



Financial Statements  
September 30, 2012 and 2011

# North Dakota Guaranteed Student Loan Program

# NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM

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## INDEPENDENT AUDITOR'S REPORT

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To the Industrial Commission  
State of North Dakota  
Bismarck, North Dakota

We have audited the accompanying financial statements of the business-type activities of the North Dakota Guaranteed Student Loan Program, a department of the State of North Dakota, as of and for the year ended September 30, 2012, which collectively comprise the North Dakota Guaranteed Student Loan Program's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the North Dakota Guaranteed Student Loan Program's management. Our responsibility is to express an opinion on these financial statements based on our audit. The September 30, 2011 financial statements were audited by other auditors whose report, dated January 26, 2012, expressed an unqualified opinion on those statements.

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

As discussed in Note 1, the financial statements of North Dakota Guaranteed Student Loan Program are intended to present the financial position, the changes in financial position, and the cash flows of only that portion of the business-type activities of the State of North Dakota that is attributable to the transactions of North Dakota Guaranteed Student Loan Program. They do not purport to, and do not, present fairly the financial position of the State of North Dakota as of September 30, 2012 and 2011, and the changes in its financial position and cash flows, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities of the North Dakota Guaranteed Student Loan Program as of September 30, 2012 and the results of its operations and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 14, 2013, on our consideration of the North Dakota Guaranteed Student Loan Program's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants 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.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion on or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming an opinion on the 2012 financial statements that collectively comprise the North Dakota Guaranteed Student Loan Program's financial statements. The accompanying 2012 supplementary information as listed in the table of contents and schedule of expenditures of federal awards, as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the 2012 financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the 2012 supplementary information and the schedule of expenditures of federal awards are fairly stated in all material respects in relation to the financial statements as a whole.

The image shows a handwritten signature in black ink that reads "Eide Sully LLP". The signature is written in a cursive, flowing style.

Aberdeen, South Dakota  
February 14, 2013

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
SEPTEMBER 30, 2012, 2011 AND 2010**

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The North Dakota Guaranteed Student Loan Program (the Program) has been designated to act as a guarantor of student loans made pursuant to the Higher Education Act of 1965, as amended (the Act), and certain other student loans if the North Dakota Industrial Commission determines that the student loans made under the terms of certain federal programs are no longer meeting the needs of North Dakota students, or are no longer available. Operationally, the Program is comprised of three components – an Agency Operating Fund (the AOF), an Alternative Loan Fund, both of which are property of the Program, and a separate group of monies administered by the Program (the Federal Student Loan Reserve Fund (FSLRF)), the net assets of which are property of the Federal Government and are reported as a liability to the Federal Government.

Note 1 to the financial statements provides a discussion of the organization and significant accounting policies of the Program. The financial statements of the Program provide accounting information similar to that of many other business entities. The balance sheet summarizes the assets, liabilities and net assets of the Program and provides the basis for analysis of the soundness and liquidity of the organization. The statement of revenues, expenses and changes in fund net assets summarizes the success of the organization in carrying out its business over the course of the most recent fiscal periods. The statement of cash flows summarizes the flow of cash through the organization as it conducts its business.

The discussion and analysis of the financial performance of the Program which follows is meant to provide additional insight into the Program's activities for the fiscal year ended September 30, 2012. Please read it in conjunction with the Program's financial statements and footnotes which are presented elsewhere in this report. Please note that the Program continues to have adequate resources to act as a guarantor of student loans and the auditor's opinions which accompany the financial statements and the supplementary information are unqualified.

## 2012 FINANCIAL HIGHLIGHTS

### *Agency Operating Fund*

The original principal amount of the Program's Federal Family Education Loan guarantees outstanding at the end of fiscal year 2012 totaled \$916 million compared to \$1.045 billion at the end of fiscal year 2011, and \$1.104 billion at the end of fiscal year 2010. This resulted in a decrease of \$30,000 in account maintenance fees to the AOF for the fiscal year.

The Program provided first time default aversion activities on \$35 million in delinquent loans held by lenders in the fiscal years ending September 30, 2012. A one-time fee of 1% is received from the FSLRF for this service.

Collection revenue during the fiscal year ending September 30, 2012 was \$1,290,000 compared to \$879,000 received in the fiscal year ending September 30, 2011, and \$899,000 for fiscal year ending September 30, 2010. The Program receives these revenues as reimbursement for collection efforts performed for the Department of Education (the Department).

The AOF unrestricted balance sheet indicates that there are adequate resources to meet the next fiscal year's obligations.

*Federal Student Loan Reserve Fund*

The reserve ratio of the FSLRF, calculated by dividing the sum of the FSLRF liability account and the allowance for loan loss by the original principal amount of guarantees outstanding, is 0.84% as of September 30, 2012. The minimum reserve ratio allowed by federal law is 0.25%.

State law requires that the Program must maintain a 0.25% reserve fund on deposit with the Bank of North Dakota (the Bank) for the original principal amount of all outstanding student loans insured or guaranteed by the Program which are subject to federal reinsurance. Sufficient reserve funds were in place at September 30, 2012.

The Program must maintain a reinsurance rate of less than 5% in order to receive the maximum reimbursement from the Federal Government on loan claims. The Program's reinsurance rate of 1.18% is well under this limitation.

The Federal Student Loan Reserve Fund 2012 balance sheet indicates that the FSLRF has adequate resources to provide for claim payments to lenders.

*Alternative Loan Fund*

State law requires that the Program must maintain a reserve fund on deposit with the Bank for all outstanding Alternative Loans. The fund level may be no less than the Bank of North Dakota historical default rate. Sufficient reserve funds were in place at September 30, 2012.

Alternative Loan Fund guarantees during the fiscal year ending September 30, 2012 were \$135 million compared to \$110 million guaranteed during the fiscal year ending September 30, 2011, and \$108 million guaranteed during the fiscal year ending September 30, 2010. A 2% administrative fee is received for loans disbursed under this program.

Alternative Loan Fund guarantees outstanding at the end of fiscal year 2012 totaled \$429 million compared to \$343 million at the end of fiscal year 2011, and \$264 million at the end of fiscal year 2010.

The Alternative Loan Fund 2012 balance sheet indicates that the Alternative Loan Fund has adequate resources to provide for new loan guarantees, claim payments to lenders and continuing obligations.

**CONDENSED BALANCE SHEETS**  
**SEPTEMBER 30, 2012, 2011 AND 2010**

	(In Thousands)		
	<u>2012</u>	<u>2011</u>	<u>2010</u>
<b>ASSETS</b>			
Current assets			
Cash and cash equivalents			
Unrestricted	\$ 2,492	\$ 3,949	\$ 1,981
Restricted	3,389	3,717	3,044
Investments			
Unrestricted	12,500	9,946	10,750
Restricted	3,500	5,500	6,500
Receivables			
Unrestricted	617	541	592
Restricted	4,541	2,346	2,502
Total current assets	<u>27,039</u>	<u>25,999</u>	<u>25,369</u>
Total assets	<u>\$ 27,039</u>	<u>\$ 25,999</u>	<u>\$ 25,369</u>
<b>LIABILITIES</b>			
Current liabilities			
Other	\$ 5,758	\$ 4,629	\$ 4,272
Total current liabilities	<u>5,758</u>	<u>4,629</u>	<u>4,272</u>
Noncurrent liabilities			
Allowance for future credit losses	6,292	6,702	6,893
Federal Student Loan Reserve Fund	5,641	6,203	6,804
Other	2,887	2,844	2,463
Total noncurrent liabilities	<u>14,820</u>	<u>15,749</u>	<u>16,160</u>
Total liabilities	<u>20,578</u>	<u>20,378</u>	<u>20,432</u>
<b>NET ASSETS</b>			
Restricted for default prevention activities	594	601	607
Unrestricted	5,867	5,020	4,330
Total net assets	<u>6,461</u>	<u>5,621</u>	<u>4,937</u>
Total liabilities and net assets	<u>\$ 27,039</u>	<u>\$ 25,999</u>	<u>\$ 25,369</u>

*Cash and Cash Equivalents*

The Program considers all cash and time deposits with original maturities of three months or less to be cash and cash equivalents for purposes of reporting cash flows.

*Receivables*

The receivable balances are comprised of interest, administrative fee, reinsurance payments and various fees due to the Program as of the end of each year. Of these amounts, 91%, 87%, and 87%, were due from the Department as of the end of fiscal years 2012, 2011, and 2010 respectively.

*Allowance for Future Credit Losses*

The Program estimates the allowance for future loan losses based on periodic evaluation of outstanding loans guaranteed and historical claim rates on the Program's guarantee activities.

*Federal Student Loan Reserve Fund*

The balance in this account represents the Federal Government's share of the total assets of the Program as discussed in Notes 1 and 3 to the financial statements.

