McGladrey & Pullen
Certified Public Accountants

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

Financial Statements
For the Year Ended June 30, 2008

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

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

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Agency Officials

Executive Director	Andrew Davis
Chief Financial Officer	John Sinsheimer
Director	Steve Di Benedetto
Director, Accounting and Finance (06/01/08 – Current)	Frank Berauer
Director, Financial Management and Control (07/1/07 – 7/23/07)	Wendy Funk

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 - *Government Auditing Standards* on pages 29-33 of this report, as finding 08-2, (Draft Financial Statements Not Accurate), finding 08-3 (Investment Policies Not Followed) and finding 08-4, (Documentation of Journal Entry Approval is Lacking). The auditors also consider findings 08-2 and 08-3 to be material weaknesses.

Exit Conference

The findings and recommendations appearing in this report were discussed with IDAPP personnel at an exit conference on February 4, 2009. Attending were:

Illinois Student Assistance Commission	
Frank Berauer	IDAPP Director, Accounting and Finance
Anne Hunter	Financial Reporting Manager
John Sinsheimer	Chief Financial Officer
Shoba Nandhan	ISAC Director, Budget and Finance
McGladrey & Pullen, LLP	
Linda Abernethy	Partner
Rolake Adedara	Manager
Office of the Auditor General	
Jon Fox	Audit Manager

The responses to the recommendations were provided by Shoba Nandhan in a letter dated February 17, 2009.

McGladrey & Pullen
Certified Public Accountants

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, 2008, 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 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 Student Assistance Commission as of June 30, 2008, 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, 2008, 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 27, 2009 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 other schedules, listed in the table of contents as supplemental information, are presented for purposes of additional analysis and are 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 27, 2009

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

Statement of Net Assets
June 30, 2008

Assets

Current assets - unrestricted	
Cash and cash equivalents	$ 6,047,941
Investments	59,724
Total current assets - unrestricted	6,107,665
Current assets - restricted	
Cash and cash equivalents	58,203,673
Notes receivable	51,585,280
Accounts receivable	
Student loans	202,683,247
Accrued interest - loans and notes	26,564,482
Federal special allowance and interest subsidy	1,785,701
Other receivables	1,587,344
Due from other funds	1,148,660
Unamortized bond issuance cost	23,621
Total current assets - restricted	343,582,008
Noncurrent assets - unrestricted	
Depreciated capital assets, net	17,311
Other assets	2,806
Total noncurrent assets - unrestricted	20,117
Noncurrent assets - restricted	
Notes receivable	42,206,138
Accounts receivable	
Student loans, net of allowance for loan losses of $6,968,059	932,355,277
Unamortized bond issuance costs	840,763
Total noncurrent assets - restricted	975,402,178
Total assets	1,325,111,968

(Continued)

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

Statement of Net Assets (Continued)
June 30, 2008

Liabilities

Current liabilities		
Accounts payable and accrued expenses	$	1,503,955
Accrued interest payable		1,466,652
Due to other funds		1,017
Compensated absences		61,061
Revolving credit line		390,770,062
Total current liabilities		393,802,747
Noncurrent liabilities		
Compensated absences		549,550
Revenue bonds payable, net		879,440,702
Total noncurrent liabilities		879,990,252
Total liabilities		1,273,792,999

Net Assets

Invested in capital assets		17,311
Restricted		47,306,770
Unrestricted		3,994,888
Total net assets	$	51,318,969

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, 2008

Operating revenues	
Investment income	
Interest - student loans	$ 70,770,105
Interest - investments	4,142,470
Total operating revenues	74,912,575
Operating expenses	
Interest and other student loan expenses	
Interest expense	
Student loan revenue bonds	70,675,086
Amortization of loan premiums and fees	3,402,513
Other student loan fees	3,716,851
Other operating expenses	
Salaries and employee benefits	9,691,250
External loan servicing	5,991,754
Line of credit fees	22,784
Occupancy	261,323
Marketing expenses	1,073,476
Management and professional services	5,118,932
Depreciation	26,626
Other	1,193,779
Total operating expenses	101,174,374
Operating loss	(26,261,799)
Nonoperating revenues	
Federal special allowance and interest subsidy	20,828,750
Loss before special item and transfers	(5,433,049)
Special Item (Note 16)	(10,854,924)
Transfers in	681,635
Transfers out	(2,500,000)
Change in net assets	(18,106,338)
Net assets, July 1, 2007	69,425,307
Net assets, June 30, 2008	$ 51,318,969

