State of Illinois
Illinois Student Assistance Commission
Illinois Designated Account Purchase Program

Financial Audit
For the Year Ended June 30, 2010

Performed as Special Assistant Auditors for the
Auditor General, State of Illinois

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Agency Officials

Executive Director	Andrew Davis
Chief Financial Officer	John Sinsheimer
Deputy Chief Financial Officer (10/16/2009 to Current)	Brian Begrowicz
Acting Director Operations	Myron Kowalski
Director, Accounting and Finance	Frank Berauer

Agency offices are located at:

1755 Lake Cook Road
Deerfield, IL 60015-5209
(847) 948-8500

Financial Statement Report

Summary

The audit of the accompanying financial statements of the Illinois Designated Account Purchase Program of the State of Illinois, Illinois Student Assistance Commission (IDAPP), was performed by McGladrey & Pullen, LLP.

Based on their audit, the auditors expressed an unqualified opinion on IDAPP's financial statements.

Summary of Findings

The auditors identified matters involving IDAPP's internal control over financial reporting that they considered to be significant deficiencies. The significant deficiencies are described in the accompanying schedule of findings listed in the table of contents as finding 10-2 (Financial Reporting Process), finding 10-3 (Student Loan Payments Not Processed Correctly), finding 10-4 (Noncompliance with Investment Policy) and finding 10-5 (Noncompliance with Write-Off Policy).

The auditors also identified instances of noncompliance and other matters. The instances of noncompliance and other matters are described in the accompanying schedule of findings listed in the table of contents as finding 10-4 (Noncompliance with Investment Policy), 10-5 (Noncompliance with Write-Off Policy) and 10-6 (Debt Covenant Violation).

Exit Conference

The findings and recommendations appearing in this report were discussed with IDAPP personnel at an exit conference on March 8, 2011. Attending were:

Illinois Student Assistance Commission	
Andrew Davis	Executive Director
Shoba Nandhan	Chief Financial Officer
Karen Salas	Interim General Counsel
Anita Geter	Director-Internal Audit
Brian Begrowicz	Deputy Chief Financial Officer
Frank Berauer	Director, Accounting and Finance-IDAPP
Anne Hunter	Assistant Comptroller

McGladrey & Pullen, LLP	
Linda Abernethy	Partner
Rolake Adedara	Director

Office of the Auditor General	
Jon Fox	Audit Manager

The responses to the recommendations were provided by Shoba Nandhan in a letter dated March 11, 2011.

McGladrey

Independent Auditors' Report

Honorable William G. Holland
Auditor General
State of Illinois, and

Mr. Donald J. McNeil
Honorable Chairman of the Governing Board
Illinois Student Assistance Commission

As Special Assistant Auditors for the Auditor General, we have audited the accompanying financial statements of the Illinois Designated Account Purchase Program of the State of Illinois, Illinois Student Assistance Commission as of and for the year ended June 30, 2010, as listed in the table of contents. These financial statements are the responsibility of the State of Illinois, Illinois Student Assistance Commission's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the 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 2, the financial statements present only the Illinois Designated Account Purchase Program, a fund of the State of Illinois, Illinois Student Assistance Commission, and do not purport to, and do not present fairly the financial position of the State of Illinois or the Illinois Student Assistance Commission as of June 30, 2010, and its changes in financial position and cash flows thereof for the year 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 Illinois Designated Account Purchase Program of the State of Illinois, Illinois Student Assistance Commission, as of June 30, 2010, and the respective changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The State of Illinois, Illinois Student Assistance Commission has not presented a management's discussion and analysis for the Illinois Designated Account Purchase Program that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be part of, the financial statements.

In accordance with *Government Auditing Standards*, we have also issued a report dated March 14, 2011 on our consideration of the State of Illinois, Illinois Student Assistance Commission's internal control over financial reporting of the Illinois Designated Account Purchase Program and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming an opinion on the financial statements of the Illinois Designated Account Purchase Program of the State of Illinois, Illinois Student Assistance Commission. The schedule of bonds outstanding, listed in the table of contents as supplemental information, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

McGladrey & Pullen, LLP

Schaumburg, Illinois
March 14, 2011

State of Illinois
Illinois Student Assistance Commission
Illinois Designated Account Purchase Program

Statement of Net Assets
June 30, 2010

Assets	
Current assets - unrestricted	
Cash and cash equivalents	$ 731,344
Current assets - restricted	
Cash and cash equivalents	49,108,104
Investments	229,436,455
Receivables	
Notes	390,950
Student loans, net of allowance of $1,599,042	177,204,831
Accrued interest - loans and notes	20,594,538
Accrued interest - investments	968,224
Other, net of allowance of $683,537	5,000
Due from other funds	6,876
Unamortized bond issuance cost	191,697
Total current assets - restricted	477,906,675
Noncurrent assets - unrestricted	
Depreciated capital assets, net	25,095
Noncurrent assets - restricted	
Receivables	
Notes	16,128,695
Student loans, net of allowance of $8,394,972	930,325,360
Unamortized bond issuance costs	1,270,492
Total noncurrent assets - restricted	947,724,547
Total assets	1,426,387,661

(Continued)

State of Illinois
Illinois Student Assistance Commission
Illinois Designated Account Purchase Program

Statement of Net Assets (Continued)
June 30, 2010

Liabilities		
Current liabilities		
Accounts payable and accrued expenses	$	1,063,867
Accrued interest payable		1,567,123
Federal special allowance and interest subsidy		2,820,002
Due to other ISAC funds		3,921,674
Due to other State funds		5,041
Due to State of Illinois component units		150,839
Compensated absences		185,410
Revenue bonds payable		88,350,000
Revolving credit lines		360,174,502
Total current liabilities		458,238,458
Noncurrent liabilities		
Compensated absences		219,280
Revenue bonds payable, net		931,350,808
Total noncurrent liabilities		931,570,088
Total liabilities		1,389,808,546
Net Assets		
Invested in capital assets		25,095
Restricted		41,368,787
Unrestricted		(4,814,767)
Total net assets	$	36,579,115

See Notes to Financial Statements.

State of Illinois
Illinois Student Assistance Commission
Illinois Designated Account Purchase Program

Statement of Revenues, Expenses, and Changes in Fund Net Assets
Year Ended June 30, 2010

Operating revenues	
Investment income	
Interest - student loans	$ 44,340,133
Interest - investments	5,237,145
Net increase in fair value of investments	3,227,098
Fees	2,268,314
Total operating revenues	55,072,690
Operating expenses	
Interest and other student loan expenses	
Interest expense	
Student loan revenue bonds	12,603,167
Amortization of loan premiums and fees	3,474,961
Other student loan fees	2,754,870
Provision for loan losses	8,155,878
Other operating expenses	
Salaries and employee benefits	6,315,995
External loan servicing	5,493,179
Bond issuance and legal fees	82,056
Occupancy	184,254
Data processing expense	128,039
Management and professional services	3,435,268
ISAC shared expense	2,684,392
Depreciation	8,796
Other	149,510
Total operating expenses	45,470,365
Operating Income	9,602,325
Nonoperating revenues (expenses)	
Federal special allowance and interest subsidy and excess interest expense (Note 6)	(11,779,288)
Loss before transfers	(2,176,963)
Transfer to ISAC	(750,000)
Change in net assets	(2,926,963)
Net assets, July 1, 2009	39,506,078
Net assets, June 30, 2010	$ 36,579,115

See Notes to Financial Statements.

State of Illinois
Illinois Student Assistance Commission
Illinois Designated Account Purchase Program

Statement of Cash Flows
Year Ended June 30, 2010

Cash flows from operating activities		
Cash payments to suppliers for goods and services	$	(12,251,629)
Cash payments to employees for services		(6,372,672)
Cash receipts from other operating activities (student loans and fees)		232,647,720
Cash payments for other operating activities (student loans)		(73,494,141)
Net cash provided by operating activities		140,529,278
Cash flows from noncapital financing activities		
Principal paid on revenue bonds and other borrowings		(136,600,000)
Proceeds from revenue bonds and other borrowings		89,994,952
Interest paid on revenue bonds and other borrowings		(12,249,328)
Federal special allowance and interest subsidy		(11,636,346)
Transfer to ISAC		(750,000)
Net cash used for noncapital financing activities		(71,240,722)
Cash flows from investing activities		
Interest received from investment securities		3,479,235
Purchase of investment securities		(510,835,945)
Proceeds from sale and maturities of investment securities		425,006,991
Net cash used for investing activities		(82,349,719)
Net decrease in cash and cash equivalents		(13,061,163)
Cash and cash equivalents, July 1, 2009		62,900,611
Cash and cash equivalents, June 30, 2010	$	49,839,448
Reported as:		
Current - unrestricted	$	731,344
Current - restricted		49,108,104
	$	49,839,448

(Continued)

State of Illinois
Illinois Student Assistance Commission
Illinois Designated Account Purchase Program

Statement of Cash Flows (Continued)
Year Ended June 30, 2010

Reconciliation of operating income to net cash provided by operating activities	
Operating income	$ 9,602,325
Adjustments to reconcile operating income to net cash provided by operating activities	
Depreciation	8,796
Interest - investments	(5,237,145)
Net increase in fair value of investments	(3,227,098)
Interest expense	12,603,167
Provision for loan loss	8,155,878
Amortization of student loan premiums and fees	3,474,961
Change in assets and liabilities	
Notes receivable	26,690,022
Accounts receivable	
Student loans	80,875,362
Accrued interest - loans and notes	4,415,753
Due from other funds	1,717,572
Other receivables	1,805,726
Accounts payable and accrued expenses	(1,005,417)
Due to other State funds and component units	843,291
Compensated absences	(193,915)
Net cash provided by operating activities	$ 140,529,278
Supplemental disclosure of noncash transactions	
Net appreciation in fair value of investments	$ 4,556,076

See Notes to Financial Statements.

