

2007-2008  
ANNUAL REPORT



MONTANA HIGHER EDUCATION  
STUDENT ASSISTANCE CORPORATION

# LETTER FROM THE CHAIR

"Adversity  
has the effect  
of eliciting  
talents, which  
in prosperous  
circumstances  
would have  
lain dormant."

- Horace

The Montana Higher Education Student Assistance Corporation (MHESAC) certainly encountered its share of adversity this year as the student loan industry struggled to meet the challenges put to it by Congress and the turbulent financial markets.

But I'm proud to say that MHESAC — with its noble mission of ensuring Montana students' access to federal student loans and lowering the cost of financing postsecondary education — confronted the obstacles with a staunch determination that can only be classified as courageous.

In a year in which student loan companies were fighting for their very existence, MHESAC forged ahead to complete a \$175 million bond financing that will provide Montana students with the funds to pay for higher education in academic year 2008-2009.

In addition, MHESAC collaborated with schools, lender partners and elected officials to ensure access to Federal Family Education Loan (FFEL) program loans for Montana families within the new parameters defined by Congress and despite the turmoil in the marketplace.

It's this commitment to Montana families that has compelled MHESAC to provide more than \$2.4 billion in capital for Montana student loans over the past 25 years and help more than 150,000 Montana students attain postsecondary education.

In addition, MHESAC has supplied more than \$38 million in borrower benefits (interest rate and principal reductions and borrower fees) and is committed to furnish more than \$11 million to fund existing Montana rebate programs in the future.

MHESAC believes in the potential of Montana students and is willing to work diligently — through whatever adversity arises — to ensure students have the opportunity to develop it fully.

Montana students' success is MHESAC's success.

*Fred Flanders*

Fred Flanders, Board Chairman  
Montana Higher Education Student Assistance Corporation

# MHESAC: AN OVERVIEW

Fiscal year 2007-2008 was a challenging one for the Montana Higher Education Student Assistance Corporation (MHESAC), but Montana families and students continued to benefit from MHESAC's dedication to providing access to federal student loans.

In a year of flux for the student loan industry, MHESAC managed to increase its number of Montana and non-Montana borrowers from 96,836 in 2007 to 107,595. Along with that rise in the number of borrowers came corresponding growth in outstanding principal in student loans in MHESAC's portfolio from \$1.39 billion in 2007 to \$1.48 billion.

As an extension of that growth activity, MHESAC's loan acquisitions and originations totaled \$231 million and the issuance of annual financings necessary for the loan acquisitions totaled \$175 million.

MHESAC also provided its Montana lending partners with more than \$123 million in capital for low-cost Federal Stafford and PLUS education loans.

As such, MHESAC's business activities continued to parallel its mission of lowering the cost of repaying student loans for Montana borrowers by reducing interest rates, providing principal reductions and eliminating up-front costs. In Fiscal Year 2008, MHESAC delivered more than \$4.3 million in such borrower benefits, after having delivered \$5.6 million the previous year.

Since 1995, more than \$38.5 million in borrower benefits have been delivered to Montana students.

# MHESAC COMPLETES \$175 MILLION BOND FINANCING

The Montana Higher Education Student Assistance Corporation (MHESAC) was one of only a few student loan companies to successfully complete a tax-exempt bond financing in the last quarter of 2007.

As a result, \$175 million is available to Montana students to fund student loans for academic year 2008-2009.

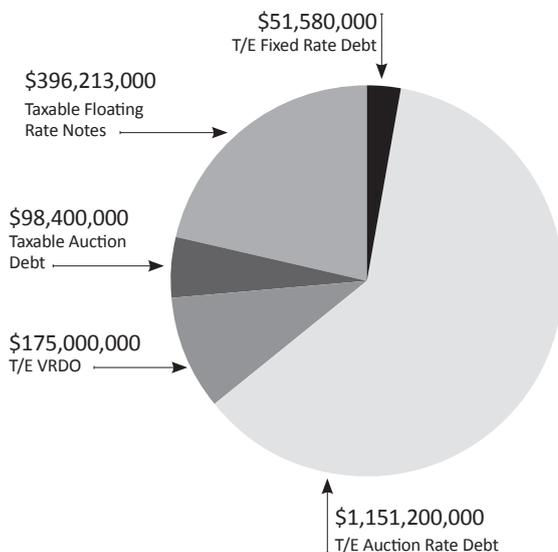
“Thanks to this successful financing, MHESAC is able to continue its outstanding tradition of service to Montana students in a year in which the availability of funds is tenuous throughout the student loan industry,” said Jim Stipcich, president/chief executive officer of MHESAC’s business manager, Student Assistance Foundation (SAF).

