Financial statements and reports of independent certified public accountants

# Oklahoma Student Loan Authority

June 30, 2005 and 2004

CONTENTS


| | Page |
|---|---|
| REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS | 1 |
| MANAGEMENT'S DISCUSSION AND ANALYSIS | 2 |
| FINANCIAL STATEMENTS | |
| BALANCE SHEETS | 9 |
| STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND EQUITY | 10 |
| STATEMENTS OF CASH FLOWS | 11 |
| NOTES TO FINANCIAL STATEMENTS | 13 |
| REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS 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* | 30 |

# Report of Independent Certified Public Accountants

Trustees
Oklahoma Student Loan Authority

We have audited the accompanying balance sheets of the Oklahoma Student Loan Authority (the Authority), a component unit of the State of Oklahoma, as of June 30, 2005 and 2004, 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 Authority'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 as established by the Auditing Standards Board of the American Institute of Certified Public Accountants and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States of America. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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, 2005 and 2004, and its changes in fund equity 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 our report dated September 21, 2005 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 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.

Management's Discussion and Analysis on pages 2 through 8 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Grant Thornton LLP

Oklahoma City, Oklahoma
September 21, 2005

Suite 1200
1 Leadership Square
211 N. Robinson
Oklahoma City, OK 73102-7148
T 405.218.2800
F 405.218.2801
W www.grantthornton.com

**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 36 other eligible lenders which are members of the OSLA Student Lending Network. In addition, the Authority provides and supports its in-house loan servicing system for remote use by other eligible lenders. As a member of the OSLA Student Lending Network, the remote servicing lenders are responsible for their own origination and interim servicing of their student loans.

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, 2005. 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, 2005 were approximately, $884,695,000, which is an increase of approximately $153,121,000 or 21% over June 30, 2004.

- The Authority's net student loans at June 30, 2005 were approximately $817,421,000, which is an increase of approximately $126,340,000 or 18% over June 30, 2004.

- The Authority's total operating revenues, net of consolidation rebate fees, was approximately $30,600,000 and interest expense was approximately $20,586,000 for the fiscal year ended June 30, 2005, resulting in a net interest margin of approximately $10,014,000. This is an increase of approximately $888,000 or 10% from the fiscal year ended June 30, 2004.

- The Authority's total other operating expenses (see page iv) for the fiscal year ended June 30, 2005 were approximately $7,018,000, which is an increase of $713,000 or 11% over the fiscal year ended June 30, 2004.

- The Authority's change in fund equity for the fiscal year ended June 30, 2005 was approximately $2,996,000, which is an increase of approximately $175,000 or 6% from the change in fund equity for the fiscal year ended June 30, 2004.

## OVERVIEW OF THE FINANCIAL STATEMENTS:

In accordance with the provisions of the Governmental Accounting Standards Board (GASB) Statement No. 20, the Authority's applies all relevant GASB pronouncements as well as

Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions, unless those pronouncements conflict with or contradict GASB pronouncements, in which case, GASB prevails. Under the accrual basis of accounting, revenues are recognized in the period in which they are earned and expenses are recognized in the period in which they are incurred. The format of the Authority's financial statements is presented in conformity with GASB Statement No. 34, "Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments".

**CRITICAL ACCOUNTING POLICIES**:

Accounting principles generally accepted in the United States of America require Authority management to make estimates and assumptions and use judgments that affect reported income, expenses, assets and liabilities and disclosure of contingent assets and liabilities during reporting periods; accordingly, actual results could differ from these estimates.

The Authority generates most of its Operating Revenues from borrower interest, and subsidized interest and special allowance from the U.S. Department of Education, on its student loan portfolio. Certain Authority policies affect the generation of Operating Revenues.

The Authority offers the following incentive programs to our borrowers:

TOP Interest Rate Reduction – Most of the Authority's Stafford Loan and PLUS borrowers, including borrowers on loans that the Authority services for the OSLA Student Lending Network and will purchase in the future, can earn a 1.5% interest rate reduction by making their first twelve payments on time. The reduced interest rate will apply for the life of the loan after it has been earned.

EZ PAY Interest Rate Reduction – Borrowers can earn a 0.33% interest rate reduction by using the Authority's electronic debit for making their monthly payments. The reduced interest rate will apply as long as the borrower uses OSLA's electronic debit, EZ PAY, for making monthly payments.

TOP Principal Reduction – Borrowers can earn a 1% reduction in the principal amount of their loans by making their first three payments on time.

Consolidation Loan Principal Reduction – Consolidation loan borrowers can earn a 1% reduction in the principal amount of their loan by making their first six payments on time.

The achievement of the TOP and EZ PAY Interest Rate Reduction programs results in a reduction, and will result in a future reduction, in Operating Revenues received and in the average yield for the total student loan portfolio.

The Authority expenses the cost associated with the TOP and Consolidation Loan Principal Reduction programs in the period the incentive was earned as a reduction to loan interest income from borrowers.

The Authority capitalizes various out-of-pocket costs and amortizes these costs over an estimated life. These capitalized costs include:

Premiums on Loan Acquisitions – Premiums are amortized as a reduction to loan interest from borrowers over the estimated life of the loans, not to exceed 72 months.

Capitalized Loan Origination Costs – The direct costs associated with originating the loans are amortized as a reduction to loan interest from borrowers over the estimated life of the loans based on loan types.

Deferred Guarantee Fees – Fees paid to guarantors between July 1, 1999 and June 30, 2001 are amortized as a reduction to loan interest from borrowers over the estimated life of the loans, not to exceed 72 months.

Deferred Financing Costs – The cost associated with the issuance of the Authority's bonds and notes payable are amortized over the estimated life of the debt issue, not to exceed 72 months.

