Vermont Student Assistance Corporation

(A Component Unit of the State of Vermont)

Basic Financial Statements and
Management's Discussion and Analysis

Years Ended June 30, 2008 and 2007

VERMONT STUDENT ASSISTANCE CORPORATION
(A Component Unit of the State of Vermont)

BASIC FINANCIAL STATEMENTS AND MANAGEMENT'S DISCUSSION AND ANALYSIS

Years Ended June 30, 2008 and 2007

TABLE OF CONTENTS

INDEPENDENT AUDITORS' REPORT

The Board of Directors
Vermont Student Assistance Corporation

We have audited the accompanying basic financial statements of the Vermont Student Assistance Corporation, a component unit of the State of Vermont, as of and for the years ended June 30, 2008 and 2007, as listed in the accompanying table of contents. These financial statements are the responsibility of the Vermont Student Assistance Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the Vermont Student Assistance Corporation, as of June 30, 2008 and 2007, and the changes in its financial position 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 October 27, 2008 on our consideration of Vermont Student Assistance Corporation'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 – 10 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 to the 2008 and 2007 information, 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.

Baker Newman & Noyes
Limited Liability Company

Portland, Maine
October 27, 2008

The Vermont Student Assistance Corporation (VSAC or the Corporation) is a public non-profit corporation created by the State of Vermont to provide opportunities for Vermont residents to pursue postsecondary education. VSAC's mission is to ensure that all Vermonters have the necessary financial and informational resources to pursue their educational goals beyond high school. VSAC awards grants and scholarships, and finances, guarantees, originates, and services education loans to students and parents. VSAC also administers student employment programs, and outreach services to students and adults seeking postsecondary education opportunities. In the past, the Corporation contracted with several schools and colleges in Vermont to serve as the financial aid office for the institution. Following changes to the Higher Education Act, this service was phased out during the year ending June 30, 2008. Finally, VSAC manages the Vermont Higher Education Investment Plan.

VSAC administers the State grant program, funded by State appropriations, at no cost to the State. VSAC administers and awards over 156 scholarship funds, including VSAC assisted scholarships and scholarship funds held and managed by VSAC.

VSAC's education loan programs are financed through issuance of limited obligation bonds. Certain education loans are guaranteed by VSAC as a guarantor and/or reinsured by the U.S. Department of Education through the Federal Family Education Loan Program (FFELP). VSAC education loans are available to Vermont students attending both in-state and out-of-state institutions, and to students of Vermont institutions.

VSAC's outreach services are funded through a variety of federal grants, including GEAR UP and Talent Search, as well as through State grants, and general corporate support.

Management's Discussion and Analysis Report includes Fiscal 2008 and Fiscal 2007 information due to the fact that the Financial Statements include Fiscal 2008 and Fiscal 2007 information.

FISCAL 2008

<u>Fiscal 2008 Highlights and Overall Financial Position</u>

- During the year ended June 30, 2008, VSAC had a loss of $14.0 million compared to a surplus of $16.0 million during the year ended June 30, 2007.
- The change in results of VSAC operations was mainly due to capital market liquidity disruptions which caused interest expense to increase $25.8 million.
- VSAC's total net assets decreased $14.0 million to $124.8 million.
- During the year ended June 30, 2008 VSAC provided over $26.3 million in grants and scholarships to Vermont students.
- VSAC originated $477.2 million in student loans, including new loans to students and parents and consolidation of existing loans. VSAC holds $2.10 billion in education loans receivable and related interest at June 30, 2008.
- VSAC returned over $6.7 million in interest and principal rebates to students in its loan programs during fiscal 2008, and paid over $4.4 million in fees on behalf of our borrowers (amortized over the life of the loans).

The Financial Statements

VSAC's financial statements are a series of reports that detail financial information using accounting methods similar to those used by private businesses, especially financial institutions.

The statement of revenues, expenses and changes in net assets presents the results of VSAC's operations. The statement reports all revenues and expenses, and reconciles the beginning and end of year net asset balances.

The statement of net assets includes all the Corporation's assets and liabilities. The statement also presents the balance of assets in excess of liabilities, or net assets.

The statement of cash flows supplements these statements providing relevant information about cash receipts and payments for the Corporation.

The notes to financial statements are an integral part of the financial statements and contain information necessary to get a complete view of VSAC's financial position.

Condensed Financial Information

Statement of Net Assets

	2008	2007
	(In Thousands)	
Assets:		
Cash and investments	$ 93,349	$ 270,109
Education loans receivable (plus interest)	2,103,775	1,895,433
Other assets	34,722	36,015
Total assets	$2,231,846	$2,201,557
Liabilities:		
Bonds and notes payable (plus interest)	$2,068,471	$2,020,066
Arbitrage earnings rebatable	25,390	32,254
Other liabilities	13,140	10,407
Total liabilities	2,107,001	2,062,727
Net assets:		
Restricted	62,302	85,581
Unrestricted	60,068	51,182
Net investment in property and equipment	2,475	2,067
Total net assets	124,845	138,830
Total liabilities and net assets	$2,231,846	$2,201,557

Statement of Revenues and Expenses

	2008	2007
	(In Thousands)	
Revenues:		
Interest earned from education loan financing	$142,286	$147,635
Other loan and guarantee program revenues	5,804	6,537
Investment interest	7,676	10,381
Vermont state appropriations	20,459	18,524
Federal grants	4,867	4,347
Scholarship and gift revenue	3,937	4,598
Other revenue	462	878
Total operating revenues	185,491	192,900
Expenses:		
Student aid	26,345	22,511
Interest rebated to borrowers	6,749	6,074
Interest on debt	100,478	74,653
Other loan financing costs	28,309	38,916
Corporate operating expenses and depreciation	37,595	34,764
Total expenses	199,476	176,918
Excess (deficit) of revenues over expenses	(13,985)	15,982
Total net assets at the beginning of the year	138,830	122,848
Total net assets at the end of the year	$124,845	$138,830

Net Assets

Cash and investment balances decreased from June 30, 2007 to 2008 from $270.1 to $93.3 million. Bonds for fiscal 2008 loan originations were issued in June 2007. The bonds for fiscal 2009 originations were issued in July 2008.

Student loans and interest receivable totaled $2.1 billion at June 30, 2008, up from $1.9 billion in 2007 representing natural growth in the student loan portfolio.

U.S. Treasury arbitrage payable is described in the expense discussion. This liability decreased as of June 30, 2008, to $25.4 million, or approximately 1.1% of total assets. Unrestricted net assets increased from $51.2 million in 2007 to $60.1 million in 2008. The unrestricted funds are used to finance student loans and for corporate working capital. Unrestricted net assets invested in student loans totaled $34.3 million at June 30, 2008.

Restricted net assets decreased from $85.6 million to $62.3 million at June 30, 2008. $58.4 million were restricted by bond resolutions, a decrease in equity within the bond trusts of $21.8 million. The remaining $3.9 million is restricted for scholarships and grants, and for programs to encourage students to pursue higher education.

Revenues

VSAC's fiscal 2008 operations resulted in a decrease in net assets of $14.0 million. All revenues for 2008 are considered operating revenues. VSAC realized $185.5 million in revenues versus $199.5 million in total expenses. VSAC revenues include interest income on student loans, various federal interest subsidies and special allowance payments, State of Vermont appropriations, and fees earned in the federal guarantee program.

Overall loan revenue to VSAC is closely related to the general interest rate environment. During 2008, interest revenue and subsidies decreased from $147.6 to $142.3 million. Interest for certain loans is paid by the U.S. Department of Education as a subsidy to qualifying borrowers. This interest subsidy represented $17.3 million in 2008.

VSAC also receives special allowance payments under certain interest rate conditions. Decreasing interest rates and changes in rules regarding eligibility of certain loans subject to floor rates, partially offset by increases in the overall size of the loan portfolio, resulted in a decrease in special allowance payments from $42.4 million in 2007 to $29.1 million in 2008. Additionally, 2008 was the first full effective year of changes in the Higher Education Act requiring certain student loan interest be returned to the U.S. Department of Education. This change reduced loan revenue in 2008 by $7.1 million.

Interest rate risk on student loan assets is managed by closely matching the coupon rate reset frequency of our debt instruments with rates that drive our loan returns. Our outstanding bond rates are reset on 7, 28 and 35 day intervals. Rates on student loans are reset each quarter and are based on short term commercial paper or LIBOR rates.