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, 2008

Cash flows from operating activities	
Cash payments to suppliers for goods and services	$ (19,383,050)
Cash payments to employees for services	(9,801,690)
Cash receipts from other operating activities (student loans)	201,410,216
Cash payments for other operating activities (student loans)	(463,787,433)
Proceeds from sale of student loan portfolio	2,644,815,319
Expenses from sale of student loan portfolio	(231,727)
Net cash provided by operating activities	2,353,021,635
Cash flows from noncapital financing activities	
Principal payments related to early extinguishment of debt (revenue bonds)	(2,607,650,000)
Principal payments related to early extinguishment of debt (credit line)	(473,397,802)
Expenses related to early extinguishment of debt	(7,189,852)
Principal paid on revenue bonds and other borrowing	(150,000)
Principal paid on revolving credit line	(20,000,000)
Proceeds from revolving credit line	688,997,757
Interest paid on revenue bonds and other borrowing	(79,298,823)
Federal special allowance and interest subsidy	39,474,803
Transfers in	681,635
Transfers out	(29,500,000)
Net cash used for noncapital financing activities	(2,488,032,282)
Cash flows from investing activities	
Interest received from investment securities	4,558,418
Proceeds from sale and maturities of investment securities	38,287,442
Net cash provided by investing activities	42,845,860
Net decrease in cash and cash equivalents	(92,164,787)
Cash and cash equivalents, July 1, 2007	156,416,401
Cash and cash equivalents, June 30, 2008	$ 64,251,614
Reported as:	
Current - unrestricted	$ 6,047,941
Current - restricted	58,203,673
	$ 64,251,614

(Continued)

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

Statement of Cash Flows (Continued)
Year Ended June 30, 2008

Reconciliation of operating loss to net cash provided by operating activities		
Operating loss	$	(26,261,799)
Adjustments to reconcile operating loss to net cash provided by operating activities		
Depreciation		26,626
Interest - investments		(4,142,470)
Interest expense		70,675,086
Amortization of student loan premiums and fees		3,402,513
Change in assets and liabilities		
Notes receivable		(10,781,925)
Accounts receivable		
Student loans		2,280,879,813
Accrued interest - loans and notes		54,627,666
Due from other funds		(360,240)
Other receivables		(1,489,263)
Other assets		13,390
Due to other funds		(18,566)
Accounts payable and accrued expenses		(13,438,756)
Compensated absences		(110,440)
Net cash provided by operating activities	$	2,353,021,635
Supplemental disclosure of noncash transactions		
Net appreciation in fair value of investments	$	50,879

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 and 98% for loans disbursed on or after October 1, 1993.

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, 2008, 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 nonexchange 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 federal special allowance and interest subsidy assistance are recognized when earned. Uncollected interest income on student loans is accrued as revenue at June 30, 2008.

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 interest on investments 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, which may arise 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 an ongoing assessment of the loan portfolio in order to determine the appropriate level of the allowance. The factors considered in this evaluation include, but are not necessarily limited to, extreme delinquencies and violations of due diligence requirements 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 external 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 and note indentures or resolutions or are pledged as security in support of bond and note 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

Bond premiums and discounts, as well as issuance costs are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt. Amortization expense is reported as a component of interest expense in the financial statements.

N. Revenue Bonds Payable

Revenue bonds payable are stated at face value net of bond premiums and discounts.

O. Net Assets

Invested in capital assets, net of related debt - 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, grantors, contributors, and the like, 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, net of related debt."

Note 2. Summary of Significant Accounting Policies (Continued)

O. Net Assets (Continued)

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.

P. 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 or Liquidity Agreements 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.

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.

As of June 30, 2008, $4,989,944 out of the $11,281,361 of IDAPP's deposit balance was exposed to custodial credit risk because it was uninsured and uncollateralized. This account was closed in December 2008.

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 $16,593 at June 30, 2008. 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.

