

**MISSISSIPPI HIGHER EDUCATION
ASSISTANCE CORPORATION
AND EDUCATION SERVICES FOUNDATION**

**COMBINED FINANCIAL STATEMENTS AND
REPORT OF INDEPENDENT
CERTIFIED PUBLIC ACCOUNTANTS**

DECEMBER 31, 2011 AND 2010

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To the Directors of Mississippi Higher
Education Assistance Corporation and
Education Services Foundation

We have audited the accompanying combined statements of financial position of Mississippi Higher Education Assistance Corporation and Education Services Foundation as of December 31, 2011 and 2010, and the related combined statements of activities and changes in unrestricted net assets and cash flows for the years then ended. These combined financial statements are the responsibility of the management of Mississippi Higher Education Assistance Corporation and the management of Education Services Foundation. Our responsibility is to express an opinion on these combined financial statements based on our audits.

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

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of Mississippi Higher Education Assistance Corporation and Education Services Foundation as of December 31, 2011 and 2010, and the changes in their net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the combined financial statements as a whole. The supplemental information is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the combined financial statements. The information has been subjected to the auditing

procedures applied in the audit of the combined financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the combined financial statements or to the combined financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the combined financial statements as a whole.

Hudson Reed Burke & Company, P.C.

March 28, 2012

**MISSISSIPPI HIGHER EDUCATION ASSISTANCE CORPORATION
AND EDUCATION SERVICES FOUNDATION**

**COMBINED STATEMENTS OF FINANCIAL POSITION
DECEMBER 31, 2011 AND 2010**

ASSETS

	<u>2011</u>	<u>2010</u>
Cash and cash equivalents	\$ 139,251,671	191,323,751
Investments	54,269,140	66,235,822
Student loans receivable	906,935,008	1,002,190,067
Interest and special allowance receivable	15,370,170	17,447,240
Deferred costs of issuance less accumulated amortization	4,735,653	5,671,337
Other assets	<u>430,652</u>	<u>487,690</u>
Total assets	\$ <u>1,120,992,294</u>	<u>1,283,355,907</u>

LIABILITIES AND UNRESTRICTED NET ASSETS

LIABILITIES:

Accounts payable and accrued expenses	\$ 1,608,405	1,899,302
Accrued interest payable	766,054	1,259,005
Excess interest and rebate payable	10,918,601	12,803,000
Bonds and notes payable	<u>962,250,000</u>	<u>1,133,300,000</u>
Total liabilities	975,543,060	1,149,261,307
UNRESTRICTED NET ASSETS	<u>145,449,234</u>	<u>134,094,600</u>
Total liabilities and unrestricted net assets	\$ <u>1,120,992,294</u>	<u>1,283,355,907</u>

The accompanying notes are an integral part of these statements.

**MISSISSIPPI HIGHER EDUCATION ASSISTANCE CORPORATION
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**COMBINED STATEMENTS OF ACTIVITIES
AND CHANGES IN UNRESTRICTED NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>	<u>2010</u>
INTEREST INCOME:		
Interest on student loans	\$ 20,560,199	25,101,754
Interest subsidy	5,315,680	8,398,337
Special allowance	(8,242,744)	(12,487,237)
Late fees	<u>305,199</u>	<u>235,683</u>
Student loans	17,938,334	21,248,537
Interest on investments	<u>537,327</u>	<u>1,275,123</u>
Total interest income	<u>18,475,661</u>	<u>22,523,660</u>
INTEREST COST:		
Interest expense	10,792,052	14,883,528
Bond and note fees	605,310	768,133
Amortization of deferred costs of issuance	<u>251,502</u>	<u>392,802</u>
Total interest cost	<u>11,648,864</u>	<u>16,044,463</u>
Net interest revenue	6,826,797	6,479,197
PROVISION FOR LOAN LOSSES	<u>170,708</u>	<u>291,351</u>
Net interest revenue after provision for loan losses	<u>6,656,089</u>	<u>6,187,846</u>
OTHER REVENUE (EXPENSE):		
Gross profit from sale of student loans	-	2,176,047
Other revenue	81,267	363,345
Program services	(4,119,434)	(5,986,225)
Support services	<u>(2,216,890)</u>	<u>(2,354,542)</u>
Total other revenue (expense)	<u>(6,255,057)</u>	<u>(5,801,375)</u>
INCREASE IN UNRESTRICTED NET ASSETS BEFORE GAINS ON EXTINGUISHMENT OF DEBT	401,032	386,471
GAINS ON EXTINGUISHMENT OF DEBT	<u>10,953,602</u>	<u>6,115,918</u>
INCREASE IN UNRESTRICTED NET ASSETS	11,354,634	6,502,389
UNRESTRICTED NET ASSETS, BEGINNING OF PERIOD	<u>134,094,600</u>	<u>127,592,211</u>
UNRESTRICTED NET ASSETS, END OF PERIOD	<u>\$ 145,449,234</u>	<u>134,094,600</u>