Other revenues associated with the loan and loan guarantee programs include consolidation fees, default aversion fees, collections revenues, and other program fees and revenues. Changes to the Higher Education Act effective October 1, 2008 reduced fees paid in the guarantee program. These fees and revenues totaled $5.8 million in 2008 and $6.5 million in 2007.

Interest rates decreased throughout the year resulting in decreased interest revenue on investments. Investments include student loan funds temporarily invested in cash and short term investments, and scholarship funds invested for long-term growth and income. Returns on all investments decreased from $10.4 million to $7.7 million, as interest rates decreased and our total invested funds decreased. The decrease in invested funds is related to the timing of student loan bond issues.

VSAC's regular appropriation increased from $18.5 million to $20.5 million. As in prior years, the State's appropriation for the grant program is used entirely to provide grant funds directly to students. VSAC receives no administrative allowance for administering the State grant program.

Federal grants increased from $4.3 million to $4.8 million in fiscal 2008.

Scholarship revenues, principally restricted gifts and grants, decreased from $4.6 million in 2007 to $3.9 million in 2008.

Expenses

VSAC has four main types of expenses: 1. Student aid, 2. Interest and other costs of debt, 3. Noninterest costs of financing loans, and 4. Costs of operations.

Student Aid – VSAC provided Vermont students with $26.3 million in student aid during fiscal 2008. $20.8 million in grant aid was provided from State appropriations. An additional $5.5 million was made available through various scholarship programs managed by VSAC. Direct aid in the form of grants and scholarships represented 13.2% of VSAC's operating expenses.

While not strictly a student aid expense, interest rebated to borrowers and fees paid on behalf of borrowers are items that help current and former students and parents manage their education debt. VSAC provided $6.7 million in rebates of interest to borrowers and $4.4 million in payment of fees on behalf of borrowers in fiscal 2008. The interest rebates represent 3.4% of VSAC's fiscal 2008 operating expenses.

It is also important to note that, while not an expense to the Corporation, the largest portion of aid to students is the $477.2 million of loans VSAC made available to students and parents in fiscal 2008.

Interest Costs – In order to provide Vermont students and parents with low cost loans, VSAC issues both tax-exempt and taxable variable interest bonds in the public markets. The interest costs of these bonds represent a major expense category for VSAC. The interest rate resets for these bonds are primarily set using an auction process that results in rates closely tracking the SIFMA auction index or one month LIBOR. The general disruption in capital markets and more specific liquidity freeze in the auction bond market negatively impacted VSAC bonds. When the auction process was not successful in resetting rates, the rates were derived using formulas. The formulas use an index (JJ Kenny or short term commercial paper) multiplied by a margin or an average of treasury bills with a margin added to that index. The formulas resulted in higher interest rates during 2008. More significantly, the indices used in these formulae diverged from the indices used in setting our FFEL loan special allowance revenue. The mismatch resulted in significantly higher interest costs without corresponding increases in loan revenue.

With the increase in bond interest rates from fiscal 2007 to 2008, VSAC interest costs rose from $74.7 to $100.5 million. This represented 50.4% of VSAC operating expenses in fiscal 2008 up from 42.2% in 2007.

Other Loan Financing Costs – Other expenses incurred in the loan financing area include credit enhancement and remarketing fees for our bond issues, consolidation and lender fees VSAC pays to the federal government, provisions for changes in arbitrage earnings liability to the U.S Treasury, and increases in VSAC's provision for uninsured loan losses, as well as a variety of other costs incurred in issuing and managing over $2.1 billion in outstanding bonds and notes. These costs totaled $28.3 million in fiscal 2008, representing approximately 14.2% of total operating expenses. Changes in these financing costs from year to year are principally due to changes in the total outstanding indebtedness, and by changes in arbitrage liability. Arbitrage liability represents earnings on tax exempt bond-financed loans and investments that would be returned to the U.S. Treasury if the loan portfolios were completely liquidated at June 30, and all bondholders were repaid. It represents earnings to date, and is a function of past and current interest rates on debt and assets held by VSAC. It is fairly volatile and is managed to minimize the probability of a liability balance at the end of a bond life cycle.

In fiscal 2008, VSAC's provision for losses on student loans was $11.8 million compared to $8.5 million in fiscal 2007.

Costs of Operations – The costs of operating VSAC's programs, as well as facilities and overhead costs totaled $37.6 million in fiscal 2008, an increase of approximately 8.1% from fiscal 2007. Salaries and benefits were $25.9 million in fiscal 2008, approximately 68.9% of costs of operations. Overall costs of operations represent 18.8% of total operating expenses.

Total expenses for 2008 totaled $199.5 million. Revenues totaled $185.5 million. The excess of expenses over revenues was $14.0 million. The change in total net assets for the year was a decrease of $14.0 million. The ending balance of net assets at June 30, 2008 was $124.8 million, as compared to $138.8 million at June 30, 2007.

FISCAL 2007

Fiscal 2007 Highlights and Overall Financial Position

- During the year ended June 30, 2007 VSAC provided over $22.5 million in grants and scholarships to Vermont students.
- VSAC originated over $620.7 million in student loans, including new loans to students and parents and consolidation of existing loans. VSAC holds $1.90 billion in education loans receivable at June 30, 2007.
- VSAC returned over $6.0 million in interest and principal rebates to students in its loan programs during fiscal 2007, and paid over $4.6 million in fees on behalf of our borrowers (amortized over the life of the loans).
- VSAC's total net assets increased $16 million to $138.8 million.

The Financial Statements

VSAC's financial statements are a series of reports that detail financial information using accounting methods similar to those used by private businesses, especially financial institutions.

The statement of revenues, expenses and changes in net assets presents the results of VSAC's operations. The statement reports all revenues and expenses, and reconciles the beginning and end of year net asset balances.

The statement of net assets includes all the Corporation's assets and liabilities. The statement also presents the balance of assets in excess of liabilities, or net assets.

The statement of cash flows supplements these statements providing relevant information about cash receipts and payments for the Corporation.

The notes to financial statements are an integral part of the financial statements and contain information necessary to get a complete view of VSAC's financial position.

Condensed Financial Information

Statement of Net Assets

	2007	2006
	(In Thousands)	
Assets:		
Cash and investments	$ 270,109	$ 152,208
Education loans receivable (plus interest)	1,895,433	1,670,870
Other assets	36,015	35,857
Total assets	$ 2,201,557	$ 1,858,935
Liabilities:		
Bonds and notes payable (plus interest)	$ 2,020,066	$1,705,825
Arbitrage earnings rebatable	32,254	23,525
Other liabilities	10,407	6,737
Total liabilities	2,062,727	1,736,087
Net assets:		
Restricted	85,581	69,951
Unrestricted	51,182	50,786
Net investment in property and equipment	2,067	2,111
Total net assets	138,830	122,848
Total liabilities and net assets	$ 2,201,557	$ 1,858,935

Statement of Revenues and Expenses

	2007	2006
	(In Thousands)	
Revenues:		
Interest earned from education loan financing	$147,635	$127,519
Other loan and guarantee program revenues	6,537	5,155
Investment interest	10,381	9,414
Vermont state appropriations	18,524	18,763
Federal grants	4,347	3,841
Scholarship and gift revenue	4,598	4,109
Other revenue	878	1,087
Total operating revenues	192,900	169,888
Expenses:		
Student aid	22,511	23,429
Interest rebated to borrowers	6,074	6,561
Interest on debt	74,653	56,371
Other loan financing costs	38,916	35,538
Corporate operating expenses and depreciation	34,764	32,985
Total expenses	176,918	154,884
Excess of revenues over expenses	15,982	15,004
Total net assets at the beginning of the year	122,848	107,844
Total net assets at the end of the year	$138,830	$122,848

Net Assets

Cash and investment balances increased from June 30, 2006 to 2007 from $152.2 to $270.1 million. Bonds for fiscal 2008 loan originations were issued in June 2007. The bonds for fiscal 2007 originations were issued in July 2006.

Student loans and interest receivable totaled $1.9 billion at June 30, 2007, up from $1.7 billion in 2006.

U.S. Treasury arbitrage payable is described in the expense discussion. This liability increased as of June 30, 2007, to $32.3 million, or approximately 1.4% of total assets. Unrestricted net assets increased from $50.8 million in 2006 to $51.2 million in 2007. The unrestricted funds are used to finance student loans and for corporate working capital. Unrestricted net assets invested in student loans totaled $42.6 million at June 30, 2007.

Restricted net assets increased from $70.0 million to $85.6 million at June 30, 2007. $80.2 million were restricted by bond resolutions, an increase in equity within the bond estates of $13.6 million. The remaining $5.4 million is restricted for scholarships and grants, and for programs to encourage students to pursue higher education.