Note 1. Description of Fund

The Illinois Student Assistance Commission (ISAC) administers the nonshared proprietary fund described below. A nonshared fund is a fund in which a single State agency is responsible for administering substantially all financial transactions of the fund.

The Illinois Designated Account Purchase Program (IDAPP), a program of ISAC, was created through an Act of the State of Illinois General Assembly to increase participation of eligible lenders in ISAC's Student Loan Programs by purchasing guaranteed student loans from lenders in order to reduce the lenders' collection and administrative costs. IDAPP is also an originator and servicer of student loans. IDAPP is an integral unit of the State. As such, designation of management and governing authority are determined by the Governor of the State. The State also maintains overall accountability for IDAPP's fiscal matters. Activities of IDAPP are subject to the authority of the Office of the Governor, the State's Chief Executive Officer, and other departments of the executive branch of government (such as the Department of Central Management Services and the State Comptroller's Office) as defined by the General Assembly.

The accompanying financial statements present the financial position, results of operations, and cash flows of IDAPP. IDAPP's financial statements are an integral part of the State's overall comprehensive annual financial report. IDAPP was initially funded by a state appropriation as of July 1977 and has operated on a self-sustaining basis beginning in fiscal year 1979 through the issuance of student loan revenue bonds and notes, collection of its student loans receivable, payments from the United States Department of Education for interest and special allowance, and payments from various guarantors on defaulted loans. All IDAPP funds are held locally in various banks and financial institutions. The guaranteed student loans must be purchased from eligible lenders under the Illinois Student Assistance Law and the Federal Higher Education Act of 1965. IDAPP generally does not purchase student loans, which are more than 90 days delinquent. The reimbursement rates to lenders, such as IDAPP, in the Federal Family Education Loan Program (FFELP) are 100% for loans disbursed before October 1, 1993. For loans disbursed between October 1, 1993 and prior to July 1, 2006 the loans are reimbursed at 98%. Loans disbursed after July 1, 2006 are reimbursed at 97%.

Note 2. Summary of Significant Accounting Policies

The financial statements of IDAPP as administered by ISAC have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), as prescribed by the Governmental Accounting Standards Board (GASB). To facilitate the understanding of data included in the financial statements, summarized below are the more significant accounting policies.

A. Reporting Entity

As defined by GAAP, the financial reporting entity consists of a primary government, as well as its component units, which are legally separate organizations for which the elected officials of the primary government are financially accountable. Financial accountability is defined as:

1. Appointment of a voting majority of the component unit’s board and either (a) the primary government’s ability to impose its will, or (b) the possibility that the component unit will provide a financial benefit to or impose a financial burden on the primary government; or

2. Fiscal dependency on the primary government.

Note 2. Summary of Significant Accounting Policies (Continued)

A. Reporting Entity (Continued)

Based upon the required criteria, IDAPP has no component units, nor is it a component unit of any other entity. However, because IDAPP is not legally separate from the State of Illinois (State), it is included in the financial statements of the State as a proprietary fund. The State of Illinois' Comprehensive Annual Financial Report may be obtained by writing to the State Comptroller's Office, Financial Reporting Department, 325 West Adams Street, Springfield, Illinois, 62704-1871.

The financial statements present only IDAPP as administered by the State of Illinois and ISAC, and do not purport to, and do not, present fairly the financial position of the State of Illinois or ISAC as of June 30, 2010, and changes in its financial position and cash flows, where applicable, for the year then ended in conformity with GAAP.

B. Basis of Presentation

In government, the basic accounting and reporting entity is a fund. A fund is defined as an independent fiscal and accounting entity with a self-balancing set of accounts recording cash and/or other resources together with all related liabilities, obligations, reserves, and equities (net assets) which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations. A Statement of Net Assets, Statement of Revenues, Expenses, and Changes in Fund Net Assets, and Statement of Cash Flows have been presented for IDAPP.

Operating revenues result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Due to the nature of IDAPP activities, income from investments and interest expense are considered operating activities in the Statement of Revenues, Expenses and Changes in Fund Net Assets. Nonoperating revenues result from non-exchange transactions (e.g. grants (subsidy payments)) or ancillary activities.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

C. Basis of Accounting

IDAPP is reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flow takes place.

D. Revenue Recognition

Revenues from fees and the federal special allowance and interest subsidy assistance are recognized when earned. Uncollected interest income on student loans is accrued as revenue at June 30, 2010.

E. Cash and Cash Equivalents

Cash and cash equivalents consist principally of deposits held in banks for locally held funds and securities with maturities of less than 90 days at the date of purchase. Cash and cash equivalents also include deposits held in the State Treasury.

Note 2. Summary of Significant Accounting Policies (Continued)

F. Investments

IDAPP presents investments in its Statement of Net Assets at fair value. The net appreciation or depreciation in the fair value of investments is included as investment income in the Statement of Revenues, Expenses, and Changes in Fund Net Assets.

G. Student Loans Receivable/Premiums

The interest rate charged on IDAPP's student loans receivable is considered market rate, therefore the carrying amount of student loans receivable is considered a reasonable estimate of their market value.

As a secondary lender, when IDAPP purchases loans from another lender, IDAPP may pay a premium on those loans. Premiums over $50,000 (in the aggregate) are capitalized and amortized on a straight-line basis over the average remaining useful lives of the student loans. Premiums under $50,000 (in the aggregate) are expensed.

H. Allowance for Possible Loan Losses

The allowance for possible loan losses is a reserve for estimated credit losses arising from the student loan portfolio. A provision for possible loan losses, which is a charge against operations, is added to bring the allowance to a level that, in management's judgment, is adequate to absorb losses in the portfolio. Management performs a quarterly assessment of the loan portfolio in order to determine the appropriate level of the allowance. The factors in this evaluation include, but are not necessarily limited to, delinquencies over 120 days, loan servicing deficiencies and the amount of unguaranteed reimbursement from the United States Department of Education as discussed in Note 5.

Management believes that the allowance for possible loan losses is adequate. While management uses available information to recognize losses on loans, future additions may be necessary based on future review of compliance with due diligence and contractual servicing requirements by IDAPP, and its outside loan servicers.

I. Interfund Transactions

IDAPP has the following type of interfund transactions with other funds of the State:

Loans - amounts provided with a requirement for repayment. Interfund loans are reported as interfund receivables (i.e. due from other funds) in lender funds and interfund payables (i.e. due to other funds) in borrower funds.

Services provided and used - sales and purchases of services between funds for a price approximating their external exchange value. Interfund services provided and used are reported as revenues in seller funds and expenditures or expenses in purchaser funds. Unpaid amounts are reported as interfund receivables and payables in the fund Statement of Net Assets.

Reimbursements - repayments from the funds responsible for particular expenditures or expenses to the funds that initially paid for them. Reimbursements are reported as expenditures/expenses in the reimbursing fund and as a reduction of expenditures/expenses in the reimbursed fund.

Note 2. Summary of Significant Accounting Policies (Continued)

J. Capital Assets

Capital assets, which include equipment, are reported at cost. Capital assets are depreciated using the straight-line method over a period of five years. IDAPP capitalizes all equipment that has a cost or value greater than or equal to $5,000.

K. Restricted Assets

Restricted assets represent those assets which are required to be held by the trustee as mandated by the bond indentures or resolutions or are pledged as security in support of bond indentures or resolutions.