**CONDENSED STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS  
YEARS ENDED SEPTEMBER 30, 2012, 2011 AND 2010**

	(In Thousands)		
	<u>2012</u>	<u>2011</u>	<u>2010</u>
<b>OPERATING REVENUES</b>			
Administrative fee	\$ 1,810	\$ 1,364	\$ 909
Loan recoveries net of DOE share	253	262	332
Rehabilitation loans net of DOE share	424	262	298
Collection cost revenues	614	354	344
Fee revenues	930	1,055	1,583
Grant income	1,802	897	269
	<u>5,833</u>	<u>4,194</u>	<u>3,735</u>
<b>OPERATING EXPENSES</b>			
Service and administrative expense	1,873	1,732	2,231
Grant expenditures	1,802	895	269
Credit loss expense	1,230	816	1,561
Other expenses	139	182	160
	<u>5,044</u>	<u>3,625</u>	<u>4,221</u>
<b>OPERATING INCOME (LOSS)</b>	<b>789</b>	569	(486)
<b>NONOPERATING REVENUES</b>			
Interest income	51	115	203
<b>CHANGE IN NET ASSETS</b>	<b>840</b>	684	(283)
<b>TOTAL NET ASSETS - BEGINNING OF YEAR</b>	<u><b>5,621</b></u>	<u>4,937</u>	<u>5,220</u>
<b>TOTAL NET ASSETS - ENDING OF YEAR</b>	<u><b>\$ 6,461</b></u>	<u>\$ 5,621</u>	<u>\$ 4,937</u>

*Operating Revenues and Expenses*

Note 1 to the financial statements contains discussion of several of the various operating revenue and expense items pertaining to Program operations.

*Service and Administrative Expense - Bank of North Dakota*

The Program has entered into a number of agreements as discussed in Note 4 to the financial statements pertaining to related party transactions. Several of these agreements resulted in payments between the various parties either to pay claims on student loans guaranteed by the Program or to fund operations of the Program.

*Economic Factors*

Discussion at Notes 1 and 6 to the financial statements indicate that the Program has an economic dependence on the Department for reinsurance of student loans guaranteed by the Program, and for the payment of certain activity based fees for the Program's administration of the loan programs for the Department.

On December 3, 2012, the Alternative Loan Fund received a transfer of \$5,000,000 from the North Dakota Student Loan Trust. These funds have been designated by the Industrial Commission for future claim payments.

*Budgetary Information*

As discussed in Note 1 to the financial statements, the North Dakota Century Code designates the Bank as the agency to administer the Program. The Bank's operations are funded under a biennial appropriation approved by the state legislature which encompasses the Bank's operations, including those of the Program. Section 15-62.1-01 of the North Dakota Century Code also provides continuing appropriation authority to expend monies received and interest earned as may be necessary to implement and administer the Program. Since the legislature does not identify separate appropriation funding for the Program, it is not possible to prepare an analysis of actual performance to appropriation for the Program.

*Contacting the North Dakota Guaranteed Student Loan Program's Financial Management*

The information in this report is intended to provide the reader with an overview of the results of the Program's operations along with the Program's accountability for those operations. If you have questions or require additional information, contact us at PO Box 5524, Bismarck, ND 58506-5524, or call us at 701-328-5654.

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM  
BALANCE SHEETS  
SEPTEMBER 30, 2012 AND 2011**

	<u>2012</u>	<u>2011</u>
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents		
Unrestricted	\$ 2,491,879	\$ 3,948,613
Restricted	<u>3,388,740</u>	<u>3,716,521</u>
Total cash and cash equivalents	<u>5,880,619</u>	<u>7,665,134</u>
Investments		
Unrestricted	12,500,000	9,946,102
Restricted	<u>3,500,000</u>	<u>5,500,000</u>
Total investments	<u>16,000,000</u>	<u>15,446,102</u>
Due from other funds		
Restricted	<u>-</u>	<u>1,290</u>
Receivables		
Unrestricted		
Interest	12,494	36,092
Department of Education	45,665	-
Account maintenance fee	144,484	156,799
Administrative fee	292,457	273,219
Other receivables	123,055	74,028
Restricted		
Interest	711	3,467
Federal reinsurance	<u>4,539,868</u>	<u>2,342,866</u>
Total receivables	<u>5,158,734</u>	<u>2,886,471</u>
Total current assets	<u>27,039,353</u>	<u>25,998,997</u>
Total assets	<u>\$ 27,039,353</u>	<u>\$ 25,998,997</u>

See Notes to Financial Statements

	<u>2012</u>	<u>2011</u>
<b>LIABILITIES</b>		
<b>CURRENT LIABILITIES</b>		
Due to other funds	\$ 136,412	\$ 235,491
Payable to lenders	2,394,885	1,800,491
Collections payable		
Department of Education	412,384	320,187
Unearned administrative fee	1,186,000	1,171,000
Allowance for future credit losses	1,509,000	1,010,000
Estimated future refunds of DAF	119,000	92,000
	<u>5,757,681</u>	<u>4,629,169</u>
Total current liabilities		
<b>NONCURRENT LIABILITIES</b>		
Unearned administrative fee	2,394,597	2,341,364
Allowance for future losses	6,291,895	6,701,895
Estimated future refunds		
of default aversion fees	493,326	502,592
Federal Student Loan Reserve Fund	5,640,938	6,202,770
	<u>14,820,756</u>	<u>15,748,621</u>
Total noncurrent liabilities		
	<u>20,578,437</u>	<u>20,377,790</u>
Total liabilities		
<b>NET ASSETS</b>		
Restricted		
Expendable for default prevention activities	594,395	600,658
Unrestricted	5,866,521	5,020,549
	<u>6,460,916</u>	<u>5,621,207</u>
Total net assets		
	<u>\$ 27,039,353</u>	<u>\$ 25,998,997</u>
Total liabilities and net assets		

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM  
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS  
YEARS ENDED SEPTEMBER 30, 2012 AND 2011**

	<u>2012</u>	<u>2011</u>
<b>OPERATING REVENUES</b>		
Administrative fee	\$ 1,809,928	\$ 1,364,318
Loan recoveries, net of remittance to Department of Education of \$1,348,307 in 2012 and \$1,343,239 in 2011	252,615	262,494
Rehabilitated loans, net of remittance to Department of Education of \$1,613,898 in 2012 and \$1,072,044 in 2011	423,785	261,863
Collection cost revenues, net of remittance to Department of Education of \$173,191 in 2012 and \$89,687 in 2011	614,036	354,360
Loan processing and issuance fees	-	7,833
Account maintenance fees	582,890	612,689
Default aversion fees	347,150	433,655
Grant income	<u>1,802,157</u>	<u>896,781</u>
Total operating revenues	<u>5,832,561</u>	<u>4,193,993</u>
<b>OPERATING EXPENSES</b>		
Service and administrative expense	1,864,499	1,731,400
Grant expenditures	1,802,157	895,160
Default prevention activities	8,806	8,184
Credit loss expense	1,229,639	816,081
DAF refund provision	<u>138,859</u>	<u>174,197</u>
Total operating expenses	<u>5,043,960</u>	<u>3,625,022</u>
<b>OPERATING INCOME</b>	<b>788,601</b>	568,971
<b>NONOPERATING REVENUES</b>		
Interest income	<u>51,108</u>	<u>114,981</u>
<b>CHANGE IN NET ASSETS</b>	<b>839,709</b>	683,952
<b>TOTAL NET ASSETS, BEGINNING OF YEAR</b>	<u>5,621,207</u>	<u>4,937,255</u>
<b>TOTAL NET ASSETS, END OF YEAR</b>	<u>\$ 6,460,916</u>	<u>\$ 5,621,207</u>

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM  
STATEMENTS OF CASH FLOWS  
YEARS ENDED SEPTEMBER 30, 2012 AND 2011**

	<u>2012</u>	<u>2011</u>
<b>OPERATING ACTIVITIES</b>		
Loan recoveries received from borrowers	\$ 1,736,278	\$ 1,780,084
Loan recoveries remitted to DOE	(1,225,861)	(1,332,530)
Credit loss claims paid to lenders - BND	(9,737,712)	(7,608,141)
Credit loss claims paid to other lenders	(5,248,368)	(4,442,801)
Credit loss claims received from DOE	11,636,041	10,953,497
Rehab loan proceeds received from lenders - BND	2,506,536	1,641,480
Rehab loan proceeds remitted to DOE	(1,660,102)	(914,714)
Collections received from borrowers	239,974	134,098
Grant proceeds received	1,753,130	822,753
Loan processing and issuance fees received from DOE	-	21,774
Account maintenance fees received from DOE	595,205	643,177
Default fees received from borrowers and lenders	-	5,296
Administrative fee received from borrowers	1,858,923	1,693,606
Service and administrative expense paid - BND	(3,774,966)	(2,803,772)
<b>NET CASH FROM (USED FOR) OPERATING ACTIVITIES</b>	<u>(1,320,922)</u>	<u>593,807</u>
<b>INVESTING ACTIVITIES</b>		
Proceeds from investment maturities - BND	24,446,102	21,797,556
Purchase of investments - BND	(25,000,000)	(19,993,658)
Interest received	90,305	241,881
<b>NET CASH FROM (USED FOR) INVESTING ACTIVITIES</b>	<u>(463,593)</u>	<u>2,045,779</u>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	(1,784,515)	2,639,586
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR</b>	<u>7,665,134</u>	<u>5,025,548</u>
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<u>\$ 5,880,619</u>	<u>\$ 7,665,134</u>

(continued on next page)