Revenues

VSAC's fiscal 2007 operations resulted in an increase in net assets of $16.0 million. All revenues for 2007 are considered operating revenues. VSAC realized $192.9 million in revenues versus $176.9 million in total expenses. VSAC revenues include interest income on student loans, as well as various federal interest subsidies and special allowance payments.

Overall loan revenue to VSAC is closely related to the general interest rate environment. During 2007, interest revenue and subsidies increased from $127.5 to $147.6 million. Interest for certain loans is paid by the U.S. Department of Education as a subsidy to qualifying borrowers. This interest subsidy represented $15.2 million in 2007. VSAC also receives special allowance payments under certain interest rate conditions. Increasing interest rates and loan portfolio growth during 2007, offset by changes in rules regarding eligibility of certain loans subject to floor rates resulted in a decrease in special allowance payments from $45.4 million in 2006 to $42.4 million in 2007.

Interest rate risk on student loan assets is managed by closely matching the coupon rate reset frequency of our debt instruments with rates that drive our loan returns. Our outstanding bond rates are reset on 7, 28 and 35 day intervals. Rates on student loans are reset each quarter and are based on short term commercial paper or LIBOR rates. Thus, the net spread on loans carries minimal interest rate risk.

Other revenues associated with the loan and loan guarantee programs include consolidation fees, default aversion fees, collections revenues, and other program fees and revenues. These fees and revenues totaled $6.5 million in 2007 and $5.2 million in 2006.

Rising interest rates resulted in increasing interest revenue on investments. Investments include student loan funds temporarily invested in cash and short term investments, and scholarship funds invested for long-term growth and income. Interest on all investments increased from $9.4 million to $10.4 million, as interest rates increased and our total invested funds increased. The increase in invested funds is related to the timing of student loan bond issues.

VSAC's regular appropriation decreased from $18.7 million to $18.5 million. As in prior years, the State's appropriation for the grant program is used entirely to provide grant funds directly to students. VSAC receives no administrative allowance for administering the State grant program.

Federal grants increased from $3.8 million to $4.3 million in fiscal 2007.

Scholarship revenues, principally restricted gifts and grants, increased from $4.1 million in 2006 to $4.6 million in 2007.

Expenses

VSAC has four main types of expenses: 1. Student aid, 2. Interest and other costs of debt, 3. Noninterest costs of financing loans, and 4. Costs of operations.

Student Aid – VSAC provided Vermont students with $22.5 million in student aid during fiscal 2007. $18.5 million in grant aid was provided from State appropriations. An additional $4.6 million was made available through various scholarship programs managed by VSAC. Direct aid in the form of grants and scholarships represented 12.7% of VSAC's operating expenses.

While not strictly a student aid expense, interest rebated to borrowers is an item that helps current and former students and parents manage their education debt. VSAC provided $6.1 million in rebates of interest to borrowers in fiscal 2007. VSAC has not been able to provide the level of borrower benefits on consolidation loans that it has on other underlying FFELP loans, since VSAC is required to pay a 1.05% annual fee to the Department of Education on consolidated loans. The decrease in interest rebated to borrowers from 2006 to 2007 is primarily the result of the continuing shift from Stafford and PLUS loans to consolidation loans in our portfolio. These rebates represent 3.4% of VSAC's fiscal 2007 operating expenses.

It is also important to note that, while not an expense to the Corporation, the largest portion of aid to students is the $620.7 million of loans VSAC made available to students and parents in fiscal 2007.

Interest Costs – In order to provide Vermont students and parents with low cost loans, VSAC issues both tax-exempt and taxable bonds in the public markets. The interest costs of these bonds represent a major expense category for VSAC. Since all bonds issued to finance loans are variable rate securities, interest costs vary from year to year as the general interest rate environment changes. The variable nature of these securities matches the variable rate structure of most of our loans, so revenues and expenses related to the bonds are highly correlated.

With the increase in interest rates from fiscal 2006 to 2007, VSAC interest costs rose from $56.4 to $74.7 million. This represented 42.0% of VSAC operating expenses in fiscal 2007.

Other Loan Financing Costs – Other expenses incurred in the loan financing area include credit enhancement and remarketing fees for our bond issues, consolidation and lender fees VSAC pays to the federal government, provisions for changes in arbitrage earnings liability to the U.S Treasury, and increases in VSAC's provision for uninsured loan losses, as well as a variety of other costs incurred in issuing and managing over $2.0 billion in outstanding bonds and notes. These costs totaled $38.9 million in fiscal 2007, representing approximately 21.9% of total operating expenses. Changes in these financing costs from year to year are principally due to changes in the total outstanding indebtedness, and by changes in arbitrage liability. Arbitrage liability represents earnings on tax exempt bond-financed loans and investments that would be returned to the U.S. Treasury if the loan portfolios were completely liquidated at June 30, and all bondholders were repaid. It represents earnings to date, and is a function of past and current interest rates on debt and assets held by VSAC. It is fairly volatile and is managed to minimize the probability of a liability balance at the end of a bond life cycle.

In fiscal 2007, VSAC's provision for losses on student loans was $8.5 million compared to $10.7 million in fiscal 2006.

Costs of Operations – The costs of operating VSAC's programs, as well as facilities and overhead costs totaled $34.8 million in fiscal 2007, an increase of approximately 5.4% from fiscal 2006. Salaries and benefits were $24.3 million in fiscal 2007, approximately 70% of costs of operations. Overall costs of operations represent 19.6% of total operating expenses.

Total expenses for 2007 totaled $176.9 million. Revenues totaled $192.9 million. The excess of revenues over expenses was $16.0 million. The change in total net assets for the year was an increase of $16.0 million. The ending balance of net assets was $138.8 million, as compared to $122.8 million at June 30, 2006.

VERMONT STUDENT ASSISTANCE CORPORATION
(A Component Unit of the State of Vermont)

STATEMENTS OF NET ASSETS

June 30, 2008 and 2007

ASSETS

	2008	2007
	(In Thousands)	
Current assets:		
Cash and cash equivalents	$ 90,587	$ 267,058
Investments	2,762	3,051
Receivables:		
Student loans, net	142,177	126,260
Student loan interest and special allowance	55,255	54,979
Investment interest	215	777
Federal administrative and program fees	440	567
Other	869	1,198
Other assets	1,634	1,526
Total current assets	293,939	455,416
Noncurrent assets:		
Receivables:		
Student loans, net	1,906,343	1,714,194
Capital assets, net	22,287	22,628
Deferred bond issuance costs, net	9,277	9,319
Total noncurrent assets	1,937,907	1,746,141
Total assets	$2,231,846	$2,201,557

LIABILITIES AND NET ASSETS

	2008	2007
	(In Thousands)	
Current liabilities:		
Bonds payable	$ 1,670	$ 41,655
Accounts payable and other liabilities	6,809	5,257
Deferred revenue	6,331	5,150
Accrued interest on bonds payable	2,506	3,746
U.S. Treasury rebates payable	–	547
Total current liabilities	17,316	56,355
Noncurrent liabilities:		
Bonds payable	2,064,295	1,974,665
U.S. Treasury rebates payable	25,390	31,707
Total noncurrent liabilities	2,089,685	2,006,372
Total liabilities	2,107,001	2,062,727
Net assets:		
Invested in capital assets, net of related debt	2,475	2,067
Restricted	62,302	85,581
Unrestricted	60,068	51,182
Total net assets	124,845	138,830
Total liabilities and net assets	$2,231,846	$2,201,557

See accompanying notes to the financial statements.

VERMONT STUDENT ASSISTANCE CORPORATION
(A Component Unit of the State of Vermont)

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

Years Ended June 30, 2008 and 2007

	2008	2007
	(In Thousands)	
Operating revenues:		
Interest and fees on student loans:		
U.S. Department of Education interest benefits	$ 17,324	$ 15,161
U.S. Department of Education special allowance	29,059	42,664
Borrower interest and fees on student loans	102,957	90,113
Borrower interest returned to Department of Education	(7,054)	(303)
Vermont state appropriations	20,459	18,524
Interest on cash and investments	7,676	10,381
Guarantee agency administrative revenues	5,804	6,537
Federal grants	4,867	4,347
Scholarship and gift income	3,937	4,598
Other income	462	878
Total operating revenues	185,491	192,900
Operating expenses:		
Interest, net of amortization	100,478	74,653
Salaries and benefits	25,895	24,324
Grants and scholarships	26,345	22,511
Interest rebated to borrowers	6,749	6,074
Other general and administrative	10,233	8,788
Interest subject to U.S. Treasury rebate	(6,529)	8,933
Credit enhancement and remarketing fees	5,917	5,443
Consolidation and lender paid fees	14,536	14,344
Other loan related expenses	1,613	1,361
Provision for losses on student loans	11,848	8,502
Depreciation and amortization	1,467	1,652
Amortization of bond issuance costs	924	333
Total operating expenses	199,476	176,918
(Deficiency) excess of operating revenues over operating expenses	(13,985)	15,982
Net assets, beginning of year	138,830	122,848
Net assets, end of year	$124,845	$138,830

See accompanying notes to the financial statements.