L. Compensated Absences

The liability for compensated absences consists of unpaid, accumulated vacation and sick leave balances for IDAPP employees. The liability has been calculated using the vesting method, in which leave amounts for both employees who currently are eligible to receive termination payments, and other employees who are expected to become eligible in the future to receive such payments upon termination are included. The liability has been calculated based on the employees' current salary level and includes salary related costs (e.g., social security and Medicare tax).

Legislation that became effective January 1, 1998 capped the paid sick leave for all State Employees' Retirement System members at December 31, 1997. Employees continue to accrue twelve sick days per year, but will not receive monetary compensation for any additional time earned after December 31, 1997. Sick days earned between 1984 and December 31, 1997 (with a 50% cash value) would only be used after all days with no cash value are depleted. Any sick days earned and unused after December 31, 1997 will be converted to service time for purposes of calculating employee pension benefits.

M. Bond Premiums, Discounts, and Issuance Costs

Revenue bonds payable are stated at face value net of bond premiums and discounts. Bond premiums and discounts, as well as issuance costs are deferred and amortized over the life of the bonds using the straight-line method. Amortization expense is reported as a component of interest expense in the financial statements.

N. Net Assets

Invested in capital assets - this consists of capital assets, net of accumulated depreciation, less the outstanding balances, if any, of bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets.

Restricted - result when constraints placed on net asset use are either externally imposed by creditors or imposed by law through constitutional provisions or enabling legislation.

Unrestricted - consists of net assets that do not meet the definition of "restricted" or "invested in capital assets."

Based on bond indentures, all IDAPP assets, except for assets relating to operations, are restricted for the benefit of debt holders until the bonds are retired. IDAPP first applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

Note 2. Summary of Significant Accounting Policies (Continued)

O. Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Note 3. Deposits and Investments

A. Permitted Deposits and Investments

Bond documents such as trust indentures place strict limitations on the type of investments that can be made by IDAPP. These limitations are set by the rating agencies and by the institutions providing third party guarantees, such as bond insurance or bank letters of credit. The limitations vary slightly from issue to issue, but in general they restrict investments to direct obligations of the federal government and government agencies, investment agreements, repurchase agreements, bank certificates of deposit, money market funds and highly rated commercial paper and municipal bonds.

The Public Funds Investment Act (Act) also restricts the investment of funds under the control of IDAPP. These restrictions apply to any funds, which are not restricted by the terms of a bond document. Permitted deposits and investments under the Act include (subject to various restrictions and limitations) direct federal obligations of the United States of America, federal guaranteed obligations, participation interests in federal obligations, federal affiliated institutions, certificates of deposit, time deposits, and other bank deposits which are fully insured by the Federal Deposit Insurance Corporation or similar federal agency or which are fully collateralized, money market funds, repurchase agreements, investment agreements with financial institutions, commercial paper, state or municipal bonds, and bankers' acceptances. IDAPP's Investment Policy, which applies to all investments, is more restrictive than the Act in that investments in money market mutual funds are restricted to those with portfolio holdings of United States obligations including bonds, notes, certificates of indebtedness, treasury bills or other securities, which are guaranteed by the full faith and credit of the United States of America as to principal and interest, and direct United States obligations (bonds, notes, debentures or other similar obligations of the United States of America or its agencies). As of year-end, IDAPP is in violation of its investment policy, which limits investments in money market mutual funds. IDAPP invests in the Federated Prime Cash Obligation Fund, which holds securities which are not guaranteed by the full faith and credit of the United States of America. In December 2010, IDAPP transferred these funds to the Federated Treasury Obligations Fund, causing them to become compliant with the investment policy.

B. Deposits – Custodial Credit Risk

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. State law (30 ILCS 230/26) requires that all deposits of public funds be covered by FDIC insurance or eligible collateral. IDAPP has no policy that would further limit the requirements under the law.

The State Treasury is the custodian of the State's cash and cash equivalents for IDAPP maintained in the State Treasury. IDAPP independently manages cash and cash equivalents maintained outside the State Treasury. Deposits in the custody of the State Treasurer totaled $1,465 at June 30, 2010. These deposits are pooled and invested with other State funds in accordance with the Deposit of State Moneys Act of the Illinois Compiled Statutes (15 ILCS 520/11). Funds held by the State Treasurer have not been addressed as to custodial credit risk because IDAPP does not own individual securities. Details on the nature of these deposits and investments are available within the State of Illinois' Comprehensive Annual Financial Report. As of June 30, 2010, IDAPP's locally held deposits were not exposed to custodial credit risk.

Note 3. Deposits and Investments (Continued)

C. Investments

Interest Rate Risk

IDAPP invests its funds in a manner that meets its cash flow needs while conforming to state statutes governing the investment of funds, including without limitation the Investment Act and all requirements/limitations of the various bond documents applicable to bonds and other securities issued by ISAC. The portfolio's maturity characteristics at June 30, 2010 are as follows:

Investment Type	Fair Value	Weighted Average Maturity (Years)
Corporate Securities	$ 41,400,374	2.2
Federal Agencies	159,352,023	3.3
Government Securities (U.S. Treasury Notes and Bonds)	28,684,058	5.3
Money Market Securities	25,170,215	0.1
Total	$ 254,606,670	
Portfolio weighted average maturity		3.0

Credit Risk

IDAPP's investment policy limits the following types of investments to the top two ratings issued by nationally recognized credit rating organizations: commercial paper, state or municipal bonds, and bankers' acceptances. The investment policy places no further limitations on investment credit quality.

As of June 30, 2010, IDAPP's investments were subject to credit risk (other than obligations of the U.S. Government or obligations explicitly guaranteed by the U.S. Government which are not considered to have credit risk) as follows:

		Rating	
Investment Type	Fair Value	Standard & Poor's	Moody's
Corporate Securities	$ 41,400,374	AAA	Aaa
Federal Agencies	159,352,023	AAA	Aaa
Money Market Securities	25,170,215	AAAm	Aaa

Note 3. Deposits and Investments (Continued)

C. Investments (Continued)

Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty, IDAPP will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party.

The Illinois Designated Account Purchase Program investments total $254,606,670 and are held by IDAPP's agent, but not in IDAPP's name.

The investment policy authorizes IDAPP to utilize a third party custodian (Trustee) to safe-keep the assets of the fund and to provide reports on a monthly basis to all necessary parties. The custodian is responsible for sweeping all interest and dividend payments and any other un-invested cash into a short-term government money market fund for re-deployment.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. IDAPP's investment policy requires IDAPP to diversify its investments by security type and institution. With the exception of the obligations set forth in the investment policy (direct federal obligations, federal guaranteed obligations, and federal affiliated institutions) or investments fully collateralized by these obligations, no more than 5% of IDAPP's total investment portfolio will be invested in the obligations of a single issuer.

As of June 30, 2010, the following investments (other than U.S. Treasury or securities explicitly guaranteed by the U.S. government) exceed 5% or more of IDAPP's total investment portfolio:

Issuer	Fair Value	Percentage of Portfolio
Federal Farm Credit Bank	$ 67,462,238	26.50%
Federal Home Loan Bank	51,114,699	20.08%
Federal Home Loan Mortgage Corporation	40,775,087	16.01%
Corporate Bonds	12,795,289	5.03%

Foreign Currency Risk

Foreign currency risk is the risk that changes in currency exchange rates will adversely affect the fair value of an investment. IDAPP's investment policy does not address foreign currency risk and IDAPP is not exposed to foreign currency risk.

Note 4. Notes Receivable

In previous years, IDAPP has made loans to institutions of higher education for the purpose of funding loans by such institutions to students or parents of students attending such institutions to finance the students' attendance at such institutions of higher education. In such case, the student loans made with the proceeds have been pledged by the borrowing institution to IDAPP to secure such institution's obligation to IDAPP. The institutions are contractually committed to selling such loans to IDAPP after the loans reach a certain aging status. The total amount of IDAPP's receivable outstanding with such educational lenders approximated $16,519,645 as of June 30, 2010. All such loans were purchased by IDAPP in early FY11. The breakdown between current and non-current Notes Receivable on the statement of net assets at June 30, 2010 is based upon an estimate of anticipated payments to be received in fiscal year 2011 and subsequent fiscal years.

Note 5. Student Loans Receivable

IDAPP's student loans receivable balance is comprised of two types of student loans: loans that are originated or purchased as part of the Federal Family Education Loan Program (FFELP) and loans that are originated as part of IDAPP's Alternative Loan Program. All FFELP loans originated or purchased by IDAPP prior to October 1, 1993 are guaranteed at 100% by Guarantors in accordance with the Higher Education Act. For loans disbursed between October 1, 1993 and prior to July 1, 2006 the loans are guaranteed at 98%. Loans disbursed after July 1, 2006 are guaranteed at 97%. All guaranteed loans are reinsured by the United States Department of Education (ED). Alternative Loans are not guaranteed by Guarantors and are not eligible for reinsurance by ED. Alternative Loans are credit-based and a provision for loan loss is set aside for the full amount of the loan when a loan becomes 120 days delinquent. The total amount of Alternative Loans outstanding was $312,100,669 at June 30, 2010.