Note 3. Deposits and Investments (Continued)

C. Investments

Interest Rate Risk

IDAPP's investments are correlated to future cash needs for operations and are generally short-term in nature. A minimal amount of GNMA securities held have longer maturities, ranging from 8 to 10 years. These GNMA securities equal approximately 0.11% of the investments held. IDAPP's investment policy generally limits investment maturities to within two years from the date of purchase. Investments matched to a specific cash flow may exceed this limitation. The portfolio's maturity characteristics at June 30, 2008 are as follows:

Investment Type	Fair Value	Weighted Average Maturity (Years)
GNMA Securities	$ 59,724	6.630
Commercial Paper	5,612,565	0.027
U.S. Government Money Market Funds	48,453,734	0.120
Total	$ 54,126,023	
Portfolio weighted average maturity		0.117

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, 2008, IDAPP's investments were subject to credit risk as follows:

		Rating	
Investment Type	Fair Value	Standard & Poor's	Moody's
Commercial Paper	$ 5,612,565	A-1+	P-1
U.S. Government Money Market Funds	48,453,734	AAAm-G	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 $54,126,023 and include $5,672,289 in securities which are uninsured and unregistered, $5,612,565 in securities which are held by IDAPP's agent but not in IDAPP's name, and $59,724 in securities which are held by the counterparty.

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, 2008, the following investments (other than U.S. government securities, and securities explicitly guaranteed by the U.S. government) exceed 5% of IDAPP's total investment portfolio.

Investment	Fair Value	Percentage of Portfolio
Commercial Paper	$ 5,612,565	10%

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

IDAPP may make 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 shall be 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 $93,791,000 as of June 30, 2008.

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, 1998 are guaranteed at 100% by Guarantors in accordance with the Higher Education Act. For loans disbursed between October 1, 1998 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 approximated $344,000,000 at June 30, 2008.

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 which will not be reimbursed by the guarantor or collected from the student. Accordingly, management has established an allowance for possible loan losses totaling $6,968,059 as of June 30, 2008, 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, 2008 of $1,135,038,524 includes $4,039,759 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, 2008.

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 2008 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.

Failure to perform due diligence on certain student loans and the subsequent loss of guaranteed status on these loans may be interpreted as an event of default under various provisions of the bond resolutions. The Bank of New York acts as Bond Trustee on all outstanding bond series. The Bond Trustee has not currently notified IDAPP of any events of default. Should the Bond Trustee declare an event of default as defined in the bond resolutions, the Bond Trustee, or holders representing not less than 25% in aggregate principal amount of outstanding bonds are entitled to declare the principal of all bonds outstanding to be due and payable immediately.

Note 5. Student Loans Receivable (Continued)

Federal Student Loan Fund

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 ED.

The cash balance in this fund as of June 30, 2008 as reported by ISAC was $50,033,691. Restricted net assets, which includes $31,910,445 of claims in process, was $56,566,872. 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 collectability of the non-federal reinsurance amount (i.e. 5% to 25%) of the IDAPP's net student loans receivable of $1,135,038,524 at June 30, 2008 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 Subsidies

The Federal government pays IDAPP 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 receivable at June 30, 2008 was approximately $2,577,000 and related revenue was approximately $13,000,000 for the year ended June 30, 2008.

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. Total special allowance revenue was approximately $7,800,000 for the year ended June 30, 2008.

Note 7. Interfund Balances and Activity

Balances Due from/to Other Funds

The following balances at June 30, 2008 represent amounts due from other ISAC funds.

Fund	Amount	Description/Purpose
Federal Student Loan Fund #663	$ 1,148,660	Claim payments - collection of these funds are anticipated in 2009.

Note 7. Interfund Balances and Activity (Continued)

Balances Due from/to Other Funds (Continued)

The following balances at June 30, 2008 represent amounts due to other ISAC funds.

Fund	Amount	Description/Purpose
Federal Student Loan Fund #663	$ 1,017	Refunds

Transfers to Other Funds

During fiscal year 2008, IDAPP transferred $2,500,000 to ISAC's Student Loan Operating Fund for default payments. An amount of $681,635 was also transferred from ISAC's Student Loan Operating Fund to IDAPP as a refund of unclaimed MAP payments.