VERMONT STUDENT ASSISTANCE CORPORATION
(A Component Unit of the State of Vermont)

STATEMENTS OF CASH FLOWS

Years Ended June 30, 2008 and 2007

	2008	2007
	(In Thousands)	
Cash flows from operating activities:		
Cash received from customers, donors and governments	$ 74,018	$ 76,813
Principal payments received on student loans	260,360	404,830
Cash paid to suppliers for goods and services	(43,133)	(41,907)
Grants and scholarship disbursements	(26,345)	(22,511)
Loans made and purchased	(477,158)	(620,741)
Cash paid to employees for salaries and benefits	(25,895)	(24,121)
Interest and fees received on student loans	86,141	78,020
Vermont state appropriations received	20,459	18,457
Net cash used in operating activities	(131,553)	(131,160)
Cash flows from noncapital financing activities:		
Proceeds from the sale of bonds	211,485	314,150
Payments on bonds	(161,285)	–
Interest paid to bond holders	(100,557)	(72,850)
Net cash (used) provided by noncapital financing activities	(50,357)	241,300
Cash flows from capital and related financing activities:		
Payments on bonds payable	(755)	(735)
Interest paid to bond holders	(961)	(977)
Acquisition and construction of fixed assets	(1,117)	(878)
Net cash used by capital and related financing activities	(2,833)	(2,590)
Cash flows from investing activities:		
Interest received on cash and investments	8,238	10,176
Purchase of investments, net	34	(1,709)
Net cash provided by investing activities	8,272	8,467
Net (decrease) increase in cash and cash equivalents	(176,471)	116,017
Cash and cash equivalents, beginning of year	267,058	151,041
Cash and cash equivalents, end of year	$ 90,587	$ 267,058

	2008	2007
	(In Thousands)	
Reconciliation of operating income to net cash used in operating activities:		
(Deficiency) excess of operating revenues over operating expenses	$ (13,985)	$ 15,982
Adjustments to reconcile the (deficiency) excess of operating revenues over operating expenses to net cash used in operating activities:		
Depreciation and amortization	1,467	1,652
Provision for losses on student loans	11,848	8,502
Amortization of loan origination fees, net	728	(145)
Amortization of bond issuance costs	924	333
Accretion of bond discount	200	200
Unrealized loss (gain) on investments	255	(175)
Loss on disposal of fixed assets	(9)	–
Investment interest received	(8,238)	(10,176)
Interest paid to bond holders	101,518	73,827
Changes in operating assets and liabilities:		
Investment interest receivable	562	(206)
Student loans receivable	(220,642)	(219,677)
Student loan interest receivable	(276)	(13,243)
Federal administrative and program fees receivable	127	(457)
Other receivables	329	1,013
Other assets	(108)	46
Deferred bond issuance costs	(881)	(1,661)
Accounts payable and other liabilities	1,551	606
Deferred revenue	1,181	3,064
Accrued interest on bonds payable	(1,240)	626
U.S. Treasury rebates payable	(6,864)	8,729
Total adjustments	(117,568)	(147,142)
Net cash used in operating activities	$(131,553)	$(131,160)

See accompanying notes to the financial statements.

VERMONT STUDENT ASSISTANCE CORPORATION
(A Component Unit of the State of Vermont)

STATEMENTS OF FIDUCIARY NET ASSETS

AGENCY FUNDS

June 30, 2008 and 2007

	Federal Loan Reserve Fund	VHEIP	2008 Total	2007 Total
	(In Thousands)			
ASSETS HELD FOR OTHERS				
Cash and cash equivalents	$12,262	$ 1,335	$ 13,597	$11,996
Investments	–	83,933	83,933	71,412
Student loans receivable and accrued student loan interest	–	7,451	7,451	5,633
Investment interest receivable	20	48	68	70
Due from U.S. Department of Education	2,071	–	2,071	1,873
Other assets	64	79	143	367
Total assets	$14,417	$92,846	$107,263	$91,351
LIABILITIES				
Accounts payable and other liabilities	$ 513	$ 202	$ 715	$ 914
Note payable	–	7,836	7,836	5,807
Federal advances	538	–	538	538
Amounts held on behalf of investors	–	84,808	84,808	72,393
Return of reserves due to U.S. Department of Education	–	–	–	276
Federal loan reserve funds held for U.S. Department of Education	13,366	–	13,366	11,423
Total liabilities	$14,417	$92,846	$107,263	$91,351

See accompanying notes to the financial statements.

1. Authorizing Legislation

The Vermont Student Assistance Corporation ("VSAC") was created as a public non-profit corporation by an act of the General Assembly of the State of Vermont in accordance with the provisions of the Higher Education Act of 1965, as amended ("the Act"). The purpose of VSAC is to provide opportunities for Vermont residents to pursue postsecondary education by awarding grants and guaranteeing, making, financing, and servicing loans to students. VSAC also administers scholarships, student employment programs, and outreach services to students seeking postsecondary education. In addition, VSAC manages the Vermont Higher Education Investment Plan (VHEIP).

Pursuant to Vermont statutes, VSAC is responsible for the administration of the Loan Finance Program. Under this program, VSAC originates, purchases, services and consolidates education loans. The majority of education loans are financed through the issuance of limited obligation bonds and are guaranteed by VSAC as a guarantor and reinsured by the U.S. Department of Education (DE) through the Federal Family Education Loan (FFEL) Program. The bonds and notes outstanding are payable primarily from interest and principal repayments on the financed loans as specified in the underlying resolutions authorizing the sale of the bonds and notes. The bonds and notes are not a general obligation of VSAC or an obligation of the State of Vermont or any of its political subdivisions.

For financial reporting purposes, VSAC is considered a component unit of the State of Vermont and is included as part of the State's financial reporting entity. VSAC's relationship with the State of Vermont primarily consists of an annual appropriation designated for grant aid to Vermont students.

The Vermont Student Development Fund, Inc. (the "Fund"), a separate non-profit 501(c)(3) corporation, was established in November of 2000. The primary purpose of the Fund is to receive, hold and manage securities, cash or other property whether real, personal or mixed, acquired by bequest, devise, gift, purchase or loan. These assets are used primarily for scholarships and other financial assistance to benefit qualified individuals seeking a postsecondary education. The Fund provides a financial benefit to VSAC, and its Board of Directors is the same as the VSAC Board of Directors, therefore, it is considered a component unit of VSAC and is included in the totals on the financial statements.

2. Summary of Significant Accounting Policies

Basis of Accounting

VSAC follows the accrual basis of accounting whereby revenues are recorded when earned and expenses are recorded when obligation for payment is incurred.

2. Summary of Significant Accounting Policies (Continued)

As permitted by Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Activities that Use Proprietary Fund Accounting*, VSAC applies all applicable Governmental Accounting Standards Board (GASB) pronouncements as well as all Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989, to the extent these pronouncements do not conflict with GASB pronouncements.

The financial statements are prepared in accordance with Governmental Accounting Standards Board Statements No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, No. 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus – an amendment of GASB Statements No. 21 and 34*, and No. 38, *Certain Financial Statement Note Disclosures*. VSAC reports as a business-type activity, as defined, in GASB No. 34.

Restrictions on Net Assets

The restricted net assets of VSAC are restricted by the bond resolutions, state statutes, donor restrictions, or various Federal regulations and program agreements and are restricted for the origination of student loans, payment of debt service on bonds and notes payable, and grant and scholarship activities. Financial activities and resulting account balances which are not so restricted are presented in the Statements of Net Assets as unrestricted net assets. VSAC's unrestricted net assets are generally reserved for educational assistance purposes.

Management Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires VSAC management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The most significant estimates utilized in the preparation of the financial statements of VSAC relate to the allowance for losses on student loans and the U.S. Treasury rebates payable.