STATEMENTS OF CASH FLOWS – page 2

	<u>2012</u>	<u>2011</u>
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH FROM (USED FOR) OPERATING ACTIVITIES</b>		
Operating income	\$ 788,601	\$ 568,971
Adjustments to reconcile operating income to net cash from (used for) operating activities		
Credit loss expense	316,094	142,895
DAF refund provision, net of refunds	17,734	74,592
Changes in assets and liabilities:		
Due from other funds	-	25,217
Administrative fee receivable - BND	(19,238)	(21,942)
Default fee receivable	42	616
Federal reinsurance receivable - DOE	(2,242,667)	125,666
Account maintenance fee receivable	12,315	30,488
Loan processing and issuance fee receivable	-	13,941
Unearned administrative fee	68,233	351,230
Due to other funds	(48,798)	(48,527)
Due to BND	(98,018)	(184,973)
Payable to lenders	367,300	(19,534)
Collections payable	92,197	166,526
Federal Student Loan Reserve Fund, net of interest	(574,717)	(631,359)
<b>NET CASH FROM (USED FOR) OPERATING ACTIVITIES</b>	<u>\$ (1,320,922)</u>	<u>\$ 593,807</u>

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM  
NOTES TO FINANCIAL STATEMENTS  
SEPTEMBER 30, 2012 AND 2011**

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**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES**

*Nature of Operations*

Section 15-62.1 of the North Dakota Century Code (NDCC) designates the Bank of North Dakota (the Bank) as the agency for the administration of the North Dakota Guaranteed Student Loan Program (the Program). The Program shall expend monies received and interest on the reserve funds established pursuant to this section of the NDCC as may be necessary to implement and administer the Program. The Program has been designated to act as a guarantor of student loans made pursuant to the Higher Education Act of 1965, as amended (the Act), and certain other student loans if the North Dakota Industrial Commission determines that student loans made under the terms of certain federal programs are no longer meeting the needs of North Dakota students, or are no longer available. As such, the Program is responsible for processing loans submitted for guarantee, issuing loan guarantees, providing collection assistance to lenders for delinquent loans, paying lender claims for loans and collecting loans on which default claims have been paid.

The Program is comprised of three components – an Agency Operating Fund (the AOF), an Alternative Loan Fund and a separate group of monies administered by the Program (the Federal Student Loan Reserve Fund (FSLRF)). The AOF and any future earnings of the fund are the property of the Program, and may be used for application processing, loan disbursement, enrollment and repayment status management, default aversion activities, default collection activities, school and lender training, financial aid awareness and related outreach activities, compliance monitoring and other student financial aid related activities as selected by the Program. The Alternative Loan Fund and any earnings on the fund are property of the Program and may be used to fund the operations of the Program in its role as a guarantor of student loans outside the scope of the Act. The FSLRF and any earnings thereon are the sole property of the Federal Government, and may only be used to pay claims and certain specified fees.

In accordance with the provisions of the Act, the Program has entered into certain contracts with the U.S. Department of Education (the Department). These contracts define the responsibilities of the Program to the Department and qualify the Program for various forms of payment available under the Act. The basic agreement provides for the qualification of borrowers and participating lenders whose loans are guaranteed by the Program for federal interest benefits. Other agreements provide for reinsurance of loans with the Federal Government.

*Reporting Entity*

In accordance with Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*, as amended by GASB Statement No. 39, the Program should include all component units over which the Program exercises such aspects as (1) appointing a voting majority of an organization's governing body and (2) has the ability to impose its will on that organization, or (3) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the Program.

Based on that criteria, no organizations were determined to be part of the Program. The Program is included as part of the primary government in the State of North Dakota's reporting.

## NOTES TO FINANCIAL STATEMENTS

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### *Accounting Standards*

The Program follows the pronouncements of the Governmental Accounting Standards Board, which is the nationally accepted standard setting body for establishing generally accepted accounting principles for governmental entities. In accordance with GASB Statement 20, the Program follows all applicable GASB pronouncements as well as private sector guidance issued on or before November 30, 1989, unless private sector guidance conflicts with GASB pronouncements.

### *Fund Accounting*

The AOF and the Alternative Loan Fund are both property of the Program and are reported herein as enterprise funds. The FSLRF is property of the Federal Government, and is administered by the Program. The net assets of the FSLRF are reported herein as a liability to the Federal Government.

### *Basis of Accounting and Measurement Focus*

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All enterprise funds are accounted using the economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of these funds are included on the balance sheet. Net assets are segregated into invested in capital assets, restricted and unrestricted components. The statements of revenues, expenses and changes in fund net assets present increases (e.g., revenues) and decreases (e.g., expenses) in total net assets. The statements of cash flows present the cash flows for operating activities, investing activities and non-capital financing activities.

The AOF and Alternative Loan Fund are enterprise funds and use the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

The FSLRF uses the accrual basis of accounting for recognition of increases and decreases in amounts due to the Federal Government.

In the process of aggregating data for the financial statements, some amounts reported as interfund activity and balances in the funds have been eliminated or reclassified.

### *Use of Estimates*

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the balance sheet and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

### *Cash and Cash Equivalents*

The Program considers all cash and time deposits with original maturities of three months or less to be cash and cash equivalents for purposes of reporting cash flows.

## NOTES TO FINANCIAL STATEMENTS

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### *Deposits and Investments*

The Program records deposits and investments in accordance with Governmental Accounting Standards Board Statement No. 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools." Nonnegotiable certificates of deposit meet the classification of Interest-earning Investment Contracts having redemption terms which do not consider market rates and are therefore carried at cost. Investment securities are carried at their market value. Unrealized gains and losses due to fluctuations in market value are included in investment income.

### *Capital Assets*

The Program has developed computer software for internal use that was capitalized. The cost of computer software is being amortized on a straight-line basis over its estimated useful life of three years and is fully amortized. Computer software with a cost of \$5,000 or more is capitalized.

Proceeds received from any sale of computer software, net of direct incremental costs of marketing, are applied against the carrying amount of the software. No profit is recognized until aggregate new proceeds from sales and amortization have reduced the carrying amount of the software to zero. Subsequent proceeds are recognized in revenue earned.

### *Administrative Fee Revenue*

Administrative fee revenue is to be used by the Program to insure loans and to cover costs incurred in the administration of the Alternative Loan Fund. In fiscal year 2012, the Program changed its methodology of recognizing administrative fee revenue. Forty percent of revenues are recognized at the time of fee collection with the remainder recognized over the estimated life of an average loan (10 years) using the sum-of-the-years digits method. In 2011, 20% of revenues were recognized at the time of fee collections with the remainder recognized over the estimated life on an average loan using the sum-of-the-years digits method. The percentage was increased to better match revenues against the expenses incurred to administer Alternative Loans. Administrative fees received and receivable which have not been recognized as revenue were recorded on the balance sheet as unearned administrative fee. This change resulted in a \$400,000 increase in the change in net assets for the statement of revenues, expenses, and changes in fund net assets for the year ended September 30, 2012. Changes in unearned administrative fees for the years ending September 30, 2012 and 2011 are as follows:

	<u>2012</u>	<u>2011</u>
Balance, beginning of year	\$ 3,512,364	\$ 3,161,134
Collections	1,878,161	1,715,548
Amortization of fees	<u>(1,809,928)</u>	<u>(1,364,318)</u>
Balance, end of year	<u>\$ 3,580,597</u>	<u>\$ 3,512,364</u>

### *Loan Recoveries, Rehabilitated Loans and Collection Cost Revenues*

Regulations require that the Program assess collection costs on all defaulted loans which it is attempting to collect for the Department. The Program is entitled to retain for its operations a portion of its collections of principal, interest and collection costs received on defaulted loans. Income is recorded when the loan collections are received.

## NOTES TO FINANCIAL STATEMENTS

### *Account Maintenance Fees*

The Act provides an account maintenance fee to be paid by the Department to compensate the Program for certain costs incurred by the Program. The Department pays the account maintenance fee to the AOF at a level of 0.06% of the original principal amount of outstanding guarantees as of September 30.

### *Default Aversion Fee and Estimated Future Refunds of Default Aversion Fees*

The Act provides a default aversion fee to be paid from the FSLRF to the AOF to compensate the Program for certain costs incurred by the Program. Payment of this fee is limited to once per loan and is equal to 1% of the principal and accrued interest receivable balances when default aversion assistance is requested by lenders, with an obligation to refund the fee in the event of default based upon principal and accrued interest receivable at the time of claim payment. The fee is recognized upon completion of the default aversion activities by the Program, net of estimated refunds.

The Program uses the percentage of income method to calculate the estimated allowance for refunds of the default aversion fee based on a periodic evaluation of default aversion fees received and a historical refund rate.

	<u>2012</u>	<u>2011</u>
Balance, beginning of year	\$ 594,592	\$ 520,000
Refund provision	138,859	174,197
Refunds paid	<u>(121,125)</u>	<u>(99,605)</u>
Balance, end of year	<u>\$ 612,326</u>	<u>\$ 594,592</u>

### *Credit Loss Expenses*

The Program estimates the allowance for future credit losses based on periodic evaluation of outstanding loans guaranteed and historical claim rates on the Program's guarantee activities.

Changes in the allowance for future credit losses for the Alternative Loan Fund for the years ending September 30, 2012 and 2011 are as follows:

	<u>2012</u>	<u>2011</u>
Balance, beginning of year	\$ 5,086,895	\$ 4,944,000
Credit loss expense	1,229,639	816,081
Recoveries	111,637	109,919
Claims paid	<u>(1,252,276)</u>	<u>(783,105)</u>
Balance, end of year	<u>\$ 5,175,895</u>	<u>\$ 5,086,895</u>

The FSLRF is reimbursed by the Federal Government for a portion of claims paid on FFELP loans as discussed in Note 6.