ED has issued detailed loan servicing requirements, which, if not strictly adhered to, may result in the loss of the loan guaranty. The United States Department of Education has also issued specific guidelines to provide for the cure of such servicing deficiencies and the reinstatement of the guaranty. Management has identified loan-servicing deficiencies, which may result in loans that will not be reimbursed by the guarantor or collected from the student. Accordingly, management has established an allowance for possible loan losses totaling $9,994,014 as of June 30, 2010, which includes the amount collected from borrowers as an insurance fee for the Alternative Loans.

In addition, the net student loans receivable at June 30, 2010 of $1,107,530,191 includes $2,942,720 that IDAPP has classified as defaulted loans. These loans have been submitted to, but have not been reimbursed by, the guarantee agencies as of June 30, 2010.

For servicing contracts established with outside vendors, contractual provisions require the contractors to indemnify IDAPP for losses due to their negligence in loan servicing. Such recoveries will be recognized as income when received.

Included in the amount of student loans originated and purchased during fiscal year 2010 are premiums and other acquisition fees paid on the origination and purchase of certain student loans. These premiums and other acquisition fees are being amortized over the average life of the related loans. Premiums and other acquisition fees totaling less than $50,000 paid to a particular party during a fiscal year are expensed. Other acquisition fees typically represent lender fees and insurance fees and are also being amortized over the average life of the related loans.

Note 5. Student Loans Receivable (Continued)

Federal Student Loan Fund

During fiscal year 2010, IDAPP sold $79,105,989 of loans to the Department of Education (DOE) under the DOE's loan purchase (PUT) program. Reflected in the Statement of Revenues, Expenses, and Changes in Fund Net Assets is $2,268,314 of fees received from the DOE. The fee is comprised of $791,939 of lender fee reimbursement and $1,476,375 of purchase fees, calculated as $75 for each loan purchased.

ISAC's Federal Student Loan Programs maintain a fund that is on deposit with the State Treasurer, known as the Illinois Student Assistance Commission Federal Student Loan Fund. This fund is used to pay defaulted loan claims. Receipts for this fund include reinsurance receipts from the DOE.

The cash balance in this fund as of June 30, 2010 as reported by ISAC was $43,693,436. Restricted net assets, which includes $37,550,946 of claims in process, was $52,577,503. If the federal reinsurance percentage were temporarily reduced from 95% to either 85% or 75% (for loans disbursed after October 1, 1998) due to excessive default claims and if the State's pledge of full faith and credit were found to be ineffective, then the full collectibility of the non-federal reinsurance amount (i.e. 5% to 25%) of the IDAPP's net student loans receivable of $1,107,530,191 at June 30, 2010 is subject to the adequacy of the annual appropriation from the Illinois Student Assistance Commission Federal Student Loan Fund and the reserve funds of the other Guarantors to pay defaulted loan claims. However, based on past loan default experience, management believes that material losses will not be incurred.

Note 6. Federal Special Allowance and Interest Subsidy

The Federal government pays IDAPP or IDAPP owes the federal government an interest subsidy on certain student loans during the time that the student is enrolled in an eligible educational institution or qualifies for deferment status. The federal interest payable at June 30, 2010 was $2,820,002.

IDAPP is also eligible to receive special allowance payments from the federal government that are paid to adjust for the low yield on student loans in comparison to other investment sources. In addition IDAPP owes the federal government excess interest on the portfolio.

Federal Interest Benefits	$ 7,335,104
Special Allowance Payments	210,151
Excess Interest	(19,324,543)
Net Amount Paid to DOE	$ (11,779,288)

Note 7. Interfund Balances and Activity

Balances Due from/to Other Funds

The following balances at June 30, 2010 represent amounts due from other ISAC funds.

Fund	Amount	Description/Purpose
Federal Student Loan Fund	$ 6,876	Claim payments - collection of these funds are anticipated in fiscal year 2011.

The following balances at June 30, 2010 represent amounts due to other ISAC and State funds, and other State component units.

Fund	Amount	Description/Purpose
Other ISAC Funds:		
Student Loan Operating Fund	$ 3,921,674	Shared services
Other State Funds:		
Audit Fund	$ 5,041	Audit fees
Other State of Illinois Component Units:	$ 150,839	Student loan premiums

Note 8. Capital Assets

Capital asset activity for the year ended June 30, 2010 was as follows:

	Equipment	Accumulated Depreciation	Capital Assets, Net
Balance, July 1, 2009	$ 543,929	$ (510,038)	$ 33,891
Additions	-	(8,795)	(8,795)
Balance, June 30, 2010	$ 543,929	$ (518,833)	$ 25,096

Note 9. Long-Term Obligations Payable

A. Revenue Bonds Payable and Pledged Revenues

On July 29, 2002, ISAC adopted a general resolution and adopted supplemental resolutions on July 29, 2002, September 19, 2003, April 2, 2004, and June 24, 2005 authorizing the issuance of Student Loan Revenue Bonds, Series I and II, Series III, IV and V, Series VI and VII, and Series VIII and IX, respectively. All bonds are at a variable rate of interest. Any subsequent bonds issued under this resolution are issued on parity and the assets acquired and revenues generated under these bond issues serve as collateral for all of these issues.

The general resolution bonds are auction rate certificates and are taxable. The variable interest rate for the debt is reset every 28 days, based on the one-month LIBOR rate. Starting in August 2007, the bond markets experienced severe disruption. As a result, an auction held on February 13, 2008 for $70 million of bonds issued under the 2002 Resolution failed to attract enough bidders. All subsequent auctions also failed and continue to do so. A “failed auction” results in the bonds being priced at the “maximum auction rate” which, as defined in the Resolution, can be no more than the lesser of the rolling twelve-month 90 day U.S. Treasury rate plus 1.2% (for “AAA” rated bonds), 1.5% (for “A” rated bonds), 1.75% (for bonds rated below the lowest category of “A”) and one-month LIBOR plus 1.5%. The average maximum rate at June 30, 2010 was 1.85%. Auctions of bonds continue during this period with the difference between the maximum rate and that rate set by the market (should a rate be determined and should it be higher than the maximum rate), classified as “Carryover Interest.”

Carryover interest is payable under certain conditions as defined in the Resolution and its supporting documents. After analysis of these documents by legal counsel, management has concluded that it is improbable that these conditions will be met. As a result, management believes that the carryover interest will not become due and payable.

IDAPP has pledged future student loan revenues, net of specified operating expenses, to repay the outstanding $884.4 million (principal) in student loan revenue bonds as described above. Proceeds from the bonds provided financing for the student loans. The bonds are payable solely from principal and interest revenues under the related student loans and are payable through the final maturity of the bonds in 2045. Annual principal and interest payments on the bonds are expected to require approximately 97 percent of these student loan revenues. The total principal and interest remaining to be paid on the bonds is approximately $1.44 billion. Interest paid for the current year was approximately $7.9 million and total related student loan principal and interest received were approximately $54.7 million and $10.5 million, respectively.

On May 19, 2009, ISAC entered into a Bond Purchase Agreement with a group of underwriters to sell $50,000,000 Student Loan Revenue Bonds, Series 2009 (State Guaranteed). The bonds mature on May 1, 2014 and bear interest at the rate of 3.15% per annum. The interest on the bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, as amended. The proceeds of the bonds were used to (a) fund eligible loans to the extent permitted under the indenture, (b) fund, together with certain funds provided by ISAC, a debt service reserve fund and (c) pay bond issuance costs.

Note 9. Long-Term Obligations Payable (Continued)

A. Revenue Bonds Payable and Pledged Revenues (Continued)

On August 12, 2009 ISAC entered into a Bond Purchase Agreement with a group of Illinois Credit Unions to sell Taxable Student Loan Revenue Bonds (Series 2009A, Series 2009B, and Series 2009C). Funds from the bond sales were used to support FFELP student loans for the 2009/2010 school year. On August 12, 2009 ISAC sold the first in the series of bonds and received $44,175,000. The Series 2008B bonds were sold for $44,175,000 on December 15, 2009. The Series 2009C bonds were not sold due to a lack of demand. Interest on the bonds is set at “AA” Financial Commercial Paper Rate plus 80 basis points (1.24% at June 30, 2010). The principal of $88,350,000 and interest of $783,650 was paid-off on August 10, 2010.

