

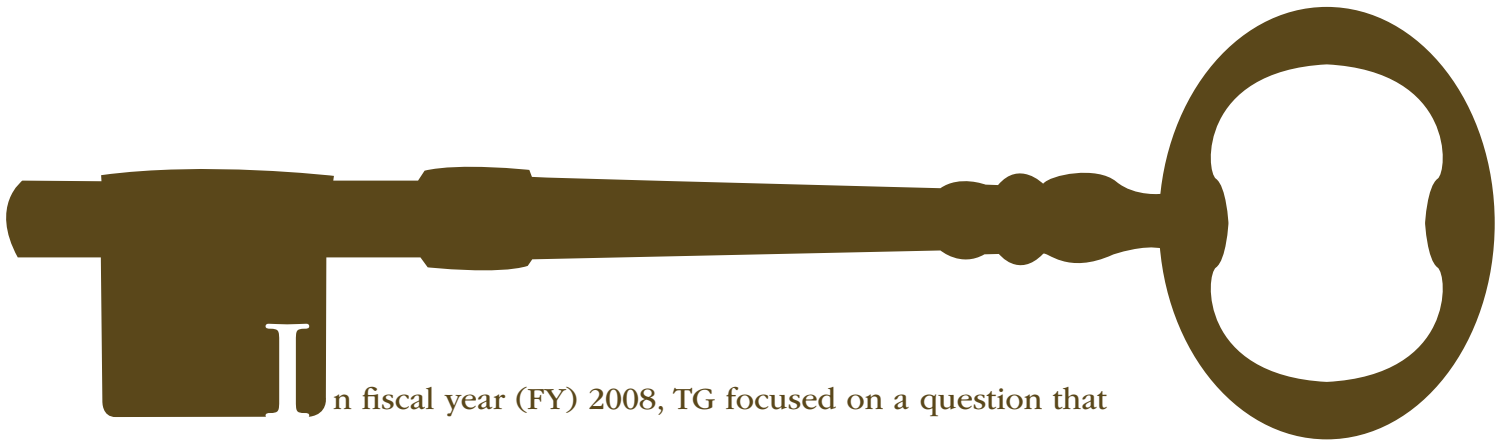


OPENING  
DOORS  
OF OPPORTUNITY

Making a difference in higher education

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In fiscal year (FY) 2008, TG focused on a question that reflects a guiding principle of its business — what makes a difference for a student, a parent, a school or lender? The answers came in a surprising variety of ways as TG served its customers over the course of the year.

Sometimes making a difference can mean something as simple as lending an ear. TG financial literacy trainers regularly encounter students who have one thing on their mind — finding an expert who can answer their questions on money management and understand their fiscal anxieties as new borrowers.

Sometimes making a difference means going the extra mile in times of industry change. In the last year, significant economic shifts have complicated borrowing for students and families. TG's many team members worked hard, especially during fall peak season, to help assure that borrowers got the funding they were eligible to receive.

Sometimes making a difference can also mean offering direct support through philanthropic efforts. For the 2007-08 academic year, TG awarded \$2 million to schools for need-based grants, and more than \$6 million in competitive grants to organizations working to advance college access, student retention, and educational research. Since 2005, TG's Public Benefit Grant Program has awarded more than \$16 million in competitive grant funding to initiatives that

serve the needs of students, many from under-represented populations. TG continues to administer this program based solely on merit and need, and without regard to our business or any form of quid pro quo consideration.

We at TG believe efforts like these offer opportunities to students and those that help them. These opportunities come in an array of forms — knowledge, empowerment as a consumer, college access and retention, better services for the administration of financial aid, and, ultimately, a stronger federal loan program.

In FY 2008, TG focused on opening the door to such opportunities. We invite you to read about our work in this year's annual report. Taken together, we believe such activities drive higher education to grow and, in turn, offer more opportunities to future generations as well as continuing prosperity to our culture at large.

## To TG's stakeholders

The last fiscal year has thrown a spotlight on what will hold value in times of economic uncertainty. Credit and liquidity issues have affected every sector of lending in the U.S., including student loans. Though the smoke hasn't cleared yet, it's still true that few investments retain their worth as well as a college degree. According to the U.S. Census Bureau, a bachelor's degree enables a graduate to take home each year almost \$20,000 more in average wages than non-degree holders.

So, despite its challenges, or perhaps because of them, last year's financial turmoil has made one thing even clearer — higher education is an opportunity students can't afford to pass up. TG's business is about making a postsecondary education available to more students. As a promoter of college retention, we're also committed to helping ensure that experience is a successful one. In FY 2008, TG pursued these objectives with vigor.

We considered how we could better prepare a generation of students who are borrowing funds in significant amounts to go to college. To help, TG offered new and more varied financial literacy tools, including interactive online resources and a symposium devoted to the creation and nurture of campus financial literacy initiatives.

We also focused on how we could serve our colleagues in the field by linking schools and lenders to electronic services that can make their work more efficient; offering ready support as a possible lender of last resort; working diligently behind the scenes to help borrowers connect with lenders and receive funding; and expanding our services in outreach and default prevention. Our comprehensive approach earned us a high customer satisfaction score of 4.53 out of 5.

At the same time, we fortified our position as one of the most financially stable of the guarantors. TG continued its commitment to the delivery of the highest quality products

and services, focusing its efforts on those initiatives that have the greatest effect on borrowers and their families, schools and lenders. By the end of the year, we made guarantees totaling over \$6.71 billion, far above expectation. To date, TG has guaranteed more than \$61 billion in Federal Family Education Loan Program (FFELP) loans.

Our efforts attest to our strength and commitment to serve our customers. In times of change, that stability makes a difference. It offers a firm foundation on which to assist students, schools, and lenders. It creates a base from which to cultivate better service for the future. And it sustains the health of enduring cultural institutions such as higher education, which are vital to our economy.

We present TG's Annual Report for FY 2008 as a testament to our strength and commitment. In the following pages, you'll learn more about the benefits that a strong, sound business can offer customers. We believe such benefits make a difference for students and families, a difference which will grow in value over the years to come.



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Sue McMillin  
President and CEO

Tommy J. Brooks  
Chair, TG Board of Directors

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The Honorable Susan Combs  
*State Comptroller of Public Accounts*  
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## TG Senior Management Team

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James Patterson  
*Chief Financial Officer and  
Senior Vice President,  
Finance and Administration*

Deanne Varner  
*Senior Vice President, Legal  
and Regulatory Affairs,  
Chief Ethics Officer*

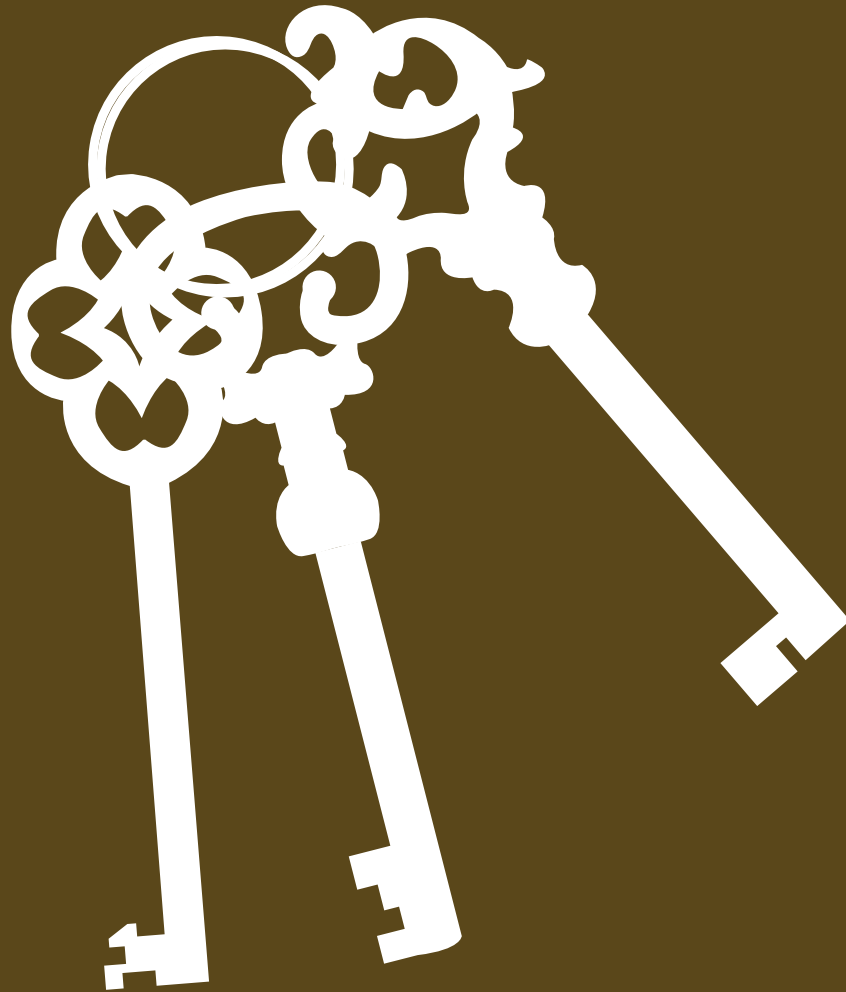
Kim Alexander  
*Vice President, Customer Focus*

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*Vice President, Collections*

Rinn Harper  
*Vice President, Operations*

Carol Lindsey  
*Vice President, Policy  
and Compliance*

John Zanot  
*Vice President, Marketing  
and Product Management*



## Service + knowledge + care = opportunity

The student loan industry saw its share of adversity in the last year. But industry challenges tell only part of the story. The other part concerns a successful effort to provide college access to a tremendous number of students — more than 6.8 million loan seekers for FY 2008 according to College Board estimates.

TG helped connect a growing portion of these students to funds that enabled them to begin or continue their education. TG's market presence grew at a significant rate nationally, while remaining dominant in Texas. Other indicators show that TG's financial health is robust and growing stronger. Our federal fund reserve ratio ranks as the best among the country's largest guarantors and second overall. TG added to its complement of products and services while reaching more students, whether in traditional brick-and-mortar classrooms or through online coursework. And TG continued to subsidize the federal

default fee for federal Stafford, PLUS, and Grad PLUS loans for FY 2008, resulting in nearly \$54 million in savings collectively for more than 600,000 borrowers last year.

TG's success testifies to the strength of its business philosophy, which begins with a pragmatic question, "What can make a difference for our customers?" Answers come in diverse forms, but generally follow a pattern: exceptional service and products that facilitate the financial aid process; guidance that illuminates the ever-changing regulatory landscape or offers insight on professional growth; and a spirit of commitment and care exemplified in every customer interaction.

This business formula has allowed TG to grow as a guarantor and, in turn, open more doors of opportunity for our customers and business associates.

# OPENING DOORS THROUGH [ INNOVATIVE SERVICE ]

Doing the unexpected, solving a problem, providing a solution — experiences like these can offer a fresh perspective on an issue, one that opens up new avenues of thinking. In FY 2008, TG offered such solutions in many ways: employing technology to reach students and teach financial literacy; promoting a culture of college access and retention through grants and a collaborative publication focused on enrollment management; and designing a paperless process to help schools manage lender list surveys.

## Doing the math: TG's expanding services for financial literacy

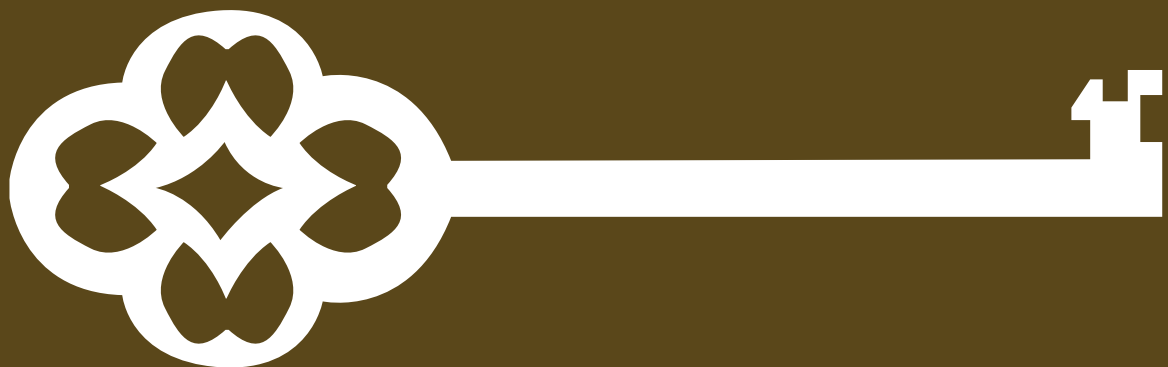
A changing economy and growing borrower debt make it imperative for students to cultivate responsible and effective money management habits early on. To help, TG expanded key offerings of its college and career



planning Web site, *Adventures In Education* ([www.AIE.org](http://www.AIE.org)). AIE™ provides a rich assortment of financial literacy tools that teach students the basics of prudent money management, such as budgeting and using credit wisely. This year, TG added interactive features that provide hands-on learning experiences, reorganized the content to make navigation more intuitive, and redesigned the Web pages to be more appealing to students.