## NOTES TO FINANCIAL STATEMENTS

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Changes in the allowance for future losses for the FSLRF for the years ending September 30, 2012 and 2011 are as follows:

	<u>2012</u>	<u>2011</u>
Balance, beginning of year	\$ 2,625,000	\$ 2,625,000
Credit loss expense	495,155	419,921
Claims paid, net of reinsurance	<u>(495,155)</u>	<u>(419,921)</u>
Balance, end of year	<u>\$ 2,625,000</u>	<u>\$ 2,625,000</u>

### *Restricted Assets and Restricted Net Assets*

Certain Program assets and net assets carry a restricted classification, either because they are property of the Federal Government or their use has been restricted by the Federal Government for default prevention activities only.

If an expense is incurred that qualifies for use of both restricted and unrestricted resources, the Program will first apply restricted resources.

### *Operating and Non-operating Revenues*

Operating revenues consist of sales of goods and services, quasi-external operating transactions with other funds, grant revenue for specific activities that are considered to be operating activities of the grantor, receipts from other agencies for reimbursement of operating transactions and other miscellaneous revenue. Grants that would qualify as an operating activity are those that do not subsidize an existing program, rather they finance a program the agency would not otherwise undertake. All other revenues that do not meet the above criteria are classified as non-operating.

### *Reclassifications*

Certain reclassifications of amounts previously reported have been made to the accompanying financial statements to maintain consistency between periods presented. The reclassifications had no impact on changes in net assets or net assets.

## **NOTE 2 - DEPOSITS AND INVESTMENTS**

All funds have their moneys invested in securities or deposits allowed by federal and state regulations. Section 682.410(a)(5) of Federal Regulations states that assets of the Program may be invested in low-risk securities, such as obligations issued or guaranteed by the United States or a State. North Dakota Century Code Section 15-62.1-05 states that securities in which moneys of the Program may be invested must meet the same requirements as those authorized for investment under the state investment board.

## NOTES TO FINANCIAL STATEMENTS

### Deposits

As of September 30, 2012 and 2011, the Program had the following deposits:

	<u>2012</u>	<u>2011</u>
Cash and savings accounts	\$ 5,880,619	\$ 7,665,134
Time deposits	<u>16,000,000</u>	<u>15,446,102</u>
	<u>\$ 21,880,619</u>	<u>\$ 23,111,236</u>

### Custodial and Concentration of Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the Program will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The Program does not have a formal policy that limits custodial credit risk for deposits. None of the Program's deposits are covered by depository insurance. The Program's deposits are uncollateralized and all of the deposits are held at the Bank of North Dakota and are guaranteed by the State of North Dakota (NDCC Section 6-09-10).

### NOTE 3 - NONCURRENT LIABILITIES

Long-term liability activity for the years ended September 30, 2012 and 2011 was as follows:

	<u>Balance 2011</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance 2012</u>	<u>Amounts Due Within One Year</u>
Unearned administrative fee	\$ 3,512,364	\$ 1,878,161	\$ (1,809,928)	\$ 3,580,597	\$ 1,186,000
Allowance for future credit losses	7,711,895	1,836,431	(1,747,431)	7,800,895	1,509,000
Estimated future refunds of default aversion fees	594,592	138,859	(121,125)	612,326	119,000
Federal Student Loan Reserve Fund	<u>6,202,770</u>	<u>17,630,708</u>	<u>(18,192,540)</u>	<u>5,640,938</u>	<u>-</u>
	<u>\$ 18,021,621</u>	<u>\$ 21,484,159</u>	<u>\$ (21,871,024)</u>	<u>\$ 17,634,756</u>	<u>\$ 2,814,000</u>

## NOTES TO FINANCIAL STATEMENTS

	Balance 2010	Additions	Reductions	Balance 2011	Amounts Due Within One Year
Unearned administrative fee	\$ 3,161,134	\$ 1,715,548	\$ (1,364,318)	\$ 3,512,364	\$ 1,171,000
Allowance for future credit losses	7,569,000	1,345,921	(1,203,026)	7,711,895	1,010,000
Estimated future refunds of default aversion fees	520,000	174,197	(99,605)	594,592	92,000
Federal Student Loan Reserve Fund	<u>6,803,704</u>	<u>13,912,875</u>	<u>(14,513,809)</u>	<u>6,202,770</u>	<u>-</u>
	<u>\$ 18,053,838</u>	<u>\$ 17,148,541</u>	<u>\$ (17,180,758)</u>	<u>\$ 18,021,621</u>	<u>\$ 2,273,000</u>

A reconciliation of the FSLRF for the years ending September 30, 2012 and 2011 is as follows:

	<u>2012</u>	<u>2011</u>
Federal Student Loan Reserve Fund, beginning of year	\$ <b>6,202,770</b>	\$ 6,803,704
Investment income	<b>12,883</b>	30,425
Default fee	<b>(42)</b>	4,680
Loan revenues, net of remittance to Department of Education and AOF of \$2,962,205 in 2012 and \$2,931,456 in 2011	<b>146,507</b>	117,932
Credit loss expense, net of reinsurance from Department of Education of \$13,833,043 in 2012 and \$10,828,382 in 2011	<b>(495,155)</b>	(419,921)
Default aversion fee	<b>(226,025)</b>	(334,050)
Federal Student Loan Reserve Fund, end of year	<u><b>\$ 5,640,938</b></u>	<u>\$ 6,202,770</u>

### NOTE 4 - INTERFUND AND RELATED PARTY TRANSACTIONS

	<u>2012</u>	<u>2011</u>
<b>BANK OF NORTH DAKOTA</b>		
Cash and cash equivalents - unrestricted	\$ <b>2,491,879</b>	\$ 3,948,613
Cash and cash equivalents - restricted	<b>3,388,740</b>	3,716,521
Investments - unrestricted	<b>12,500,000</b>	9,946,102
Investments - restricted	<b>3,500,000</b>	5,500,000
Interest receivable - unrestricted	<b>12,494</b>	36,092
Interest receivable - restricted	<b>711</b>	3,467
Administrative fee receivable - unrestricted	<b>292,457</b>	273,219
Due to other funds	<b>136,412</b>	235,491
Payable to lenders	<b>2,067,742</b>	1,442,205

## NOTES TO FINANCIAL STATEMENTS

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In addition, the Program reimburses the Bank for expenses paid by the Bank on behalf of the Program. The reimbursements are based on an allocation of indirect costs and assignment of direct costs. Servicing and administrative expenses; including grant expenditures, totaled \$3,646,980 in 2012 and \$2,626,560 in 2011. The payable to the Bank for such expenses, amounting to \$129,315 and \$235,491 at September 30, 2012 and 2011, respectively, is included in "Due To Other Funds" on the balance sheet.

At September 30, 2012 and 2011, the Program has guaranteed approximately \$1.088 billion and \$1.090 billion of loans owned by the Bank and the North Dakota Student Loan Trust (Trust). The Program paid claims of approximately \$10,705,000 and \$8,521,000 to the Bank and the Trust for the years ended September 30, 2012 and 2011, respectively. Some of those loans were subsequently rehabilitated and sold to the Bank.

### NOTE 5 - GUARANTEE RESERVE AGREEMENTS

According to the Act, the Program is required to maintain a reserve ratio of the FSLRF at a minimum level of 0.25% of the original principal amount of guarantees outstanding. The reserve ratio is calculated by dividing the sum of the FSLRF liability account and the allowance for loan loss by the original principal amount of guarantees outstanding. The Program had a reserve ratio of 0.84% and 0.84% at September 2012 and 2011, respectively.

For the Alternative Loan Fund, the Program must maintain a minimum guarantee fund that is no less than the Bank of North Dakota historical default rate. The Program has chosen to use a similar calculation as the reserve ratio in the FSLRF for this minimum amount. The ratio is calculated by dividing the sum of the unearned administrative fees, the allowance for future loan loss and the fund balance by the outstanding principal balance. The Program had a ratio of 2.67% in 2012 and 3.24% in 2011, which is well above the current Bank's historical default rate on alternative student loans.

### NOTE 6 - FEDERAL REINSURANCE OF STUDENT LOANS

In the event of borrower default on a guaranteed loan, the Act provides for reinsurance by the Federal Government based on the level of federal reinsurance associated with the Program's annual reinsurance rate (reinsurance claims paid by the Federal Government during the fiscal year divided by the amount of loans in repayment at the beginning of the year).

The Program is reimbursed by the Federal Government upon payment of claims on FFEL Program loans. The Program is, therefore, economically dependent on the Department of Education for these reimbursements and for its continued existence. The Program incurred claims totaling \$14,328,198 and \$11,248,303 for the years ended September 30, 2012 and 2011, respectively, of which \$4,539,868 and \$2,342,866 remains as a receivable from the Federal Government at September 30, 2012 and 2011, respectively. Reimbursement of default claims on FFEL Program loans is determined according to the following schedule. Reimbursement of claims on FFEL Program loans for reasons other than default is at 100%. There is no reimbursement of claims paid by the Alternative Loan Fund.