The Authority maintains an Allowance for Loan Losses to provide for estimated losses in the loan portfolio. The Authority will write off loans as uncollectible when that determination is made and will write off 2% of the principal balance upon payment of default claims filed with guarantors. The balance of the Allowance for Loan Losses is an estimate of losses in the Authority's current portfolio of student loans. The Authority updates the balance of the Allowance for Loan Losses by periodic expenses through the Provision for Loan Losses.

## FINANCIAL ANALYSIS OF THE AUTHORITY:

The Authority's total fund equity at June 30, 2005 was approximately $73,170,000, which is an increase of approximately $2,996,000 or 4% over June 30, 2004. Components of the Authority's balance sheet as of June 30, 2005 and June 30, 2004 were as follows:

| | 2005 | 2004 |
|---|---|---|
| Current assets | $ 14,869,837 | $ 4,615,138 |
| Capital assets | 983,130 | 1,170,961 |
| Other noncurrent assets | 16,235,727 | 27,868,021 |
| Restricted assets | 852,606,446 | 697,919,935 |
| Total Assets | $ 884,695,140 | $731,574,055 |
| Current liabilities | $ 404,549 | $ 302,039 |
| Current liabilities payable From restricted assets | 4,395,595 | 2,388,328 |
| Noncurrent liabilities payable From restricted assets | 806,724,831 | 658,710,021 |
| Total Liabilities | 811,524,975 | 661,400,388 |
| Fund equity: | | |
| Invested in capital assets | 983,130 | 1,170,961 |
| Restricted | 41,486,020 | 36,821,586 |
| Unrestricted | 30,701,015 | 32,181,120 |
| Total Fund Equity | 73,170,165 | 70,173,667 |
| Total Liabilities and Fund Equity | $ 884,695,140 | $731,574,055 |

The growth in the Authority's total assets is the continuation of a trend of significant growth in prior years. Net student loans grew from approximately $691,082,000 at June 30, 2004 to approximately $817,421,000 at June 30, 2005. The growth in liabilities over the past year relates to the issuance of the Series 2004A-2 bonds in October, 2004 totaling $40,625,000; the issuance of the Series 2004A-3 bonds and notes in November, 2004 totaling $100,000,000, the issuance of the Series 2005A bonds in March, 2005 totaling $65,045,000 net of a decrease in the commercial bank line of credit usage by $44,525,000. The growth noted in the Authority's Fund Equity is the continuation of a trend of significant loan growth and positive operating results of the Authority.

For the fiscal year ended June 30, 2005, the Authority acquired or originated student loans with a principal balance of approximately $284,733,000. This was a 4% increase compared to the $274,603,000 acquired or originated in the fiscal year ended June 30, 2004. This increase was due primarily to increased origination of Consolidation Loans, mostly consolidating loans currently in our own portfolio. At June 30, 2005, consolidation loans represented approximately 48% of our repayment status portfolio.

The Authority's change in fund equity for the fiscal year ended June 30, 2005 was approximately $2,996,000, which is an increase of approximately $175,000 or 6% from the change in fund equity for the fiscal year ended June 30, 2004. Components of the statement of revenues, expenses and changes in fund equity for the fiscal years ending June 30, 2005 and June 30, 2004 are as follows:

| | 2005 | 2004 |
|---|---|---|
| Loan interest income, net of consolidation rebate fees | $ 29,251,411 | $ 19,221,958 |
| Investment interest income | 1,348,711 | 356,856 |
| Operating revenue | 30,600,122 | 19,578,814 |
| Less: Interest expense | 20,585,785 | 10,452,080 |
| Net Interest Margin | 10,014,337 | 9,126,734 |
| Less: Other operating expenses: | | |
| General administration | 5,298,154 | 4,984,844 |
| External loan servicing | 187,176 | 132,501 |
| Professional fees | 358,509 | 291,764 |
| Provision for loan losses | 1,174,000 | 896,000 |
| Total other operating expenses | 7,017,839 | 6,305,109 |
| Change in fund equity | $ 2,996,498 | $ 2,821,625 |

The Change in Fund Equity of approximately $2,996,000 for the year ended June 30, 2005 relates to both the Authority's debt service funds ( restricted fund equity which serve as collateral on outstanding bonds and notes) and to the Authority's general funds (unrestricted equity).

The increase in loan interest income for the fiscal year ended June 30, 2005 is related to increased Special Allowance from the Department of Education due to increasing interest rates after the variable interest rates on the student loans were reset. The variable interest rates on student loans are reset annually on July 1st. The variable rates for the fiscal year ended June 30, 2005 ranged from 2.77% to 4.17% and the variable rates for the fiscal year ended June 30, 2004 ranged from 2.82% to 4.22%. The Special Allowance payments from the Department of Education are intended to give the holders of student loans a current market yield during period of increasing interest rates.

The Authority funds the origination or acquisition of student loans by periodically issuing bonds and notes and by reinvesting principal payments received on existing loans. The increase in interest expense for the fiscal year ended June 30, 2005 is related to increasing interest rates for the fiscal year ended June 30, 2005 and the increase of $148,170,000 principal amount in bonds and notes outstanding during the fiscal year ended June 30, 2005.

The increase in provision for loan losses is related to the growth in the Authority's student loan notes receivable and the projected loan losses based on historical trends over the life of the related student loans.

The Authority's other operating expenses for the fiscal year ended June 30, 2005 grew by only 11% over the previous fiscal year. The increase in other operating expenses was related to increased expenses related to the growth in our loan servicing activities such as postage, telecommunications, professional fees and personnel costs. 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, 2005.

## 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, 2005, the Authority had $806,580,000 principal amount of bonds and notes payable outstanding, an increase of 23% from the $658,410,000 principal amount outstanding at June 30, 2004. Detailed information on the Authority's debt is presented in note E to the financial statements.