TG also hosted a unique financial literacy forum that gathered financial literacy experts and financial aid administrators from a variety of public and private institutions. The TG Financial Literacy Counseling Symposium initiated a dialogue in which participants could share techniques for helping students manage their finances more responsibly. In particular, the symposium focused on how schools could spearhead campus-wide financial literacy initiatives.

The symposium was the first in a series of ongoing financial literacy efforts, several of which were in development during FY 2008, including the new Positive+Balance Community<sup>SM</sup> Web site ([www.positivebalance.org](http://www.positivebalance.org)). The Positive+Balance Community serves as a collaborative resource for schools interested in creating campus-based financial literacy programs. The Web site houses TG's Positive+Balance™ financial literacy courses, presentations, and training materials, which are all free to download and use. The site also provides a virtual meeting place where counselors, educators, and financial aid professionals can share their ideas and educational materials related to financial literacy. Additionally, members can blog about financial literacy or use the file library of prepared presentations and information. The Positive+Balance Community is just one more tool TG offers schools interested in exploring an area of growing importance to students and schools.



## Promoting a culture of college access and retention

In January 2008, TG launched the inaugural edition of a new scholarly publication, *Enrollment Management Journal: Student Access, Finance, and Success in Higher Education*. Developed in collaboration with the University of Nebraska–Lincoln, this refereed journal publishes substantive articles on enrollment management research and offers strategies for improving student access and success. Available by subscription, the *Enrollment Management Journal* was published twice in 2008 and becomes a quarterly publication in 2009.



TG worked jointly with the Educational Policy Institute to produce a new publication that studies the reasons for the success and failure of students on campus. *Engaging Faculty and Staff: An Imperative for Fostering Retention, Advising, and Smart Borrowing* was written to provide insights and strategies that institutions could use to increase student retention, persistence, and postsecondary success — and to reduce the burdens of student loan defaults.

For the fourth consecutive year, TG awarded competitive grants through its Public Benefit Grant Program, the company's primary philanthropic initiative. For the 2007-08 academic year, TG awarded more than \$6 million in competitive grants to 46 institutions and nonprofit organizations to advance college access, student retention, and educational research.

TG expanded its Charley Wootan Grant Program, providing \$2 million in need-based grants nationwide to be disbursed during the 2008-09 academic year. The first-come, first-served, need-based grant program provides up to \$4,245 per student. TG has awarded nearly \$6 million since 2000 when it established the program, named in honor of the late Dr. Charley V. Wootan, a former chairman of TG's Board of Directors.

## Simplifying processes through technology

In today's student loan market, borrowers need as much information as they can gather to make smart consumer choices. Many schools recognize the value of a recommended lender list but grapple with how to compile and evaluate lender information efficiently. In the last fiscal year, TG developed an online tool for schools to use to generate and manage lender surveys — List Assist<sup>SM</sup>. List Assist focuses on creating efficiencies for schools by providing a convenient way to query lenders, compare information, and even print reports for documentation purposes. For lenders, the tool can serve in tracking survey requests from multiple schools. The product offers a library of over 100 suggested questions, which jumpstarts the survey process and allows schools to concentrate on gathering information important to students and families.

# OPENING DOORS THROUGH

## INDUSTRY INSIGHT

Administering financial aid requires careful study of a virtual library of legislative and regulatory requirements. TG has a history of providing valuable insight on policy and regulations — from written guidance to in-person training to industry workgroup support. This year, TG’s expertise — like the larger industry’s — was tested as market pressures altered the lending landscape. TG met those challenges, offering more resources to borrowers, and, at the same time, serving a record number of students.

### Helping ensure a borrower safety net

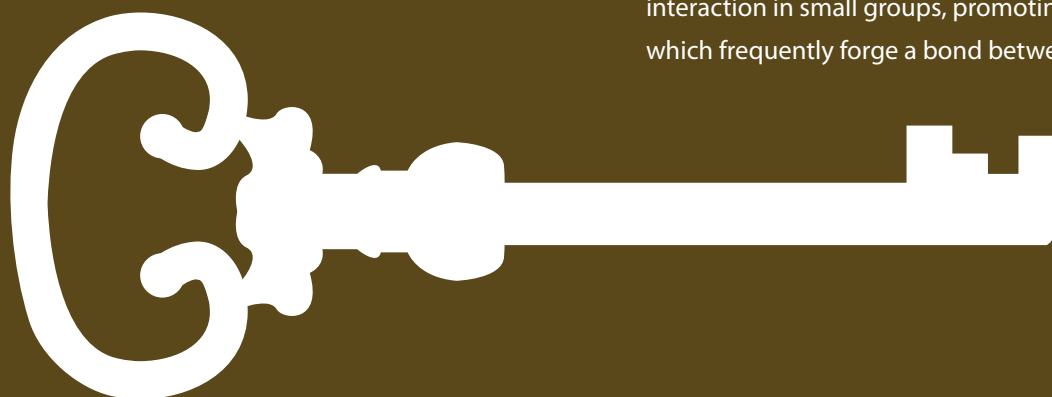
Earlier in 2008, Congress passed and the President signed into law the Ensuring Continued Access to Student Loans Act (ECASLA). ECASLA granted the Secretary of Education the ability to provide FFELP-eligible lenders access to funding from the U.S. Treasury. It also enacted new and additional lender-of-last-resort provisions. The lender of last resort (LLR) is a “fail-safe” mechanism whereby eligible borrowers unable to locate a lender are assured of FFELP funds. In these cases, guarantors or designated lenders can offer the necessary loans. To meet the special provisions of ECASLA, TG formed a task force of team members from across the company to marshal resources and implement system changes quickly and efficiently. The implementation process went smoothly with TG frequently updating customers on progress. To date, no borrowers have had to access the LLR program.

### Meeting the demands of a changing marketplace

As lender participation levels changed, TG’s teams, including Guarantee, Support, and Reporting (GSR), pulled together to connect eligible borrowers with available lenders. GSR also helped direct system modifications required by regulatory changes, including the reauthorization of the Higher Education Act and the enactment of ECASLA. At the same time, TG experienced one of its busiest fall peak seasons, guaranteeing its biggest single-day volume of loans — some 31,680 loans for a total of \$136,409,022. Overall, guarantees increased by 72 percent over this same period last year. Simultaneously, TG’s many customer-facing teams, including GSR, fielded a huge number of calls from borrowers, schools, and other customers. In a true team effort, GSR worked to meet this unprecedented demand — an all-time high of 6,556 calls for August.

### Educating tomorrow’s financial aid leaders today

Since 2006, TG has offered a one-of-a-kind learning experience to supervisors and managers looking to advance in financial aid — the Financial Aid Leadership Symposium. The symposium is a week-long workshop on the principles of good leadership in the context of a financial aid office. Among other things, participants learn how to build trust and create a vision for a team. The great advantage to attendees is that they grasp these concepts by discussing real-world issues drawn from their own work experiences. To provide insight, the symposium stresses a format of interaction in small groups, promoting the trust and candor which frequently forge a bond between participants.



TG offers industry and skill development programs to its customers and industry-based organizations through other services, including the TG Speakers Bureau and TG's Positive+Balance™ workshop series. TG Speakers Bureau programs are available on a variety of regulatory, industry, and professional development topics. TG presented over 143 sessions at various events in the last year. Positive+Balance, a comprehensive program of financial literacy and default prevention trainings, had another successful year, providing information to session attendees at over 40 events.

TG also published a new book geared specifically for financial aid offices looking to polish their customer service. *Customer Service in Financial Aid: Strategies to Engage Students and Make a Difference* defines specific principles of good customer service and suggests a surprising variety of ways to put those principles into practice. The book is one of the only publications of its kind written specifically for financial aid officers.

### Offering the sure hand of experience

One way a corporation measures success is by the loyalty of its staff. By this standard, TG is truly fortunate. A growing cohort of team members at TG have marked or will soon celebrate over a quarter century with the company. Their combined experience represents a legacy of enduring knowledge and commitment to the "craft" of supporting students, schools, and lenders, whether through information, funding, or training. Here are just a few of those dedicated team members.

#### Cal Abbott

TG's portfolio manager

Cal Abbott came on board when TG was still a developing organization, and his path has come full circle in that time. He started out as the company's controller, overseeing its financial well-being. After taking a series of other positions, he's returned to his financial roots as TG's portfolio manager and chairman of the Pension Committee. Throughout the course of his career, Cal has shown an instinctive awareness of how best to nurture the company's financial health and growth.

#### Sheila Casey

events coordinator

As an events coordinator, Sheila Casey works behind the scenes to ensure the success of scores of events that TG presents each year. She handles much of the legwork for these training opportunities, finding suitable locations and coordinating logistics. In all, Sheila takes part in planning over 70 events each year, including the TG Annual Training Conference, which takes months of meticulous preparation.

#### Nina Hold

assistant vice president of policy and regulatory affairs

Nina Hold secured her reputation as a policy expert at TG and to the wider industry in the months after the 1992 reauthorization of the HEA. During that time, Nina worked jointly with other industry representatives to forge a uniform standard, or protocol, for managing student loans. Her collaborative work with colleagues resulted in some of the seminal documents that help guide FFELP administration to this day, including federal common forms and the *Common Manual*.

# OPENING DOORS THROUGH CARE AND COMMITMENT

For TG, dedication to the customer has always meant keeping a sharp focus on the needs of students and TG stakeholders. That dedication shows in the TG brand of customer service, which is synonymous in the minds of our customers with diligence, respect, and speed. In particular, TG works to empower students by providing information in a variety of ways, whether through online sources or via one-to-one communications offered by our call centers.

## Reaching out to the 'virtual student'

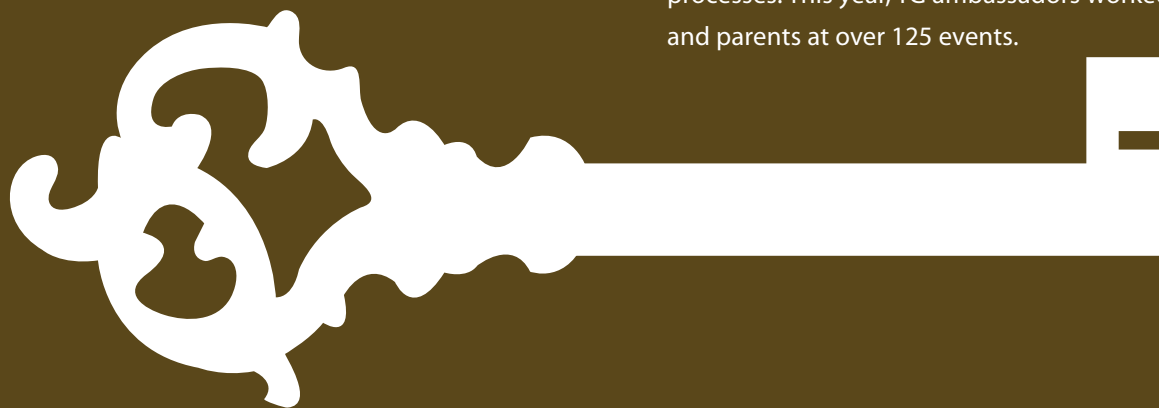
In FY 2008, the *Los Angeles Times* cited *Adventures In Education* (AIE) as a featured resource for students seeking help on financial aid, and for good reason. AIE packs a great deal of information on college and career planning into an informative, interactive format. It offers two subscription newsletters — one geared to students and one for high school counselors. And it teaches financial literacy skills using a variety of Web-based techniques. The site is also reaching more students, parents, counselors, and others involved in higher education; page views rose more than 160 percent over last year. Subscriptions to *AIEmail*, the student newsletter, exceed 3,900. The *Counselors Network* tops 1,400. And, by July, AIE was communicating with more students on-the-go through its new AIE mobile feature, a modified version of the Web site viewable on portable electronic devices.

## Providing information that matters

TG's Customer Assistance (CUST) team offers comprehensive loan support, answering questions about every phase in the life of a loan. The team fields upwards of 160,000 calls annually and, at the same time, acts as the Texas Financial Aid Information Center for Texas students and families. TG offers the Center in partnership with the Texas Higher Education Coordinating Board and at no cost to the State of Texas. This fall, with market and legislative changes, CUST experienced one of its busiest peak seasons. Through the volunteer support of an extended team made up of staff from across TG, CUST answered some 23,000 calls in August. In September, the team handled over 13,000 calls, a 44 percent increase in volume over the previous year. And the team managed this large volume while earning its highest peak season customer satisfaction score — 4.9 out of 5.

## Inspiring with the right answer

Members of the TG Ambassador Program meet students and parents regularly, often offering that essential piece of financial aid knowledge or personal inspiration that makes college seem more possible. TG ambassadors attend financial aid fairs and college preparation workshops at high schools, colleges, community centers, and faith-based venues. They offer short presentations and answer questions, describing the benefits of a postsecondary education and explaining the financial aid and admissions processes. This year, TG ambassadors worked with students and parents at over 125 events.



# TG — a source of stability in times of change

In 2008, TG marked its 29th year, a sign of our capacity to serve as a strong partner for our many customers and business associates. We also continued our positive trajectory as a corporation, guaranteeing a growing percentage of national loans, expanding our default prevention services, and serving borrowers by administering post-graduation services like the Teacher Loan Forgiveness Program.

