the Authority has entered into various loan purchase commitments with certain financial institutions for which it performs interim status loan servicing. Under such loan purchase commitments, the seller is required to offer these FFEL Program loans to the Authority and the Authority is required to purchase the loans under certain terms and conditions. As of June 30, 2002 and 2001, the Authority was committed to purchase approximately $71,064,000 and $60,400,000, respectively, in such FFEL Program loans that the Authority is servicing.

Proceeds from the Authority's tax-exempt debt that are invested in student loans are subject to the Federal government yield adjustment payment rebate law which limits the earnings rate on funds received by an organization which issues tax exempt debt. Any excess student loan interest over the allowable debt yield and spread would be rebated to the student loan borrowers as interest rate reductions or loan principal forgiveness, or rebated to the IRS at the maturity of the related debt. Management is actively monitoring and managing this spread and will take necessary action to maintain student loan yields within the allowable spread over the life of the respective debt issuances.



(Continued)

**(8) Student Loan Legislation**

Legislation signed into law on December 17, 1999 changed the index for Special Allowance Payments rates for loans first disbursed on or after January 1, 2000 and before June 30, 2003 from the 91-day U.S. Treasury Bill average auction rate to the average rates of the quotes of the 3-month commercial paper (financial) rates in effect for each of the days in such quarter and changed the Special Allowance Payments formulas for such loans.

**(9) Fair Value of Financial Instruments**

Fair value estimates, methods, and assumptions are set forth below for the Authority's financial instruments. Carrying amounts and estimated fair values of financial instruments at June 30 are summarized as follows:

| | 2002 | | 2001 | |
|---|---|---|---|---|
| | **Carrying amount** | **Estimated fair value** | **Carrying amount** | **Estimated fair value** |
| Financial assets: | | | | |
| Cash | $ 798,212 | 798,212 | 85,548 | 85,548 |
| Investments | 87,336,905 | 87,336,905 | 73,048,165 | 73,048,165 |
| Interest receivable | 14,070,657 | 14,070,657 | 11,935,906 | 11,935,906 |
| Loans, net | 475,441,425 | 475,441,425 | 395,553,750 | 395,553,750 |
| Financial liabilities: | | | | |
| Accrued interest payable | 1,441,639 | 1,441,639 | 2,408,468 | 2,408,468 |
| Notes payable | 80,000,000 | 80,000,000 | 99,435,000 | 99,435,000 |
| Bonds payable | 435,930,000 | 437,334,386 | 323,650,000 | 325,075,264 |

The carrying amount for cash, interest receivable, and accrued interest payable approximates fair value because of the short maturity of these financial instruments. The fair value of investments is based upon quoted prices.

The carrying value of loans approximates fair value because of the variable rate nature of the majority of loans and the special allowance payments by USDE.

The carrying value of notes payable approximates fair value for 2002 and 2001 because all notes were variable rate and approximated rates currently available for notes with similar terms and remaining maturities. The fair value of bonds payable has been determined based on a fair value appraisal performed by a third-party broker.