Student Loans

Student loans consist of guaranteed and nonguaranteed loans made to undergraduate, graduate, or professional students, and parents of students attending eligible postsecondary educational institutions. Student loans also include consolidation loans which are loans to eligible students that refinance existing student loans.

2. Summary of Significant Accounting Policies (Continued)

Student loans are stated at their unpaid principal balance net of allowances for loan losses and deferred loan origination fees, net of costs. Loan origination fees received and fees paid by the corporation on behalf of borrowers are deferred and amortized over the estimated life of the loan using a method that approximates the level yield method.

Allowance for Loan Losses

VSAC issues loans that are either guaranteed by VSAC, as guarantor under the FFEL Program, or that carry no guarantee against default. Loans not guaranteed create the greatest loss exposure for VSAC and make up the majority of management's loan loss allowance. The amount of the allowance, which is established through a provision for losses on student loans charged to expense, is based on management's estimation of the probable losses within the portfolio. Primary considerations in establishing the allowance are the amounts of loans in the portfolio, loss rate, delinquencies, current economic conditions and historical loss experience. The loss exposure for nonguaranteed loans is 100 percent of estimated defaults. For guaranteed loans, the loss exposures are either 2 percent or 3 percent of estimated defaults based on the origination date of the loan.

Operating Revenue and Expenses

Operating revenues include interest earned on student loans and investments, fees received from providing services, state appropriations, and grant and scholarship revenue. Operating expenses include interest on bonds, the costs of providing services and operating all programs, and grant and scholarship awards.

Cash Equivalents

VSAC considers all highly liquid investments with original maturities of three months or less to be cash equivalents. Cash equivalents include funds held in an institutional money market fund account.

Investments

Investments are carried at fair value in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools.*

VSAC invests in various investment securities. Investment securities are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the financial statements.

2. Summary of Significant Accounting Policies (Continued)

Capital Assets

Capital assets are stated at historical cost. Depreciation of capital assets that are placed in service is calculated using the straight-line method over the estimated useful lives of the assets. Capital asset acquisitions that equal or exceed $2.5 are capitalized.

Bond Issuance Costs

Costs of bond issuances, which are comprised of underwriters' fees, legal fees and other related financing costs, are deferred and amortized over the lives of the respective bond issues using the straight-line method.

Bond Discount and Deferred Loss on Refunding

Bond discounts are amortized using a method which approximates the level yield method over the life of the bonds. Any unamortized deferred loss related to refunded bonds is deferred and amortized over the life of the original or refunded bonds, whichever is shorter.

Grants

Unrestricted grants are recorded as revenue when received. Restricted grants are recorded as revenue upon compliance with the restrictions. Amounts received for grant programs that are restricted are recorded in deferred revenue until they become unrestricted.

FFEL Program Support

VSAC receives a percentage of the amounts collected on defaulted loans, an origination fee, a portfolio maintenance fee and a default aversion fee from DE as its primary support for the administration of the FFEL Program. These fees are recorded as guarantee agency administrative revenues when earned, as the services are provided.

Compensated Absences

Employees may accumulate, subject to certain limitations, unused vacation earned and upon retirement, termination or death, may be compensated for certain amounts at their then current rates of pay. The amount of vacation recognized as expense is the amount earned and this obligation is accrued.

(Dollars in Thousands)

2. Summary of Significant Accounting Policies (Continued)

Income Tax Status

VSAC is exempt from Federal and state income taxes under Section 115 of the Internal Revenue Code and, accordingly, no provision for income taxes has been made in the accompanying financial statements.

3. Cash, Cash Equivalents and Investments

VSAC's deposit and investment policy complies with the underlying bond resolution requirements. In accordance with those bond resolutions, all deposits and investments meet the requirements and approval of the letter of credit and bond insurance providers. Additionally, such requirements mandate specific classes of investment vehicles including: bank time deposits, certificates of deposit, direct obligations of the United States of America unconditionally guaranteed by the United States of America, indebtedness issued by certain Federal agencies, collateralized repurchase agreements secured by obligations of the United States of America with collateral held by or at the direction of the trustee, guaranteed investment contracts with banks or bank holding companies, commercial paper and open ended investment funds. Funds not related to the various bond resolutions may also be invested in domestic equities or corporate bonds.

Cash and Cash Equivalents

The carrying amounts which represent both cost and fair value of cash and cash equivalents as of June 30, 2008 and 2007 are presented below:

	2008	2007
Cash and repurchase agreements	$ 5,360	$ 7,822
Money market accounts	85,227	259,236
	$ 90,587	$267,058

At June 30, 2008 and 2007, cash and repurchase agreements are comprised of various bank accounts and principal cash held by a bank trust department. The bank balances at June 30, 2008 were $ 6,268 and the bank balances at June 30, 2007 were $8,996. The difference between the net bank balances and the amounts recorded on the financial statements is outstanding checks and deposits in transit. Additionally, $5,074 and $8,198 of the bank balances at June 30, 2008 and 2007, respectively, were covered by Federal depository insurance or collateralized by repurchase agreements for which the securities are held by the bank's trustee in VSAC's name. The remainder of bank balances of $1,194 and $798 at June 30, 2008 and 2007, respectively, were uninsured and uncollateralized.

(Dollars in Thousands)

3. Cash, Cash Equivalents and Investments (Continued)

At June 30, 2008 and 2007, the money market accounts are primarily invested in the Federated Prime Cash Obligations Fund. The Fund objective is to provide current income consistent with stability of principal and liquidity. The Prime Cash Obligations Fund invests primarily in a portfolio of short-term, high quality fixed income securities insured by banks, corporations and the U.S. Government. The underlying assets are not held in the name of VSAC.

A significant portion of cash and cash equivalents are limited to their use for the repayment of bond and note obligations, and to satisfy certain reserve requirements specified by the bond and note indentures.

Investments

VSAC held the following investments at June 30, 2008 and 2007:

	2008		2007	
	Cost	Fair Value	Cost	Fair Value
Domestic equities	$ 2,063	$ 1,967	$ 1,804	$ 2,004
Corporate bonds	534	537	647	641
U.S. Government bonds	255	258	409	406
	$ 2,852	$ 2,762	$ 2,860	$ 3,051

At June 30, 2008, the ratings for investments in debt securities are summarized as follows:

Investment		Maturities	Fair Value	Standard & Poor's Rating
Corporate bonds:				
Bankamerica Corp	7.125%	3/1/2009	20	AA-
Boeing Cap Corp	4.750%	8/25/2008	40	A+
Caterpiller Fin Crp	4.250%	12/1/2010	24	A
Conoco Funding Co	6.350%	10/15/2011	37	A
Costco Wholesale Corp	5.300%	3/15/2012	26	A
FPL Group Cap Inc	7.375%	6/1/2009	21	A-
General Dynamics	4.500%	8/15/2010	26	A
Gen Elec Cap Crp	4.875%	10/21/2010	25	AAA
Goldman Sachs Group	6.875%	1/15/2011	26	AA-
Honeywell Int'l	4.250%	3/1/2013	25	A
Household Fin Co	6.375%	10/15/2011	15	AA-
IBM Corp	5.375%	2/1/2009	20	A+

(Dollars in Thousands)

3. Cash, Cash Equivalents and Investments (Continued)

Investment		Maturities	Fair Value	Standard & Poor's Rating
JP Morgan Chase	5.715%	6/28/2009	21	AA-
Lehman Bros Hldgs	7.875%	11/1/2009	19	A
Occidental Petroleum	6.750%	1/15/2012	27	A
Quebec Prov	6.125%	1/22/2011	26	A+
SBC Communications	5.300%	11/15/2010	26	A
Target Corp	5.400%	10/1/2008	20	A+
Texaco Capital	5.500%	1/15/2009	20	AA
United Tech Corp	6.100%	5/15/2012	48	A
Wells Fargo & Co	5.125%	9/1/2012	25	AA
			537	
U.S. Government bonds:				
Tenn Valley Auth	5.625%	1/18/2011	26	AAA
U.S. Treasury Bonds	5.500%	5/15/2009	26	
U.S. Treasury Bonds	6.000%	8/15/2009	26	
U.S. Treasury Bonds	6.500%	2/15/2010	27	
U.S. Treasury Bonds	5.750%	8/15/2010	27	
U.S. Treasury Note	5.000%	7/31/2008	25	
U.S. Treasury Note	4.875%	1/31/2009	25	
U.S. Treasury Note	4.500%	2/15/2009	25	
U.S. Treasury Note	4.500%	3/31/2009	25	
U.S. Treasury Note	4.875%	6/30/2009	26	
			258	

Interest Rate Risk: Through its investment policy, VSAC manages its interest rate risk by establishing a target range of 10% to 55% of its investments in fixed rate securities. VSAC's current investment manager works with a target of 30% of investments in fixed rate securities with a target duration of no greater than three years.