$778,805,000 of Authority debt was publicly held and had 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 Rating(s) | Principal Amount | Type of Security |
|---|---|---|
| Aaa Moody's/AAA S&P | $716,395,000 | Senior Lien or Insured |
| Aaa Moody's | $25,200,000 | Over Collateralized |
| A2 Moody's/A S&P | $37,210,000 | Subordinate Bonds |

$256,250,000 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 was $150,000,000, of which $27,775,000 principal amount was outstanding at June 30, 2005. The line of credit is not rated by a credit rating agency.

**CONDITIONS AFFECTING FINANCIAL POSITION**:

At June 30, 2005, the Authority was servicing student loans from members of the OSLA Student Lending Network with a principal balance of approximately $115,705,000. The total portfolio of gross student loans that the Authority owns or services for members of the OSLA Student Lending Network was approximately $922,929,000 at June 30, 2005. This is an increase of approximately $144,889,000 or 19% over this total as of June 30, 2004.

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 growth in the total loan portfolio serviced by the Authority, particularly the growth in repayment status loans; the Authority's fiscal year 2006 budget reflects continued growth. The Authority's budgeted administrative expenses for fiscal year 2006 reflect the additional costs to be incurred as a result of the Authority's growth.

Higher market interest rates at June 30, 2005 means that student loan interest rates on outstanding loans will increase during the fiscal year ending June 30, 2006. The variable student loan rates on Stafford and PLUS loans for the fiscal year ending June 30, 2006 range from 4.70% to 6.10% compared to 2.77% to 4.17% for the fiscal year ended June 30, 2005.

The Federal Consolidation Loan portfolio continues to grow and become a larger percentage of the Authority's total portfolio. At June 30, 2005, the Federal Consolidation Loans were 33% of the Authority's gross student loans, an increase from 28% at June 30, 2004. In addition, consolidation loan applications totaling approximately $97,000,000 were pending funding at June 30, 2005 which will increase the concentration of consolidation loans in the Authority's portfolio. This growth results in a proportionate growth in the volume of Consolidation Rebate Fees that the Authority pays to the US Department of Education on our outstanding portfolio of Federal Consolidation Loans.

The majority of the Authority's bonds and notes payable bear a short-term variable rate of interest. In the fiscal year ending June 30, 2006, it is generally expected that interest rates on borrowed funds will increase, resulting in an increased interest expense. In that event, except for PLUS loans, we expect that the increase in cost of funds will be offset by an increase in Special Allowance paid by the U.S. Department of Education. The increased Special Allowance payments would increase our loan interest income and have the effect of increasing the yield on the student loans that we hold, and those that we are committed to purchase from the OSLA Student Lending Network.

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

# Oklahoma Student Loan Authority

## BALANCE SHEETS

June 30,

| ASSETS | 2005 | 2004 |
|---|---|---|
| Current assets | | |
| Cash | $ - | $ 1,226 |
| Investments | 14,866,988 | 4,468,166 |
| Interest receivable | 2,849 | 145,746 |
| Total current assets | 14,869,837 | 4,615,138 |
| Noncurrent assets | | |
| Loans, net of allowance for loan losses | 15,878,254 | 27,635,072 |
| Capital assets, net of accumulated depreciation | 983,130 | 1,170,961 |
| Other noncurrent assets | 357,473 | 232,949 |
| Total noncurrent assets | 17,218,857 | 29,038,982 |
| Restricted assets | | |
| Cash | 453,549 | 178,422 |
| Investments | 33,140,827 | 20,429,740 |
| Interest receivable | 15,532,400 | 11,767,828 |
| Loans, net of allowance for loan losses | 801,543,020 | 663,446,532 |
| Other restricted assets | 1,936,650 | 2,097,413 |
| Total restricted assets | 852,606,446 | 697,919,935 |
| TOTAL ASSETS | $884,695,140 | $731,574,055 |
| LIABILITIES AND FUND EQUITY | | |
| Current liabilities | | |
| Accounts payable and other accrued expenses | $ 404,549 | $ 302,039 |
| Current liabilities payable from restricted assets | | |
| Accounts payable and other accrued expenses | 1,974,602 | 951,594 |
| Accrued interest payable | 2,420,993 | 1,436,734 |
| Total current liabilities payable from restricted assets | 4,395,595 | 2,388,328 |
| Noncurrent liabilities payable from restricted assets | | |
| Arbitrage rebate payable | 144,831 | 300,021 |
| Notes payable | 106,375,000 | 150,900,000 |
| Bonds payable | 700,205,000 | 507,510,000 |
| Total noncurrent liabilities payable from restricted assets | 806,724,831 | 658,710,021 |
| Total liabilities | 811,524,975 | 661,400,388 |
| Commitments and contingencies | | |
| Fund equity | | |
| Invested in capital assets | 983,130 | 1,170,961 |
| Restricted | 41,486,020 | 36,821,586 |
| Unrestricted | 30,701,015 | 32,181,120 |
| Total fund equity | 73,170,165 | 70,173,667 |
| TOTAL LIABILITIES AND FUND EQUITY | $884,695,140 | $731,574,055 |

The accompanying notes are an integral part of these statements.

# Oklahoma Student Loan Authority

## STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND EQUITY

Year ended June 30,

| | **2005** | 2004 |
|---|---|---|
| Operating revenues | | |
| Loan interest income | | |
| From borrowers | **$15,848,024** | $13,767,756 |
| From U.S. Department of Education (USDE) | **15,831,733** | 7,180,932 |
| Investment interest income | **1,348,711** | 356,856 |
| Total operating revenues | **33,028,468** | 21,305,544 |
| Operating expenses | | |
| Interest | **20,585,785** | 10,452,080 |
| General administration | **5,298,154** | 4,984,844 |
| External loan servicing fees | **187,176** | 132,501 |
| Professional fees | **358,509** | 291,764 |
| Consolidation rebate fees | **2,428,346** | 1,726,730 |
| Provision for loan losses | **1,174,000** | 896,000 |
| Total operating expenses | **30,031,970** | 18,483,919 |
| CHANGE IN FUND EQUITY | **2,996,498** | 2,821,625 |
| Fund equity at beginning of year | **70,173,667** | 67,352,042 |
| Fund equity at end of year | **$73,170,165** | $70,173,667 |

The accompanying notes are an integral part of these statements.