The funds involved in the financing included \$100 million of 2007 volume cap approved by the state of Montana and \$75 million of carry-forward allocation from the 2006 volume cap.

For this financing, MHESAC elected to use a different kind of financing — variable rate demand obligations (VRDOs). This form of financing bears interest at a variable rate which is adjusted at specified intervals and can be redeemed at the bondholder’s option when the rate changes under a liquidity agreement that supports the VRDO’s.

Jolene Selby, SAF’s chief financial officer, explained that the management team selected the VRDOs for the financing based on the corporation’s desire to diversify MHESAC’s debt mix.

Total Debt Outstanding by Debt Type



# PRUDENT BUSINESS CHOICES HELP MHESAC WEATHER AUCTION MARKET CRASH

Thanks to prudent business practices on the part of the Montana Higher Education Student Assistance Corporation (MHESAC), it was able to minimize losses associated with the auction market crash that affected student loan companies across the country.

“Fortunately, MHESAC had reserves to rely upon to help it weather such a storm,” said Jim Stipcich, president/CEO of MHESAC’s business manager, Student Assistance Foundation (SAF). “MHESAC was able to use \$14.7 million from its Fiscal Year 2008 student loan earnings and \$5 million from prior earnings to help cover the costs associated with the auction market disruption.”

As a result, MHESAC experienced a loss of \$8 million, but emerged from Fiscal Year 2008 with a \$30 million fund balance for the future.

The auction rate market had been functioning smoothly for almost two decades and was the accepted funding vehicle for bonds such as those issued by MHESAC and other student loan companies, according to Jolene Selby, chief financial officer for Student Assistance Foundation.

“The auction rate market is a \$330 billion market that was used extensively by student loan companies, tax-exempt institutions, municipalities and other such organizations,” Selby said. “It was a popular market for investors because they were, in theory, short-term investments with respectable yields.”

Bloomberg.com explained in a March 2008 article that investors began to shun the auction rate securities out of fear that the bond insurers’ AAA ratings were in jeopardy as a result of trickle-down from the subprime crisis. At the same time, banks that ran the bidding to set yields on the debt refused to buy unwanted securities — this drove borrower costs higher.

“As a result, the bond issuer — MHESAC — had to pay interest at the fail rate and this is where we really began to feel the effects of the market instability,” Selby said. “Average rates on tax-exempt bonds climbed to almost 7 percent compared with the norm of 4 percent or lower.”

While stability has not yet returned to the auction rate market, the rates on tax-exempt bonds had dropped and had at least stabilized by the end of FY 2007-2008.

“By the end of the fiscal year, MHESAC was operating with a positive cash flow position,” Selby said. “We continue to explore options to successfully restructure these bonds.”

# FINANCIAL MARKETS/NEW LEGISLATION TRANSFORM LANDSCAPE OF STUDENT LOAN INDUSTRY

Turmoil in the financial markets and new legislation changed the way that student loans were delivered in FY 2007-2008, but concerned parties, including the Montana Higher Education Student Assistance Corporation (MHESAC) continued to work together to ensure the delivery of federal student loans in Montana and across the country.

The climate in the student loan industry began to change in October 2007 following the passage of the federal College Cost Reduction and Access Act. The intent of the act was to decrease college costs for students, increase federal programs directed toward improving access to college and to implement school and lender regulations directed toward ensuring that students have more choice in selecting student loans.

“This action by Congress provided some very real benefits for students,” said Jim Stipcich, president/CEO of MHESAC’s business manager, Student Assistance Foundation. “Those ranged from greater availability of funds through federal programs such as Pell Grants, to the adoption of codes of conduct by lenders across the nation.”

However, the act also required significant increases in loan fees and decreases in returns to lenders in the Federal Family Education Loan (FFEL) program totaling \$20 billion in order to pay for the changes. As a result, student loan companies were prompted to evaluate all of their student loan products and the profitability associated with them.