IDAPP has pledged future student loan revenues, net of specified operating expenses, to repay the outstanding $138.3 million (principal) in student loan revenue bonds, series 2009 (all issues). Proceeds from the bonds provided financing for the student loans. The bonds are payable solely from principal and interest revenues under the related student loans and are payable through the final maturity of the bonds in 2014. Annual principal and interest payments on the bonds are expected to require approximately 95.9% percent of these student loan revenues. The total principal and interest remaining to be paid on the bonds is approximately $145.4 million. Interest paid for the current year was approximately $1.5 million and total related student loan principal and interest received were approximately $3.3 million and $.6 million, respectively.

B. Changes in Long-term Obligations Payable

Changes in long-term obligations payable for the year ended June 30, 2010 were as follows:

	Balance July 1, 2009	Additions	Deletions	Balance June 30, 2010	Amounts Due Within One Year
Compensated absences payable	$ 598,605	$ 230,394	$ (424,309)	$ 404,690	$ 185,410
Revenue bonds payable	1,030,500,000	88,350,000	(96,100,000)	1,022,750,000	88,350,000
Unamortized discounts	(3,200,220)	-	151,028	(3,049,192)	-
	$ 1,027,898,385	$ 88,580,394	$ (96,373,281)	$ 1,020,105,498	$ 88,535,410

Note 9. Long-Term Obligations Payable (Continued)

C. Future Maturities of Revenue Bonds Payable

IDAPP issues bonds to provide funds for student loan originations and purchases. IDAPP pledges the income derived from its assets to pay debt service. Annual debt service requirements to maturity for revenue bonds are as follows (amounts in thousands):

Year Ending June 30	Principal	Interest	Total
2011	$ 88,350	$ 18,702	$ 107,052
2012	-	17,919	17,919
2013	-	17,919	17,919
2014	50,000	17,919	67,919
2015	-	16,344	16,344
2016-2020	-	81,719	81,719
2021-2025	-	81,719	81,719
2026-2030	-	81,719	81,719
2031-2035	-	81,719	81,719
2036-2040	-	81,719	81,719
2041-2045	884,400	65,300	949,700
	1,022,750	$ 562,698	$ 1,585,448
Less:			
Unamortized bond discounts	(3,049)		
Net long-term principal outstanding	$ 1,019,701		

A majority of IDAPP’s outstanding revenue bonds are comprised of variable rate debt. As such, the interest figures shown above are calculated assuming the current interest rate of 1.85% on taxable auction rate debt. Actual interest paid in future years could be materially different.

Note 10. Mid-Term Credit Facility and Short Term Revolving Credit Line and Pledged Revenues

On July 27, 2007, ISAC entered into a Three-Year Asset Backed Revolving Credit Facility (the "Facility") in a maximum amount outstanding at any one time of $500,000,000 through an affiliate of Citibank (the "Lender") pursuant to which ISAC has borrowed funds for the purpose of purchasing certain student loans. Advances made under the Facility are secured by a portfolio of student loans, which loans were largely financed with proceeds of the advances (the "Collateral"). Amounts due under the Facility constitute limited obligations of ISAC, payable solely and only from the Collateral and the revenues derived therefrom. The costs of borrowing under the Program will not exceed Citibank's commercial paper rate. The rate at June 30, 2010 was .35375%. On July 27, 2010, the final maturity date under the Facility, approximately $355 million remaining outstanding under the Facility became due and payable. Due in part to conditions currently existing in the credit markets, ISAC has been unable to refinance this debt and is currently in payment default under the Facility. ISAC has reached an agreement with the Lender pursuant to which, subject to certain conditions, the Lenders will refrain from exercising their rights to require payment in full of amounts due under the Facility until July 27, 2011 or such later date as may be negotiated.

Under the terms of the agreement all revenues generated by the underlying student loan portfolio are transferred to a trust. The trust pays all expenses related to the debt service and student loan servicing costs (capped at 65 basis points of the outstanding average balance in the portfolio). During fiscal year 2010 there was $32,500,671 in principal and $9,613,723 in interest collected. The total amount transferred to the trust was $40,514,265. During the same period the trust paid $2,962,712 for interest expense and other professional fees and $2,988,248 for servicing fees.

On December 22, 2008 ISAC/IDAPP executed a $7,000,000 credit and security agreement with ShoreBank. The revolving credit line was used for the purchase or origination of student loans under the Capstone program established in 2007. The credit line currently has a 5% interest rate and matures on December 22, 2010. The agreement was amended on November 12, 2009 and the credit line was reduced to $4,717,675.

Changes in the revolving credit lines are as follows:

	Balance, July 1, 2009	Borrowings	Repayments	Balance, June 30, 2010	Amounts Due Within One Year
Citibank	$ 395,956,827	$ -	$ (40,500,000)	$ 355,456,827	$ 355,456,827
ShoreBank	2,990,109	1,727,566	-	4,717,675	4,717,675
Total	$ 398,946,936	$ 1,727,566	$ (40,500,000)	$ 360,174,502	$ 360,174,502

In addition, IDAPP believes that it is in breach of the Coverage Condition ratio for the Citibank revolving credit line. Since the Coverage condition cannot be satisfied within two business days, this would qualify as an Event of Termination under which Citibank would be eligible for remedies under the indenture. The agreement with the lender discussed in paragraph 1 and 2 above also extends to the breach of the coverage condition ratio.

As a result of the Citibank breach, the ShoreBank Credit and Security Agreement are considered to be in default. ShoreBank granted IDAPP a deferment of exercising its rights in connection with such default until July 31, 2010. On August 20, 2010 Shorebank was taken over by the FDIC. The Credit and Security Agreement was assigned to the new Urban Partnership Bank. The forbearance letter from Citibank was forwarded to ShoreBank for their credit committee consideration. An extension of the deferment was requested until the maturity of the credit line. As of March 14, 2011, IDAPP has not heard on the status of the deferment.

Note 11. Pension Plan

Substantially all of ISAC's full-time employees who are not eligible for participation in another state-sponsored retirement plan participate in the State Employees' Retirement System (SERS), which is a pension trust fund in the State of Illinois reporting entity. SERS is a single-employer defined benefit public employee retirement system (PERS) in which State employees participate, except those covered by the State Universities, Teachers', General Assembly, and Judges' Retirement Systems. The financial position and results of operations of SERS for fiscal year 2010 are included in the State of Illinois' Comprehensive Annual Financial Report (CAFR) for the year ended June 30, 2010. SERS issues a separate CAFR that may be obtained by writing to SERS, 2101 South Veterans Parkway, Springfield, Illinois, 62794-9255.

A summary of SERS benefit provisions, changes in benefit provisions, employee eligibility requirements including eligibility for vesting, and the authority under which benefit provisions are established are included as an integral part of SERS' CAFR. Also included is a discussion of employer and employee obligations to contribute and the authority under which those obligations are established.

IDAPP pays employer retirement contributions based upon an actuarially determined percentage of their payrolls. IDAPP's required and actual contributions for fiscal year 2010, 2009 and 2008 were $1,081,869, $828,291 and $1,058,674, respectively. For fiscal year 2010, 2009 and 2008, the employer contribution rate was 28.4%, 21.0% and 16.6%, respectively.

Note 12. Post-Employment Benefits

The State provides health, dental, vision, and life insurance benefits for retirees and their dependents in a program administered by the Department of Healthcare and Family Services along with the Department of Central Management Services. Substantially all State employees become eligible for post-employment benefits if they eventually become annuitants of one of the State sponsored pension plans. Health, dental, and vision benefits include basic benefits for annuitants and dependents under the State's self-insurance plan and insurance contracts currently in force. Annuitants may be required to contribute towards health, dental, and vision benefits with the amount based on factors such as date of retirement, years of credited service with the State, whether the annuitant is covered by Medicare, and whether the annuitant has chosen a managed health care plan. Annuitants who retired prior to January 1, 1998, and who are vested in the State Employees' Retirement System do not contribute towards health, dental, and vision benefits. For annuitants who retired on or after January 1, 1998, the annuitant's contribution amount is reduced five percent for each year of credited service with the State allowing those annuitants with twenty or more years of credited service to not have to contribute towards health, dental, and vision benefits. Annuitants also receive life insurance coverage equal to the annual salary of the last day of employment until age 60, at which time the benefit becomes $5,000.

The total cost of the State's portion of health, dental, vision, and life insurance benefits of all members, including post-employment health, dental, vision, and life insurance benefits, is recognized as an expenditure by the State in the Illinois Comprehensive Annual Financial Report. The State finances the costs on a pay-as-you-go basis.

Note 12. Post-Employment Benefits (Continued)

The total costs incurred for health, dental, vision, and life insurance benefits are not separated by department or component unit for annuitants and their dependents nor active employees and their dependents.