The accompanying notes are an integral part of these statements.

**MISSISSIPPI HIGHER EDUCATION ASSISTANCE CORPORATION
AND EDUCATION SERVICES FOUNDATION**

**COMBINED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>	<u>2010</u>
RECEIPTS (DISBURSEMENTS) IN CASH AND CASH EQUIVALENTS:		
Cash flows from operating activities:		
Interest on student loans	\$ 11,414,359	14,448,719
Interest subsidy	5,594,471	9,858,805
Special allowance	(8,377,881)	(14,863,810)
Late fees	305,199	235,683
Interest on investments	676,258	1,251,063
Other program services revenue	82,136	363,471
Interest expense	(11,285,003)	(15,509,176)
Program and support services	(6,588,481)	(8,566,863)
Bond and note fees	<u>(407,307)</u>	<u>(725,899)</u>
Net cash used by operating activities	<u>(8,586,249)</u>	<u>(13,508,007)</u>
Cash flows from investing activities:		
Additions to equipment	(229,778)	(7,653)
Collection of student loan principal	107,396,888	109,259,128
Proceeds from sale of student loans	-	6,252,334
Purchases/origination of student loan principal	(4,451,786)	(102,183,568)
Purchases of student loan accrued interest	-	(629,633)
Investments matured/redeemed	11,966,682	3,288,837
Loan premiums and origination costs	<u>-</u>	<u>(1,992,452)</u>
Net cash provided by investing activities	<u>114,682,006</u>	<u>13,986,993</u>
Cash flows from financing activities:		
Collection of excess and rebate interest liability	1,327,036	1,099,010
Payment of rebate interest	(131,859)	(340,971)
Proceeds from line of credit	-	14,300,000
Payments on line of credit	-	(28,800,000)
Proceeds from DOE loan participation	-	113,686,161
Payments on DOE loan participation	-	(8,072,814)
Payments to redeem bonds and notes	(159,363,014)	(96,041,098)
Payments for costs of issuance	<u>-</u>	<u>(60,540)</u>
Net cash used by financing activities	<u>(158,167,837)</u>	<u>(4,230,252)</u>

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**COMBINED STATEMENTS OF CASH FLOWS - CONTINUED:
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>	<u>2010</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS	\$ (52,072,080)	(3,751,266)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	<u>191,323,751</u>	<u>195,075,017</u>
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ <u>139,251,671</u>	<u>191,323,751</u>
 RECONCILIATION OF INCREASE IN UNRESTRICTED NET ASSETS TO NET CASH USED BY OPERATING ACTIVITIES:		
Increase in unrestricted net assets	\$ <u>11,354,634</u>	<u>6,502,389</u>
Adjustments to reconcile increase in unrestricted net assets to net cash used by operating activities:		
Amortization and depreciation	5,350,294	6,403,120
Capitalized interest on student loans	(15,717,953)	(16,607,978)
Provision for loan losses	170,708	291,351
Gains on extinguishment of debt	(10,953,602)	(6,115,918)
Gross profit from sale of student loans	-	(2,176,047)
(Increase) decrease in interest and special allowance receivable	1,852,875	(892,616)
Decrease in other assets	210,909	614,313
Decrease in accounts payable	(361,162)	(900,972)
Decrease in accrued interest payable	<u>(492,952)</u>	<u>(625,649)</u>
Total adjustments	<u>(19,940,883)</u>	<u>(20,010,396)</u>
Net cash used by operating activities	\$ <u>(8,586,249)</u>	<u>(13,508,007)</u>

The accompanying notes are an integral part of these statements.