Note 8. Capital Assets

Capital asset activity for the year ended June 30, 2008 was as follows:

	Equipment	Accumulated Depreciation	Capital Assets, Net
Balance, July 1, 2007	$ 514,172	$ (470,235)	$ 43,937
Additions	-	(26,626)	(26,626)
Balance, June 30, 2008	$ 514,172	$ (496,861)	$ 17,311

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, 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 rate" which, as defined in the 2002 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) or 1.5% (for "A" rated bonds) and One Month LIBOR plus 1.5%. The maximum rate at June 30, 2008 was 2.44%. Auctions of bonds continue during this period of failed auctions; 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."

Note 9. Long-Term Obligations Payable (Continued)

A. Revenue Bonds Payable and Pledged Revenues (Continued)

Carryover interest is payable under certain conditions as defined in the 2002 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 83 percent of these student loan revenues. The total principal and interest remaining to be paid on the bonds is $1.7 billion. Principal and interest paid for the current year was $190,203,145 and total related student loan principal and interest received were $158,441,398 and $29,917,990, respectively.

B. Changes in Long-term Obligations Payable

Changes in long-term obligations payable for the year ended June 30, 2008 were as follows:

	Balance July 1, 2007	Additions	Deletions	Balance June 30, 2008	Amounts Due Within One Year
Compensated absences payable	$ 721,051	$ 418,922	$ (529,362)	$ 610,611	$ 61,061
Revenue bonds payable	3,492,200,000	-	(2,607,800,000)	884,400,000	-
Unamortized discounts	(12,625,762)	-	7,666,464	(4,959,298)	-
	$ 3,480,295,289	$ 418,922	$ (2,600,662,898)	$ 880,051,313	$ 61,061

C. Bond Covenant Non-compliance

Certain bond indentures require IDAPP to deliver to bond trustees audited financial statements within 150 days after its fiscal year ended June 30, 2008. Although IDAPP is not in compliance with the 150-day filing requirement, there has been no notice of nonperformance of this provision by the bond trustees and, therefore, no event of default. IDAPP would have 30 days after receiving notice to remedy the condition.

Note 9. Long-Term Obligations Payable (Continued)

D. 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
2009	$ -	$ 21,579	$ 21,579
2010	-	21,579	21,579
2011	-	21,579	21,579
2012	-	21,579	21,579
2013	-	21,579	21,579
2014-2018	-	107,897	107,897
2019-2023	-	107,897	107,897
2024-2028	-	107,897	107,897
2029-2033	-	107,897	107,897
2034-2038	-	107,897	107,897
2039-2043	209,400	103,757	313,157
2044-2045	675,000	25,620	700,620
	884,400	$ 776,757	$ 1,661,157
Less:			
Unamortized bond discounts	(4,959)		
Net long-term principal outstanding	$ 879,441		

All of IDAPP's debt outstanding revenue bonds are comprised of variable rate debt. As such, the interest figures shown above are calculated assuming the current interest rate of 2.44% 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/IDAPP executed a $500,000,000 mid-term revolving credit agreement through an affiliate of Citibank, CIESCO LLC. The revolving credit line was used to purchase alternative loans and FFELP student loans (guaranteed or insured or is an eligible loan under the Higher Education Act), and was due to expire on July 25, 2008. The line was extended to September 8, 2008 (see Note 17). Bank of New York is the Trustee (the Trust) for this credit line.

The terms of the Citibank credit line are as follows:

Citicorp North America through CIESCO, LLC facilitates an asset backed commercial paper program for up to $500 million for the benefit of IDAPP. CIESCO places the commercial paper and passes the interest cost on to IDAPP. The cost approximates the LIBOR rate, which was 2.68% at June 30, 2008. IDAPP's borrowing is supported by a liquidity line of credit provided by Citibank NA, Inc. Citibank receives 43 basis points on the outstanding debt for providing the back credit facility and for serving as the administrative agent. As of June 30, 2008 there was $390,770,062 outstanding under this line.