# Oklahoma Student Loan Authority

## STATEMENTS OF CASH FLOWS

Year ended June 30,

| | 2005 | 2004 |
|---|---|---|
| Cash flows from operating activities | | |
| Receipts of interest income from borrowers | $ 19,917,390 | $ 18,376,139 |
| Receipts of interest income from USDE | 12,752,641 | 6,768,229 |
| Receipts of interest on investments | 1,358,987 | 423,138 |
| Payments for interest on notes and bonds payable | (19,026,307) | (9,651,458) |
| Payments to Internal Revenue Service for arbitrage rebate | (269,334) | (3,000) |
| Payments to employees and suppliers | (6,890,091) | (6,426,871) |
| Net cash provided by operating activities | 7,843,286 | 9,486,177 |
| Cash flows from noncapital financing activities | | |
| Advances on notes payable | 15,475,000 | 67,700,000 |
| Proceeds from issuance of bonds | 205,670,000 | 40,625,000 |
| Payments of debt financing costs | (896,821) | (281,566) |
| Payments on notes payable | (60,000,000) | - |
| Payments on bonds payable | (12,975,000) | - |
| Net cash provided by non-capital financing activities | 147,273,179 | 108,043,434 |
| Cash flows from investing activities | | |
| Proceeds from maturity of investments | 364,154,917 | 292,567,373 |
| Receipts of loan principal payments | 172,284,795 | 149,844,718 |
| Increase in student loan notes receivable | (303,821,697) | (291,172,744) |
| Purchases of investments | (387,264,826) | (269,436,813) |
| Net cash used in investing activities | (154,646,811) | (118,197,466) |
| Cash flows from capital activities | | |
| Purchases of capital assets | (195,753) | (123,547) |
| NET INCREASE (DECREASE) IN CASH | 273,901 | (791,402) |
| Cash at beginning of year (including $178,422 and $961,956 for 2005 and 2004, respectively, reported in restricted assets) | 179,648 | 971,050 |
| Cash at end of year (including $453,549 and $178,422 for 2005 and 2004, respectively, reported in restricted assets) | $ 453,549 | $ 179,648 |

## Oklahoma Student Loan Authority

STATEMENTS OF CASH FLOWS - CONTINUED

Year ended June 30,

| | 2005 | 2004 |
|---|---|---|
| Reconciliation of change in fund equity to net cash provided by operating activities | | |
| Change in fund equity | $ 2,996,498 | $ 2,821,625 |
| Adjustments to reconcile change in fund equity to net cash provided by operating activities | | |
| Depreciation on capital assets | 383,584 | 411,479 |
| Amortization of loan origination costs, guarantee fees and premiums on loan acquisition | 4,508,081 | 3,796,484 |
| Amortization of deferred financing costs | 575,219 | 457,054 |
| Provision for loan losses | 1,174,000 | 896,000 |
| Loss on long-term investment | - | 60,251 |
| (Increase) decrease in assets | | |
| Interest receivable | (3,621,675) | 430,714 |
| Other assets | (127,008) | 156,869 |
| Increase (decrease) in liabilities | | |
| Accounts payable and other accrued expenses | 1,125,518 | 80,371 |
| Accrued interest payable | 984,259 | 343,568 |
| Arbitrage rebate payable | (155,190) | 31,762 |
| Net cash provided by operating activities | $ 7,843,286 | $ 9,486,177 |

The accompanying notes are an integral part of these statements.

## NOTE A - REPORTING ENTITY AND NATURE OF 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 student 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 (Higher Education Act), 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).

The FFEL Program loans are 98% guaranteed with certain exceptions 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 (the USDE), or guaranteed by other guarantors approved by the USDE (Guarantee Agencies). As of June 30, 2005, approximately $799,895,000 of the Authority's loans were guaranteed at the 98% level.

As of June 30, 2005 and 2004, the Authority serviced approximately $115,705,000 and $92,184,000, 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.

The Authority also originates and holds private loans through our Supplemental Higher Education Loan Financing (SHELF™) Program. These loans are not guaranteed under the Higher Education Act. The Authority retains a percentage of SHELF™ loan proceeds as a reserve against loan losses.

## NOTE B - SUMMARY OF ACCOUNTING POLICIES

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

### 1. 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 the Governmental Accounting Standards Board (GASB) Statement No. 20, the Authority applies all relevant GASB pronouncements as well as Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions, unless those pronouncements conflict with or contradict GASB pronouncements, in which case, GASB prevails.

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 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.

### 2. 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 (the 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, Rebate Account and General Investment Account.

### 3. Cash

The Authority considers cash in demand deposit accounts and certain money market funds to be cash equivalents. The Authority utilizes bank deposit accounts which periodically sweep cash into uninsured short-term investment securities. The Authority has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on such accounts.

### 4. 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, 2005 and 2004, the Authority is in compliance with these investment requirements.

NOTE B - SUMMARY OF ACCOUNTING POLICIES - CONTINUED

4. Investments - Continued

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.

5. 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 not to exceed 60 months as an adjustment to interest income. Loan origination costs are capitalized when the loan is made and are amortized, using the interest method, over the estimated life of the loan.

All of the FFEL Program 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 loan principal in the event a default claim is filed.

The allowance for loan losses was established by the Authority's management to provide for these two types of losses, as well as losses on non-guaranteed SHELF™ loans. 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.

6. Capital Assets

The Authority capitalizes expenditures for equipment, system development and leasehold improvements. Depreciation and amortization are calculated primarily on a straight-line basis of three to ten years. Accumulated depreciation and amortization on capital assets at June 30, 2005 and 2004 were approximately $1,700,000 and $1,363,000, respectively. Maintenance of equipment and other assets is expensed as incurred.