## NOTES TO FINANCIAL STATEMENTS

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Claim Percentage of Loans in Repayment	Levels of Federal Reinsurance
0% to 5% (On loans disbursed prior to 10/01/93)	100%
0% to 5% (On loans disbursed on or after 10/01/93 and before 10/01/98)	98%
0% to 5% (On loans disbursed on or after 10/01/98)	95%
More than 5% but less than or equal to 9% (On loans disbursed prior to 10/01/93)	100% of claims up to 5% and 90% of claims over 5% but less than or equal to 9%
More than 5% but less than or equal to 9% (On loans disbursed on or after 10/01/93 and before 10/01/98)	98% of claims up to 5% and 88% of claims over 5% but less than or equal to 9%
More than 5% but less than or equal to 9% (On loans disbursed on or after 10/01/98)	95% of claims up to 5% and 85% of claims over 5% but less than or equal to 9%
Over 9% (On loans disbursed prior to 10/01/93)	100% of claims up to 5% and 90% of claims over 5% but less than or equal to 9% and 80% of claims over 9%
Over 9% (On loans disbursed on or after 10/01/93 and before 10/01/98)	98% of claims up to 5% and 88% of claims over 5% but less than or equal to 9% and 78% of claims over 9%
Over 9% (On loans disbursed on or after 10/01/98)	95% of claims up to 5% and 85% of claims over 5% but less than or equal to 9% and 75% of claims over 9%

Each year the Department of Education calculates the Program's reinsurance rate for the ensuing year based on historical levels of claims paid. At no time has the Program's reinsurance rate exceeded the 5% level discussed above.

## NOTES TO FINANCIAL STATEMENTS

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### NOTE 7 - RISK MANAGEMENT

The Program is exposed to various risks of loss related to torts and errors and omissions. The Program is administered by the Bank and, therefore, is eligible to the same funds/pools established by the State for risk management issues. These include:

The 1995 Legislative Session established the Risk Management Fund (RMF), an internal service fund, to provide a self-insurance vehicle for funding the liability exposures of State Agencies resulting from the elimination of the State's sovereign immunity. The RMF manages the tort liability of the State, its agencies' employees, and the University System. All State agencies participating in the RMF and their fund contribution was determined using a projected cost allocation approach. The statutory liability of the State is limited to a total of \$250,000 per person and \$1,000,000 per occurrence.

The State Bonding Fund currently provides the Bank with blanket employee fidelity bond coverage in the amount of \$2,000,000. The State Bonding Fund does not currently charge any premium for this coverage.

There have been no significant reductions in insurance coverage from the prior year and settled claims resulting from these risks have not exceeded insurance coverage.

### NOTE 8 – SUBSEQUENT EVENTS

On December 3, 2012, the Alternative Loan Fund received a transfer of \$5,000,000 from the North Dakota Student Loan Trust. These funds have been designated by the Industrial Commission for future claim payments.



Supplementary Information  
September 30, 2012 and 2011

# North Dakota Guaranteed Student Loan Program

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM**  
**COMBINING BALANCE SHEET**  
**SEPTEMBER 30, 2012**

	2012				
	Agency Operating Fund	Alternative Loan Fund	Federal Student Loan Reserve Fund	Eliminations	Total
<b>ASSETS</b>					
<b>CURRENT ASSETS</b>					
Cash and cash equivalents					
Unrestricted	\$ 1,298,372	\$ 1,193,507	\$ -	\$ -	\$ 2,491,879
Restricted	594,395	-	2,794,345	-	3,388,740
Investments					
Unrestricted	1,500,000	11,000,000	-	-	12,500,000
Restricted	-	-	3,500,000	-	3,500,000
Due from other funds					
Unrestricted	1,054	260	-	(1,314)	-
Restricted	-	-	144	(144)	-
Receivables					
Unrestricted					
Interest	493	12,001	-	-	12,494
Default aversion fee	16,210	-	-	(16,210)	-
Department of Education	45,665	-	-	-	45,665
Account maintenance fee	144,484	-	-	-	144,484
Administrative fee	-	292,457	-	-	292,457
Other receivables	123,055	-	-	-	123,055
Restricted					
Interest	-	-	711	-	711
Federal reinsurance	-	-	4,539,868	-	4,539,868
Total receivables	329,907	304,458	4,540,579	(16,210)	5,158,734
Total current assets	3,723,728	12,498,225	10,835,068	(17,668)	27,039,353
<b>NONCURRENT ASSETS - UNRESTRICTED</b>					
Capital assets					
Computer software	3,819,514	-	-	-	3,819,514
Accumulated amortization	(3,819,514)	-	-	-	(3,819,514)
Total capital assets	-	-	-	-	-
Total assets	\$ 3,723,728	\$ 12,498,225	\$ 10,835,068	\$ (17,668)	\$ 27,039,353

	2012				
	<u>Agency Operating Fund</u>	<u>Alternative Loan Fund</u>	<u>Federal Student Loan Reserve Fund</u>	<u>Eliminations</u>	<u>Total</u>
<b>LIABILITIES</b>					
<b>CURRENT LIABILITIES</b>					
Due to other funds	\$ 105,522	\$ 31,143	\$ 1,205	\$ (1,458)	\$ 136,412
Default aversion fee payable	-	-	16,210	(16,210)	-
Payable to lenders	-	227,094	2,167,791	-	2,394,885
Collections payable					
Department of Education	28,460	-	383,924	-	412,384
Unearned administrative fee	-	1,186,000	-	-	1,186,000
Allowance for future credit losses	-	916,000	593,000	-	1,509,000
Estimated future refunds of default aversion fees	<u>119,000</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>119,000</u>
Total current liabilities	<u>252,982</u>	<u>2,360,237</u>	<u>3,162,130</u>	<u>(17,668)</u>	<u>5,757,681</u>
<b>NONCURRENT LIABILITIES</b>					
Unearned administrative fee	-	2,394,597	-	-	2,394,597
Allowance for future losses	-	4,259,895	2,032,000	-	6,291,895
Estimated future refunds of default aversion fees	493,326	-	-	-	493,326
Federal Student Loan Reserve Fund	<u>-</u>	<u>-</u>	<u>5,640,938</u>	<u>-</u>	<u>5,640,938</u>
Total noncurrent liabilities	<u>493,326</u>	<u>6,654,492</u>	<u>7,672,938</u>	<u>-</u>	<u>14,820,756</u>
Total liabilities	<u>746,308</u>	<u>9,014,729</u>	<u>10,835,068</u>	<u>(17,668)</u>	<u>20,578,437</u>
<b>NET ASSETS</b>					
Restricted					
Expendable for default prevention activities	594,395	-	-	-	594,395
Unrestricted	<u>2,383,025</u>	<u>3,483,496</u>	<u>-</u>	<u>-</u>	<u>5,866,521</u>
Total net assets	<u>2,977,420</u>	<u>3,483,496</u>	<u>-</u>	<u>-</u>	<u>6,460,916</u>
Total liabilities and net assets	<u>\$ 3,723,728</u>	<u>\$ 12,498,225</u>	<u>\$ 10,835,068</u>	<u>\$ (17,668)</u>	<u>\$ 27,039,353</u>

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM**  
**COMBINING BALANCE SHEET**  
**SEPTEMBER 30, 2011**

	2011				
	Agency Operating Fund	Alternative Loan Fund	Federal Student Loan Reserve Fund	Eliminations	Total
<b>ASSETS</b>					
<b>CURRENT ASSETS</b>					
Cash and cash equivalents					
Unrestricted	\$ 2,344,168	\$ 1,604,445	\$ -	\$ -	\$ 3,948,613
Restricted	100,281	-	3,616,240	-	3,716,521
Investments					
Unrestricted	-	9,946,102	-	-	9,946,102
Restricted	500,000	-	5,000,000	-	5,500,000
Due from other funds					
Unrestricted	14,870	260	-	(15,130)	-
Restricted	-	-	12,583	(11,293)	1,290
Receivables					
Unrestricted					
Interest	274	35,818	-	-	36,092
Default aversion fee	23,610	-	-	(23,610)	-
Account maintenance fee	156,799	-	-	-	156,799
Administrative fee	-	273,219	-	-	273,219
Other receivables	74,028	-	-	-	74,028
Restricted					
Interest	377	-	3,090	-	3,467
Federal reinsurance	-	-	2,342,866	-	2,342,866
Total receivables	255,088	309,037	2,345,956	(23,610)	2,886,471
Total current assets	3,214,407	11,859,844	10,974,779	(50,033)	25,998,997
<b>NONCURRENT ASSETS - UNRESTRICTED</b>					
Capital assets					
Computer software	3,819,514	-	-	-	3,819,514
Accumulated amortization	(3,819,514)	-	-	-	(3,819,514)
Total capital assets	-	-	-	-	-
Total assets	\$ 3,214,407	\$ 11,859,844	\$ 10,974,779	\$ (50,033)	\$ 25,998,997