## Growing on a stable base

Various TG statistics paint a picture of a healthy organization growing stronger on a solid foundation of financial aid services. TG's total loan volume topped \$6.71 billion in the last year. At the same time, TG earned a customer satisfaction score of 4.53. Since its inception, TG has administered loans to benefit students at over 6,000 schools and guaranteed loans for close to 1,700 lenders. Our federal fund reserve ratio ranks at the top in a comparison with other national guarantors. And this is the third consecutive year that TG has subsidized the federal default fee, helping cumulatively more than 1.3 million borrowers.

## Maintaining the connection with borrowers

Each month, the Default Prevention team provides guidance to borrowers in thousands of conversations conducted via phone and e-mail. Their work is vital to students and parents, especially as economic uncertainty affects more consumers entering repayment. To provide even more effective default prevention services, TG invested in its new auto-dialer system and hired additional specialized staff to maximize use of this technology and to locate borrowers without currently known addresses. Our efforts have paid off. Over the course of the year, TG's Default Prevention team helped close to 367,000 borrowers avoid default on over \$3 billion in student loans.

## Continuing to help after college

In the last year, a large cohort of teachers applying for loan forgiveness through the federal Teacher Loan Forgiveness (TLF) Program became eligible to receive benefits. The CUST team processed these applications, many during the challenging times of peak season. Through the end of the fiscal year, TG had forgiven over \$16.9 million in loans for 2,545 teachers.

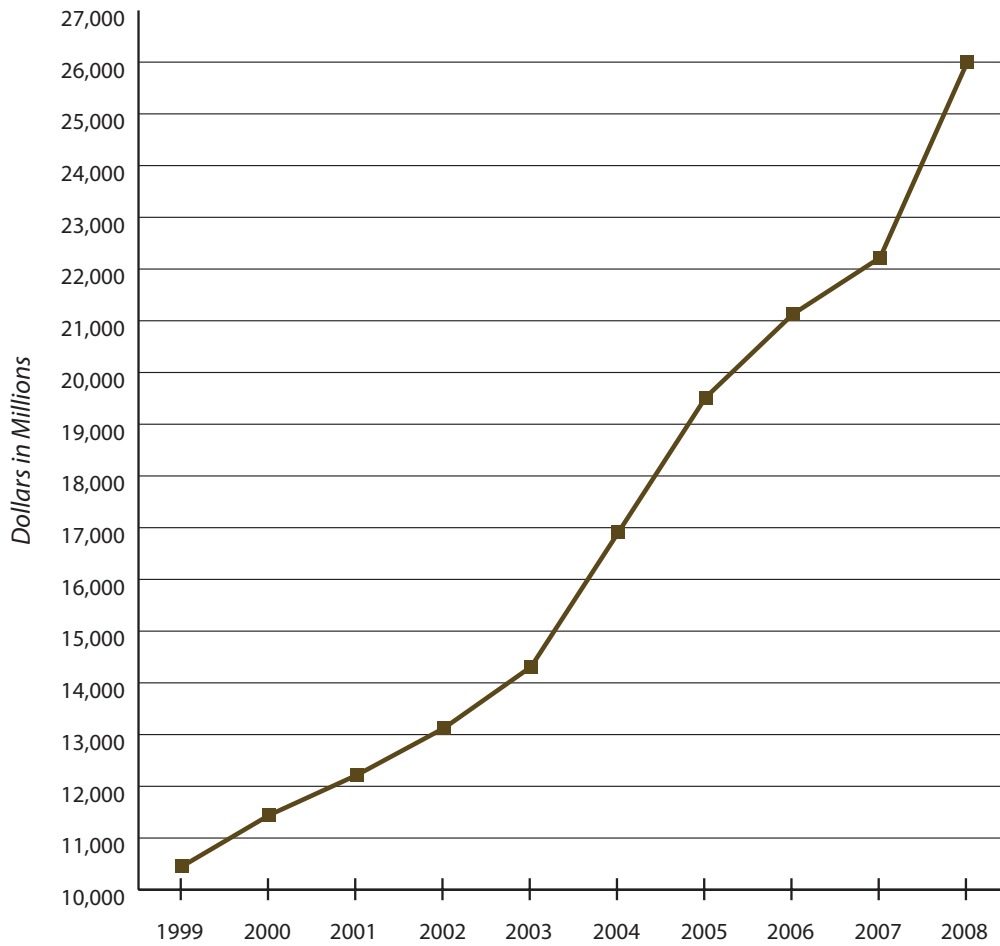
## Building on a tradition of care

The FFELP serves an important role in federal student aid, providing access to higher education for the majority of Americans. As a national guarantor, TG takes its responsibility in contributing to the success of the FFELP seriously. To date, we've helped more than 3.9 million borrowers by guaranteeing nearly \$61.9 billion in student loans. Such a record of service attests to our commitment to higher education and offers proof of TG's growing strength as a corporation. It also shows that TG's focus on providing excellent customer service, effective technology, and industry expertise is a winning combination for our many customers, one that will help ensure TG's continuing support of higher education.

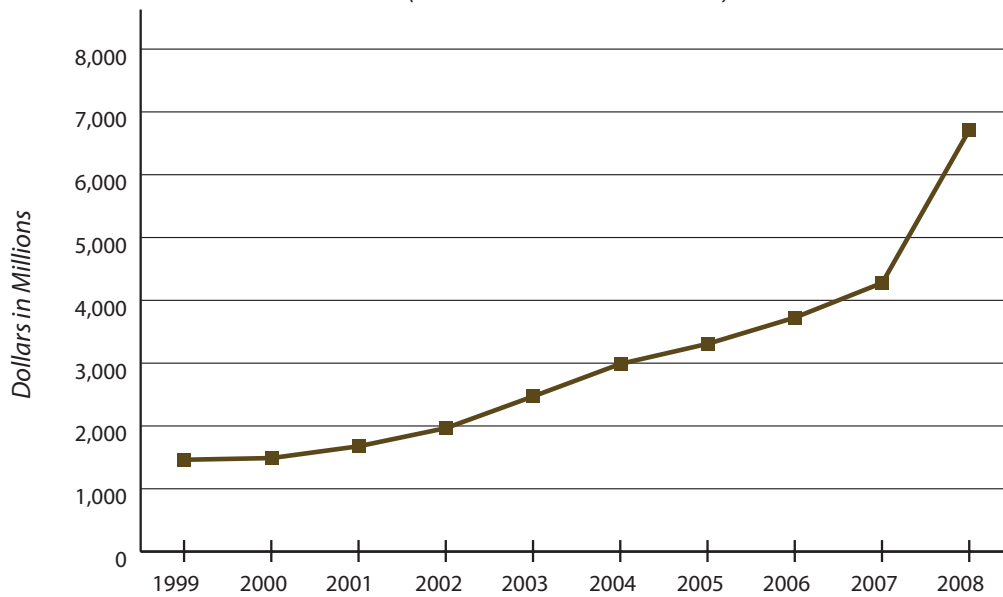
**\$6,716,322,961**  
TG's total loan volume for FY 2008  
(excluding Consolidation loans)

# Guarantee Volume

*Loan Volume — Original Principal Balance Outstanding*



*Loan Volume Guaranteed  
(excludes Consolidation loans)*



# Top 25 Schools and Lenders

## Top 25 Schools

(ranked by total gross amount for Stafford and PLUS loan types as of September 30, 2008)

1. University of Phoenix
2. University of Texas at Austin
3. University of North Texas
4. Texas A&M University
5. University of Houston
6. University of Texas at San Antonio
7. University of South Florida
8. Texas Tech University
9. University of Missouri — Kansas City
10. University of Texas at Arlington
11. Florida International University
12. Capella University
13. Loyola University — Chicago
14. Baylor University
15. Northwestern University
16. Texas Southern University
17. Southern Methodist University
18. University of Chicago
19. Life University
20. University of Texas at El Paso
21. American Intercontinental University
22. Emory University
23. Stephen F. Austin State University
24. Westwood College — Denver North
25. Texas Woman's University

## Top 25 Lenders

(ranked by total gross amount\* for Stafford and PLUS loan types as of September 30, 2008)

1. Wachovia Education Finance
2. Bank of America
3. Wells Fargo Education Financial Services
4. Sallie Mae Corporation
5. Citibank
6. JP Morgan Chase Bank
7. Edamerica
8. Access Group
9. Nelnet
10. Compass Bank
11. University Federal Credit Union
12. First Financial Bank
13. Suntrust Education Loans
14. Arizona Higher Education Loan Authority
15. Commerce Bank
16. National City
17. U.S. Bank
18. Regions Bank
19. Emory University
20. First National Bank of Texas
21. Parker College of Chiropractic
22. PNC Bank
23. Saint Louis University
24. Devry University
25. Discover Bank

\* Amounts represent total loan volume for all U.S. Department of Education codes owned by a lender.

# Advisory Committees for FY 2008

## Lender Advisory Committee

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Katherine Carson  
Texas Higher Education  
Coordinating Board  
*Austin, Texas*

Juan Antonio Ruiz  
San Antonio Credit Union  
*San Antonio, Texas*

Brian Sunshine  
Nelnet  
*Bryan, Texas*

Nanci Twardowski  
Access Group  
*Wilmington, Delaware*

Joe Vargas  
Security Service Federal  
Credit Union  
*San Antonio, Texas*

Beth Zachary — Chair  
Citibank  
*Fayetteville, Arkansas*

## School Advisory Committee

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University of Texas  
at San Antonio  
*San Antonio, Texas*

Toni Bryant  
Schreiner University  
*Kerrville, Texas*

Heather Crowson, Ed.D.  
Sam Houston State  
University  
*Huntsville, Texas*

Carolyn Cunningham  
University of North Texas  
*Denton, Texas*

Laura Elizondo  
Texas A&M International  
University  
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Christine Gauger  
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Karen LaQuey  
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Joe Pettibon  
Texas A&M University  
*College Station, Texas*

Jim Reed  
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Peggy Rogers  
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*Dallas, Texas*

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Steve Johnson  
Texas Association of  
Community Colleges  
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Henry Garcia  
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Linda Gonzalez-Hensgen  
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Lois Hollis  
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Coordinating Board  
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*San Antonio, Texas*

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David Ximenez  
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**The National School Committee was inactive during FY 2008.**

## TG Users Group Board

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Sallie Mae  
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Blinn College  
*Bryan, Texas*

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Panhandle Plains Student  
Loan Center  
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*College Station, Texas*

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Corpus Christi  
*Corpus Christi, Texas*

Beverly Wallwork  
Citibank  
*Pittsford, New York*

Grace Zapata  
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*San Antonio, Texas*

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Austin Community College  
*Austin, Texas*

Ron Brown  
University of Mary Hardin –  
Baylor  
*Belton, Texas*

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*Lincoln, Nebraska*

Jeff Dennis  
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University  
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Wachovia Education Finance  
*Austin, Texas*

Jeannie Gage  
Texas A&M University –  
Corpus Christi  
*Corpus Christi, Texas*

Jose Guerrero  
North Texas Higher  
Education Authority  
*Arlington, Texas*

Robert Hogeda  
Access Group  
*Austin, Texas*

Melet Leafgreen  
Texas Christian University  
*Ft. Worth, Texas*

Michael O'Rear  
Stephen F. Austin State  
University  
*Nacogdoches, Texas*

Jennifer Phillips  
Western Technical College  
*El Paso, Texas*

Tyler Pruett  
New Mexico State University  
*Las Cruces, New Mexico*

Javier Salinas  
Chase Bank  
*Austin, Texas*

Robert Sheridan  
University of Houston –  
Downtown  
*Houston, Texas*

Brian Sunshine — Lender Chair  
Nelnet  
*Bryan, Texas*

Phillip Wambsgans  
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## Physical Address

TG

301 Sundance Parkway

Round Rock, TX 78681

## TG Distribution Center

(Shipping, receiving, and overnight deliveries)

3500 Wadley Place, Bldg. C, Ste. 303

Austin, TX 78728-1244

## TG Web Sites

[www.tgslc.org](http://www.tgslc.org)

[www.AIE.org](http://www.AIE.org)

[www.positivebalance.org](http://www.positivebalance.org)

[www.ConsolidationStation.org](http://www.ConsolidationStation.org)

## Ask TG™

Search TG's FAQ database, submit a question to our support staff, review the status of your question, or give us your feedback — all from one convenient resource, designed for schools, lenders, students, and borrowers.

[www.tgslc.org](http://www.tgslc.org)

## Collections

Collections works with borrowers after default and informs them of TG's many repayment options.

(800) 222-6297

(512) 219-4739 — fax

[collections@tgslc.org](mailto:collections@tgslc.org)

## Communications

Communications provides publications and printed materials, subscriptions, Web sites, and media information.

(800) 252-9743, ext. 4732

(512) 219-4850 — fax

[communications@tgslc.org](mailto:communications@tgslc.org)

## Customer Assistance

The Customer Assistance team answers questions about all aspects of the FFELP for a wide range of TG customers: borrowers, schools, lenders and servicers, prospective students, and their families.

(800) 845-6267

(512) 219-4633 — fax

[cust.assist@tgslc.org](mailto:cust.assist@tgslc.org)

## Default Prevention

The Default Prevention team works with schools and lenders to prevent the default of student loans. Default Prevention also works with borrowers to avoid default, informs them of TG's many repayment options, and offers TG's financial literacy training program, Positive+Balance™.