7. 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 E).

NOTE B - SUMMARY OF ACCOUNTING POLICIES - CONTINUED

8. Operating Revenues and Expenses

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

9. Interest Income

Interest is earned from the borrowers on the various types of student loans, from the USDE and from investments. The USDE makes two types of interest payments to the Authority. One is for the interest on Subsidized Stafford and certain Consolidation loans when the borrower is not currently required to make principal and interest payments under the terms of the loan. Such interest income from the USDE for the years ended June 30, 2005 and 2004 was approximately $5,194,000 and $4,511,000, 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 three-month commercial paper (financial) in effect for each of the days in such quarter. Special Allowance Payments from the USDE for the years ended June 30, 2005 and 2004 were approximately $10,638,000 and $2,670,000, respectively.

10. Arbitrage Rebate

The proceeds from the Authority's tax-exempt debt issuances 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.

11. 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.

NOTE B - SUMMARY OF ACCOUNTING POLICIES - CONTINUED

12. Recent Accounting Pronouncements

In 2004, GASB issued Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans* (OPEB plans). GASB Statement No. 43 establishes uniform financial reporting standards for OPEB plans and supersedes the interim guidance included in GASB Statement No. 26, *Financial Reporting for Postemployment Healthcare Plans Administered by Defined Benefit Pension Plans.* The approach followed in this Statement generally is consistent with the approach adopted in GASB Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contributions Plans,* with modifications to reflect differences between pension plans and OPEB plans. The provisions of this Statement are effective for fiscal periods beginning after December 15, 2005, with earlier application encouraged. Management has not yet determined the effect this Statement will have on the Authority's financial condition or changes in fund equity.

In 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions.* GASB Statement No. 45 establishes standards for the measurement, recognition and display of OPEB expense/expenditures and related liabilities (assets), note disclosures and, if applicable, required supplementary information ("RSI") in the financial reports of state and local governmental employers. The provisions of this Statement are effective for fiscal periods beginning after December 15, 2006, with earlier application encouraged. Management has not yet determined the effect this Statement will have on the Authority's financial condition or changes in fund equity.

NOTE C - INVESTMENTS

The Authority invests its idle cash in collateralized repurchase agreements and U.S. Government securities-based money market mutual funds in accordance with the Authority's investment policy. Generally, the policy requires investments in U.S. Government Obligations or obligations explicitly guaranteed by the U.S. Government to reduce the Authority's related credit risk, custodial credit risk and interest rate risk.

The U.S. Government securities-based money market mutual funds, at June 30, 2005, are rated AAA by the Standards & Poor's Corporation, AAA by Moody's Investor Services, AAA by Duff & Phelps and AAA/V1+ by Fitch IBCA, except for approximately $3,596,000 which are unrated. The Authority's restricted investment in U.S. Government securities-based money market mutual funds totalled approximately $30,840,000 and $17,708,000 at June 30, 2005 and 2004, respectively. The Authority's unrestricted investment in U.S. Government securities-based money market mutual funds totalled approximately $14,867,000 and $4,468,000 at June 30, 2005 and 2004, respectively.

## NOTE C – INVESTMENTS - CONTINUED

Investments at fair value consist of the following at June 30:

| | 2005 | 2004 |
|---|---|---|
| Restricted | | |
| U.S. Government securities-based money market mutual funds | $30,839,522 | $17,708,435 |
| Repurchase agreements | 2,301,305 | 2,721,305 |
| Total restricted investments | 33,140,827 | 20,429,740 |
| Unrestricted | | |
| U.S. Government securities-based money market mutual funds | 14,866,988 | 4,468,166 |
| Total investments | $48,007,815 | $24,897,906 |

## NOTE D - LOANS AND ALLOWANCE FOR LOAN LOSSES

The Authority originates, purchases and holds various types of student loans as described in Note A. The terms of these loans, which vary on an individual basis depending upon loan type and the date the loan was originated, generally provide for repayment in monthly installments of principal and interest over a period of up to 30 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 Stafford 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 2.0% to 11.0% for the fiscal year ended June 30, 2005, depending upon the type and date of origination of the individual loan. Loans consist of the following as of June 30:

| | 2005 | 2004 |
|---|---|---|
| Stafford subsidized | $290,600,103 | $264,159,833 |
| Stafford unsubsidized | 213,877,901 | 191,301,258 |
| PLUS/SLS | 36,520,323 | 32,422,687 |
| Consolidation | 263,332,785 | 195,099,592 |
| SHELF™ | 2,893,016 | 2,871,936 |
| Total gross loans | 807,224,128 | 685,855,306 |
| Unamortized loan premiums and loan origination costs | 12,835,528 | 10,779,007 |
| Unprocessed loan advances and (payments) | 3,120,127 | (500,494) |
| Allowance for loan losses | (5,758,509) | (5,052,215) |
| Net loans | $817,421,274 | $691,081,604 |

## NOTE D - LOANS AND ALLOWANCE FOR LOAN LOSSES - CONTINUED

An analysis of the change in the allowance for loan losses is as follows as of June 30:

| | 2005 | 2004 |
|---|---|---|
| Balances at beginning of year | $5,052,215 | $4,640,668 |
| Loans charged off, net recoveries of $20,094 and $22,783 for 2005 and 2004, respectively | (467,706) | (484,453) |
| Provision for loan losses | 1,174,000 | 896,000 |
| Balance at end of year | $5,758,509 | $5,052,215 |

All FFEL Program student loans are guaranteed as to principal and accrued interest. The Guarantee Agencies are entitled to charge fees for these services, and, if such fees are charged, they are withheld from the loan disbursements to the borrower and remitted to the Guarantee Agencies. The Authority paid the guarantee fees on all loans disbursed when the Guarantee Agencies did not waive those fees during the period from July 1, 1999 through June 30, 2001. Guarantee fees paid by the Authority were capitalized when the loan was made and are amortized over the estimated life of the loan. The capitalized guarantee fees, net of accumulated amortization, at June 30, 2005 and 2004 were approximately $483,000 and $976,000, 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, 2005 and 2004, approximately $226,000 and $268,000, respectively, of loans were no longer guaranteed.