	2011				
	Agency Operating Fund	Alternative Loan Fund	Federal Student Loan Reserve Fund	Eliminations	Total
<b>LIABILITIES</b>					
<b>CURRENT LIABILITIES</b>					
Due to other funds	\$ 214,058	\$ 32,629	\$ 15,227	\$ (26,423)	\$ 235,491
Default aversion fee payable	-	-	23,610	(23,610)	-
Payable to lenders	-	-	1,800,491	-	1,800,491
Collections payable					
Department of Education	12,506	-	307,681	-	320,187
Unearned administrative fee	-	1,171,000	-	-	1,171,000
Allowance for future credit losses	-	548,000	462,000	-	1,010,000
Estimated future refunds of default aversion fees	92,000	-	-	-	92,000
Total current liabilities	<u>318,564</u>	<u>1,751,629</u>	<u>2,609,009</u>	<u>(50,033)</u>	<u>4,629,169</u>
<b>NONCURRENT LIABILITIES</b>					
Unearned administrative fee	-	2,341,364	-	-	2,341,364
Allowance for future losses	-	4,538,895	2,163,000	-	6,701,895
Estimated future refunds of default aversion fees	502,592	-	-	-	502,592
Federal Student Loan Reserve Fund	-	-	6,202,770	-	6,202,770
Total noncurrent liabilities	<u>502,592</u>	<u>6,880,259</u>	<u>8,365,770</u>	<u>-</u>	<u>15,748,621</u>
Total liabilities	<u>821,156</u>	<u>8,631,888</u>	<u>10,974,779</u>	<u>(50,033)</u>	<u>20,377,790</u>
<b>NET ASSETS</b>					
Restricted					
Expendable for default prevention activities	600,658	-	-	-	600,658
Unrestricted	1,792,593	3,227,956	-	-	5,020,549
Total net assets	<u>2,393,251</u>	<u>3,227,956</u>	<u>-</u>	<u>-</u>	<u>5,621,207</u>
Total liabilities and net assets	<u>\$ 3,214,407</u>	<u>\$ 11,859,844</u>	<u>\$ 10,974,779</u>	<u>\$ (50,033)</u>	<u>\$ 25,998,997</u>

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM**  
**COMBINING STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS**  
**YEAR ENDED SEPTEMBER 30, 2012**

	2012		
	Agency Operating Fund	Alternative Loan Fund	Total
<b>OPERATING REVENUES</b>			
Administrative fee	\$ -	\$ 1,809,928	\$ 1,809,928
Loan recoveries, net of remittance to Department of Education of \$1,348,307	252,615	-	252,615
Rehabilitated loans, net of remittance to Department of Education of \$1,613,898	423,785	-	423,785
Collection cost revenues net of remittance to Department of Education of \$173,191	614,036	-	614,036
Account maintenance fees	582,890	-	582,890
Default aversion fees	347,150	-	347,150
Grant income	1,802,157	-	1,802,157
	<u>4,022,633</u>	<u>1,809,928</u>	<u>5,832,561</u>
Total operating revenues			
<b>OPERATING EXPENSES</b>			
Service and administrative expense	1,495,525	368,974	1,864,499
Grant expenditures	1,802,157	-	1,802,157
Default prevention activities	8,806	-	8,806
Credit loss expense	-	1,229,639	1,229,639
DAF refund provision	138,859	-	138,859
	<u>3,445,347</u>	<u>1,598,613</u>	<u>5,043,960</u>
Total operating expenses			
<b>OPERATING INCOME</b>	<b>577,286</b>	<b>211,315</b>	<b>788,601</b>
<b>NONOPERATING REVENUES</b>			
Interest income	6,883	44,225	51,108
	<u>6,883</u>	<u>44,225</u>	<u>51,108</u>
<b>CHANGE IN NET ASSETS</b>	<b>584,169</b>	<b>255,540</b>	<b>839,709</b>
<b>TOTAL NET ASSETS, BEGINNING OF YEAR</b>	<b>2,393,251</b>	<b>3,227,956</b>	<b>5,621,207</b>
	<u>2,393,251</u>	<u>3,227,956</u>	<u>5,621,207</u>
<b>TOTAL NET ASSETS, END OF YEAR</b>	<b>\$ 2,977,420</b>	<b>\$ 3,483,496</b>	<b>\$ 6,460,916</b>
	<u>\$ 2,977,420</u>	<u>\$ 3,483,496</u>	<u>\$ 6,460,916</u>

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM**  
**COMBINING STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS**  
**YEAR ENDED SEPTEMBER 30, 2011**

	2011		
	Agency Operating Fund	Alternative Loan Fund	Total
<b>OPERATING REVENUES</b>			
Administrative fee	\$ -	\$ 1,364,318	\$ 1,364,318
Loan recoveries, net of remittance to Department of Education of \$1,343,239	262,494	-	262,494
Rehabilitated loans, net of remittance to Department of Education of \$1,072,044	261,863	-	261,863
Collection cost revenues net of remittance to Department of Education of \$89,687	354,360	-	354,360
Loan processing and issuance fees	7,833	-	7,833
Account maintenance fees	612,689	-	612,689
Default aversion fees	433,655	-	433,655
Grant income	896,781	-	896,781
<b>Total operating revenues</b>	<b>2,829,675</b>	<b>1,364,318</b>	<b>4,193,993</b>
<b>OPERATING EXPENSES</b>			
Service and administrative expense	1,389,168	342,232	1,731,400
Grant expenditures	895,160	-	895,160
Default prevention activities	8,184	-	8,184
Credit loss expense	-	816,081	816,081
DAF refund provision	174,197	-	174,197
<b>Total operating expenses</b>	<b>2,466,709</b>	<b>1,158,313</b>	<b>3,625,022</b>
<b>OPERATING INCOME</b>	<b>362,966</b>	<b>206,005</b>	<b>568,971</b>
<b>NONOPERATING REVENUES</b>			
Interest income	7,231	107,750	114,981
<b>CHANGE IN NET ASSETS</b>	<b>370,197</b>	<b>313,755</b>	<b>683,952</b>
<b>TOTAL NET ASSETS, BEGINNING OF YEAR</b>	<b>2,023,054</b>	<b>2,914,201</b>	<b>4,937,255</b>
<b>TOTAL NET ASSETS, END OF YEAR</b>	<b>\$ 2,393,251</b>	<b>\$ 3,227,956</b>	<b>\$ 5,621,207</b>

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM**  
**COMBINING STATEMENT OF CASH FLOWS**  
**YEAR ENDED SEPTEMBER 30, 2012**

	2012				
	Agency Operating Fund	Alternative Loan Fund	Federal Student Loan Reserve Fund	Eliminations	Total
<b>OPERATING ACTIVITIES</b>					
Loan recoveries received from borrowers	\$ 210,248	\$ 111,637	\$ 1,414,393	\$ -	\$ 1,736,278
Loan recoveries remitted to DOE	-	-	(1,225,861)	-	(1,225,861)
Credit loss claims paid to lenders - BND	-	(1,002,504)	(8,735,208)	-	(9,737,712)
Credit loss claims paid to other lenders	-	(22,678)	(5,225,690)	-	(5,248,368)
Credit loss claims received from DOE	-	-	11,636,041	-	11,636,041
Rehab loan proceeds received from lenders - BND	813,801	-	1,692,735	-	2,506,536
Rehab loan proceeds remitted to DOE	-	-	(1,660,102)	-	(1,660,102)
Collections received from borrowers	239,974	-	-	-	239,974
Grant proceeds received	1,753,130	-	-	-	1,753,130
Account maintenance fees received from DOE	595,205	-	-	-	595,205
Default aversion fees received from FFEL Program	233,425	-	(233,425)	-	-
Administrative fee received from borrowers	-	1,858,923	-	-	1,858,923
Service and administrative expense paid - BND	(3,404,506)	(370,460)	-	-	(3,774,966)
<b>NET CASH FROM (USED FOR) OPERATING ACTIVITIES</b>	<b>441,277</b>	<b>574,918</b>	<b>(2,337,117)</b>	<b>-</b>	<b>(1,320,922)</b>
<b>INVESTING ACTIVITIES</b>					
Proceeds from investment maturities - BND	2,000,000	12,946,102	9,500,000	-	24,446,102
Purchase of investments - BND	(3,000,000)	(14,000,000)	(8,000,000)	-	(25,000,000)
Interest received	7,041	68,042	15,222	-	90,305
<b>NET CASH FROM (USED FOR) INVESTING ACTIVITIES</b>	<b>(992,959)</b>	<b>(985,856)</b>	<b>1,515,222</b>	<b>-</b>	<b>(463,593)</b>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>(551,682)</b>	<b>(410,938)</b>	<b>(821,895)</b>	<b>-</b>	<b>(1,784,515)</b>
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR</b>	<b>2,444,449</b>	<b>1,604,445</b>	<b>3,616,240</b>	<b>-</b>	<b>7,665,134</b>
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<b>\$ 1,892,767</b>	<b>\$ 1,193,507</b>	<b>\$ 2,794,345</b>	<b>\$ -</b>	<b>\$ 5,880,619</b>
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH FROM (USED FOR) OPERATING ACTIVITIES</b>					
Operating income	\$ 577,286	\$ 211,315	\$ -	\$ -	\$ 788,601
Adjustments to reconcile operating income to net cash from (used for) operating activities					
Credit loss expense	-	316,094	-	-	316,094
DAF refund provision, net of refunds	17,734	-	-	-	17,734
Changes in assets and liabilities:					
Due from other funds	(35,211)	-	12,439	22,772	-
Administrative fee receivable - BND	-	(19,238)	-	-	(19,238)
Default fee receivable	-	-	42	-	42
Federal reinsurance receivable - DOE	(45,665)	-	(2,197,002)	-	(2,242,667)
Account maintenance fee receivable	12,315	-	-	-	12,315
Default aversion fee receivable	7,400	-	-	(7,400)	-
Unearned administrative fee	-	68,233	-	-	68,233
Due to other funds	(10,518)	(1,486)	(14,022)	(22,772)	(48,798)
Due to BND	(98,018)	-	-	-	(98,018)
Payable to lenders	-	-	367,300	-	367,300
Collections payable	15,954	-	76,243	-	92,197
Federal Student Loan Reserve Fund	-	-	(574,717)	-	(574,717)
Default aversion fee payable	-	-	(7,400)	7,400	-
<b>NET CASH FROM (USED FOR) OPERATING ACTIVITIES</b>	<b>\$ 441,277</b>	<b>\$ 574,918</b>	<b>\$ (2,337,117)</b>	<b>\$ -</b>	<b>\$ (1,320,922)</b>