(800) 338-4752

(512) 219-4630 — fax

[tgcares@tgslc.org](mailto:tgcares@tgslc.org)

## Educational Alliances and Partnerships

Educational Alliances and Partnerships works within the Title IV community and with other educational, financial aid, and civic organizations to promote awareness. They make middle school and high school students aware of requirements for getting into college as well as administer TG's Public Benefit Program.

(800) 252-9743, ext. 4964

(512) 219-4932 — fax

## Guarantee, Support, and Reporting

Guarantee, Support, and Reporting (GSR) includes the Loan Guarantee Operations, Product Support, and Data Reporting teams. GSR works with TG borrowers and business customers to process loan guarantees and disbursement changes.

The team is also responsible for federal reporting on loans and provides technical support for TG's products and services.

Loan Guarantee Operations — (800) 446-5616

[lgo.helps@tgslc.org](mailto:lgo.helps@tgslc.org)

Product Support — (800) 332-1455

[product.support@tgslc.org](mailto:product.support@tgslc.org)

Data Reporting — (800) 801-8416

[good.data@tgslc.org](mailto:good.data@tgslc.org)

## Ombudsman

The TG Ombudsman provides assistance to resolve specific borrower issues when other means have been exhausted.

(800) 252-9743

## Relationship Management and Consulting

The Relationship Management and Consulting team serves TG's school and lender customers. The team responds to customer needs, provides on-site consulting, and works to enhance customer relationships.

(800) 892-1357

(512) 219-4989 — fax

[relationship.management@tgslc.org](mailto:relationship.management@tgslc.org)

## Texas Financial Aid Information Center

This call center is a collaborative effort between TG and the Texas Higher Education Coordinating Board. TG's Customer Assistance team receives calls through this toll-free number, used by college-bound students, families, guidance counselors, and others seeking general information about planning and paying for higher education.

(888) 311-8881

[www.collegeforalltexas.com](http://www.collegeforalltexas.com)

# Financials

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# Management's Discussion and Analysis

This section of the Texas Guaranteed Student Loan Corporation (TG) annual financial report presents discussion and analysis of its financial performance during the fiscal years (FY) ended September 30, 2008, and 2007, and should be read in conjunction with TG's financial statements, which follow this section.

## Financial Highlights

- ▼ Beginning January 1, 2008, upon termination of its Voluntary Flexible Agreement (VFA), TG operated under the current statutory guarantor financing model. Primary changes are as follows:
  - Operating Fund – Elimination of Delinquency Prevention Fees (DPF); Default Aversion Fee (DAF) reversion to the statutory one-time, 1 percent fee paid from the Federal Fund upon initial Default Aversion Assistance Request (DAAR), refundable in the event of default; and, reduction of recovery rates to the statutory standards of 16 percent for direct collections, 10 percent for consolidation collections and 18.5 percent plus cost for rehabilitations.
  - Federal Fund – De-escrow of assets with the corresponding elimination of the escrow liability; cessation of weekly advanced 100 percent re-insurance on claim payments to lenders in favor of semi-monthly funding at the then effective statutory rates, typically 95 percent, along with creation of an allowance for the estimated future non-reinsured claims anticipated in the loan portfolio; and, estimated future payment of refundable DAF to the Operating Fund, which was provided from Department of Education (ED) under the VFA. While maintaining the second highest reserve ratio among Federal Family Education Loan Program (FFELP) guarantors at 0.90 percent, the decrease in Fund Equity, after VFA termination, was anticipated by management.
- ▼ Recent challenges in the credit markets coupled with lender fee reductions have resulted in potential ED participation and purchase of FFELP loans as well as activation of guarantor-funded and U.S. Treasury advance-funded Lender of Last Resort (LLR) programs. ED-purchased and federal advance-funded LLR loans lose their guarantee and related fees. Although \$52 million have been purchased by ED with no federal advance-funded LLR loans, the future volume of such loans, if any, cannot be reasonably estimated.
- ▼ TG has committed to pay the required 1 percent of loan disbursement Federal Default Fee (FDF) into its Federal Fund

on behalf of its borrowers from the inception of this practice in July 2006, through June 2009, resulting in FY 2008 and 2007 Operating Fund expenditures totaling \$54 million and \$34 million, respectively. The continuation of this practice may be subject to extension by action of the Board of Directors.

- ▼ Account Maintenance Fee (AMF) rates were reduced from 0.10 percent annually to 0.06 percent in FY 2008.
- ▼ TG has authorized annual expenditure of up to 5 percent of its available Operating Fund balance for public benefits, including scholarships and education related grants, totaling \$7.9 million and \$5.0 million in fiscal years 2008 and 2007, respectively.

## Overview of the Financial Statements

This report consists of four parts — Management's Discussion and Analysis (this section), Independent Auditors' Report, Financial Statements (Balance Sheets, Statements of Revenue and Expenses and Changes in Fund Equity, and Statements of Cash Flows), and Notes to the Financial Statements that explain some of the information in the financial statements and provide more detailed data.

TG is comprised of two funds: the Operating Fund and the Federal Fund. These distinct funds are defined in the Federal legislation which governs the FFELP within which TG functions as a guarantor. The Operating Fund, which is the property of TG, reports the guarantor activities as specified in the law including loan guarantee and supporting systems, guarantee maintenance, delinquency and default prevention, claims processing, and default recoveries, as well as financial aid awareness and related outreach activities. Operating Fund revenues are derived principally from "life of the student loan" activities funded by ED. The Federal Fund, which is considered to be the property of the United States, reports TG's student loan insurance activity and receives FDF. Without the VFA, this includes establishing an allowance for the non-reinsured portion of future default claims against the existing guaranteed loan portfolio, as well as payment of refundable DAF to the Operating Fund. Under the VFA, Federal Fund net assets at VFA inception were set aside in escrow, with TG receiving advance funding of 100 percent of eligible lender claims, and ED paying refundable DAF directly to the Operating Fund. Although not an operating entity, the Federal Fund derives revenue from FDF, recoveries on non-VFA defaults, refunds of non-VFA default aversion fees in the

event of loan default, interest on loans repurchased by lenders, and interest earned on non-escrowed assets. Interest on VFA escrowed assets is not Federal Fund revenue, and serves to increase both the VFA escrow as well as the Liability Payable from escrowed assets.

TG's funds are reported as proprietary component units of the State of Texas, and as such are accounted for using the flow of economic resources measurement focus and accrual basis of accounting. Accordingly, revenues are recognized when earned,

and expenses are recognized when the liability is incurred, regardless of the timing of the related cash flow, similar to private sector companies. The most significant examples include the Allowance for Non-reinsured Loan Defaults, which is a historical loan segment performance based estimate of the future nonreinsured claims recorded upon student loan guarantee; and the Default Aversion Refund Allowance, for which an estimated refund liability is recorded upon fee billing, in recognition of the long-term obligation to refund the fee in the event of subsequent loan default.

## Condensed Financial Information (in 000s)

	Operating Fund			Federal Fund		
	2008	2007	2006	2008	2007	2006
<b>Fund Equity</b>						
Current Assets	\$ 466,919	\$ 463,584	\$ 392,444	\$ 270,107	\$ 226,927	\$ 176,090
Capital Assets	40,788	38,600	35,332		1	4
Other Non-current Assets	(9,405)	(2,761)	(3,276)	9,499	4,667	5,203
Total Assets	498,302	499,423	424,500	279,606	231,595	181,297
Current Liabilities	12,878	25,407	20,507	24,545	15,795	15,938
Non-current Liabilities	94,414	99,576	92,961	250,410	138,527	130,615
Total Liabilities	107,292	124,983	113,468	274,955	154,322	146,553
Fund Equity:						
Invested in Capital Assets	32,795	28,984	24,169		1	4
Restricted			207	4,651	77,272	34,740
Unrestricted	358,215	345,456	286,656			
Total Fund Equity	\$ 391,010	\$ 374,440	\$ 311,032	\$ 4,651	\$ 77,273	\$ 34,744
<b>Changes in Fund Equity</b>						
Operating Revenues:						
Non-Recovery	\$ 47,183	\$ 79,684	\$ 78,656	\$ 58,978	\$ 37,309	\$ 11,677
Recovery	87,307	79,752	51,707	461	397	426
Total	134,490	159,436	130,363	59,439	38,706	12,103
Operating Expenses:						
Operations	82,896	76,684	68,578	5,405	3	6
Development Projects	2,474	2,838	3,267			
Provision Loan Defaults				134,286		
Total	85,370	79,522	71,845	139,691	3	6
Operating Income	49,120	79,914	58,518	(80,252)	38,703	12,097
Non-operating Rev(Exp):						
Investments	29,561	23,509	13,851	7,637	3,833	1,306
FDF Expense	(53,834)	(34,477)	(9,192)			
Public Benefits	(7,892)	(5,040)	(3,414)			
Other	(385)	(498)	(566)	(7)	(7)	
Total	(32,550)	(16,506)	679	7,630	3,826	1,306
Income (Deficit)	\$ 16,570	\$ 63,408	\$ 59,197	\$ (72,622)	\$ 42,529	\$ 13,403

## Overall Financial Analysis

TG has grown its combined total assets by \$47 million, or 6.5 percent, in FY 2008 and over \$125 million, or over 21 percent in FY 2007, while combined liabilities increased by \$103 million and \$19.3 million in FY 2008 and 2007, respectively. In both years, assets grew as a result of TG's operational performance, more so in 2007, while TG was operating for a full year under the VFA. Liabilities increased in 2008 from the establishment of the post-VFA Allowance for Non-reinsured Loan Defaults, partially offset by amounts no longer due ED upon termination of the VFA's weekly advance claim funding. The resulting \$56 million decrease and \$106 million increase in combined Fund Equity in fiscal years 2008 and 2007, respectively, are driven primarily by establishment of the post-VFA Allowance for Non-reinsured Loan Defaults and TG's operational performance, respectively. Elements of TG's financial performance are described in the Individual Fund Financial Analysis.

## Individual Fund Financial Analysis

### Operating Fund

Current Assets increased by \$3.3 million or 1 percent in FY 2008, due to the second quarter transition from the VFA to the statutory guarantor financing model restricted revenues and FDF driven Interfund Receivables, Payables. By comparison, the significant components of the \$71 million, 18 percent increase, in Current Assets in FY 2007 are as follows. Operating Fund investments grew by approximately \$75 million in FY 2007 from VFA-driven Operating Fund income and investment portfolio market valuation increases. Receivables Due from Department of Education were down \$5.3 million primarily from reduced September Default Aversion Fee (DAF) performance.

Capital Asset acquisitions in FY 2008 totaling \$5.1 million were information technology-focused, and included the acquisition of mainframe upgrades, servers, desktop, automated dialers and related software. During the FY 2007, TG acquired its previously leased warehouse facility for approximately \$4 million, funding this acquisition from its own cash reserves. Other significant 2007 asset purchases were predominantly technology oriented, and included desktop PCs, servers, software and upgrading to a new mainframe.

Other Non-current Assets decreased \$6.6 million or 240 percent in FY 2008, and resulted from anticipated future DAF refunds due upon underlying loan default to the Federal Fund on post-VFA DAF. By comparison, Other Non-current Assets increased \$0.5 million in FY 2007 as pre-VFA DAF refunds were paid to the Federal Fund.

Current Liabilities decreased \$13 million or 50 percent in FY 2008, leaving a comparable \$13 million for accounts payable, accrued liabilities and the current portion of notes payable between FY 2008 and 2007. This reduction results from the 2008 recognition into revenue of \$6.2 million DPF and \$7.6 million Recovery fees collected, but deferred in prior years, pending resolution of rate change applicability under the now terminated VFA. By comparison, Current Liabilities increased \$4.9 million in FY 2007 due to improved performance against corporate goals and success in the national market. Improved performance in the national market also increased corporate performance and related compensation earned by TG's staff by \$2.4 million, paid in the first quarter of the following FY. Amounts Due to Department of Education also increased \$2.5 million due to changes in Collections and DAF revenues.

Non-current Liabilities decreased \$5.2 million or 5 percent in FY 2008 as the estimated VFA DAF refund allowance is paid to ED upon underlying loan default, with no increase associated with post-VFA DAF paid by the Federal Fund, partially offset by default performance-driven expected future DAF refund increases. The estimated refund rate continues to exceed 50 percent. By comparison, Non-current Liabilities increased \$6.6 million or 7 percent in FY 2007 from refund allowance associated with FY 2007 VFA DAF and related loan default performance.