Major disruption in the real estate mortgage market and other areas compounded the problem as its effects rippled to other segments of the financial markets, including student loans.

In order to make sure the changes in the industry didn’t limit the availability of student loans, Congress passed emergency legislation — the Ensuring Continued Access to Student Loans Act (HR 5715) — in May. The legislation provided the Department of Education (DOE) and the U.S. Treasury with the authority to enhance access to federal loans for students. The legislation created loan purchase and loan participation programs designed to provide additional liquidity in the market and to encourage lenders to stay in the FFEL program for another year.

“The recent changes in the industry have required MHESAC to scale back the borrower benefits it can offer to borrowers and some of its services, such as student loan consolidation,” said Stipcich. “However, students can be confident that Montana’s Choice student loans are still available and they can rely on the superior customer service they have always received from MHESAC’s lender partners and from SAF’s capable employees.”

MONTANA HIGHER EDUCATION  
STUDENT ASSISTANCE CORPORATION  
CONDENSED BALANCE SHEET

June 30, 2008 and comparative totals for 2007

(expressed in thousands)

<b>ASSETS</b>	<b>2008</b>	2007
CURRENT ASSETS	<b>3,059</b>	5,254
RESTRICTED ASSETS	<b>1,899,263</b>	1,846,516
OTHER ASSETS	<b>21,428</b>	5,230
TOTAL ASSETS	<b>\$ 1,923,750</b>	\$ 1,867,000

**LIABILITIES AND NET FUND ASSETS**

CURRENT LIABILITIES	<b>49,426</b>	39,138
LONG-TERM DEBT	<b>1,830,662</b>	1,772,416
OTHER LIABILITIES	<b>13,471</b>	17,009
TOTAL LIABILITIES	<b>1,893,559</b>	1,828,563
FUND NET ASSETS	<b>30,191</b>	38,437
	<b>\$ 1,923,750</b>	\$ 1,867,000

MONTANA HIGHER EDUCATION  
STUDENT ASSISTANCE CORPORATION  
STATEMENTS OF REVENUE, EXPENSE AND  
CHANGES IN FUND NET ASSETS

Year ended June 30, 2008 and comparative totals for 2007

(expressed in thousands)

	<b>2008</b>	2007
TOTAL OPERATING REVENUE	<b>\$113,287</b>	\$128,444
TOTAL OPERATING EXPENSE	<b>124,643</b>	113,710
OPERATING INCOME (LOSS)	<b>(11,356)</b>	14,734
NONOPERATING REVENUES (EXPENSES)	<b>3,110</b>	858
INCREASE (DECREASE) IN NET ASSETS	<b>(8,246)</b>	15,592
FUND NET ASSETS, BEGINNING OF YEAR	<b>38,437</b>	22,845
FUND NET ASSETS, END OF YEAR	<b>\$30,191</b>	\$38,437

MHESAC BOARD  
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HELENA

ROYAL JOHNSON,  
VICE CHAIR  
BILLINGS

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BOZEMAN

KERRA MELVIN,  
STUDENT REGENT  
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MARK SEMMENS  
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JUDY CHAPMAN,  
SECRETARY  
BILLINGS

BRUCE MARKS,  
TREASURER  
HELENA

# SINCE 1983, MHESAC HAS HELPED MORE THAN 150,000 MONTANA STUDENTS BY:

PROVIDING more than \$2.4 billion in capital to fund federal student loans.

GIVING \$38 million in borrower benefits in the form of interest and principal reductions and rebates.

COMMITTING more than \$11 million to fund future Montana rebate programs.

BELIEVING in their dreams of building a better future through higher education!

MONTANA HIGHER EDUCATION STUDENT ASSISTANCE CORPORATION (MHESAC) IS A MONTANA PRIVATE, NONPROFIT CORPORATION ORGANIZED UNDER SECTION 150(d) OF THE U.S. TAX CODE TO PROVIDE MONTANA CITIZENS WITH FINANCIAL ACCESS TO HIGHER EDUCATION.



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

For general information  
call MHESAC's business manager,  
Student Assistance Foundation:  
(406) 495-7800

For loan-related questions call:  
(800) 852-2761

For lender services call:  
(800) 223-2914

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