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM**  
**COMBINING STATEMENT OF CASH FLOWS**  
**YEAR ENDED SEPTEMBER 30, 2011**

	2011				
	Agency Operating Fund	Alternative Loan Fund	Federal Student Loan Reserve Fund	Eliminations	Total
<b>OPERATING ACTIVITIES</b>					
Loan recoveries received from borrowers	\$ 259,658	\$ 135,136	\$ 1,385,290	\$ -	\$ 1,780,084
Loan recoveries remitted to DOE	-	-	(1,332,530)	-	(1,332,530)
Credit loss claims paid to lenders - BND	-	(752,497)	(6,855,644)	-	(7,608,141)
Credit loss claims paid to other lenders	-	(30,608)	(4,412,193)	-	(4,442,801)
Credit loss claims received from DOE	-	-	10,953,497	-	10,953,497
Rehab loan proceeds received from lenders - BND	516,751	-	1,124,729	-	1,641,480
Rehab loan proceeds remitted to DOE	-	-	(914,714)	-	(914,714)
Collections received from borrowers	134,098	-	-	-	134,098
Grant proceeds received	822,753	-	-	-	822,753
Loan processing and issuance fees received from DOE	21,774	-	-	-	21,774
Account maintenance fees received from DOE	643,177	-	-	-	643,177
Default aversion fees received from FFEL Program	335,763	-	(335,763)	-	-
Default fees received from borrowers and lenders	-	-	5,296	-	5,296
Administrative fee received from borrowers	-	1,693,606	-	-	1,693,606
Service and administrative expense paid - BND	(2,477,485)	(326,287)	-	-	(2,803,772)
<b>NET CASH FROM (USED FOR) OPERATING ACTIVITIES</b>	<b>256,489</b>	<b>719,350</b>	<b>(382,032)</b>	<b>-</b>	<b>593,807</b>
<b>INVESTING ACTIVITIES</b>					
Proceeds from investment maturities - BND	2,499,684	10,798,936	8,498,936	-	21,797,556
Purchase of investments - BND	(1,499,684)	(10,995,038)	(7,498,936)	-	(19,993,658)
Interest received	6,927	174,574	60,380	-	241,881
<b>NET CASH FROM (USED FOR) INVESTING ACTIVITIES</b>	<b>1,006,927</b>	<b>(21,528)</b>	<b>1,060,380</b>	<b>-</b>	<b>2,045,779</b>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>1,263,416</b>	<b>697,822</b>	<b>678,348</b>	<b>-</b>	<b>2,639,586</b>
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR</b>	<b>1,181,033</b>	<b>906,623</b>	<b>2,937,892</b>	<b>-</b>	<b>5,025,548</b>
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<b>\$ 2,444,449</b>	<b>\$ 1,604,445</b>	<b>\$ 3,616,240</b>	<b>\$ -</b>	<b>\$ 7,665,134</b>
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH FROM (USED FOR) OPERATING ACTIVITIES</b>					
Operating income	\$ 362,966	\$ 206,005	\$ -	\$ -	\$ 568,971
Adjustments to reconcile operating income to net cash from (used for) operating activities					
Credit loss expense	-	142,895	-	-	142,895
DAF refund provision, net of refunds	74,592	-	-	-	74,592
Changes in assets and liabilities:					
Due from other funds	(52,107)	25,217	(12,361)	64,468	25,217
Administrative fee receivable - BND	-	(21,942)	-	-	(21,942)
Default fee receivable	-	-	616	-	616
Federal reinsurance receivable - DOE	551	-	125,115	-	125,666
Account maintenance fee receivable	30,488	-	-	-	30,488
Loan processing and issuance fee receivable	13,941	-	-	-	13,941
Default aversion fee receivable	1,713	-	-	(1,713)	-
Unearned administrative fee	-	351,230	-	-	351,230
Due to other funds	10,831	15,945	(10,835)	(64,468)	(48,527)
Due to BND	(184,973)	-	-	-	(184,973)
Payable to lenders	-	-	(19,534)	-	(19,534)
Collections payable	(1,513)	-	168,039	-	166,526
Federal Student Loan Reserve Fund	-	-	(631,359)	-	(631,359)
Default aversion fee payable	-	-	(1,713)	1,713	-
<b>NET CASH FROM (USED FOR) OPERATING ACTIVITIES</b>	<b>\$ 256,489</b>	<b>\$ 719,350</b>	<b>\$ (382,032)</b>	<b>\$ -</b>	<b>\$ 593,807</b>

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
YEAR ENDED SEPTEMBER 30, 2012**

**EXHIBIT A-1**

<u>Federal Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Expenditures</u>
DEPARTMENT OF EDUCATION		
Direct Program		
Federal Family Education Loan (FFEL) Program (Note 2)	84.032	
Direct subsidies:		
Reinsurance Payments		\$ 13,833,043
Guarantee Agency's Equitable Share of Loan Collections		822,577
Default Aversion Fee		226,025
Account Maintenance Fee		582,890
		<u>15,464,535</u>
Total FFEL Program Direct Subsidies		
Guaranteed FFEL Program Student Loans (Note 3)		
Original principal amount of loans from previous years on which there are continuing compliance requirements		<u>1,045,327,997</u>
		<u>1,060,792,532</u>
Total FFEL Program		
Pass-through programs from:		
Bank of North Dakota		
College Access Challenge Grant (Note 4)	84.378A	<u>1,802,157</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS		<u>\$ 1,062,594,689</u>

**NOTE 1** - The schedule of expenditures of federal awards includes the federal grant activity of the North Dakota Guaranteed Student Loan Program and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

**NOTE 2** - See Notes 5 and 6 to the financial statements for information relative to the existence and value of federal loan guarantee programs.

**NOTE 3** - At September 30, 2012, the original principal amount of guaranteed student loans outstanding on which there are continuing compliance requirements is \$916,028,953.

**NOTE 4** – Of the federal expenditures presented in the schedule, the North Dakota Guaranteed Student Loan Program provided federal awards to subrecipients as follows:

<u>CFDA Number</u>	<u>Program Name</u>	<u>Amount Provided to Subrecipients</u>
84.378A	College Access Challenge Grant	\$ <u>261,323</u>

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
YEAR ENDED SEPTEMBER 30, 2012**

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**EXHIBIT A-2**

There were no prior audit findings reported for the North Dakota Guaranteed Student Loan Program.

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON AND OTHER  
COMPLIANCE MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS  
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

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The Industrial Commission  
State of North Dakota  
Bismarck, North Dakota

We have audited the financial statements of the business-type entities of the North Dakota Guaranteed Student Loan Program, a department of the State of North Dakota, as of and for the year ended September 30, 2012, which collectively comprise North Dakota Guaranteed Student Loan Program's basic financial statements and have issued our report thereon dated February 14, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

*Internal Control over Financial Reporting*

Management of North Dakota Guaranteed Student Loan Program is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered North Dakota Guaranteed Student Loan Program's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of North Dakota Guaranteed Student Loan Program's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of North Dakota Guaranteed Student Loan Program's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies, or material weaknesses and; therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings and questioned costs, we identified a certain deficiency in internal control over financial reporting that we consider to be a material weakness.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described as item 2012-1 in the accompanying schedule of findings and questioned costs to be a material weakness.

*Compliance and Other Matters*

As part of obtaining reasonable assurance about whether North Dakota Guaranteed Student Loan Program's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

North Dakota Guaranteed Student Loan Program's response to the finding in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit North Dakota Guaranteed Student Loan Program's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the North Dakota Industrial Commission, Legislative Audit and Fiscal Review Committee, management, others within the entity, and the U.S. Department of Education, and is not intended to be, and should not be, used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Eide Sully LLP".

Aberdeen, South Dakota  
February 14, 2013



CPAs & BUSINESS ADVISORS

**EXHIBIT A-4**

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

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The Industrial Commission  
State of North Dakota  
Bismarck, North Dakota

*Compliance*

We have audited North Dakota Guaranteed Student Loan Program's compliance with the types of compliance requirements described in the OMB Circular A-133, *Compliance Supplement*, that could have a direct and material effect on each of North Dakota Guaranteed Student Loan Program's major federal programs for the year ended September 30, 2012. North Dakota Guaranteed Student Loan Program's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of North Dakota Guaranteed Student Loan Program's management. Our responsibility is to express an opinion on North Dakota Guaranteed Student Loan Program's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. And audit includes examining, on a test basis, evidence about North Dakota Guaranteed Student Loan Program's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of North Dakota Guaranteed Student Loan Program's compliance with those requirements.

In our opinion, North Dakota Guaranteed Student Loan Program complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended September 30, 2012.

*Internal Control Over Compliance*

Management of North Dakota Guaranteed Student Loan Program is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered North Dakota Guaranteed Student Loan Program's internal control over compliance with requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of North Dakota Guaranteed Student Loan Program's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the North Dakota Industrial Commission, Legislative Audit and Fiscal Review Committee, management, others within the entity, and the U.S. Department of Education, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Eide Bailly LLP".