Operating Revenues decreased by \$25 million in FY 2008 as record loan guarantee volume gains were offset by statutory rate reductions and the loss of TG's performance-based VFA after the first fiscal quarter. DAF decreased \$32 million in FY 2008 as post-VFA standard rates were reduced from 1.25 percent to 1 percent without the prospect of rebilling or increased performance rates, and default performance reductions necessitated increases in the DAF refund allowance. Increases in Loan Processing Issuance Fees (LPIF) and AMF primarily from a 70 percent national market increase resulting in guaranteed loan disbursements totaling \$5.33 billion, up from \$3.79 billion in FY 2007, were offset by a statutory AMF rate decrease from 0.10 percent to 0.06 percent in FY 2008. Reductions in DPF, which were eliminated post-VFA, were offset by the recognition of prior-year fees previously deferred pending VFA rate change applicability. Despite post-VFA Recovery commission rate decreases from 20 percent to 10 percent for consolidation and 23 percent to 16 percent for cash collections, Recovery Revenue increased \$7.5 million in FY 2008 from an \$82 million increase in gross collection volume and the recognition of prior year fees previously

deferred pending VFA rate change applicability. By comparison, Operating Revenues increased by \$29 million in FY 2007, with Recovery revenue providing \$28 million of the increase as collections volumes increased from \$254 million to \$372 million, primarily due to TG's successful culmination of its strategic shift in focus from loan consolidation to rehabilitation as a collection tool sustaining TG's VFA top-tier performance. These Recovery revenues have been reduced by the deferral of collected fees pending VFA rate change applicability. Non-Recovery Operating Revenues increased by a net \$1.0 million from the following: LPIF increased \$1.9 million in FY 2007 due to continued guarantee volume growth; AMF, earned at 0.10 percent of outstanding portfolio in FY 2007 and 2006, increased \$1.8 million with TG's additions to its loan portfolio in FY 2007, and outpaced consolidations of loans out of the portfolio, claims and loans paid in full; the VFA's Delinquency Prevention Fees (DPF) increased approximately \$4.7 million due to TG improving performance from the VFA-base tier in FY 2006, to the VFA second performance tier in FY 2007; DAF, which was both a volume- and performance-driven fee under the VFA, decreased \$14 million due to a cure rate performance decrease from 89.6 percent in 2006 to 87.2 percent in 2007, resulting from VFA base tier performance during eight months of the FY. This DAF reduction was partially offset by recognition of \$6.8 million in prior-year collected fees, previously deferred pending VFA applicability.

Operating Expenses increased \$6.2 million or 8 percent in FY 2008, driven primarily by a budgeted \$4.9 million increase in personnel costs, including merit raises, benefits and additional customer- and delinquency-focused positions, as well as a \$1.0 million increase in employee performance awards. By comparison, Operating Expenses increased \$7.7 million or 11 percent in FY 2007, also driven primarily by a \$2.7 million increase in personnel costs including: merit raises, benefits and additional positions; a \$2.9 million increase in employee performance bonuses; and \$4.8 million increase in outsourced loan recovery commissions. These increases were partially offset by a \$1 million decrease in other operations costs primarily related to the data loss event remediation and a \$0.4 million decrease in depreciation as TG extended its utilization of existing desktop and server technology.

Non-operating Revenue (Expense) decreased \$16 million in FY 2008 primarily from a volume-driven FDF Expense increase, which was partially offset by investment portfolio results. The FDF Expense increased directly in proportion with the \$1.5 billion guaranteed loan disbursement increase on guaranteed loan volume gains in FY 2008. TG's Public Benefit program continued to expand by \$2.9 million toward its funding maximum of 5 percent available fund balance. Offsetting these expense increases, higher market valuations of TG's held-to-maturity investment portfolio at fiscal year-end 2008 from the recent economic downturn, resulted in a \$9.2 million improvement in the net change in fair value of investments, while interest increased \$1.9 million in FY 2008 due to the operating income driven investment portfolio increases. By comparison, Non-operating Revenue (Expense) decreased \$17 million in FY 2007 from the first full year of FDF Expense and an increase in Public Benefit distributions, partially offset by investment portfolio results. FDF and its payment by TG's Operating Fund commenced in the fourth quarter of FY 2006, which when coupled with a \$473 million increase in guaranteed loan disbursements, resulted in a \$25 million FDF Expense increase. TG's Public Benefit program expanded expense by \$1.6 million, moving expenditures toward its programmatic funding maximum. Offsetting these expense increases, higher market valuations at fiscal year-end 2007 resulted in a \$5.8 million improvement in the net change in fair value of investments, and interest increased \$3.8 million in FY 2007 due to larger operating income driven investment portfolio increases.

## **Federal Fund**

Current Assets increased \$43 million or 19 percent in FY 2008, primarily from the \$54 million in FDF-paid by TG's Operating Fund and \$8.2 million interest earned on investments no longer VFA escrowed, offset by post-VFA non-reinsured portion of default claim payments and DAF payments to the Operating Fund. ED's post-VFA in arrears funding of claim reinsurance results in \$39 million of the current asset increase being amounts due from ED. By comparison, Current Assets increased \$51 million or 28 percent in FY 2007, primarily from the \$34 million of FDF-paid by TG's Operating Fund; the increase in other Federal Fund Income, an increase of \$8 million in cash to support expected claims; and a \$4 million increase in VFA Escrowed Assets resulting from market growth and interest earnings after funding the final \$4.2 million reserve return payment to U.S. Treasury, required under the 1998 HEA Reauthorization.

Other Non-current Assets increased \$4.8 million or 104 percent in FY 2008 from the post-VFA DAF refund receivable, partially offset by writing off \$1.8 million in decade-old recovery commissions due from ED deemed uncollectible since they were not settled by VFA transition. By comparison, Other Non-current Assets decreased by \$0.5 million or 10 percent in FY 2007 from the continuing collections on the pre-VFA DAF refund receivable.

Current Liabilities increased by \$8.8 million or 56 percent in FY 2008 due to the Federal Fund's \$13 million receipt of VFA DAF refunds from the Operating Fund, awaiting establishment of a post-VFA settlement mechanism with ED. This increase is partially offset by a lack of September rehabilitations resulting in a net \$4.9 million decrease in amounts due ED from September collections activity. By comparison, Current Liabilities remained consistent in FY 2007. TG's payment of final scheduled \$4.2 million return of reserves, reduction in liabilities, was offset by an increase in amounts Due to Department of Education as a result of increased collection activity from TG's shift to a rehabilitation collection strategy.

Non-current Liabilities increased \$112 million or 81 percent with the establishment of a post-VFA Allowance for Non-reinsured Loan Defaults. While default claims under the VFA were 100 percent reinsured by ED, post-VFA reinsurance reverts to the statutory rates in effect at loan guarantee ranging from 95 percent to 100 percent, with the majority of TG's portfolio carrying 95 percent reinsurance. The allowance represents management's estimate of the non-reinsured portion of projected future default claims against TG's existing \$26 billion guaranteed loan portfolio based upon historical loan segment performance. This allowance increase was partially offset by eliminating, at VFA escrow transition, \$6.9 million in Federal Section 422 Advances whose payment is no longer reasonably probable. By comparison, Non-current Liabilities increased \$7.9 million in FY 2007 from VFA escrowed investment earnings.

Fund Equity decreased \$73 million in 2008 from establishment of the post-VFA Allowance for Non-reinsured Loan Defaults. Management has continually monitored this potential obligation throughout the operation of the VFA, and has always been aware that upon termination of the VFA, the 100 percent reinsurance would give way to the statutory re-insurance rates. Therefore the magnitude of the allowance and its impact upon Federal Fund Equity was anticipated. By comparison, Federal Fund Equity increased almost \$43 million in FY 2007 under the VFA's 100 percent reinsurance and the first full year of FDF revenue.

Operating Revenues increased \$21 million or 54 percent in FY 2008 from FDF related to TG's record increase in guaranteed loan disbursements, as well as, Non-current Asset and Liability reductions referenced previously. By comparison, Operating Revenues increased by \$27 million, more than tripling in FY 2007, as the first full year of FDF following the fourth fiscal quarter 2006 fee initiation.

Operating Expenses increased \$140 million in FY 2008 primarily from the post-VFA provision for future non-reinsured loan defaults, \$95 million of which relates to loans guaranteed prior to FY 2008, while \$39 million relates to FY 2008 loan guarantees. Also contributing to the increase is \$13 million post-VFA DAF paid to the Operating Fund, net of \$7.1 million expected future refunds.

Non-operating Revenue (Expense) increased \$3.8 million, or nearly doubled in FY 2008, as all post-VFA investment earnings have been recognized into income rather than a portion remaining within the VFA escrow. By comparison, FY 2007 Non-operating Revenues included investment interest derived primarily from non-escrowed Federal Fund investments, which increased in FY 2007 due to the first full year of FDF revenue. While investment purchases have been at progressively higher coupon rates over the period, revenues have also been positively impacted by changes in investment market value.

## Capital Assets and Long Term Debt

TG's most significant capital asset is its primary operating facility with an original cost of almost \$33 million. The FY 2003 acquisition of this facility was partially financed with a \$16.25 million, 10-year, 4.75 percent fixed-rate loan from an institutional lender, of which \$8.0 million remains outstanding at September 30, 2008. In addition, in FY 2007, TG acquired its previously leased warehouse facility for approximately \$4 million, funding this acquisition from its own cash reserves. Other significant asset purchases were predominantly technology-oriented, and included the acquisition of mainframe upgrades, desktop PCs, servers, telephony, and related software.

TG continues to provide stand-by liquidity under a Prime Broker margin facility with borrowing capacity up to 95 percent of the investment portfolio fair value. To facilitate TG's cash management strategy for security reinvestment, the facility was accessed on several occasions in FY 2008 and 2007 typically on a one day basis. Draws ranged in size up to \$9.5 million, with the total of all draws approximating \$67 million for 2008.

In April 2007, TG renewed its \$5 million, no commitment fee, unsecured line of credit with its depository institution, bearing interest at the institution's prime rate. The facility, which expires April 30, 2009, has not been accessed.

TG provides a unified student loan funding service (EFT), which upon participant approval, draws funds from participating lenders while simultaneously distributing the funds to participating schools using commercial bank overnight Automated Clearing House (ACH) transactions. While rare, failure of a participating lender to fund its draw would result in an overdraft position in TG's ACH clearing account. EFT daily volume is typically less than \$10 million. However, during FY 2008 August and January peaks, there were four days with disbursements exceeding \$100 million, the highest single day being \$273 million.

### **Significant Known Facts, Decisions, or Conditions**

Recent credit market challenges have the potential to impact TG and its operations in future years. Lender liquidity issues, coupled with recent statutory reductions in FFELP lender profitability, have resulted in some lenders exiting the student loan market. In an effort to mitigate this issue, recent legislation has provided lenders, operating under specific conditions, with the option to sell participation interests in student loan portfolios, originated between July 1, 2008 and June 30, 2010 to ED; or to "put" or sell the loans outright to ED. While participation loans retain their guarantee, "put" loans do not, resulting in the removal from the guarantor's portfolio and eliminating the possibility of future revenues from those loans. In addition, TG has established a fully functional Lender of Last Resort (LLR) process, under which TG will first access funds available through its one participating lender, after which with TG participating as a FFELP lender using up to \$50 million of its available assets, as well as available U.S. Treasury advances, as necessary. LLR loans made with such advances do not enter the guarantor portfolio. The extent of put or advance LLR loans and their resulting impact on future TG results from operations cannot be determined. Also, FFELP lenders' participation in consolidation and rehabilitation recovery loans has been reduced by these circumstances with potential future impact to TG results of operations.

TG has committed to pay the FDF from its Operating Fund on behalf of its customers through June 2009, subject to extension. Given current volume estimates, this commitment could exceed \$43 million in FY 2009.

TG financial modeling indicates that FY 2009 loan guarantee, volume-driven FDF revenues are expected to exceed related allowance requirements, resulting in an increase in Federal Fund Equity.

TG has entered into negotiation with ED for a new VFA which would include substantially lower performance fees as compared to the compensation formula under TG's original VFA to achieve ED's assessment of required cost neutrality for such agreements. A new VFA would have corresponding terms which would require the escrow of reserve assets and provide for 100 percent claims reinsurance. TG is unable to currently determine the outcome of these negotiations.

In May 2006, an employee of a company which TG engaged to devise a document management system lost a device which contained non-public information of a portion of TG's borrowers. At that time, TG undertook remediation measures and statutorily-required notification to the affected borrowers. At this time TG, has not received any credible report of any information theft regarding any affected borrower arising from the incident and does not currently anticipate any resulting litigation which would have a material, adverse financial impact on TG.

### **Contacting TG's Financial Management**

This financial report is designed to provide our customers, business associates, and creditors with a general overview of TG's finances. Questions about this report can be directed to TG's Chief Financial Officer, James Patterson at (512) 219-4611 or [james.patterson@tgscl.org](mailto:james.patterson@tgscl.org), or to TG's Controller, Mark Zarsky, at (512) 219-4617 or [mark.zarsky@tgscl.org](mailto:mark.zarsky@tgscl.org).

# Independent Auditors' Report

Board of Directors

Texas Guaranteed Student Loan Corporation:

We have audited the accompanying financial statements of the Texas Guaranteed Student Loan Corporation (TG), a component unit of the State of Texas, as of and for the years ended September 30, 2008 and 2007, which collectively comprise TG's basic financial statements as listed in the table of contents. These financial statements are the responsibility of TG'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 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 TG's internal control over financial reporting. Accordingly, we express no such opinion. An audit 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 opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of TG as of September 30, 2008 and 2007, and the respective changes in financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In accordance with the Government Auditing Standards, we have also issued our report dated November 26, 2008, on our consideration of TG'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.