**MISSISSIPPI HIGHER EDUCATION ASSISTANCE CORPORATION
AND EDUCATION SERVICES FOUNDATION**

**NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

NOTE 1 - ORGANIZATIONS

Mississippi Higher Education Assistance Corporation ("MHEAC") is a nonprofit corporation organized on January 23, 1980, under the laws of the State of Mississippi. MHEAC is not an agency or instrumentality of the State of Mississippi or any agency or political subdivision thereof. MHEAC operates in accordance with the Higher Education Act for the exclusive purpose of acquiring student loans incurred under the Federal Family Education Loans Program ("FFELP"). Prior to 2009, MHEAC's primary source of funds for this purpose was the issuance of both tax-exempt and taxable revenue bonds. During 2009 and 2010, MHEAC's primary source of funds for the purpose of acquiring student loans was the U.S. Department of Education ("DOE") Loan Participation Program. On March 30, 2010, Federal legislation was signed into law that eliminated funding for new FFELP originations made on or after July 1, 2010, and required that all new Federally funded student loans made on or after July 1, 2010 be originated directly by the Federal government. MHEAC's acquisition of FFELP loans has since declined substantially.

Education Services Foundation ("ESF") is a nonprofit corporation organized on March 24, 1995, under the laws of the State of Mississippi. ESF is not an agency or instrumentality of the State of Mississippi or any agency or political subdivision thereof. ESF operates for the purpose of engaging in a variety of activities intended to increase the level of appropriate quality education in the State of Mississippi and elsewhere. These activities include free college planning services, awarding of scholarships, and prior to July 1, 2010, origination of FFELP student loans. ESF's primary source of funds is from the provision of management services to MHEAC. Prior to 2011, ESF's source of funds also included the provision of student loans services to MHEAC, sales of the loans that it originated and the provision of loan origination services to financial institutions. ESF is currently working to become a qualified nonprofit loan servicer for student loans originated by the Federal government.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Combination

Because the boards of MHEAC and ESF are identical and because MHEAC has a management contract with ESF whereby ESF manages MHEAC's daily operations, generally accepted accounting principles ("GAAP") require that the financial statements of MHEAC and ESF be combined. Accordingly, the accompanying financial statements present the combination of the financial statements of MHEAC and ESF. Material intercompany transactions and balances have been eliminated in the financial statements.

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**NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES - CONTINUED:

Principles of Combination - continued:

MHEAC and ESF continue to be operated as separate and distinct organizations. There has been no merger or other type of business combination. Any combination of MHEAC and ESF in these financial statements and the accompanying notes is strictly for GAAP reporting purposes only. The financial statements of MHEAC are presented separately in the accompanying supplemental financial statements.

Cash and Cash Equivalents

MHEAC and ESF consider all checking accounts, money market accounts and investment agreements with an original maturity of three months or less to be cash and cash equivalents.

Investments

Investments are reported at their cost or amortized cost, which management believes approximates the fair value based upon the monthly resetting of interest rates.

Student Loans Receivable

Student loans are reported at their unpaid principal balances, net of expected loan losses, plus unamortized costs related to loan originations and premiums related to loan purchases. Origination costs and premiums are amortized over sixteen years for consolidation loans and eight years for all other loans using the effective interest method. There are no quoted prices in active markets for student loans and, as a result, a reasonable estimate of fair value was not deemed practical and could not be made without incurring excessive costs.

Deferred Costs of Issuance

The costs of issuing bonds and notes, which are composed of underwriter's discount, legal costs and other related financing costs, are capitalized and amortized over the expected life of the related debt issue on a weighted average basis.