Aberdeen, South Dakota  
February 14, 2013

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM  
 SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
 YEAR ENDED SEPTEMBER 30, 2012**

**EXHIBIT A-5**

**PART I - SUMMARY OF AUDITOR'S RESULTS**

**Financial Statements**

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

- Material weakness(es) identified?       x       yes                      no
- Significant deficiencies identified that are not considered to be material weaknesses?                      yes       x       none reported

Noncompliance material to financial statements noted?                      yes       x       no

**Federal Awards**

Internal control over major programs:

- Material weakness(es) identified?                      yes       x       no
- Significant deficiencies identified that are not considered to be material weaknesses?                      yes       x       none reported

Type of auditor's report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133?                      yes       x       no

Identification of major programs:

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Cluster</u>
84.032	Federal Family Education Loan Program

Dollar threshold used to distinguish between type A and type B programs?                      \$           300,000          

Auditee qualified as low-risk auditee?       x       yes                      no

**PART II - FINDINGS RELATING TO THE FINANCIAL STATEMENTS****Material Weakness****2012-1 –Documentation Supporting Significant Estimates**

**Condition** – Management does not have a formally documented process for evaluating and reconciling significant estimates in the financial statements, including the allowance for loan losses on DEAL and FFELP loans, the estimated future refunds of default aversion fees, and revenue recognition over administrative fee revenue, including support for the estimated useful lives of DEAL loans and the percentage of fees to be deferred to future periods.

**Criteria** – A good system of internal control over financial reporting contemplates an adequate system for evaluating and reconciling significant estimates in the financial statements.

**Cause** – The Organization does not have an internal control system designed to formally evaluate or reconcile significant estimates in the financial statements.

**Effect** – Significant estimates including the allowance for loan losses on DEAL loans, FFELP loans, future refunds of default aversion fees, and revenue recognition of administrative fee revenue could be misstated.

**Recommendation** – We recommend that management formally document a process for evaluating and estimating the allowance for loan losses on DEAL loans and FFELP loans, including a reconciliation of the historical cumulative default rate to the allowance for loan losses as a percentage of loans (reserve ratio) and future trends in the portfolio. Management should also formally document its revenue recognition methodology for administrative fee revenue, including documentation supporting the estimated lives of the underlying loans and estimating the percentage of fees to be deferred to future periods. Management should also formally document its process for evaluating and estimating the future refunds of default aversion fees (DAF).

**Management Response** – Management agrees with this recommendation and will formally document all estimates used in the financial statements

**PART III - FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARD PROGRAMS**

There are no findings or questioned costs relating to the federal award programs which are required to be reported in accordance with Section 510(a) of OMB Circular A-133.



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EXHIBIT A-6

**NORTH DAKOTA GUARANTEED STUDENT LOAN PROGRAM  
AUDITOR'S SPECIFIC COMMENTS REQUESTED BY THE  
NORTH DAKOTA LEGISLATIVE AUDIT AND FISCAL REVIEW COMMITTEE  
YEAR ENDED SEPTEMBER 30, 2012**

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The Industrial Commission  
State of North Dakota  
Bismarck, North Dakota

The Legislative Audit and Fiscal Review Committee require that certain items be addressed by independent certified public accountants performing audits of state agencies. The items and our responses are as follows:

**1. What type of opinion was issued on the financial statements?**

*Unqualified*

**2. Was there compliance with statutes, laws, rules, regulations under which the agency was created and is functioning?**

*Yes - A review was made of Chapter 15-62.1 and other pertinent chapters of the North Dakota Century Code and we felt the Agency operated within the statutes, laws, rules and regulations under which it was created.*

**3. Was internal control adequate and functioning effectively?**

*No – An internal control deficiency was identified. See schedule of findings and questioned costs.*

**4. Were there any indications of lack of efficiency in financial operations and management of the agency?**

*No*

**5. Has action been taken on findings and recommendations included in prior year audit reports?**

*There were no prior year findings.*

**6. Was a management letter issued? If so, provide a summary below, including any recommendations and the management response.**

*No*

**Audit Committee Communications**

- 1. Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.**

*During fiscal year 2012, the Program changed its methodology of recognizing administrative fee revenue. Forty percent of revenues are recognized at the time of fee collection with the remainder recognized over the estimated life of an average loan (10 years) using the sum-of-the-years digits method. In 2011, twenty percent of revenues were recognized at the time of fee collection with the remainder recognized over the estimated life of an average loan (10 years) using the sum-of-the-years digits method.*

- 2. Identify any significant accounting estimates and the process used by management to determine those estimates.**

*Management's estimate of the amortization of administrative fee revenue is based on management's evaluation of a number of factors, including length of term of student loans, prepayment speeds, and industry standards.*

*Management's estimate of future refunds of default aversion fees for which the percentage of income method is used to calculate the estimated allowance for refunds of the default aversion fee based on a periodic evaluation of default aversion fees received and a historical refund rate.*

*Management's estimate of the allowance for loan losses is based on management's evaluation of a number of factors, including recent loan loss experience, continuous evaluation of the loan portfolio quality, current and anticipated economic conditions, and other pertinent factors.*

- 3. Identify any significant audit adjustments.**

*None*

- 4. Identify any disagreements with management, whether or not resolved to the auditor's satisfaction, relating to financial accounting, reporting, or auditing matters that could be significant to the financial statements.**

*None*

- 5. Identify any serious difficulties encountered in performing the audit.**

*None*

- 6. Identify any major issues discussed with management prior to retention.**

*None*

7. **Identify any management consultations with other accountants about auditing and accounting matters.**

*None*

8. **Identify any high-risk information technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six audit report questions to be addressed by auditors are directly related to the operations of an information technology system.**

*Based on the audit procedures performed, the North Dakota Guaranteed Student Loan Program's critical information technology system is the Priority Guarantee System (PGS). There were no exceptions identified that were directly related to this application.*

This report is intended solely for the information and use of the North Dakota Industrial Commission, Legislative Audit and Fiscal Review Committee, management, and the U.S. Department of Education, and is not intended to be, and should not be, used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Eide Sully LLP".

Aberdeen, South Dakota  
February 14, 2013



CPAs & BUSINESS ADVISORS

EXHIBIT B-1

**INDEPENDENT AUDITOR'S COMMUNICATION  
TO THE INDUSTRIAL COMMISSION OF NORTH DAKOTA**

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To the Industrial Commission  
North Dakota Guaranteed Student Loan Program  
Bismarck, North Dakota

We have audited the financial statements of the business-type activities of North Dakota Guaranteed Student Loan Program for the year ended September 30, 2012. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and, if applicable, *Government Auditing Standards* and OMB Circular A-133, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated November 9, 2012. Professional standards also require that we communicate to you the following information related to our audit.

**Significant Audit Findings**

*Qualitative Aspects of Accounting Practices*

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by North Dakota Guaranteed Student Loan Program are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year ended September 30, 2012, except as follows.

In 2012, the North Dakota Guaranteed Student Loan Program had a change in estimate related to the amortization of administrative fee revenue on DEAL loans disbursed. Management had previously recognized 20% of the administrative fee charged on new DEAL loans in the year the loan was disbursed. Beginning in 2012, the North Dakota Guaranteed Student Loan Program recognizes 40% of the administrative fee revenue in the year the loan was disbursed. The application of the change in estimate was applied prospectively.

We noted no transactions entered into by the governmental unit during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the North Dakota Guaranteed Student Loan Program's financial statements were:

Management's estimate of the amortization of administrative fee revenue is based on management's evaluation of a number of factors, including length of term of student loans, prepayment speeds, and industry standards. We evaluated the key factors and assumptions used to develop the amortization of administrative fee revenue in determining that it is reasonable in relation to the financial statements taken as a whole.

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Management’s estimate of future refunds of default aversion fees for which the percentage of income method is used to calculate the estimated allowance for refunds of the default aversion fee based on a periodic evaluation of default aversion fees received and a historical refund rate. We evaluated the key factors and assumptions used to develop the estimates in determining that it is reasonable in relation to the financial statements taken as a whole.

Management’s estimate of the allowance for loan losses is based on management’s evaluation of a number of factors, including recent loan loss experience, continuous evaluation of the loan portfolio quality, current and anticipated economic conditions, and other pertinent factors. We evaluated the key factors and assumptions used to develop the estimates in determining that it is reasonable in relation to the financial statements taken as a whole.

The financial statement disclosures are neutral, consistent, and clear.

*Difficulties Encountered in Performing the Audit*

We encountered no significant difficulties in dealing with management in performing and completing our audit.

*Corrected and Uncorrected Misstatements*

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. Uncorrected misstatements of the financial statements are summarized below. Management has determined that their effects are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

Administrative expenses	\$31,138	
Accounts payable		31,138
<i>To accrue for payments made after year-end on expenses incurred prior to year-end</i>		

In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole.

*Disagreements with Management*

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor’s report. We are pleased to report that no such disagreements arose during the course of our audit.

*Management Representations*

We have requested certain representations from management that are included in the management representation letter dated February 14, 2013.

*Management Consultations with Other Independent Accountants*

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a “second opinion” on certain situations. If a consultation involves application of an accounting principle to the governmental unit’s financial statements or a determination of the type of auditor’s opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

*Other Audit Findings or Issues*

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the governmental unit's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

**Other Matters**

With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

This information is intended solely for the use of the Industrial Commission and management of North Dakota Guaranteed Student Loan Program and is not intended to be, and should not be, used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Eide Sully LLP".

Aberdeen, South Dakota  
February 14, 2013