The management's discussion and analysis on pages 18 through 23 is not a required part of the basic financial statements but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurements and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP  
Austin, Texas  
November 26, 2008

## Balance Sheets (in 000s)

	September 30, 2008			September 30, 2007		
	Operating Fund	Federal Fund	Total	Operating Fund	Federal Fund	Total
<b>Assets</b>						
Current Assets:						
Cash & Cash Equivalents	\$ 9,438	\$ 13,855	\$ 23,293	\$ 3,449	\$ 19,728	\$ 23,177
Receivables						
Due from Department of Education	16,418	38,739	55,157	18,451		18,451
Accrued Interest & Other	4,015	2,082	6,097	4,368	476	4,844
Investments	438,862	212,104	650,966	436,063	69,939	506,002
Interfund Receivables, Payables	(3,327)	3,327	-	(47)	47	-
Other Current Assets	1,513		1,513	1,300		1,300
Escrowed Assets - VFA	-	-	-	-	136,737	136,737
<b>Total Current Assets</b>	<b>466,919</b>	<b>270,107</b>	<b>737,026</b>	<b>463,584</b>	<b>226,927</b>	<b>690,511</b>
Non-current Assets:						
Capital Assets, Net	40,788		40,788	38,600	1	38,601
Interfund Default Aversion Fee Refund Allowance	(9,499)	9,499	-	(2,877)	2,877	-
Escrowed Assets — VFA			-		1,790	1,790
Other Non-current Assets, Net	94	-	94	116	-	116
<b>Total Non-current Assets</b>	<b>31,383</b>	<b>9,499</b>	<b>40,882</b>	<b>35,839</b>	<b>4,668</b>	<b>40,507</b>
<b>Total Assets</b>	<b>\$ 498,302</b>	<b>\$ 279,606</b>	<b>\$ 777,908</b>	<b>\$ 499,423</b>	<b>\$ 231,595</b>	<b>\$ 731,018</b>
<b>Liabilities and Fund Equity</b>						
Current Liabilities:						
Accounts Payable and Accrued Liabilities	\$ 11,176	\$ 96	\$ 11,272	\$ 10,496	\$ 328	\$ 10,824
Due to Department of Education		10,599	10,599	13,288	15,467	28,755
Due to Department of Education — Default Aversion Fee Refunds		13,850	13,850			-
Note Payable	1,702	-	1,702	1,623	-	1,623
<b>Total Current Liabilities</b>	<b>12,878</b>	<b>24,545</b>	<b>37,423</b>	<b>25,407</b>	<b>15,795</b>	<b>41,202</b>
Non-current Liabilities:						
Due to Department of Education Default Aversion Fee Refund Allowance	87,301		87,301	90,563		90,563
Note Payable	6,291		6,291	7,993		7,993
Allowance for Non-reinsured Loan Defaults		250,410	250,410			-
Liabilities Payable from Escrowed Assets			-		138,527	138,527
Other	822	-	822	1,020	-	1,020
<b>Total Non-current Liabilities</b>	<b>94,414</b>	<b>250,410</b>	<b>344,824</b>	<b>99,576</b>	<b>138,527</b>	<b>238,103</b>
<b>Total Liabilities</b>	<b>107,292</b>	<b>274,955</b>	<b>382,247</b>	<b>124,983</b>	<b>154,322</b>	<b>279,305</b>
Fund Equity:						
Net Assets Invested in Capital Assets, net of related debt	32,795	-	32,795	28,984	1	28,985
Restricted Net Assets		4,651	4,651		77,272	77,272
Unrestricted Net Assets	358,215	-	358,215	345,456	-	345,456
<b>Total Fund Equity</b>	<b>391,010</b>	<b>4,651</b>	<b>395,661</b>	<b>374,440</b>	<b>77,273</b>	<b>451,713</b>
<b>Total Liabilities &amp; Fund Equity</b>	<b>\$ 498,302</b>	<b>\$ 279,606</b>	<b>\$ 777,908</b>	<b>\$ 499,423</b>	<b>\$ 231,595</b>	<b>\$ 731,018</b>

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

## Statements of Revenue and Expenses and Changes in Fund Equity (in 000s)

	Fiscal Year Ended September 30, 2008			Fiscal Year Ended September 30, 2007		
	Operating Fund	Federal Fund	Total	Operating Fund	Federal Fund	Total
<b>Operating Revenues</b>						
Loan Processing and Issuance Fee	\$ 21,336	\$ -	\$ 21,336	\$ 15,173	\$ -	\$ 15,173
Account Maintenance Fee	17,077		17,077	23,304		23,304
Delinquency Prevention Fee	9,334		9,334	9,693		9,693
Default Aversion Fee (net of \$24,540 and \$29,142 refund provision)	(2,494)		(2,494)	29,900		29,900
Recovery Revenue	87,307	461	87,768	79,752	397	80,149
Other Revenue	1,930	5,144	7,074	1,614	3,832	5,446
Federal Default Fee	-	53,834	53,834	-	34,477	34,477
<b>Total Operating Revenues</b>	<b>134,490</b>	<b>59,439</b>	<b>193,929</b>	<b>159,436</b>	<b>38,706</b>	<b>198,142</b>
<b>Operating Expenses</b>						
Operations	82,896		82,896	76,684		76,684
Development Projects	2,474		2,474	2,838		2,838
Provision for Loan Defaults		39,246	39,246			
Provision for Loan Defaults — Post VFA Transition		95,040	95,040			
Default Aversion Expense (net of \$7,114 anticipated refunds)		5,348	5,348			
Other Expenses	-	57	57	-	3	3
<b>Total Operating Expenses</b>	<b>85,370</b>	<b>139,691</b>	<b>225,061</b>	<b>79,522</b>	<b>3</b>	<b>79,525</b>
<b>Operating Income (Deficit)</b>	<b>49,120</b>	<b>(80,252)</b>	<b>(31,132)</b>	<b>79,914</b>	<b>38,703</b>	<b>118,617</b>
<b>Non-operating Revenues (Expenses)</b>						
Federal Default Fee Expense	(53,834)		(53,834)	(34,477)		(34,477)
Public Benefits	(7,892)		(7,892)	(5,040)		(5,040)
Net Increase (Decrease) in the Fair Value of Investments	9,239	(599)	8,640	5,127	1,006	6,133
Investment Interest	20,322	8,236	28,558	18,382	2,827	21,209
Net Gain (Loss) on Sale of Assets	31		31			
Interest Expense	(416)	(7)	(423)	(498)	(7)	(505)
<b>Total Non-operating Revenues (Expenses)</b>	<b>(32,550)</b>	<b>7,630</b>	<b>(24,920)</b>	<b>(16,506)</b>	<b>3,826</b>	<b>(12,680)</b>
<b>Income (Deficit)</b>	<b>16,570</b>	<b>(72,622)</b>	<b>(56,052)</b>	<b>63,408</b>	<b>42,529</b>	<b>105,937</b>
<b>Fund Equity, Beginning</b>	<b>374,440</b>	<b>77,273</b>	<b>451,713</b>	<b>311,032</b>	<b>34,744</b>	<b>345,776</b>
<b>Fund Equity, Ending</b>	<b>\$ 391,010</b>	<b>\$ 4,651</b>	<b>\$ 395,661</b>	<b>\$ 374,440</b>	<b>\$ 77,273</b>	<b>\$ 451,713</b>

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

## Statements of Cash Flows (in 000s)

	Fiscal Year Ended September 30, 2008			Fiscal Year Ended September 30, 2007		
	Operating Fund	Federal Fund	Total	Operating Fund	Federal Fund	Total
<b>Cash Flows from Operating Activities:</b>						
Claims Reinsurance Received	\$ -	\$ 647,086	\$ 647,086	\$ -	\$ 605,137	\$ 605,137
Collection of Defaulted Loans		271,287	271,287		257,059	257,059
Fees Received (Paid)	129,206	(25,062)	104,144	170,237	(35,699)	134,538
Proceeds from Other Revenues	2,355	6,934	9,289	1,019	3,832	4,851
Claims Payments		(705,066)	( 705,066)		(604,538)	(604,538)
Collection Payments to Department of ED		(204,905)	( 204,905)		(184,497)	(184,497)
Payments to Suppliers for Goods and Services	(39,113)	( 288)	(39,401)	(37,587)	-	(37,587)
Payments to Employees	(43,609)	-	(43,609)	(37,182)	-	(37,182)
<b>Net Cash Provided By (Used In) Operating Activities</b>	<b>48,839</b>	<b>(10,014)</b>	<b>38,825</b>	<b>96,487</b>	<b>41,294</b>	<b>137,781</b>
<b>Cash Flows from Non-Capital Financing Activities:</b>						
Proceeds from Margin Facility	8,310	59,037	67,347	24,564	12,278	36,842
Principal Payments on Margin Facility	(8,310)	(59,037)	(67,347)	(24,564)	(12,278)	(36,842)
Interest Paid	(1)	(7)	(8)	(8)	(8)	(16)
Federal Default Fees Paid	(55,095)	-	(55,095)	(33,142)	-	(33,142)
Public Benefits	(7,892)	-	(7,892)	(5,040)	-	( 5,040)
<b>Net Cash Used In Non-Capital Financing Activities</b>	<b>(62,988)</b>	<b>(7)</b>	<b>(62,995)</b>	<b>(38,190)</b>	<b>(8)</b>	<b>(38,198)</b>
<b>Cash Flows from Capital and Related Financing Activities:</b>						
Proceeds from Sale of Assets	50	-	50	5	-	5
Purchases of Property, Plant and Equipment	(4,595)	-	(4,595)	(5,814)	-	( 5,814)
Principal Payments on Note Payable	(1,623)	-	(1,623)	(1,548)	-	( 1,548)
Interest Paid	(384)	-	(384)	(453)	-	(453)
<b>Net Cash Used In Capital and Related Financing Activities</b>	<b>(6,552)</b>	<b>-</b>	<b>(6,553)</b>	<b>(7,810)</b>	<b>-</b>	<b>( 7,810)</b>
<b>Cash Flows from Investing Activities:</b>						
Purchases of Investments	(132,624)	(154,473)	( 287,097)	(127,865)	(71,523)	(199,388)
Proceeds from Maturity or Sale of Investments	139,064	147,551	286,615	57,540	31,000	88,540
Interest Received	20,250	9,853	30,103	18,111	8,708	26,819
<b>Net Cash Provided By (Used In) Investing Activities</b>	<b>26,690</b>	<b>2,931</b>	<b>29,621</b>	<b>(52,214)</b>	<b>(31,815)</b>	<b>(84,029)</b>
<b>Increase (Decrease) in Cash and Cash Equivalents</b>	<b>5,989</b>	<b>(7,090)</b>	<b>(1,101)</b>	<b>(1,727)</b>	<b>9,471</b>	<b>7,744</b>
<b>Cash and Cash Equivalents, Beginning</b> <i>(Including \$1,217 and \$125 in Federal Fund Escrowed Cash Equivalents at September 30, 2007 and 2006, respectively)</i>	<b>3,449</b>	<b>20,945</b>	<b>24,394</b>	<b>5,176</b>	<b>11,474</b>	<b>16,650</b>
<b>Cash and Cash Equivalents, Ending</b> <i>(Including \$0 and \$1,217 in Federal Fund Escrowed Cash Equivalents at September 30, 2008 and 2007, respectively)</i>	<b>\$ 9,438</b>	<b>\$ 13,855</b>	<b>\$ 23,293</b>	<b>\$ 3,449</b>	<b>\$ 20,945</b>	<b>\$ 24,394</b>
<b>Operating Income (Deficit)</b>	<b>\$ 49,120</b>	<b>\$ (80,252)</b>	<b>\$ ( 31,132)</b>	<b>\$ 79,914</b>	<b>\$ 38,703</b>	<b>\$ 118,617</b>
Adjustments to Reconcile Operating Income (Deficit) to Net Cash Provided By (Used In) Operating Activities:						
Depreciation	2,900	1	2,901	2,681	3	2,684
Other	22	-	22	22	-	22
Change in Assets & Liabilities (Including Escrowed Assets & Liabilities):						
Receivables	2,458	(36,950)	(34,492)	4,710	385	5,095
Other Assets	( 213)	-	(213)	(45)	-	(45)
Interfund Receivables, Payables	11,163	(9,902)	1,261	(3,681)	2,346	( 1,335)
Liabilities Payable from Escrowed Assets		-	-		(4,208)	( 4,208)
Accounts Payable & Accrued Liabilities	(60)	(232)	(292)	2,096	15	2,111
Due to Department of Education	(16,551)	8,983	(7,568)	10,790	4,050	14,840
Allowance for Non-Reinsured Loan Defaults and Other Costs	-	108,338	108,338	-	-	-
<b>Total Adjustments</b>	<b>(281)</b>	<b>70,238</b>	<b>69,957</b>	<b>16,573</b>	<b>2,591</b>	<b>19,164</b>
<b>Net Cash Provided By (Used In) Operating Activities</b>	<b>\$ 48,839</b>	<b>\$ (10,014)</b>	<b>\$ 38,825</b>	<b>\$ 96,487</b>	<b>\$ 41,294</b>	<b>\$ 137,781</b>

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

# Notes to Financial Statements

## 1] Organization and Operations

**Initial structure:** The Texas Guaranteed Student Loan Corporation (TG) is a Texas public, nonprofit corporation, organized under the provisions of House Bill 38 of the 66th Texas Legislature, to operate as a guaranty agency under the Federal Guaranteed Student Loan Program. TG was organized in February 1980, with initial loan guarantee operations beginning in January 1981. TG is subject to the Texas Sunset Act (Chapter 325, Government Code) and as a result of Sunset Review completed in 2004, the Texas Legislature enacted legislation to extend TG's existence until September 1, 2017. The Comptroller of Public Accounts serves as trustee to administer its assets should it liquidate, and to pursue its obligations in that capacity would satisfy all of TG's outstanding obligations.