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

The Authority is also required to pay to the 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.

The capitalized loan origination costs, net of accumulated amortization, at June 30, 2005 and 2004 were approximately $1,453,000 and $1,348,000, respectively.

Premiums paid on student loans purchased, net of accumulated amortization, at June 30, 2005 and 2004 were approximately $11,383,000 and $9,431,000, 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 held are in the custody of Bank of Oklahoma, N.A. in its capacity as custodian for the Authority.

## NOTE E - NOTES AND BONDS PAYABLE

The Authority periodically issues notes and bonds 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 Authority is in compliance with all significant financing agreement requirements and bond covenants.

Notes payable at June 30, 2005 and 2004 consist of the following:

$150,000,000 Taxable Variable Rate Revenue Note (line of credit), Series 1993L (1993L), dated March 1, 2005, payable at the offices of JP Morgan Chase Bank, N.A., as administrative agent. The interest rate is adjusted periodically based on a LIBOR index plus 0.5% and is payable on a quarterly basis. The interest rates were 3.77% and 2.38% as of June 30, 2005 and 2004, respectively. The principal is due at maturity on December 15, 2006. 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 3.00% and 1.27% as of June 30, 2005 and 2004, 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 3.20% and 1.75% as of June 30, 2005 and 2004, respectively. The principal is due at maturity on September 1, 2025.

$50,000,000 Senior Notes, Series 2001A-4 (2001A-4) dated December 20, 2001. The interest rate is adjusted quarterly to the three-month financial Commercial Paper Rate with rates of 3.23% and 1.23% as of June 30, 2005 and 2004, respectively. Interest is payable on a quarterly basis. The principal is due at maturity on December 1, 2011.

Interest on the Authority's notes payable is payable on a semi-annual basis unless noted otherwise.

NOTE E - NOTES AND BONDS PAYABLE - CONTINUED

The following schedules summarize the notes payable outstanding as of June 30:

| | 2005 | | | |
|---|---|---|---|---|
| | Beginning balance | Additions | Retirements | Ending balance |
| 1993L | $ 72,300,000 | $15,475,000 | $60,000,000 | $27,775,000 |
| 1995A-1 | 21,600,000 | - | - | 21,600,000 |
| 1995A-2 | 7,000,000 | - | - | 7,000,000 |
| 2001A-4 | 50,000,000 | - | - | 50,000,000 |
| | $150,900,000 | $15,475,000 | $60,000,000 | $106,375,000 |

| | 2004 | | | |
|---|---|---|---|---|
| | Beginning balance | Additions | Retirements | Ending balance |
| 1993L | $ 4,600,000 | $67,700,000 | $ - | $ 72,300,000 |
| 1995A-1 | 21,600,000 | - | - | 21,600,000 |
| 1995A-2 | 7,000,000 | - | - | 7,000,000 |
| 2001A-4 | 50,000,000 | - | - | 50,000,000 |
| | $83,200,000 | $67,700,000 | $ - | $150,900,000 |

The following schedules summarize the bonds payable outstanding as of June 30:

| | 2005 | | | |
|---|---|---|---|---|
| | Beginning balance | Additions | Retirements | Ending balance |
| 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 |

NOTE E - NOTES AND BONDS PAYABLE - CONTINUED

| | 2005 | | | |
|---|---|---|---|---|
| | Beginning balance | Additions | Retirements | Ending balance |
| 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 demand obligations Series 2002A-1, due 12-1-31 | 40,625,000 | - | - | 40,625,000 |
| 5.30% Series, 2003A-1, due 12-1-32 | 9,670,000 | - | - | 9,670,000 |
| Variable rate demand obligations Series 2003A-2, due 12-1-32 | 30,955,000 | - | - | 30,955,000 |
| Variable rate Series 2004A-1, due 12-1-33 | 40,625,000 | - | - | 40,625,000 |
| Variable rate Series 2004A-2, due 6-1-34 | - | 40,625,000 | - | 40,625,000 |
| Senior floating rate Series 2004A-3, due 9-1-34 | - | 100,000,000 | - | 100,000,000 |
| Variable rate demand obligations Series 2005A, due 12-1-34 | - | 65,045,000 | - | 65,045,000 |
| | $507,510,000 | $205,670,000 | $12,975,000 | $700,205,000 |

| | 2004 | | | |
|---|---|---|---|---|
| | Beginning balance | Additions | Retirements | Ending balance |
| 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 |

NOTE E - NOTES AND BONDS PAYABLE - CONTINUED

| | 2005 | | | |
|---|---|---|---|---|
| | Beginning balance | Additions | Retirements | Ending balance |
| 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 demand obligations Series 2002A-1, due 12-1-31 | 40,625,000 | - | - | 40,625,000 |
| 5.30% Series, 2003A-1, due 12-1-32 | 9,670,000 | - | - | 9,670,000 |
| Variable rate demand obligations Series 2003A-2, due 12-1-32 | 30,955,000 | - | - | 30,955,000 |
| Variable rate Series 2004A-1, due 12-1-33 | - | 40,625,000 | - | 40,625,000 |
| | $466,885,000 | $40,625,000 | $ - | $507,510,000 |

NOTE E - NOTES AND BONDS PAYABLE - CONTINUED

The variable interest rates on the Student Loan Revenue Auction Rate Bonds, Series 1994A 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 3.05% and 1.25% as of June 30, 2005 and 2004, respectively. The Series 1994A-2 Bonds are based on a one-year auction period with a rate of 1.85% as of June 30, 2004 and was paid in full during 2005.