On August 29, 2007 IDAPP retired its existing Bank of America credit line. Changes in the revolving credit lines are as follows:

	Balance, July 1, 2007	Additions	Deletions	Balance, June 30, 2008
Citibank	$ -	$ 410,770,062	$ (20,000,000)	$ 390,770,062
Bank of America, N.A.	195,170,107	278,227,695	(473,397,802)	-
	$ 195,170,107	$ 688,997,757	$ (493,397,802)	$ 390,770,062

IDAPP has also pledged the future student loan revenues of the above described portfolio to repay the $390,770,062 principal outstanding on the Citibank credit line. Under the terms of the agreement all revenues generated by the underlying student loan portfolio are transferred to the Trust. The Trust then 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 2008 there was $35,424,426 in principal and $15,094,110 in interest collected. The total amount transferred to the trust was $50,518,536. During the same period the Trust paid $16,233,080 for interest expense and other professional fees and $2,132,170 for servicing fees.

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 2008 are included in the State of Illinois' Comprehensive Annual Financial Report (CAFR) for the year ended June 30, 2008. SERS issues a separate CAFR that may be obtained by writing to SERS, 2101 South Veterans Parkway, Springfield, Illinois, 62794-9255.

Note 11. Pension Plan (Continued)

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 2008, 2007 and 2006 were $1,058,674, $853,909 and $575,840, respectively. For fiscal year 2008, 2007 and 2006, the employer contribution rate was 16.6%, 11.5% and 7.8%, 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 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, 2008.

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. FFELP loans are guaranteed by the Federal Department of Education. IDAPP is committed to disbursing the funds for the FFELP loans purchased by these lenders. The total amount of the purchase commitment is not specified in the individual contracts. IDAPP's obligation under these purchase agreements is estimated to range from $0.3 to $46 million. The total amount of loans purchased by IDAPP with all lenders in FY2008 was approximately $125.8 million.

Note 15. New Governmental Accounting Standards

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

Statement No. 51, *Accounting and Financial Reporting for Intangible Assets,* establishes accounting and financial reporting requirements for intangible assets. All intangible assets not specifically excluded by the scope of this Statement should be classified as capital assets. All existing authoritative guidance for capital assets should be applied to these intangible assets, as applicable. The Commission is required to implement this Statement for the year ending June 30, 2010.

Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, addresses the recognition, measurement, and disclosure of information regarding derivative instruments entered into by state and local governments. Derivative instruments are often complex financial arrangements used by governments to manage specific risks or to make investments. The Commission is required to implement this Statement for the year ending June 30, 2010.

Management has not currently determined what impact, if any, these Statements may have on its financial statements.

Note 16. Special Item

A. Sale of Student Loans

During fiscal year 2008, the Illinois Student Assistance Commission sold student loans receivable from the Illinois Designated Account Purchase Program Fund with a carrying amount of $2,639 million for $2,645 million. The loans receivable constituted 78% of IDAPP's total student loan portfolio as of the beginning of the year.

The gross premium from the sale of $77,314,410 less the expenses related to the sale of $231,727, the corresponding write-off of unamortized premiums, origination and default fees of $75,962,843 and the recovery of loan loss reserve of $3,245,738 are reported as special items in the Statement of Revenues, Expenses and Changes in Fund Net Assets.

B. Early Extinguishment of Related Debt

ISAC also retired $2,607,650,000 in revenue bonds associated with the student loan portfolio which was sold in July and August 2008. Expenses related to the early extinguishment of $7,189,852 and write-offs of unamortized bond discounts and costs of issuance of $8,030,651 are reported as special items in the Statement of Revenues, Expenses and Changes in Fund Net Assets.

Note 16. Special Item (Continued)

Details of the amount reported as a special item are as follows:

Special Item	
Sale of student loan portfolio	
Premium from sale of loans	$ 77,314,410
Expenses related to sale of loans	(231,727)
Gain from loan sale, net of direct expenses	77,082,683
Write-off of capitalized premiums, origination, and default fees	(72,717,104)
Net gain from sale of student loans	4,365,579
Early extinguishment of debt	
Expenses related to retirement of bonds	(7,189,852)
Write-off of unamortized discounts for bonds retired	(8,030,651)
Net loss related to early extinguishment of debt	(15,220,503)
Net special item	$ (10,854,924)