A summary of post-employment benefit provisions, changes in benefit provisions, employee eligibility requirements, including eligibility for vesting, and the authority under which benefit provisions are established are included as an integral part of the financial statements of the Department of Healthcare and Family Services. A copy of the financial statements of the Department of Healthcare and Family Services may be obtained by writing to the Department of Healthcare and Family Services, 201 South Grand Ave., Springfield, Illinois, 62763-3838.

Termination Benefits

During the fiscal year ended June 30, 2010, the Illinois Student Assistance Commission (ISAC) engaged in a workforce reduction, which resulted in the elimination of certain positions within the Illinois Designated Account Purchase Program (the Program). Applicable accounting standards require that a liability and expense for involuntary termination benefits (such as severance benefits) be recognized when a plan of termination has been approved by those with the authority to commit the government to the plan, the plan has been communicated to the employees and the amounts can be reasonably determined.

In relation to the workforce reduction, the Program has accrued approximately $137,000 in severance benefits, representing 60 days of salary continuation for 19 affected employees. This amount was paid to the employees subsequent to the year ended June 30, 2010 and is included with accounts payable and accrued expenses on the Statement of Net Assets.

Note 13. Risk Management

IDAPP, through the Commission, is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; workers compensation and natural disasters. The State retains the risk of loss (i.e., self insured) for these risks except for insurance purchased by the Commission for the building and EDP equipment. There has been no reduction in insurance coverage from coverage in the prior year. Settlement amounts have not exceeded coverage for the current or prior two fiscal years. The Commission's risk management activities for workers compensation are financed through appropriations to the Illinois Department of Central Management Services and are accounted for in the general fund of the State. The claims are not considered to be a liability of the Commission and, accordingly, have not been reported in the Commission's financial statements for the year ended June 30, 2010.

Note 14. Commitments and Contingencies

IDAPP has entered into a number of contracts with lenders, to act as IDAPP's agents and facilitate the purchase of Federal Family Education Loan Program (FFELP) student loans for IDAPP. This program ended during fiscal year 2009. IDAPP is committed to disbursing the funds for the FFELP loans purchased by these lenders. The total amount of loans purchased by IDAPP with all lenders in FY2010 was approximately $24.9 million. The remaining obligation under these purchase agreements is estimated to be approximately $16.5 million.

Note 15. New Governmental Accounting Standards

The Governmental Accounting Standards Board (GASB) has issued the following statements:

Statement No. 59, *Financial Instruments Omnibus*. The objective of this Statement is to update and improve existing standards regarding financial reporting and disclosure requirements of certain financial instruments and external investment pools. The Illinois Designated Account Purchase Program is required to implement the provisions of this Statement for the year ending June 30, 2011.

Statement No. 62 – *Codification of Accounting and Financial Reporting Guidance contained in pre-November 1989 FASB and AICPA Pronouncements*, was established to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in certain FASB and AICPA pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements. The Commission is required to implement this Statement for the year ending June 30, 2013.

Management has not yet completed its assessment of these Statements; however, they are not expected to have a material effect on the overall financial statement presentation.

Note 16. Subsequent Events

A. Department of Education Loan Purchase Program

The provisions of the 2009A, B & C Taxable Student Loan Revenue Bonds Indenture required IDAPP to sell the loans held under this Indenture to the Department of Education (DOE) pursuant to IDAPP's Master Loan Sale Agreement with the DOE. As a result of this agreement, IDAPP sold $46,136,717 of loans to the DOE. The proceeds of the Loan Purchase Program (PUT) and the existing cash in the Trust at the time of sale were used to pay-off the principal of $88,350,000 and interest of $783,650 on August 10, 2010.

B. Revenue Bond Refinancing

On October 27, 2010 ISAC issued $604,000,000 of Floating Rate Notes. The Notes were issued in three tranches with different maturities and interest rates. The tranches are $181,000,000 maturing April 25, 2017 with a rate of 3-Month LIBOR plus 0.48%, $269,000,000 maturing April 25, 2022 with a rate of 3-Month LIBOR plus 1.05% and $154,000,000 maturing July 25, 2045 with a rate of 3-Month LIBOR plus 0.90%. The proceeds of the Notes and the existing cash in the existing UBS trust were used to redeem principal amounts of $782,050,000 of the senior and $67,900,000 of the subordinate bonds, respectively, plus $269,302 of accrued interest (2002 Resolution Revenue Bonds). There are $34,450,000 of 2002 Resolution auction rate bonds that remain outstanding in the UBS trust, $32,350,000 senior bonds and $2,100,000 subordinate bonds.

State of Illinois
Illinois Student Assistance Commission
Illinois Designated Account Purchase Program

Schedule of Bonds Outstanding
June 30, 2010

A summary of bonds and notes outstanding at June 30, 2010 is presented as follows:

	Series 2002 I and Series 2002 II	Series 2003 III 2003 IV and 2003 V	Series 2004 VI and 2004 VII	Series 2005 VIII and 2005 IX	2009 Series A, B and C	Series 2009
Original amount	$ 250,000,000	$ 350,000,000	$ 250,000,000	$ 600,000,000	$ 88,350,000	$ 50,000,000
Principal retirements	(150,150,000)	(240,450,000)	(175,000,000)	-	-	-
Unamortized discount	(345,810)	(354,667)	(255,691)	(1,828,182)	-	(264,842)
Balance at June 30, 2010	$ 99,504,190	$ 109,195,333	$ 74,744,309	$ 598,171,818	$ 88,350,000	$ 49,735,158
Effective interest rate (1)	Variable	Variable	Variable	Variable	Variable	Fixed
Date of bonds	8/20/02	10/2/03	4/21/04	7/19/05 12/08/05	08/12/09 12/15/09	05/28/09
Interest dates	Varies	Varies	Varies	Varies	08/10/10	November 1 and May 1
Paying agents	Bank of New York New York, NY	Bank of New York New York, NY	Bank of New York New York, NY	Bank of New York New York, NY	Wells Fargo Chicago, IL	Wells Fargo Chicago, IL
Optional call feature beginning:	At issuance 100%	At issuance 100%	At issuance 100%	At issuance 100%		05/01/10 100%
Taxable/Tax-exempt	Taxable	Taxable	Taxable	Taxable	Taxable	Tax-exempt

	Total
Original amount	$ 1,588,350,000
Principal retirements	(565,600,000)
Unamortized discount	(3,049,192)
Balance at June 30, 2010	$ 1,019,700,808

<u>Debt outstanding per Statement of Net Assets</u>

Current portion of :	
Revenue bonds payable	$ 88,350,000
Long-term revenue bonds payable, net	931,350,808
Total debt outstanding	$ 1,019,700,808

(1) As of June 30, 2010 variable interest rates were 1.85% for taxable auction rate securities debt and 1.24% for the 2009 Series A and B bonds.

McGladrey

Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Honorable William G. Holland
Auditor General
State of Illinois, and

Mr. Donald J. McNeil
Honorable Chairman of the Governing Board
Illinois Student Assistance Commission

As Special Assistant Auditors for the Auditor General, we have audited the financial statements of the Illinois Designated Account Purchase Program of the State of Illinois, Illinois Student Assistance Commission (Commission), as of and for the year ended June 30, 2010 and have issued our report thereon dated March 14, 2011**.** 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

In planning and performing our audit, we considered the Commission's internal control over financial reporting of the Illinois Designated Account Purchase Program as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Commission's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Commission's internal control over financial reporting.

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 Commission's financial statements will not be prevented or detected and corrected on a timely basis.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in the internal control over financial reporting that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses as defined above. However, we identified certain deficiencies in internal control over financial reporting described in findings 10-2, 10-3, 10-4 and 10-5 in the accompanying schedule of findings that we consider to be significant deficiencies in internal control over financial reporting. A *significant deficiency* is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Commission'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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings as findings 10-4, 10-5 and 10-6.

The Commission's responses to the findings identified in our audit are described in the accompanying Schedule of Findings. We did not audit the Commission's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, Commission management, and the Commission Board and is not intended to be and should not be used by anyone other than these specified parties.

McGladrey & Pullen, LLP

Schaumburg, Illinois
March 14, 2011

Current Findings – *Government Auditing Standards*

(Note: Finding 10-1 is reported in the Illinois Student Assistance Commission – Illinois Prepaid Tuition Program financial audit. It is also reported in the Department-wide audit of the Illinois Student Assistance Commission.)

Finding 10-2 Financial Reporting Process

(Note: This finding is also reported in the Department-wide audit of the Illinois Student Assistance Commission)

The Illinois Student Assistance Commission (Illinois Designated Account Purchase Program) did not provide the auditors with complete and accurate financial statements on a timely basis. Also, the Illinois Designated Account Purchase Program (IDAPP) does not have sufficient control over financial reporting.