**Purpose:** The Federal Family Education Loan Program (FFELP) under which TG operates, was established by Congress and is administered by the U.S. Department of Education (ED) as a means of making loans available to students attending colleges, universities and postsecondary educational and vocational schools. FFELP provides for TG to guarantee the repayment of principal and accrued interest to lenders for eligible student loans. TG is responsible for processing loans submitted for guarantee, issuing loan guarantees, providing collection assistance to lenders for delinquent loans, paying lender claims for loans in default, and collecting loans on which default claims have been paid. TG also informs schools, students, lenders, secondary markets and servicers of FFELP requirements and encourages participation. In addition, TG engages in outreach activities to make students and parents aware of the loan programs and other means to promote access.

**Portfolio:** FFELP loan volume guaranteed during the FY, by school type is as follows, net of cancellations (in 000s):

	Sept. 30, 2008	Sept. 30, 2007
Four-Year	\$ 5,029,500	\$ 3,593,840
Two-Year	456,530	357,620
Proprietary	1,230,300	326,500
Consolidation	662,810	1,461,390
Total	\$ 7,379,140	\$ 5,739,350

Outstanding guaranteed student loans, by school type, are as follows (in 000s):

	Sept. 30, 2008	Sept. 30, 2007
Four-Year	\$ 12,636,551	\$ 9,767,663
Two-Year	1,465,887	1,181,070
Proprietary	1,794,989	1,098,851
Consolidation	10,102,504	10,172,739
Total	\$ 25,999,931	\$ 22,220,323

**Subsidiary:** In FY 1995, TG established Educational Assistance Services, Inc. (EAS) as a for-profit, wholly owned subsidiary for the furtherance of its student loan and higher education mission. While EAS has been dormant throughout the periods presented, in November 2008, TG invested an additional \$100,000 to fund EAS's upcoming loan collections operations.

## 2] Significant Accounting Policies

**Fund accounting:** The accounts of TG are maintained in accordance with the principles of fund accounting. This is a system under which resources are classified for accounting and reporting purposes into funds established according to their purpose.

Major Funds — TG's Operating Fund is property of the guaranty agency and incurs substantially all FFELP operational costs, as well as costs related to financial aid awareness initiatives, related outreach activities and other student financial aid activities, as selected by the guaranty agency. TG's Federal Fund, which finances FFELP insurance activities, is considered to be the property of the United States. Recall of Federal Fund assets requires Congressional action.

TG is reported as a proprietary component unit in the State of Texas financial statements. Proprietary component units are accounted for using the flow of economic resources measurement focus and the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when the liability is incurred, regardless of the timing of the related cash flow. Accordingly, TG has adopted the provisions of Governmental Accounting Standards Board (GASB) Statement Number 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting, which specifies that in addition to adopting all applicable GASB pronouncements, TG has adopted Statements and Interpretations of the Financial Accounting Standards Board,

Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure issued prior to November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

**Voluntary Flexible Agreement:** ED terminated TG's Voluntary Flexible Agreement (VFA), effective January 1, 2008, at which time, TG reverted to the currently effective statutory guarantor funding model.

In March 2001, TG entered into a VFA with ED as provided for in Reauthorization. TG's VFA increased the focus upon borrower delinquency and default prevention, and included the following feature: the escrow of all Federal Reserve cash, cash equivalents, and investments; 100 percent by ED of reinsurance of default claims paid during the VFA; continued loan processing and portfolio maintenance revenues as provided under HEA; creation of a new delinquency prevention-focused fee; and the establishment of a performance-based fee structure for default aversion and collection activities.

**Cash and cash equivalents:** For purposes of the statement of cash flows, TG considers as cash equivalents, certificates of deposits with original maturity of three months or less, overnight repurchase agreements, and all money market account and mutual fund assets.

**Custodial Credit Risk** — To minimize this risk, TG employs U.S. Government and Agency instrument overnight repurchase agreements to minimize cash in its depository institution. Repurchase agreements totaled \$1.78 million and \$4.66 million for the Operating fund and \$16.0 million and \$44.9 million for the Federal Fund at September 30, 2008 and 2007, respectively. Remaining balances, if any, are subject to FDIC and SIPC insurance and up to \$3 million in pledged collateral.

**Investments:** Investments are reported at fair value, based upon quoted market prices, with the change in fair value of investments captioned as Net Increase (Decrease) in the Fair Value of Investments, and interest income reported at the relevant stated interest rate.

TG's Operating Fund, in accordance with Texas Public Funds Investment Act provisions, is authorized to invest in: US Government obligations, including agencies and instrumentalities, State of Texas direct obligations, Texas-based financial institution certificates of deposit, as well as, subject to certain restrictions, obligations of states, agencies, counties, cities, and other political subdivisions of any state; collateralized

mortgage obligations; commercial paper; direct and reverse repurchase agreements; no-load money market and mutual funds and investment pools. Individual investment maturities are limited to a maximum of 10 years. Average maturities will depend upon cash flow requirements of TG and the safety, liquidity, and yield parameters set forth in TG's policy.

TG's Federal Fund investments are limited by HEA provisions to US Government obligations, including agencies and instrumentalities and State of Texas direct obligations, as well as, subject to certain restrictions, obligations of states, agencies, counties and other political subdivisions of any state; no-load money market and mutual funds and direct and reverse repurchase agreements investing exclusively in obligations described herein.

TG's investment policies and practice address various investment risks as follows:

**Credit Risk** — TG minimizes credit risk, the risk of loss due to the failure or downgrade of the security issuer or backer, by: limiting investments to investment grade securities as authorized by TG's investment policy, prequalifying the financial institutions and broker/dealers with which TG will do business, and diversifying the investment portfolio so that potential losses on individual securities will be minimized. TG's U.S. Agency Obligations and Municipalities investments are Aaa rated by Moody's.

**Concentration of Credit Risk** — TG maintains maximum percent of portfolio limits by instrument type, and limits single security issues to no more than \$10 million, or 5 percent, of the applicable fund's portfolio.

**Interest Rate Risk** — TG minimizes the risk that the market value of securities in the portfolio will fall due to changes in general interest rates by: structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, avoiding the need to sell securities prior to maturity; investing operational funds primarily in shorter-term securities, money market mutual funds and similar investment pools; and diversifying the investment portfolio maturities over a reasonable time horizon to limit exposure to unusual yield curves, maintaining the duration of each fund's portfolio at six or less.

**Foreign Currency Risk** — TG's authorized investments are not subject to this risk.

**Capital Assets:** Capital Assets are recorded at cost. Depreciation is provided on the straight-line method using estimated useful lives of three to 10 years for vehicles, equipment, furniture and software, the shorter of 10 years or the remaining lease period for the leasehold improvements, and 40 years for buildings. Internal development costs associated with software utilized in TG operations are expensed as incurred. Purchased software is capitalized in accordance with the capital asset policy.

**Escrowed Assets - VFA:** Escrowed assets were returned to TG's Federal Fund reserves post-VFA, and reported as fund equity, with the concurrent elimination of the corresponding Liabilities Payable from Escrowed Assets. Under the VFA, Federal Fund cash, cash equivalents and investments at VFA inception and subsequent earnings thereon were escrowed. These escrowed assets were as follows (in 000s):

	<u>Sept. 30, 2007</u>
<b>Current Assets</b>	
Cash & Cash Equivalents	\$ 1,217
Accrued Interest & Other	1,609
Investments	<u>133,911</u>
Total	<u>\$ 136,737</u>
<b>Non-current Assets</b>	
Due from ED	\$ 1,790
Total	<u>\$ 1,790</u>
Total	<u>\$ 138,527</u>

As provided for in the VFA, ED was a party to the escrow agreement and while escrowed, these assets were due to ED, with no stated repayment term. Accordingly, TG utilized agency accounting, offsetting the escrowed assets with an obligation to ED captioned "Liabilities Payable from Escrowed Assets."

**Classification of Operating and Non-Operating Revenues and Expenses:** Program revenues and expenses related to FFELP and other education-related activities as determined by TG are classified as operating, the primary components of which include the revenues further described in this note, as well as the Operating Funds; personnel, facility, contractual obligations, travel, maintenance, development and depreciation costs and the Federal Fund's Provision for Loan Defaults and post-VFA DAF. Consistent with GASB Statement Number 9, Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting, operating revenues and expenses exclude financing, investing

and capital assets disposition activities. Other revenues and expenses which do not meet the operating categorization requirements are also classified as non-operating.

**Revenue Recognition:**

Loan Processing and Issuance Fee (LPIF) — LPIF is paid quarterly by ED to TG's Operating Fund equal to 0.40 percent of non-consolidation FFELP loans guaranteed. Loan disbursement typically occurs after guarantee and in two installments. VFA status did not impact LPIF rates.

Account Maintenance Fee (AMF) — AMF is paid quarterly by ED to TG's Operating Fund equal to 0.06 percent and 0.10 percent of TG's FY end guarantee portfolio's original principal balance outstanding in fiscal years 2008 and 2007, respectively. VFA status did not impact AMF rates.

Delinquency Prevention Fee (DPF) — Post-VFA, TG is no longer eligible for DPF. Under the VFA, TG's Operating Fund received monthly DPF from ED, at an annual base rate of 0.042 percent of TG's beginning of year loans in repayment portfolio, with performance rate increases up to 0.10 percent based upon reductions in annual Default Aversion Assistance Requests (DAAR), relative to loans in repayment. TG performed at the 3rd level for the first three months of FY 2008 and the 2nd level in FY 2007, resulting in fee rates of 0.085 percent and 0.06 percent, respectively.

Default Aversion Fee (DAF) — Post-VFA DAF is limited to 1 percent of delinquent loan principal and interest when reported to TG by the holder for the first time under regulatory required DAAR, paid by the Federal Fund. VFA DAF equaled 1.25 percent of a regulatory required DAAR, with potential increases up to 4 percent based upon monthly cohort cure rate performance, paid by ED. TG's weighted average VFA DAF performance fee rate was 1.25 percent and 1.66 percent for the first three months of FY 2008 and FY 2007, respectively. Unlike statutory provisions, the VFA permitted DAF billing on a specific loan once every 12 months. Regardless of VFA status, all related DAF is refundable upon underlying loan default. Accordingly, DAF is recognized upon DAAR reporting to TG and the VFA cure performance when applicable, net of anticipated future refunds which total \$96.80 million and \$93.44 million at September 30, 2008 and 2007, respectively. As of September 30, 2008, the Federal Fund had received \$13.85 million in refunds from the Operating Fund applicable to DAF fees billed under the VFA, which are refundable to ED.

Recovery Revenue — Upon default claim payment, TG is

statutorily required to pursue collection on behalf of the Federal government. TG collected approximately \$454 million and \$372 million on defaulted student loans, which includes loans collected through Federal income tax offsets and Federal Direct Loan Program consolidations of defaulted student loans in FY 2008 and 2007, respectively. Post-VFA recovery revenue rates are reduced to 16 percent for borrower payments, 10 percent for consolidation collections, and 18.5 percent plus cost for rehabilitation collections. Based upon recovery performance under the VFA, TG retained 23 percent of borrower payments, 20 percent consolidation collections, and 20 percent plus cost of rehabilitation collections, in the first three months of FY 2008 and the entire FY 2007.

**Federal Default Fee (FDF)** — A fee equal to 1 percent of guaranteed student loan disbursement must be deposited into the Federal Fund. FDF can be paid from student loan proceeds or any other non-Federal source. TG's Operating Fund has paid FDF on behalf of its borrowers since the fee's July 2006 inception and is committed to continue through June 2009, subject to extension.

**Interfund Activities:** Interfund activity depicts transactions between TG's Operating and Federal funds as stipulated in the legislation, regulation and requirements governing FFELP.

**Interfund Receivables, Payables** — The interfund balance is primarily related to September FDF due the Federal Fund, offset by September Recovery Revenue and post-VFA DAF due the Operating Fund.

**Interfund Default Aversion Fee Refund Allowance** — This interfund balance consists of the anticipated refunds due the Federal Fund related to pre-VFA and post-VFA DAF.

**Public Benefits Program:** TG has authorized the annual expenditure of up to 5 percent of its available Operating Fund balance for public benefits. Expenditures include \$1.8 million and \$1 million in Charley Wootan Grants, and \$6.1 million and \$4 million in competitive-based, education-related grants, in fiscal years 2008 and 2007, respectively.

**Use of estimates:** The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, 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. Management estimates include useful lives in depreciating Capital Assets, anticipated Allowance for Non-reinsured Loan Defaults and Default Aversion Fee Refund Allowance based upon historical loan segment performance. Actual results could differ from those estimates.

**Risk Management:** In addition to FFELP guarantee activity risks, TG is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; job-related illnesses or injuries to employees; and natural disasters, for which it carries commercial insurance at levels consistent with that of the prior FY. Risk retention is substantially confined to customarily nominal policy deductibles, with the exception of typically higher deductible limits for directors' and officers' liability, and umbrella coverage, as well as the retrospective rating of job-related illnesses or injuries to employees' policy premiums, which have outperformed the industry standard for three of the last four years. Resulting risk management liabilities, if any, are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. There were no claims that exceeded insurance coverage in fiscal years 2008 or 2007.