Credit Risk: VSAC minimizes its credit risk by requiring marketable bonds, debentures, notes, or instruments to be rated BBB or better by Standard and Poor's and Baa or better by Moody's Investors Service.

(Dollars in Thousands)

3. Cash, Cash Equivalents and Investments (Continued)

Concentration of Credit Risk: VSAC places no limit on the amount of investments in any one issuer. However, VSAC's investment manager is currently instructed to invest approximately 70% of the total portfolio in equity issues, balanced between growth and value styles, biased toward large and mid-cap. As of June 30, 2008 and 2007, 9% and 13%, respectively, of VSAC's investments were invested in U.S. Treasuries. No other single issuer represented more than 5% of VSAC's investments at either June 30, 2008 or 2007

Custodial Credit Risk

All of the investments are held by VSAC's agent in VSAC's name.

4. Student Loans Receivable

At June 30, 2008, VSAC held student loans with interest rates ranging from 2.875% to 12%; the majority are insured by DE and the U.S. Department of Health and Human Services. There are certain student loans that are not guaranteed. Most of VSAC's borrowers are located in the New England states.

Student loans are classified as being in "interim" status during the period from the date the loan is made until a student is out of school either for six or nine months. Subsequent to this period, student loans are classified as being in "repayment" status. "Deferral" status is a period during the life of the loan when repayment is suspended for authorized purposes.

Student loans receivable as of June 30, 2008 and 2007 are summarized as follows:

	2008	2007
Status:		
Interim status	$ 436,510	$ 387,861
Deferral status	324,728	310,029
Repayment status	1,315,862	1,170,425
Less: Allowance for loan losses	(29,822)	(25,987)
Deferred origination fees, net	(5,049)	(5,587)
Plus: Deferred fees paid on borrowers behalf	6,291	3,713
Total student loans receivable	2,048,520	1,840,454
Less: noncurrent student loans receivable	1,906,343	1,714,194
Current student loans receivable	$ 142,177	$ 126,260

(Dollars in Thousands)

4. Student Loans Receivable (Continued)

	2008	2007
Guarantee type:		
U.S. Department of Education	$1,765,999	$1,591,414
U.S. Department of Health and Human Services	10,163	11,810
Other – Guaranteed	36,470	30,688
Nonguaranteed	264,468	234,403
Less: Allowance for loan losses	(29,822)	(25,987)
Deferred origination fees, net	(5,049)	(5,587)
Plus: Deferred fees paid on borrowers behalf	6,291	3,713
Total student loans receivable	2,048,520	1,840,454
Less: noncurrent student loans receivable	1,906,343	1,714,194
Current student loans receivable	$ 142,177	$ 126,260

$2,042,126 and $1,824,999 of student loans were pledged to the repayment of bonds as of June 30, 2008 and 2007 respectively.

Transactions in the allowance for loan losses for the years ended June 30, 2008 and 2007 were as follows:

	2008	2007
Balance July 1	$25,987	$21,265
Net loans charged off	(8,013)	(3,780)
Provision for losses on student loans	11,848	8,502
Balance June 30	$29,822	$25,987

The allowance for loan losses represents management's estimate of probable losses on student loans. Management uses the amounts of loans in the portfolio, loss rate, delinquencies, current economic conditions, and historical loss experience. Should any of these factors change significantly from those currently used by management, the estimate will change.

(Dollars in Thousands)

5. Net Assets Held for the U.S. Department of Education

Under the Higher Education Act Amendments of 1998, all assets related to the FFEL Program guaranty functions were transferred to the Federal Loan Reserve Fund on October 1, 1998. The Federal Loan Reserve Fund is administered by VSAC on behalf of DE and is the property of the Federal government. VSAC also established the Guarantee Agency Operating Fund on October 1, 1998, in accordance with the Higher Education Act Amendments of 1998. The Guarantee Agency Operating Fund, which is included within the Statements of Net Assets, is the property of VSAC and is used to account for the activities under the FFEL Program that fall outside of the Federal Loan Reserve Fund.

Changes in Federal loan reserve funds held for DE for the years ended June 30, 2008 and 2007 were as follows:

	2008	2007
Additions:		
Reimbursement from DE on default loan purchases	$22,218	$18,755
Default loan collections	125	123
Loan administrative fees	2,778	2,445
Investment income	417	511
Total additions	25,538	21,834
Deductions:		
Purchases of defaulted loans from lenders	22,983	19,381
Default aversion fee paid	713	664
Other, net	(101)	(118)
Total deductions	23,595	19,927
Federal loan reserve funds held, at beginning of year	11,423	9,516
Federal loan reserve funds held, at end of year	$13,366	$11,423

To provide security and liquidity against potential defaults, VSAC is required to maintain reserves as specified by Title 16, Vermont Statutes Annotated §2864, Section 422 of Act 20 United States Code 1072, and under various agreements with the bond liquidity and credit enhancement providers. The Higher Education Act Amendments of 1998 require VSAC to maintain reserves equal to .25% of student loans guaranteed. During 2008 and 2007, VSAC maintained sufficient reserves to fully comply with these requirements.

(Dollars in Thousands)

5. Net Assets Held for the U.S. Department of Education (Continued)

Total outstanding loans issued under the FFEL Program were $1,765,999 and $1,591,414 at June 30, 2008 and 2007, respectively. Defaults on FFEL Program loan guarantees are paid by DE through the Federal Loan Reserve Fund.

6. Net Assets Held for the Vermont Higher Education Investment Plan (VHEIP)

VHEIP was established by the Vermont Legislature in April 1998. VHEIP encourages Vermont residents to save for college or other post-secondary education through tax favorable investments. The program has been designed to comply with the requirements for treatment as a "Qualified Tuition Program" under Section 529 of the Internal Revenue Code. There are three plans available: the Managed Allocation Option, the 100% Equity Option, and the Interest Income Option. The Managed Allocation Option and the 100% Equity Option are managed by TFI. TFI is part of TIAA-CREF, a New York-based financial services organization. Funds in the Managed Allocation Option are directed into special investment portfolios based on the age of the beneficiary. Funds in the 100% Equity Option are not age based and remain 100% in equity investments. Investments in the Managed Allocation and 100% Equity option are not guaranteed. The Interest Income Option is managed by VSAC. Funds in the Interest Income Option are invested in an interest-bearing note to VSAC, which is expected to return at least the 91-day U.S. Treasury Bill rate. VSAC uses the proceeds from the note to make federally guaranteed education loans.

The changes in assets held on behalf of investors for the years ended June 30, 2008 and 2007 were as follows:

	2008	2007
Additions:		
Investment income	$ 2,468	$ 2,023
Net realized and unrealized gains	(5,563)	5,736
Student loan interest income	455	336
Net participant subscriptions/redemptions	15,159	11,090
Total additions	12,519	19,185
Deductions:		
Operational expenses	104	51
Total deductions	104	51
Assets held on behalf of investors, at beginning of year	72,393	53,259
Assets held on behalf of investors, at end of year	$84,808	$72,393

(Dollars in Thousands)

7. Capital Assets

A summary of capital assets activity for the years ended June 30, 2008 and 2007, were as follows:

	Estimated Lives	Balance July 1, 2006	Net Acqui-sitions	Balance June 30, 2007	Net Acqui-sitions	Balance June 30, 2008
Land	–	$ 3,150	$ –	$ 3,150	$ –	$ 3,150
Furniture and equipment	3 – 15 Years	7,373	825	8,198	(321)	7,877
Software	3 – 5 Years	1,247	57	1,304	561	1,865
Building	5 – 30 Years	16,653	(4)	16,649	62	16,711
		28,423	878	29,301	302	29,603
Less accumulated depreciation		5,021	1,652	6,673	643	7,316
Capital assets, net		23,402	$ (774)	22,628	$ (341)	22,287
Less bonds payable, net		21,291		20,561		19,812
Net investment in property and equipment		$ 2,111		$ 2,067		$ 2,475

Depreciation charged to operations for the years ended June 30, 2008 and 2007 was $1,467 and $1,652, respectively. Disposals of fully depreciated capital assets were $815 in 2008.