During the audit entrance conference on May 11, 2010, a deadline for submission of IDAPP's draft financial statements was determined and agreed to by the auditors and IDAPP management. The deadline for delivery of the complete draft financial statements to the auditors for fiscal year 2010 was October 1, 2010. An initial draft was provided to the auditors on September 30, 2010, which was incomplete and had not been fully reviewed by the Commission and all parties involved with the preparation and approval of the financial statements. Changes and adjustments to the initial draft occurred as late as November 15, 2010, 46 days after the agreed upon deadline, when several reclassifications and other changes were made affecting the financial statements and note disclosures.

Several errors and omissions were identified and corrected during the audit of the draft financial statements for IDAPP. Some of the more significant items were as follows:

- Transfers in and out were out of balance, requiring an adjusting entry in the amount of $750,000 to the general ledger. In accordance with fund accounting, transfers between funds and departments within the entity should net to zero.

- Severance accruals relating to benefits for terminated employees were not recorded in the draft financial statements. Upon review of the agency's severance policy, it was determined that an adjusting journal entry in the amount of $137,000 was needed to properly record severance accrual at the end of the fiscal year. In accordance with GASB Statement No. 47 *Accounting for Termination Benefits*, a liability and expense for involuntary termination benefits (for example, severance benefits) should be recognized when a plan of termination has been approved by those with the authority to commit the government to the plan, the plan has been communicated to the employees, and the amount can be estimated.

- Student loan premiums recorded in the general ledger did not agree to individual supporting schedules provided to the auditors, resulting in an adjusting entry of $265,000 to the general ledger accounts. In accordance with good internal control, all balance sheet accounts should be reconciled to subsidiary ledgers or other supporting information on a regular basis, including at year-end. Differences should be investigated and adjustments recorded as necessary.

- An adjustment to write off uncollectible amounts relating to notes receivable from an external service provider, in the amount of $683,000 was not made timely and required an adjustment at year-end. IDAPP was in violation of its policy requiring the Loan Accounting department to write-off uncollectible balances within 3 business days of receiving the completed and approved write-off form. (See finding 10-5)

Current Findings – *Government Auditing Standards (Continued)*

Finding 10-2 Financial Reporting Process (Continued)

- Weighted average maturities (WAM) of investments were calculated incorrectly. As a result, the related interest rate risk disclosure schedule was inaccurate for three of the four types of securities reported. In accordance with good internal control, each schedule on the financial statement should be reviewed and reconciled to underlying supporting information. Differences should be investigated and corrections made prior to providing financial statements to auditors.

- Pledged revenue disclosures were not reported for the 2009 series debt issuances in the draft financial statements. In accordance with GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues* "For each period in which the secured debt remains outstanding, pledging governments should disclose, in the notes to financial statements, information about specific revenues pledged." The most significant items that should be reported include the approximate amount of the pledge, the specific revenues that are pledged, the term of the commitment, pledged revenues during the reporting period compared to the principal and interest requirements for the same period and the approximate portion of the specific revenue stream that has been pledged.

The Fiscal Control and Internal Auditing Act, 30 ILCS 10/3001 requires all State agencies to establish and maintain a system, or systems, of internal fiscal and administrative controls, which shall provide assurance that revenues, expenditures, and transfers of assets, resources, or funds applicable to operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the State's resources.

According to IDAPP management, changes subsequent to the initial delivery of the draft financial statements were the result of the ongoing review of the financials by the Commission and the Illinois Office of the Comptroller. The Commission made all efforts and was in constant communication with the Illinois Office of the Comptroller and the auditors prior to the end of the fiscal year to ensure that the year-end process was timely and accurate.

Submitting incomplete and inaccurate draft financial statements delays completion of the audit process and the timely release of IDAPP's and the Commission's financial reports to users. Also, insufficient and/or ineffective controls over financial reporting could lead to significant reporting inaccuracies in the financial statements and notes to the financial statements. (Finding Nos. 10-2, 09-3, 08-5)

Recommendation

We recommend the Commission improve controls over financial reporting to ensure accurate presentation and disclosure of IDAPP's annual financial statements. The Commission should take a comprehensive look at the entire financial reporting process and make changes needed to timely release financial reports to users and to auditors.

Commission Response

We accept the recommendation.

IDAPP is reviewing all of its policies and procedures regarding the close process and the preparation of the financial statements. Quality control checks will be put in place to ensure the submission of accurate financial statements.

Current Findings – *Government Auditing Standards (Continued)*

Finding 10-3 Student Loan Payments Not Processed Correctly

(Note: This finding is also reported in the Department-wide audit of the Illinois Student Assistance Commission)

The Illinois Student Assistance Commission (Illinois Designated Account Purchase Program) did not properly apply student loan payments to principal and interest.

The Illinois Designated Account Purchase Program (IDAPP) utilizes several external service organizations to manage and monitor its student loan portfolio. During our testing of student loan payments, we noted that for four out of twelve (33%) payments sampled for one of the service organizations, there were errors in the application of the payments between principal and interest.

IDAPP management acknowledged it was aware of a system problem relating to the processing of payments at this service provider. Subsequent to IDAPP's fiscal year ended June 30, 2010, the service provider performed a retrospective calculation for each loan possibly affected by this situation. In addition, IDAPP has hired an independent third party entity to review this retrospective calculation for propriety. Based on the review performed by the service provider, misapplied payments as of June 30, 2010 totaled approximately $291,000, resulting in an understatement of IDAPP's student loan receivable balance by the same amount. This amount was deemed immaterial and was not recorded at year end.

The Fiscal Control and Internal Auditing Act, 30 ILCS 10/3001 requires all State agencies to establish and maintain a system, or systems, of internal fiscal and administrative controls, which shall provide assurance that revenues, expenditures, and transfers of assets, resources, or funds applicable to operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the State's resources. A good internal control environment includes checks and balances to ensure accounting transactions are recorded accurately. This extends to those transactions processed by third parties such as service organizations.

According to IDAPP management, this situation occurred due to the way the computer program used by the service organization handled forbearances, deferments and the related capitalized interest.

The service provider in question manages approximately $312 million of IDAPP's student loan portfolio as of June 30, 2010. This represents 28% of the student loan receivable balance of $1,107 million at fiscal year end 2010. Misapplication of student loan payments between interest and principal could result in IDAPP's student loan receivable and operating revenue being misstated. Additionally, misapplication of payments could lead to certain borrowers "paying off their loan" when a balance actually remains, or over-paying the remaining loan balance. Although individual payments misapplied during the year ended June 30, 2010 appear to be insignificant, these amounts can accumulate throughout the years to a more significant amount. (Finding Code No. 10-3)

Recommendation

We recommend IDAPP management closely monitor each service organization used to manage its student loan portfolio. Reviews of the service organization's processes and controls should be performed on a periodic basis. This should include a review of the service organization's "Report on controls placed in operation and tests of operating effectiveness", prepared and issued by independent auditors, in accordance with the Statement on Auditing Standards No. 70. Any noted variances in application of borrower repayments should be investigated and corrected in a timely manner.

Current Findings – *Government Auditing Standards (Continued)*

Finding 10-3 Student Loan Payments Not Processed Correctly (Continued)

Commission Response

We accept the recommendation.

The Commission was aware of the system problem relating to the processing of payments at this service provider. Commission believes that these adjustments to borrower balances are insignificant and immaterial. The Commission has hired an independent consultant and is working with the service provider to ensure the integrity of the borrower balances. Any questions raised by borrowers regarding their balance are investigated and corrected in a timely basis.

Please also note that IDAPP has a process where it reviews the SAS 70 reports of all the outside service providers and follows up on any findings that are deemed material weaknesses. The service provider's report for the period of July 1, 2009 through August 15, 2010 was reviewed by IDAPP and IT management in September 2010 with no material weaknesses noted.

Current Findings – *Government Auditing Standards (Continued)*

Finding 10-4 Noncompliance with Investment Policy

(Note: This finding is also reported in the Department-wide audit of the Illinois Student Assistance Commission)

The Illinois Student Assistance Commission (Illinois Designated Account Purchase Program) invested in a money market mutual fund with holdings in securities not permitted by its investment policy.

As of June 30, 2010, the Illinois Designated Account Purchase Program (IDAPP) had invested $13.4 million in a Fund, which invests in corporate debt securities that were not guaranteed by the full faith and credit of the United States of America as required by the investment policy. This investment was approximately 5% of IDAPP's total investment balance as of the fiscal year end 2010.

Section 5.5 of IDAPP's current investment policy only allows investments in money market mutual funds with portfolio holdings of United States obligations including bonds, notes, certificates of indebtedness, treasury bills or other securities, which are guaranteed by the full faith and credit of the United States of America as to principal and interest, and direct United States obligations (bonds, notes, debentures or other similar obligations of the United States of America or its agencies).