**Income taxes:** As an organization described in Internal Revenue Code (IRC) section 501(c)(3), TG is exempt from federal and state income tax on income from activities related to its exempt purpose. No material amounts of unrelated income were earned in the FY ended September 30, 2008, and 2007. Accordingly no accrual for income taxes is included in the financial statements.

**Reclassification:** Reclassification of certain prior year amounts have been made to conform with current year presentation.

### 3] Reinsurance

Annual default rates (“Trigger rates”) are calculated by dividing claims paid during the year by the original guarantee amount of loans in repayment at the preceding fiscal year- end. The annual default rates were 3.32 percent and 3.01 percent for fiscal years 2008 and 2007, respectively. Post-VFA claims paid, are eligible for semi-monthly Federal reinsurance depending upon annual Trigger rates and the underlying loan origination date. Claims at or exceeding 5 percent and 9 percent Trigger rates result in reduced reinsurance as follows: 95 percent/85 percent/75 percent for loans disbursed after September 30, 1998, 98 percent/88 percent/78 percent for loans disbursed after September 30, 1993, and 100 percent/90 percent/80 percent for loans disbursed on or before September 30, 1993. The Federal Fund’s Allowance for Non-reinsured Loan Defaults represents an estimate of future non-reinsured default claims anticipated from TG’s current guaranteed student loan portfolio based upon historical loan segment performance. \$95 million of the FY 2008 Provision for Loan Defaults relates to loans guaranteed during the VFA. Under the VFA, all eligible default claims received 100 percent weekly advance Federal reinsurance. TG paid default claims, net of \$14 million and \$32 million in claim repurchases and partial refunds, and is eligible for reinsurance thereon totaling approximately \$672.0 million and \$572.5 million in fiscal years 2008 and 2007, respectively.

### 4] Investments

TG’s investments are as follows (in 000s):

	September 30, 2008				September 30, 2007			
	Operating Fund	WAM*	Federal Fund	WAM*	Operating Fund	WAM*	Federal Fund	WAM*
<b>Investments</b>								
U.S. Treasury Notes	\$ 116,661	3.84	\$ 56,043	1.78	\$ 112,660	4.06	\$ 19,973	1.53
U.S. Agency Obligations								
FHLB	71,262	3.58	34,102	2.46	66,561	3.27	20,376	.47
FHLMC	67,765	4.87	22,894	4.47	76,516	3.80	11,977	1.52
FNMA	116,567	5.69	67,901	3.25	125,902	5.07	6,403	1.34
FFCB	29,932	5.73	21,120	5.71	15,523	3.26	11,210	4.09
GNMA	1,723	5.59			1,997	5.04		
FAMC			6,243	3.36				
Other	3,249	5.74	3,801	3.70	2,977	6.76		
	<u>290,498</u>	5.05	<u>156,061</u>	3.60	<u>289,476</u>	4.29	<u>49,966</u>	1.63
Municipalities	<u>31,703</u>	4.57			<u>33,927</u>	4.57		
Total	<u>\$ 438,862</u>	4.71	<u>\$ 212,104</u>	3.13	<u>\$ 436,063</u>	4.25	<u>\$ 69,939</u>	1.60
<b>Escrowed Assets – VFA</b>								
U.S. Treasury Notes							\$ 37,734	2.71
U.S. Agency Obligations								
FHLB							26,821	2.07
FHLMC							15,771	1.35
FNMA							41,543	1.48
FFCB							2,224	.87
FAMC							6,040	4.38
Other							3,778	4.71
							<u>96,177</u>	1.91
Total							<u>\$ 133,911</u>	2.13

\*WAM is weighted average maturities.

## 5] Capital Assets

Capital Assets include the following (in 000s):

	Sept. 30, 2006	Additions	Deletions	Sept. 30, 2007	Additions	Deletions	Sept. 30, 2008
<b>Operating Fund</b>							
Land	\$ 3,315			\$ 3,315			\$ 3,315
Building	29,410	\$ 4,100		33,510	\$ 563		34,073
Furniture & Equipment	9,084	1,555	\$ (96)	10,543	2,902	\$ (1,274)	12,171
Software	5,859	298		6,157	1,619		7,776
Leasehold Improvements	2			2			2
Vehicles	51			51	23		74
Capital Assets	47,721	5,953	(96)	53,578	5,107	(1,274)	57,411
Accumulated Depreciation	(12,389)	(2,681)	92	(14,978)	(2,900)	1,255	(16,623)
Capital Assets, Net	\$ 35,332	\$ 3,272	\$ (4)	\$ 38,600	\$ 2,207	\$ (19)	\$ 40,788

During FY 2007, TG acquired its warehouse facility for approximately \$4 million. TG funded this acquisition from its own cash reserves. A portion of this facility had been under lease by TG through September 2019 for approximately \$15,000 per month.

Operating Fund Capital Assets include \$0.65 million and \$0.14 million in accrued purchases at fiscal year end 2008 and 2007, respectively.

## 6] Accounts Payable and Accrued Liabilities

Accounts Payable and Accrued Liabilities include the following (in 000s):

	September 30, 2008		September 30, 2007	
	Operating Fund	Federal Fund	Operating Fund	Federal Fund
Trade Payables	\$ 2,908	\$ 96	\$ 2,981	\$ 328
Compensated Absences	1,677		1,487	
Incentives	6,478		5,851	
Other	113		177	
Total	\$11,176	\$ 96	\$10,496	\$ 328

## 7] Short-Term Financing

**Margin Facility:** In December 1997, TG entered into an agreement with its investment Prime Broker providing borrowing capacity, with certain exceptions, at 95 percent of its U.S. Treasury and U.S. Agency investment portfolio fair value, and up to 95 percent of other portfolio investments, subject to Federal Reserve regulations. Outstanding balances bear interest at the Broker Call Rate minus 3/8 percent or 3.375 percent at September 30, 2008, with payments required to the extent that outstanding principal and interest exceeds the borrowing capacity level.

The facility was accessed several times in FY 2008 and 2007, typically on a one-day basis to facilitate cash management. There is no outstanding balance under this facility at September 30, 2008 and 2007.

**Line of Credit:** In April 2007, TG renewed its \$5 million, no commitment fee, unsecured line of credit with its depository institution, bearing interest at the institution's prime rate. The facility, which expires April 30, 2009, has not been accessed.

## 8] Non-Current Liabilities

Non-current liabilities include the following net of the Current Portion (in 000s):

	Sept. 30, 2006	Additions	Payments/ Deletions	Sept. 30, 2007	Additions	Payments/ Deletions	Sept. 30, 2008	Current Portion
<b>Operating Fund</b>								
Due to ED:								
DAF Refund	\$ 82,316	\$ 29,142	\$ (20,895)	\$ 90,563	\$ 17,426	\$ (20,688)	\$ 87,301	
Notes Payable:								
Building Note	11,164		(1,548)	9,616		(1,623)	7,993	\$ 1,702
Other	5,995	7,297	(4,934)	8,358	8,237	(7,617)	8,978	8,156
<b>Federal Fund</b>								
Escrowed Assets	134,823	9,450	(5,746)	138,527	3,545	(142,072)	-	
Allowance for Loan Defaults	-			-	275,837	(25,427)	250,410	

**Building Note:** In FY 2003, TG entered into a \$16.25 million, 10-year, 4.75 percent fixed rate loan from an institutional lender to finance a portion of the acquisition of office space and building finish out, collateralized by the real estate and improvements, due in equal monthly installments of \$170,378, subject to a minimum 1 percent prepayment penalty.

Future note payments are as follows:

Fiscal Year	Principal	Interest	Total
2009	\$1,701,589	\$342,942	\$2,044,531
2010	1,784,197	260,334	2,044,531
2011	1,870,816	173,715	2,044,531
2012	1,961,640	82,891	2,044,531
2013	674,819	6,691	681,510
2014 & After			
Total	\$7,993,061	\$866,573	\$8,859,634

**Other:** Other non-current liabilities consist primarily of accrued compensated absences and amounts due under TG's corporate incentive plans. The current portion of these liabilities is reported as a component of accounts payable and accrued liabilities.

## 9] Retirement Benefits

TG maintains a defined contribution retirement plan, the TGSLC Money Purchase Pension Plan and Trust (the Plan), which covers substantially all employees. While employees do not contribute to the Plan, TG's contributions to the Plan are generally based on 9.0 percent of gross annual salaries, net of forfeitures. Total payroll and covered payroll was approximately \$33.1 million and \$31.6 million, respectively, in the Plan year ended June 30, 2008, and approximately \$31.5 million and \$29.5 million, respectively, in Plan year ended June 30, 2007. Total TG contributions, in accordance with this Plan requirement, were approximately \$2.7 million and \$2.5 million for the years ended September 30, 2008 and 2007, respectively. Plan amendments are subject to the Plan's Board of Trustees' approval and TG's Board of Directors' ratification.

## 10] Lease Commitments

TG obtains various equipment under operating lease agreements. Rent expense for fiscal years 2008 and 2007 was approximately \$0.62 million and \$1.1 million, respectively. Future minimum lease payments under the agreements are as follows (in 000s):

Fiscal Year	
2009	\$193
2010	145
Total	\$338

## 11] Credit Risk

TG's credit risk is principally inherent in student loan guarantees as follows: Outstanding guaranteed student loans, including loans transferred to TG, are composed of 48 percent four-year schools, 7 percent proprietary schools, 6 percent two-year schools, and 39 percent consolidation loans at September 30, 2008. The proprietary school increase is primarily attributable to TG's single largest participating school. Based upon the historical default characteristics of this portfolio, an Allowance for Non-reinsured Default Claims of \$250.41 million is estimated at September 30, 2008. Assuming all outstanding guaranteed loans default simultaneously resulting in the highest Trigger rate, and therefore minimum reinsurance, the maximum credit risk exposure to TG approximates \$6.37 billion at September 30, 2008, net of Federal reinsurance.

## 12] Contingencies

Recent credit market challenges have the potential to impact TG and its operations in future years. Lender liquidity issues, coupled with recent statutory reductions in FFELP lender profitability, have resulted in some lenders exiting the student loan market. In an effort to mitigate this issue, recent legislation has provided lenders, operating under specific conditions, with the option to sell participation interests in student loan portfolios, originated between July 1, 2008, and June 30, 2010 to ED; or to "put" or sell the loans outright to ED. While participation loans retain their guarantee, "put" loans do not, resulting in the removal of "put" loans from the guarantor's portfolio, and eliminating the possibility of future revenues from those loans. In addition, TG has established a fully functional Lender of Last Resort (LLR) process, under which TG will first access funds available through its one participating lender, after which with TG participating as a FFELP lender using up to \$50 million of its available assets, as well as available U.S. Treasury advances, as necessary. LLR loans made with such advances do not enter the guarantor portfolio. The extent of "put" or federal advance LLR loans, and their resulting impact on future TG results from operations cannot be determined. Also, FFELP lenders' participation in consolidation and rehabilitation recovery loans has been reduced by these circumstances, with potential future impact to TG results of operations.

TG has committed to pay the FDF from its Operating Fund on behalf of its customers through June 2009, subject to extension. Given current volume estimates, this commitment could exceed \$43 million in FY 2009.

TG has entered into negotiation with ED for a new VFA, which would include substantially lower performance fees as compared to the compensation formula under TG's original VFA to achieve ED's assessment of required cost neutrality for such agreements. A new VFA would have corresponding terms which would require the escrow of reserve assets and provide for 100 percent claims reinsurance. TG is unable to currently determine the outcome of these negotiations.

TG provides a unified student loan funding service (EFT), which upon participant approval, draws funds from participating lenders, while simultaneously distributing the funds to participating schools using commercial bank overnight Automated Clearing House (ACH) transactions. While rare, failure of a participating lender to fund its draw would result in an overdraft position in TG's ACH clearing account. EFT daily volume is typically less than \$10 million. However, during January and August 2008 peaks, there were four days with disbursements exceeding \$100 million, the highest single day being \$273 million.

In May 2006, an employee of a company which TG engaged to devise a document management system lost a device which contained non-public information of a portion of TG's borrowers. At that time, TG undertook remediation measures and statutorily-required notification to the affected borrowers. At this time TG, has not received any credible report of any information theft regarding any affected borrower arising from the incident, and does not currently anticipate any resulting litigation which would have a material adverse financial impact on TG.

Recent investigations of the student loan industry have questioned the business practices of certain members of the industry. The primary focus of much of the inquiry is into the area of prohibited inducements. TG does not engage in the conduct of business through prohibited inducements and has strong policies and controls against their use. Laws, rules and regulations, which are anticipated to result from the investigations at both the state and federal level, may apply to TG and its business partners. TG is prepared to address any new requirements addressed in any pending legislation or regulation. TG does not anticipate that such future changes, if any, would materially impact the results of its operations.

In the ordinary course of business TG is subject to a range of claims, administrative proceedings (including reviews by federal agencies which may result in refunds or adjustments) and legal proceedings, such as lawsuits that relate to contractual allegations, employment related matters and actions brought or threatened by third- parties under various state and federal laws and regulations. Although it is not possible to predict with certainty the outcome or costs of these matters, TG management believes that these matters will not have a material adverse effect on its financial position, results of operations or cash flows.



The **Guarantor of Choice**<sup>SM</sup>

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