The variable rates on the Variable Rate Demand Obligations, Series 1996A are set on a weekly basis by the Remarketing Agent, with a rate of 2.27% and 1.05% as of June 30, 2005 and 2004, respectively.

The variable rates of the Variable Rate Demand Obligations, Series 1997A are set on a weekly basis by the Remarketing Agent, with a rate of 2.34% and 1.10% as of June 30, 2005 and 2004, respectively.

The variable rates on the Variable Rate Demand Obligations, Series 1998A are set on a weekly basis by the Remarketing Agent, with a rate of 2.34% and 1.10% as of June 30, 2005 and 2004, respectively.

The variable interest rates on the Senior Taxable Auction Rate Bonds, Series 2000A-1,2,3 and Variable Rate Demand Obligations, Series 2000A-4 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 3.33%, 3.20% and 3.08% as of June 30, 2005 and 1.45%, 1.40% and 1.32% as of June 30, 2004. Interest is payable on each 28-day auction period. The Series 2000A-4 Bonds are set on a weekly basis by the Remarketing Agent, with a rate of 2.34% and 1.10% as of June 30, 2005 and 2004, respectively.

The variable rates of the Subordinate Auction Rate Obligations, Series 2001B-1 are based on a 35-day auction period with a rate of 3.15% and 1.40% as of June 30, 2005 and 2004, respectively.

The variable rates of the Senior Taxable Auction Rate Bonds, Series 2001A-2 and Series 2001A-3 are based on a 28-day auction rate with rates of 3.23% and 3.25% as of June 30, 2005 and 1.42% and 1.40% as of June 30, 2004 for the Series 2001A-2 and 2001A-3 Bonds, respectively. Interest is payable on each 28-day auction period.

The rates of the Variable Rate Demand Obligations, Series 2002A-1 are set on a weekly basis by the Remarketing Agent, with a rate of 2.34% and 1.10% as of June 30, 2005 and 2004, respectively.

The rates of the Variable Rate Demand Obligations, Series 2003A-2 are set on a weekly basis by the Remarketing Agent, with a rate of 2.34% and 1.10% as of June 30, 2005 and 2004, respectively.

## NOTE E - NOTES AND BONDS PAYABLE - CONTINUED

The variable rates of the Senior Auction Rate Bonds, Series 2004A-1 are based on a 35-day auction period with a rate of 3.30% and 1.32% as of June 30, 2005 and 2004, respectively.

The variable rates of the Senior Auction Rate Bonds, Series 2004A-2 are based on a 35-day auction period with a rate of 2.75% as of June 30, 2005.

The floating rates of the Senior Taxable Bonds, Series 2004A-3 are based on the three-month LIBOR rate plus a spread factor of 0.18% with a rate of 3.50% as of June 30, 2005. Interest is payable on a quarterly basis.

The rates of the Variable Rate Demand Obligations, Series 2005A are set on a weekly basis by the Remarketing Agent, with a rate of 2.34% as of June 30, 2005.

Interest on the Authority's bonds payable is payable on a semi-annual basis unless noted otherwise.

Fiscal year debt service requirements to maturity or redemption date, assuming interest rates on variable rate debt remains at June 30, 2005 levels, are as follows:

| | Principal | Interest | Total |
|---|---|---|---|
| Year ending June 30 | | | |
| 2006 | $ - | $ 23,890,661 | $ 23,890,661 |
| 2007 | 27,775,000 | 24,203,777 | 51,978,777 |
| 2008 | - | 23,714,481 | 23,714,481 |
| 2009 | 8,230,000 | 23,328,596 | 31,558,596 |
| 2010 | - | 23,280,751 | 23,280,751 |
| 2011 - 2015 | 50,000,000 | 86,066,617 | 136,066,617 |
| 2016 - 2020 | - | 83,771,792 | 83,771,792 |
| 2021 - 2025 | 25,200,000 | 80,062,580 | 105,262,580 |
| 2026 - 2030 | 252,205,000 | 66,321,025 | 318,526,025 |
| 2031 - 2035 | 443,170,000 | 39,631,724 | 482,801,724 |
| | $806,580,000 | $474,272,004 | $1,280,852,004 |

## NOTE F - RETIREMENT PLAN

The Authority contributes to the Teachers Retirement System of Oklahoma (the TRS), a cost-sharing multiple-employer public employee retirement system which is self-administered. The 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. 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 the TRS. The TRS issues a publicly available annual financial report that includes financial statements and required supplementary information for the TRS. That annual report may be obtained by writing to the TRS, P. O. Box 53524, Oklahoma City, OK 73152 or by calling 1-405-521-2387.

## NOTE F - RETIREMENT PLAN - CONTINUED

Employees of the Authority, as TRS members, are required to contribute to the plan at a rate set by State Statute (employees' contributions). The contribution rate for TRS members is based on 7% of their covered salary. The Authority made the system members' required contribution on behalf of its employees in 2005 and 2004.

The Authority itself is required to contribute a statutory percentage of participating employees' regular annual compensation for administration of the plan (employer's contributions). In 2005 and 2004, the contribution rate for the Authority was 7.05%. The Authority's total payments to the TRS for the employees' and employer's contributions were approximately $383,000 and $360,000 for the years ended June 30, 2005 and 2004, respectively.

## NOTE G - 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, 2005 and 2004, the Authority was committed to purchase approximately $143,700,000 and $101,906,000, 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 Internal Revenue Service at the maturity of the related debt. The Authority's 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. In previous years, the excess interest estimate had shown an increasing trend, but in 2004 and 2005 the trend had reversed.

USDE issued a ruling on May 15, 2005 that allowed student loan borrowers that were still in school to waive their applicable grace period and consolidate their Stafford loans at historically low interest rates if the consolidation application was post marked or received by the lender on or before June 30, 2005. As a result of this ruling, the Authority had approximately 4,200 consolidation applications for approximately $97,000,000 pending disbursement at June 30, 2005.