8. Bonds

VSAC has issued the following bonds at June 30, 2008 and 2007, which were issued to finance the origination of student loans:

Bonds Payable:	2008	2007
1985 Series A, dated December 27, 1985; comprised of floating rate monthly demand bonds with the balance maturing in January 2008; interest is payable monthly at variable rates which ranged from 3.400% to 3.860% during fiscal year 2008.	$ –	$ 40,900
1995 Series A, B, C and D, dated June 29, 1995; comprised of auction rate bonds maturing December 2025; interest is reset every 35 days and payable semi-annually at rates which ranged from 2.888% to 8.601% during fiscal year 2008 (2.888% to 4.163% at June 30, 2008).	96,000	96,000

(Dollars in Thousands)

8. Bonds (Continued)

	2008	2007
1996 Series F, G, H and I, dated May 22, 1996; comprised of auction rate bonds maturing December 2036; interest is reset every 35 days and payable semi-annually at rates which ranged from 3.063% to 8.594% during fiscal year 2008 (3.063% to 4.331% at June 30, 2008).	$ 100,000	$ 100,000
1998 Series K-O, dated June 24, 1998; comprised of auction rate bonds maturing December 2032; interest is reset every 35 days and payable semi-annually at rates which ranged from 2.8% to 8.573% during fiscal year 2008 (2.8% to 4.288% at June 30, 2008).	165,000	165,000
2000 Series R, S, T and U, dated May 31, 2000; comprised of auction rate bonds maturing December 2034. Interest is reset every 35 days and payable semi-annually at rates which ranged from 2.975% to 8.487% during fiscal year 2008 (2.975% to 4.342% at June 30, 2008).	172,550	172,550
2001 Series V, W and Z dated June 27, 2001; comprised of auction rate bonds maturing December 2035. Interest is reset every 35 days for Series V and W, and every 7 days for Series Z. Interest is payable semi-annually at rates which ranged from 2.940% to 8.632% during fiscal year 2008 (2.940% to 4.965% at June 30, 2008).	84,750	84,750
2001 Series X, Y and AA dated June 27, 2001; comprised of auction rate bonds maturing December 2036; interest is reset, and payable, every 28 days for Series X and Y, and every 7 days for Series AA. Interest rates ranged from 0.00% to 18.00% during fiscal year 2008 (0.00% to 4.964% at June 30, 2008).	80,000	80,000
2002 Series BB, CC and DD dated October 8, 2002; comprised of auction rate bonds maturing December 2036. Interest is reset every 35 days and payable semi-annually at rates which ranged from 2.80% to 8.553% during fiscal year 2008 (2.80% to 3.15% at June 30, 2008).	112,500	112,500
2003 Series FF, GG, HH and LL dated May 30, 2003; comprised of auction rate bonds with maturity dates ranging from June 2009 through December 2015; interest is reset every 35 days and payable semi-annually at rates which ranged from 3.07% to 3.92% during fiscal year 2008 (2.80% to 3.238% at June 30, 2008).	165,900	165,900

(Dollars in Thousands)

8. Bonds (Continued)

	2008	2007
2003 Series II, JJ and KK dated May 30, 2003; comprised of auction rate bonds maturing December 2037; interest is reset every 35 days and payable semi-annually at rates which ranged from 2.442% to 8.140% during fiscal year 2008 (3.115% to 3.203% at June 30, 2008).	$ 150,000	$ 150,000
2004 Series MM dated June 3, 2004; comprised of auction rate bonds maturing December 2038; interest is reset every 35 days and payable semi-annually at rates which ranged from 3.115% to 8.553% during fiscal year 2008 (2.888% at June 30, 2008).	74,700	74,700
2004 Series NN and PP dated June 3, 2004; comprised of auction rate bonds maturing December 2038; interest is reset every 35 days and payable semi-annually at rates which ranged from 2.888% to 8.140% during fiscal year 2008 (2.853% and 3.997% at June 30, 2008).	134,500	134,500
2004 Series OO dated June 3, 2004; comprised of auction rate bonds maturing December 2038; interest is reset and payable every 28 days at rates which ranged from 0.00% to 18.00% during fiscal year 2008 (0.00% at June 30, 2008).	65,800	65,800
2005 Series QQ dated June 21, 2005; comprised of floating rate weekly demand bonds maturing December 2039; interest is reset every 7 days and payable semi-annually at rates which ranged from 3.03% to 8.00% during fiscal year 2008.	–	120,385
2005 Series RR/SS dated June 21, 2005; comprised of auction rate bonds maturing December 2039; interest is reset and payable every 28 days at rates which ranged from 0.00% to 18.00% during fiscal year 2008 (0.00% June 30, 2008).	119,600	119,600
2006 Series TT-VV dated July 12, 2006; comprised of auction rate bonds maturing December 2040; interest is reset every 35 days for the Series TT and UU and every 7 days for the Series VV. Interest is payable semi-annually at rates which ranged from 2.625% to 6.75% during fiscal year 2008 (2.80% to 2.888% at June 30, 2008).	175,250	175,250
2007 Series WW/XX dated June 19, 2007; comprised of auction rate bonds maturing December 2041; interest is reset every 35 days and payable semi-annually at rates which ranged from 2.625% to 7.15% during fiscal year 2008 (2.80% at June 30, 2008).	138,900	138,900

(Dollars in Thousands)

8. Bonds (Continued)

	2008	2007
2007 Series YY dated December 7, 2007; comprised of auction rate bonds maturing December 2041; interest is reset and payable every 7 days at rates which ranged from 0.00% to 18.00% during fiscal year 2008 (0.00% at June 30, 2008).	$ 91,100	$ –
2008 Series B-1 dated June 26; 2008 comprised of variable rate demand bonds maturing December 2039; interest is reset every 7 days and payable semi-annually with initial interest rates of 1.70%.	120,385	–
2003 General Obligation bond dated December 9, 2003, with a final maturity date of March 1, 2034, interest rates are fixed ranging from 2.00% to 5.00% payable semi-annually.	19,940	20,695
Total bonds	2,066,875	2,017,430
Bond discount, net	(129)	(134)
Deferred loss on refunding, net	(781)	(976)
Total bonds	2,065,965	2,016,320
Less current portion of bonds	1,670	41,655
Noncurrent portion bonds	$2,064,295	$1,974,665

All bonds, except the 2003 General Obligation bonds, are limited obligations of VSAC and are secured, as provided in the underlying bond resolutions, by an assignment and pledge to the Trustee of all VSAC's rights, title and interest in student loans and revenues derived thereon and the guarantee thereof, including the insurance of certain student loans by DE. In addition, a significant portion of cash and cash equivalents (including debt service reserve accounts which may be used to replenish any deficiency in funds required to pay principal and interest due on the bonds) are held in trust to secure the bonds, except the 2003 General Obligation bonds.

In 2008, due to disruptions in the capital markets, the interest rates paid on auction bonds fluctuated significantly due to failed auction formulae. These rates varied from as low as 0% to as high as 18% over 2008. This variability is tied to the variable indices in the failed auction formula and the maximum rates defined in the bond indentures. The resulting rates increased interest costs in 2008.

(Dollars in Thousands)

8. Bonds (Continued)

The 1995 Series A-D, 1996 Series F-I, 1998 Series K-N, 2000 Series R-U, 2001 Series V-AA, 2002 Series BB-DD, 2003 Series FF-LL, 2004 Series MM-OO, 2005 Series QQ-SS, 2006 TT-VV, and the 2007 WW-YY bonds are secured for credit-worthiness by AMBAC Assurance Corporation. The 2003 General Obligation bonds and the 1998 Series O bonds payable have no credit support. The 2005 Series QQ and 2008 Series B-1 bonds have liquidity support by a Standby Bond Purchase Agreement issued by the Bank of New York.

All bonds, except the 2003 General Obligation bonds, are subject to redemption prior to maturity at the principal amounts outstanding plus accrued interest at date of redemption. At June 30, 2008, all bonds authorized under the underlying bond resolutions have been issued.

Proceeds from issuance of the bonds payable, except the 2003 General Obligation bonds, and all revenues thereon are held in trust and are restricted as follows: to repurchase bonds; finance student loans; pay interest on the bonds; maintain required reserves; and pay reasonable and necessary program expenses.

The 2003 General Obligation bonds are payable from available revenues of VSAC. The bonds were issued for the purpose of financing the acquisition of land, construction, renovation, and equipment outfitting of a new corporate headquarters for VSAC.