Note 17. Subsequent Events

A. Citibank Mid-Term Asset Backed Commercial Paper Program:

On July 27, 2007, ISAC entered into a $500,000,000 Mid-Term Asset Backed Commercial Paper Program through an affiliate of Citibank, CIESCO, LLC (Note 10). ISAC has pledged as collateral to CIESCO a portfolio of certain student loans. CIESCO acts as a conduit lender, issuing commercial paper, lending those funds at cost to ISAC. A back-up facility issued by Citibank N.A. on behalf of ISAC supports this Program. This back-up facility expired on September 8, 2008 resulting, by terms of the Indenture, in the commencement of the Liquidation Period. During the Liquidation Period, cash flow generated by the underlying student loans are applied as follows: First, to pay any fees due the U. S. Department of Education; Second, to pay operating costs of ISAC; Third, to pay fees of the Trustee; Fourth, to pay interest; Fifth, to pay program fees of Citibank; Sixth, to pay down principal outstanding under the Program. The Liquidation Period continues, by its term, until July 27, 2010, at which point any amounts not paid are due and payable. On October 2, 2008, ISAC reduced the size of this Program to $415,000,000. Management anticipates reducing the size of the Program from time to time as is deemed feasible. During the Liquidation Period, costs of borrowing under the Program will not exceed Citibank's commercial paper rate plus 43 basis points for dealer commission. Bank of New York Trust Company, N.A. is Trustee.

B. Sale of Bonds to Credit Union

On September 23, 2008, ISAC entered into a Bond Purchase Agreement with a group of Illinois Credit Unions to sell Taxable Student Loan Revenue Bonds (Series 2008A, Series 2008B, and Series 2008C) for an aggregate amount up to, but not to exceed $100,100,000. Funds from the bond sales will be used to support FFELP student loans for the 2008/2009 school year. On September 23, 2008 ISAC sold the first in the series of bonds and received $40,050,000. The Series 2008B bonds were sold for $40,050,000 on December 15, 2008. The Series 2008C bonds can be sold for up to $20,000,000 on or about the week ending March 27, 2009. Interest on the bonds is set at "AA" Financial Commercial Paper Rate plus 80 basis points. Interest and principal is due and payable on all three series of bonds upon maturity, which is set at August 20, 2009. An Indenture of Trust and Credit Agreement was also signed September 23, 2008 with Wells Fargo Bank, NA to serve as Trustee for the bond sale.

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

Schedule of Bonds Outstanding
June 30, 2008

A summary of bonds and notes outstanding at June 30, 2008 is presented as follows:

	Series 2002 I and Series 2002II	Series 2003 III 2003IV and 2003V	Series 2004 VI and 2004 VII	Series 2005 VIII and 2005 IX
Original amount	$ 250,000,000	$ 350,000,000	$ 250,000,000	$ 600,000,000
Principal retirements	(150,150,000)	(240,450,000)	(175,000,000)	-
Unamortized discount	(920,462)	(1,202,447)	(902,895)	(1,933,494)
Balance at June 30, 2008	$ 98,929,538	$ 108,347,553	$ 74,097,105	$ 598,066,506
Effective interest rate (1)	Variable	Variable	Variable	Variable
Date of bonds	8/20/02	10/2/03	4/21/04	7/19/05 12/08/05
Interest dates	Varies	Varies	Varies	Varies
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
Optional call feature beginning:	At issuance 100%	At issuance 100%	At issuance 100%	At issuance 100%
Taxable/ Tax-exempt	Taxable	Taxable	Taxable	Taxable

	Total
Original amount	$ 1,450,000,000
Principal retirements	(565,600,000)
Unamortized discount	(4,959,298)
Balance at June 30, 2008	$ 879,440,702
Debt outstanding per Statement of Net Assets	
Current portion of :	
Revenue bonds payable	$ -
Long-term revenue bonds payable, net	879,440,702
Total debt outstanding	$ 879,440,702

(1) As of June 30, 2008 variable interest rates were 2.44% for taxable auction rate securities debt.

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, 2008 and have issued our report thereon dated March 27, 2009. 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.

Our consideration of the internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in the accompanying schedule of Current Findings – *Government Auditing Standards* to be significant deficiencies in internal control over financial reporting (findings 08-2 through 08-4).