The Fiscal Control and Internal Auditing Act, 30 ILCS 10/3001 requires all State agencies to establish and maintain a system, or systems, of internal fiscal and administrative controls, which shall provide assurance that funds held outside the State Treasury are managed, used and obtained in strict accordance with the terms of their enabling authorities and that no unauthorized funds exist. Good internal controls include checks and balances to ensure policies established by the Board are followed and adhered to.

According to IDAPP management, the Series 2002, 2003, 2004 and 2005 Bond Indenture which guides permitted investments of the related Bond Indenture Trust allow that investments may be made in money market funds rated Aa2 or higher by Moody's and, if rated by Fitch, rated AA- or higher, provided, however, that such rating, if any, shall be AA/F1+ or higher for any money market fund which has the ability to maintain a stable one-dollar net asset value per share and whose shares are freely transferable on a daily basis. IDAPP management was following the guidelines of allowable investments specified in the bond documents, but not the current IDAPP investment policy.

This money market mutual fund invests in non-governmental securities which are more volatile than United States obligations and direct United States obligations. By investing in the money market mutual fund, IDAPP has failed to comply with its investment policy and has exposed its investments to a higher risk of loss than agreed to by its Board. (Finding Code No.10-4)

Recommendation

We recommend IDAPP improve controls over investments to ensure that it is in compliance with its investment policies. Further IDAPP should reinvest the money invested in the money market fund in violation of its investment policy to an allowable investment vehicle.

Current Findings – *Government Auditing Standards (Continued)*

Finding 10-4 Noncompliance with Investment Policy (Continued)

Commission Response

We accept the recommendation.

The non-compliant investment was sold and the funds moved into a compliant investment on December 16, 2010.

The investment was first purchased in March 2009 and was compliant with the investment policy. Over the course of the year, the fund shifted its investments to some non-governmental securities.

The investments held by the various trusts will be reviewed by the investment committee on a quarterly basis to assure compliance with the investment policy. Investments not in compliance will be sold and the funds moved into other investments.

Current Findings – *Government Auditing Standards (Continued)*

Finding 10-5 Noncompliance with Write-Off Policy

(Note: This finding is also reported in the Department-wide audit of the Illinois Student Assistance Commission)

The Illinois Student Assistance Commission (Illinois Designated Account Purchase Program) was not in compliance with its non-cash write-off policy regarding the student loan receivable balances.

During our analysis of the Illinois Designated Account Purchase Program's (IDAPP) student loan receivable balance, we noted that IDAPP's current write-off policy requires the Operations Director and the Director of Accounting and Operations to review and approve write-offs on IDAPP owned alternative student loan balances. Alternative student loans are credit-based loans originated by IDAPP that are not guaranteed by the Federal Family Education Loan Program. We noted that one out of the six selections reviewed (17%) did not contain proper approval. In addition, IDAPP is in violation of its current write-off policy requiring the Loan Accounting department to write-off the balance within 3 business days of receiving the completed and approved write-off form. Four out of the six selections (67%) were not written-off within 3 business days, as required by the policy. They were written off in timeframes ranging from 10 and 45 days.

The Fiscal Control and Internal Auditing Act, 30 ILCS 10/3001 requires all State agencies to establish and maintain a system, or systems, of internal fiscal and administrative controls, which shall provide assurance that revenues, expenditures, and transfers of assets, resources, or funds applicable to operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the State's resources. Good internal controls include checks and balances to ensure policies established by management are followed.

According to IDAPP management, the write-offs processed without approval were an error. Timeliness of the write-offs was the result of reductions in the workforce occurring within IDAPP and changes in IDAPP's management structure.

Without proper approval for the write-off of IDAPP's student loans receivables, loans may be written off in error when collection of receivable amounts may still be viable. Unauthorized write-offs of student loans increases the risk of fraud. In addition, not posting the write-off within the reasonable time period of 3 days could result in interest being inaccurately accrued on outstanding balances. Although individual write-off amounts were immaterial (an average of $250), these amounts could accumulate throughout the year to a more significant amount. (Finding Code No. 10-5)

Recommendation

We recommend that IDAPP improve its controls to ensure that IDAPP accounting staff complies with current policy and procedures in place regarding the authorization and timing of the write-offs of student loan receivables.

Current Findings – *Government Auditing Standards (Continued)*

Finding 10-5 Noncompliance with Write-Off Policy (Continued)

Commission Response

We accept the recommendation.

IDAPP is reviewing all of its policies and procedures regarding the write-off of student loans. The policies and procedures will take into account the outsourcing of the loan servicing operations and the current number of employees.

Current Findings – *Government Auditing Standards (Continued)*

Finding 10-6 Debt Covenant Violation

(Note: This finding is also reported in the Department-wide audit of the Illinois Student Assistance Commission)

The Illinois Student Assistance Commission (Illinois Designated Account Purchase Program) was not in compliance with one of the covenants relating to the agency's revolving line of credit agreement.

During the audit of the agency's June 30, 2009 financial statements, the Illinois Designated Account Purchase Program (IDAPP) management brought to our attention that they had violated one of the covenants relating to the agency's revolving credit line (loan) agreement with a bank. The non-compliance pertained to the "Coverage condition ratio" covenant. According to the line of credit agreement with the bank, the "Forbearance Excess Amount", defined as the aggregate value of all eligible student loans that are subject to forbearance, is to be used in the calculation of the coverage condition ratio covenant. When IDAPP completed the report, created by the bank, and as instructed by the bank, the report produced an inaccurate calculation of the amount for the loans in forbearance. Once the error was discovered and the Coverage condition ratio was recalculated, it resulted in a lack of compliance with the Coverage condition ratio by IDAPP.

During our audit of the agency's June 30, 2010 financial statements, we noted that IDAPP continued to be in violation of the same covenant noted above. However, we noted that IDAPP had improved internal controls related to reporting requirements of the various indentures. IDAPP has a master checklist that incorporates all reporting requirements of the various indentures. The checklist is monitored and maintained on a monthly basis. All of the reporting requirements are reviewed and signed-off by management.

As a result of the violation, the bank has certain remedies available to it under the terms of the loan agreement, principal of which would be rights to call the loan and take possession of the collateral (the underlying student loan portfolio). The bank has been made aware of the event of default and has not communicated to IDAPP any intent to exercise the remedies available to it under the terms of the loan agreement. Management believes the bank would have little incentive to call the line of credit and begin servicing the student loans itself, particularly because IDAPP has made all of its required payments in a timely fashion. The balance of the line of credit with the bank was $355,456,827 at June 30, 2010. According to ISAC management, the bank has agreed to refrain from exercising their rights under the Agreement until July 27, 2011.

The debt covenant violation with the bank also triggered a default in one of the covenants in the loan agreement with another bank. This bank granted IDAPP a deferment from exercising its rights in connection with such default until July 31, 2010. Shortly thereafter, the bank was taken over by the FDIC. Since that time, IDAPP has been pursuing an agreement with the new institution for an extension on the July 31, 2010 deferment date. This issue has not yet been resolved. The balance in the line of credit with this bank was $4,717,675 at June 30, 2010.

According to IDAPP management, the cause of the Coverage Condition breach was due to the level of forbearances exceeding the limit. This was due to the policy of treating student borrowers who had both loans guaranteed by the Federal Family Education Loan Program (FFELP) and other loans not guaranteed by FFELP as if all its loans were guaranteed by FFELP.

Current Findings – *Government Auditing Standards (Continued)*

Finding 10-6 Debt Covenant Violation (Continued)

Failure to comply with debt covenants could result in the debt becoming due and payable in advance of scheduled retirement dates. As a result of the violation, both banks may have certain remedies under the terms of the loan agreements, principal of which would be the right to call the loans and take possession of the collateral (the underlying student loan portfolio of IDAPP). (Finding Code Nos. 10-6, 09-1)

Recommendation

We recommend that IDAPP continue to monitor these loan covenant violations and continue seeking remedies from the lenders involved.

Commission Response

We accept the recommendation.

IDAPP will continue to monitor these loan covenants. Commission management has been in constant communication with both parties and is working with them to resolve the violations and to refinance the facilities.

Prior Finding Not Repeated

A. Unapplied Cash

(Note: This prior finding not repeated is also reported in the Department-wide audit of the Illinois Student Assistance Commission.)

During our fiscal year 2009 audit, we noted the Illinois Designated Account Purchase Program (IDAPP) did not apply cash collections (student loan payments) in a timely manner. (Finding Code No. 09-2)

During our fiscal year 2010 audit, our sample testing indicated that all remittances are being processed timely by the applicable service organizations.