The debt service requirements, which are based on the interest rates at June 30, 2008, through 2013 and in five-year increments thereafter to maturity for VSAC, are as follows:

Year ending June 30,	Principal	Interest	Total
FY09	$ 1,670	$ 97,473	$ 99,143
FY10	795	97,409	98,204
FY11	820	97,384	98,204
FY12	40,435	97,263	137,698
FY13	25,450	94,815	120,265
FY14 – 18	102,575	456,739	559,314
FY19 – 23	3,290	446,889	450,179
FY24 – 28	100,205	434,498	534,703
FY29 – 33	170,360	418,036	588,396
FY34 – 38	701,040	317,197	1,018,237
FY39 – 43	920,235	80,492	1,000,727
Total	$2,066,875	$2,638,195	$4,705,070

The actual maturities and interest may differ due to changes in interest rates or other factors.

(Dollars in Thousands)

8. Bonds (Continued)

The following summarizes the debt activity for VSAC for the years ended June 30, 2008 and 2007:

	2008	2007
Balance at beginning of year	$2,016,320	$1,702,705
Issuance	211,485	314,150
Redemptions and refundings	(162,040)	(735)
Accretion of discount	200	200
Balance at end of year	$2,065,965	$2,016,320

9. U.S. Treasury Rebates Payable

The bonds issued by VSAC are subject to Internal Revenue Service regulations which limit the amount of income which may be earned on certain cash equivalents, investments and student loans acquired with bond proceeds. Any excess earnings are to be refunded to the U.S. Treasury. VSAC has estimated that there is an arbitrage liability at June 30, 2008 and 2007 of $25,390 and $32,254, respectively. VSAC has estimated the current portion to be $0 and $547 at June 30, 2008 and 2007, respectively. VSAC refunded the U.S. Treasury $335 and $233 in excess earnings in 2008 and 2007, respectively.

10. Student Loan Interest and Special Allowance Revenues

DE makes quarterly interest subsidy payments on behalf of certain qualified students until the student is required under the provisions of the Act to begin repayment. Repayment on Stafford Student Loans normally begins within six months after students complete their course of study, leave school or cease to carry at least one-half the normal full-time academic load as determined by the educational institution. Repayment of PLUS, SLS and Consolidation loans normally begins within sixty days from the date of loan disbursement unless a deferment of payments has been granted. In these cases, full repayment of principal and interest would resume at the expiration of the deferment. Interest accrues during this deferment period. HEAL loans enter repayment status nine months after the expiration date of an interim period.

10. Student Loan Interest and Special Allowance Revenues (Continued)

DE provides a special allowance to lenders participating in the Stafford, PLUS, SLS, and Consolidation student loan programs. Special allowance is paid based on a rate that is established quarterly. For loans first disbursed before January 1, 2000, the rate is based on the average rate established in the auction of the thirteen-week U.S. Treasury bills, plus a pre-determined factor, less the interest rate on the loan. For loans first disbursed on or after January 1, 2000, financed with obligations issued after October 1, 1993, the rate is based on the average rate established in the auction of three-month Financial Commercial Paper, plus a pre-determined factor, less the interest rate on the loan. Certain loans made or purchased prior to February 8, 2006 with funds obtained through the issuance of tax-exempt obligations issued before October 1, 1993, are eligible for one-half of the special allowance rate, subject to a minimum return of 9.5%. Loans made or purchased with these obligations on or after February 8, 2006 are eligible for full special allowance and are not subject to a minimum return. Loans made or purchased with funds obtained through the issuance of tax-exempt obligations originally issued after October 1, 1993, are eligible for full special allowance and are not subject to a minimum return.

DE restricts student loan interest revenue for loans first disbursed after April 1, 2006. VSAC is required to return student loan interest in excess of the special allowance formulae rates for certain Stafford, PLUS, and Consolidation loans. The return of interest totaled $7,054 and $303 in 2008 and 2007, respectively and is reflected as a reduction of interest and fees and student loans in the Statements of Revenues, Expenses and Changes in Net Assets.

11. Endowment funds

Donors have established a number of endowment funds through the Vermont Student Development Fund, Inc. All endowment funds are restricted to provide scholarship funds to Vermont students. All endowment funds are guided by specific agreements and instructions from donors regarding the uses of earnings and appreciation on invested funds.

In 1998, the Vermont General Assembly enacted a version of the Uniform Prudent Investor Act. The Act does not address in any explicit or clear manner a trustee's ability to spend net appreciation of donor-restricted endowments. The VSAC Board of Directors has established a policy, and most endowment agreements specify gains and appreciation on these funds be treated with a total return approach. In this approach, the amount of funds that may be expended from an endowment is based on a percentage of the fund's total value, and may come from the total return on the fund, including interest and dividend earnings, appreciation or original gift value. Total investment return in excess of the established spending rate is considered to be nonexpendable in future periods. The spending rate may be adjusted by the Board of Directors at their discretion.

At June 30, 2008 and 2007, the total net assets related to endowment funds were $2,901 and $3,152, respectively. Expendable restricted net assets totaled $81 and $240, respectively. The remaining $2,820 and $2,912, respectively, of net assets related to endowment funds were nonexpendable.

(Dollars in Thousands)

12. Restricted Net Assets

Restrictions on net assets are the result of bond resolutions, state statutes, various federal regulations and program agreements, and donor restrictions. Bond resolutions restrict net assets to the origination of student loans and payment of debt service on bonds and notes payable. State statutes and federal regulations and program agreements restrict various net assets to use for specific grant, scholarship and educational activities. Donors have restricted a number of endowment funds for scholarship awards. Restricted net assets as of June 30, 2008 and 2007 are as follows:

	2008	2007
Restricted by bond resolutions	$58,410	$80,176
Restricted for grants and scholarships	981	1,509
Donor restricted for scholarships	2,901	3,152
Restricted appropriation for educational programs	10	744
Total restricted net assets	$62,302	$85,581

13. Retirement Benefits

Full-time employees of VSAC that meet specific eligibility requirements are participants in a retirement annuity plan. This plan is a multi-employer defined contribution plan sponsored by Teachers Insurance and Annuity Association and College Retirement Equities Fund (TIAA-CREF). The payroll for employees covered under the plan for the fiscal year ended June 30, 2008 and 2007 amounted to $17,733 and $16,428, respectively; VSAC's total payroll was $17,752 and $17,343, respectively. Total contributions by VSAC amounted to $1,773 and $1,643 in 2008 and 2007, respectively, which represented 10% of the covered payroll.

In June of 2004 the Governmental Accounting Standards Board issued Statement 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions*. This statement requires recognition of current period costs related to expected future expenditures for Other Post Employment Benefits ("OPEB"). VSAC employees who complete 15 years of continuing service and who are not otherwise eligible for Medicare coverage may elect to continue to buy in to VSAC's health care coverage at COBRA rates. VSAC has determined that this obligation is not material and has not recorded a liability for OPEB at June 30 2008.

14. Contingencies

VSAC participates in various federally funded programs. These programs are subject to financial and compliance audits and resolution of identified questioned costs. The amount, if any, of expenditures which may be disallowed by the granting agency cannot be determined at this time.

(Dollars in Thousands)

14. Contingencies (Continued)

VSAC is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. VSAC manages these risks through a combination of commercial insurance packages purchased in the name of VSAC, and through self insurance programs for medical and dental claims. With respect to its commercial insurance packages, VSAC has not experienced or settled claims resulting from these risks which have exceeded its commercial insurance coverage. In addition, VSAC has purchased stop-loss insurance for its self-insurance programs and has transferred the risk of loss to the commercial insurance carrier.

A summary of the reserve for self-insured medical and dental liabilities included in accounts payable and other liabilities on the statement of net assets for the years ended June 30, 2008 and 2007 is as follows:

	2008	2007
Balance, beginning of year	$ 312	$ 419
Claims paid	(4,349)	(3,680)
Accrual for estimated claims	4,440	3,573
Balance, end of year	$ 403	$ 312

15. Loan Commitments

At June 30, 2008 and 2007, VSAC had commitments to extend credit for student loans of approximately $58,885 and $56,726, respectively. Commitments to extend credit are agreements to lend to a borrower as long as there is no violation of any condition established in the commitment agreement. Commitments generally have fixed expiration dates or other termination clauses. VSAC uses the same credit policies in making commitments as it does for student loans receivable.

16. Subsequent Events

In July 2008, VSAC issued tax-exempt 2008 Series A-1 floating rate weekly demand bonds totaling $113,050. In September 2008, VSAC issued tax-exempt 2008 Series C-1 and C-2 floating rate weekly demand bonds totaling $200,000.