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider findings 08-2 and 08-3 to be material weaknesses.

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 an instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of Current Findings – *Government Auditing Standards* as finding 08-3.

We also noted certain matters which we have reported to management of the Commission in a separate letter dated March 27, 2009.

The Commission's responses to the findings identified in our audit are described in the accompanying schedule of Current Findings – *Government Auditing Standards*. 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, the Commission Board and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

McGladrey & Pullen, LLP

Schaumburg, Illinois
March 27, 2009

Current Findings – ***Government Auditing Standards***

(Note: Finding 08-1 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 08-2 Draft Financial Statements Not Accurate

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

The Illinois Designated Account Purchase Program (IDAPP) of the Illinois Student Assistance Commission (Commission) did not have sufficient controls over financial reporting.

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

- Unamortized bond issuance costs that totaled approximately $840,000 were inappropriately classified as unrestricted other assets instead of restricted unamortized bond issuance costs.
- Approximately $16 million of student loans, net of allowance for loan losses, were inappropriately classified as unamortized bond issuance costs.
- Net assets were not properly categorized as to restricted and unrestricted.
- Generally Accepted Accounting Standards Board (GASB) Statement No. 40 disclosure of custodial credit risk for deposits and investments was not complete.
- Cash flows from operating activities were not properly classified.

All material transactions should be recorded in accordance with generally accepted accounting principles (GAAP), and financial statement amounts should be supported with complete and accurate disclosures in the form of notes to the financial statements. The errors and omissions described above resulted in certain aspects of the draft financial statements for IDAPP to be prepared not in accordance with GAAP.

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 Commission management, the primary issues noted above were caused by a change in procedures and reductions in the workforce resulting from the outsourcing of the servicing of alternative loans.

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. 08-2, 07-3)

Recommendation

We recommend the Commission review its procedures over outsourced services, allocate the resources necessary, and improve controls over financial reporting to ensure accurate presentation and disclosure of IDAPP's annual financial statements.

Current Findings – ***Government Auditing Standards (Continued)***

Finding 08-2 Draft Financial Statements Not Accurate (Continued)

Commission Response

Agree.

Subsequent to the audit being performed the Commission has implemented several changes to address the issues noted above. The Accounting department has been reorganized to better utilize existing talent and also a new financial reporting manager (with a CPA certificate) has been hired who will assist in the review process. In addition a formal review and sign-off process has been implemented.

Current Findings – ***Government Auditing Standards (Continued)***

Finding 08-3 Investment Policies Not Followed

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

The Illinois Designated Account Purchase Program (IDAPP) does not have adequate collateral to cover 100% of its bank deposit balances that exceed FDIC insured amounts, and investments in a single issuer exceeded investment policy established limits.

IDAPP is in violation of its current investment policy restricting investments in a single issuer to no more than 5% of the total investment portfolio of the agency. In addition, during testing of cash and investments, a lack of sufficient collateral for deposits in excess of FDIC insured amounts was noted. IDAPP has an uninsured uncollateralized deposit balance of approximately $5 million at June 30, 2008, consisting of 2 locally held accounts in violation of the State Officers and Employees Money Disposition Act (Act).

At June 30, 2008, IDAPP held over $5.6 million in commercial paper issued by another financial institution. This investment is approximately 10% of IDAPP's total investment balance at its fiscal year-end. IDAPP's investment policy requires IDAPP to diversify its investments by security type and institution. With the exception of certain obligations as set forth in the investment policy (direct federal obligations, federal guaranteed obligations, and federal affiliated institutions) or investments fully collateralized by these obligations, IDAPP's investment policy states that no more than 5% of IDAPP's total investment portfolio will be invested in the obligations of a single issuer.

Good business practices require that an entity's bank balances be adequately insured or collateralized to prevent losses in the event of a bank failure and to properly safeguard the entity's assets. In addition, a good internal control environment includes checks and balances to ensure policies established by the Board are followed. The Act (30 ILCS 230/2c) states, "Whenever funds deposited with a bank or savings and loan association exceed the amount of federal deposit insurance coverage, a bond, pledged securities, or other eligible collateral shall be obtained."