## NOTE G - COMMITMENTS AND CONTINGENCIES – CONTINUED

The Authority leases certain facilities and equipment under noncancelable operating leases that expire at various dates through December 2007. Related rent expense for the years ended June 30, 2005 and 2004 was approximately $280,000 and $228,000, respectively. The following is a schedule of future minimum rental payments under operating leases as of June 30, 2005:

| | |
|---|---|
| Year ending June 30 | |
| 2006 | $262,500 |
| 2007 | 245,000 |
| 2008 | 121,000 |
| | $628,500 |

## NOTE H - STUDENT LOAN LEGISLATION

The Higher Education Act (HEA) is the subject of frequent amendments, including amendments by the federal government budget process. In addition, the HEA is subject to reauthorization every six years, and was last updated in 1998. No legislation to reauthorize the HEA was enacted in 2004. Instead, a temporary extension was enacted through September 30, 2005. Although reauthorization bills have been introduced in both the U. S. House of Representatives (House) and the U. S. Senate (Senate), it is expected that there will be no reauthorization of the HEA enacted by September 30, 2005. On September 20, 2005, legislation was passed by the House to extend the provisions of the HEA that are set to expire on September 30, 2005 for three months through December 31, 2005.

The reauthorization bills in the House and the Senate propose various and conflicting changes in the FFEL Program including, among other things: (1) increasing annual loan limits for Stafford loan borrowers; (2) providing for a return to the government of excess interest when the lender rate is lower than the borrower rate; (3) repealing the ability to bill special allowance at the 9.5% floor rate on recycled loans in certain financings; (4) reducing the insurance payment on defaulted loans from 98% to 97% or 96%; (5) repealing the single holder rule, a requirement that borrowers with a single lender consolidate only with that lender; (6) increasing the lender origination fee on consolidation loans from 0.5% to 1.0%; (7) offering consolidation borrowers a choice between the current fixed rate and a variable rate; and (8) reducing, over time, federal origination fees withheld from a borrower's loan proceeds.

It is not possible to predict whether, when or the final content of proposals for reauthorization or any other amendments to the HEA or their effect on the Authority's FFEL Program.

## NOTE I - RELATED PARTIES

Three members of the Authority's Board of Trustees are officers or directors of three lenders in the Authority's student lending network. The following relates to these three lenders:

| | June 30, 2005 | June 30, 2004 |
|---|---|---|
| Loans purchased by the Authority for the year | $30,895,000 | $24,620,000 |
| Loans being serviced at year end | 24,030,000 | 979,000 |

These related party lenders participate in the Authority's student lending network on terms and conditions available to other network lenders similarly situated.

## NOTE J - 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 are summarized as follows at June 30:

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | Carrying amount | Estimated fair value | Carrying amount | Estimated fair value |
| Financial assets | | | | |
| Cash | $ 453,549 | $ 453,549 | $ 179,648 | $ 179,648 |
| Investments | 48,007,815 | 48,007,815 | 24,897,906 | 24,897,906 |
| Interest receivable | 15,535,249 | 15,535,249 | 11,913,574 | 11,913,574 |
| Loans, net | 817,421,274 | 817,421,274 | 691,081,604 | 691,081,604 |
| Financial liabilities | | | | |
| Accrued interest payable | 2,420,993 | 2,420,993 | 1,436,734 | 1,436,734 |
| Notes payable | 106,375,000 | 106,375,000 | 150,900,000 | 150,900,000 |
| Bonds payable | 700,205,000 | 701,951,743 | 507,510,000 | 507,729,000 |

## NOTE J - FAIR VALUE OF FINANCIAL INSTRUMENTS - CONTINUED

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 the USDE.

The carrying value of notes payable approximates fair value for 2005 and 2004 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.

## NOTE K - SUBSEQUENT EVENTS

On August 25, 2005, the Authority entered into a non-revolving, multiple advance 2005B Financing Agreement with a commercial lender for a $100,000,000 tax-exempt line of credit. Under the line of credit, variable rate notes for lump sum advances may be issued from time to time during a commitment period ending on September 1, 2008. If any outstanding notes are not prepaid, the lender has a put option on September 1, 2010 and each year thereafter for redemption of any outstanding notes. Repayment of the notes is non-recourse, it is an obligation of the Authority limited to the collateral pledged to the lender. Withdrawals from the collateral may be made only if the asset coverage ratio will be at least 100% after the withdrawal.

On September 2, 2005, the Authority received a supplemental tax-exempt "cap" allocation from the State of Oklahoma in the amount of $43,692,057. The Authority expects to issue a note in the "cap" allocation amount under the line of credit described in the preceding paragraph. The proceeds from the note will be used by the Authority to provide funds to finance FFEL program loans and to acquire restricted investments.

# Report of Independent Certified Public Accountants 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*

Board of Trustees
Oklahoma Student Loan Authority

We have audited the financial statements of the Oklahoma Student Loan Authority (the Authority) as of and for the year ended June 30, 2005, and have issued our report thereon dated September 21, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America as established by the Auditing Standards Board of the American Institute of Certified Public Accountants 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 Authority'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 assurance on the internal control over financial reporting. Accordingly, we express no such opinion. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving internal controls over financial reporting, which we have reported to management of the Authority in a separate letter dated September 21, 2005.

Compliance and Other Matters
As part of obtaining reasonable assurance about whether the Authority'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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management, the Board of Trustees and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

Grant Thornton LLP

Oklahoma City, Oklahoma
September 21, 2005

Grant Thornton

Grant Thornton LLP
US Member of
Grant Thornton International


Suite 1200
1 Leadership Square
211 N. Robinson
Oklahoma City, OK 73102-7148
T 405.218.2800
F 405.218.2801
W www.grantthornton.com