According to Commission management, one of the bank accounts had an uncollateralized deposit ($435k) at year end. The account was set-up incorrectly, resulting in the balances being uncollateralized. An additional $4.7 million in a different bank was set up as a collateral account based on a contractual agreement. It was an oversight that a reciprocal collateralization was not provided (by the bank) for the funds that IDAPP provided to the bank as collateral. The $5,612,565 of commercial paper at another financial institution was also set-up in error.

IDAPP's uncollateralized and uninsured deposits are susceptible to loss in the event of a bank failure, as the amount of deposits in excess of FDIC insured limits may not be recoverable. In addition, IDAPP has failed to comply with State Statute and its investment policy and has exposed itself to concentration of credit risk in excess of levels deemed appropriate by its governing officials. (Finding No. 08-3)

Recommendation

We recommend IDAPP obtain sufficient collateral to cover uninsured deposit balances at each applicable bank. In addition, IDAPP should improve monitoring controls over deposit balances at each bank to make sure collateral is sufficient to cover deposit balances in the event of a bank failure. We also recommend IDAPP improve controls to ensure that it adheres to its investment policy.

Current Findings – ***Government Auditing Standards (Continued)***

Finding 08-3 Investment Policies Not Followed (Continued)

Commission Response

Agree.

The $5.6 million of commercial paper at June 30, 2008 has subsequently been reduced to $3.5 million and invested in treasury bills. Therefore we no longer have over 10% of our investments with one issuer. With the switch in investments to treasury bills, the funds are now collateralized.

The $435k of investments had been held at LaSalle Bank, which was acquired by Bank of America subsequent to 6/30/08. With the switch to Bank of America, the funds are now fully collateralized.

The $4.7 million uncollateralized deposit at Guarantee Bank was held pending the resolution of a legal dispute which was resolved in December 2008. The account has now been closed.

Additionally, ISAC's Commissioners approved a new Investment Policy at its November 2008 meeting. This included the restructuring of IDAPP's Investment Committee, chaired by ISAC's Chief Investment Officer.

Current Findings – ***Government Auditing Standards***

Finding 08-4 Documentation of Journal Entry Approval is Lacking

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

The Illinois Designated Account Purchase Program (IDAPP) does not have adequate controls over the preparation and posting of journal entries.

During our testing of internal controls over accounting for the federal special allowance revenues and receivables, we noted that there was no evidence of review of the journal entries prepared to record this revenue and related receivables by an appropriate supervisor. The federal special allowance and interest subsidy revenue was $20,828,750 and the related receivable at year-end was $1,785,701.

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 system of internal control requires that journal entries and supporting documentation related to significant accounts should be reviewed by an appropriate supervisor.

According to Commission management, IDAPP's accounting personnel are aware of the requirement to have all journal entries reviewed and initialed to document the review. In an effort to meet closing deadlines, sign-offs were not always obtained.

Lack of supervisory review of journal entries could result in federal special allowance revenues and related receivables being misstated. In addition, errors in analyses and journal entries will not be detected if not reviewed by an appropriate supervisor. (Finding No. 08-4)

Recommendation

We recommend that account reconciliations, analyses and journal entries prepared for all significant accounts be reviewed by a supervisor other than the preparer. In addition, these reviews should be documented by dating and signing or initialing the item. Journal entries lacking documentation of supervisory review should not be posted until after written documentation of such review has been obtained.

Commission Response

Agree.

IDAPP's Accounting personnel are aware of the requirement to have all journal entries reviewed and initialed to document the review. In an effort to meet closing deadlines, sign-offs were not always obtained.

The Commission has re-emphasized this requirement for fiscal year 2009, both in writing and in departmental meetings and will continue to monitor this requirement.

Prior Finding Not Repeated

(Note: Prior finding not repeated A. 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.)

B. Internal Auditing

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

During our fiscal year 2007 audit and examination we noted the Commission failed to perform internal audits of 4 of its 12 (33%) major systems of internal accounting and administrative controls within the last two years. (Finding Code Nos. 07-2, 06-3)

We noted during the fiscal year 2008 audit that internal audits were performed that addressed the required major internal accounting and administrative control systems.