Bonds and Notes Payable

Bonds and notes payable are reported at their principal amount outstanding. Substantially all bonds and notes are auction rate securities. Since mid-February 2008, the normal functioning of the auction market has been disrupted. As a result, a reasonable estimate of fair value was not deemed practical and could not be made without incurring excessive costs.

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**NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED:

Advertising

Advertising costs are charged to operations when incurred.

Income Taxes

MHEAC and ESF are tax-exempt organizations under Section 501(c)(3) of the Internal Revenue Code, and are not private foundations within the meaning of Section 509(a) of the Internal Revenue Code. MHEAC and ESF file separate tax returns. MHEAC and ESF believe that they have appropriate support for any tax positions taken, and as such, do not have any uncertain tax positions that are material to the combined financial statements. MHEAC and ESF are no longer subject to income tax examinations by the U.S. Federal, state or local tax authorities for years before 2008.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Key accounting policies that include significant judgments and estimates include valuation and income recognition related to allowance for loan losses, loan effective interest rate method (student loan premiums), excess interest and rebate.

NOTE 3 - CASH AND INVESTMENTS

Financial instruments which potentially subject MHEAC and ESF to concentrations of credit risk consist principally of cash and investments. Generally, deposits with banks are in excess of the FDIC insurance limit. Management routinely assesses the financial strength of the institutions and, as a consequence, believes that cash and investment credit risk exposure is limited.

At December 31, 2011 and 2010, cash and cash equivalents and investments consisted of:

	<u>2011</u>	<u>2010</u>
Cash and cash equivalents:		
Cash	\$ 1,476,377	1,154,338
Money market instruments	<u>137,775,294</u>	<u>190,169,413</u>
	\$ <u>139,251,671</u>	<u>191,323,751</u>

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**NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

NOTE 3 - CASH AND INVESTMENTS - CONTINUED:

		<u>2011</u>	<u>2010</u>
	<u>Maturity</u>		
Investments:			
Societe Generale	9/1/35 - 3/1/37	\$ 4,179,500	5,140,000
Westdeutsche Landesbank	8/1/29 - 9/1/33	18,193,500	18,377,500
Bayerische Landesbank	9/1/16	27,160,492	29,010,492
Certificates of Deposit	4/28/10 - 4/30/12	<u>4,735,648</u>	<u>13,707,830</u>
		<u>\$ 54,269,140</u>	<u>66,235,822</u>

Investments consist of repurchase agreements and FDIC-insured certificates of deposit. Substantially all cash and investments are restricted for the acquisition of student loans, repayment of bond and note obligations and to satisfy certain reserve requirements specified by the various bond indentures.

NOTE 4 - STUDENT LOANS RECEIVABLE

Student loans include FFELP Stafford loans, Parent Loans for Undergraduate Students ("PLUS") loans, and Consolidation loans. The terms of the loans, which vary on an individual basis, generally provide for repayment in monthly installments of principal and interest over a period of up to ten years for Stafford and PLUS loans and up to thirty years for Consolidation loans. Stafford loans generally do not require repayment while the borrower is in school and during the grace period immediately upon leaving school. Repayment for PLUS and Consolidation loans generally begins after the final disbursement of the loan. Repayment of FFELP loans may be delayed during periods of deferment or forbearance that are granted based on need. Interest continues to accrue on loans in the in-school, grace, deferment, and forbearance periods. For certain Stafford loans and certain Consolidation loans, DOE pays the loan interest while the loan is in the in-school, grace, or deferment period. This interest is paid quarterly to MHEAC and ESF by DOE and is referred to as interest subsidy. Interest rates on FFELP loans are either a stated fixed rate or a variable rate, depending on when the loan was originated and the loan type. Variable rates are subject to a cap and are reset annually on July 1 of each year.

For loans disbursed prior to April 1, 2006, MHEAC and ESF earn interest at the greater of the loan rate or a floating rate based on the special allowance payment ("SAP") formula, with any interest earned at the SAP rate that exceeds the interest earned at the loan rate being paid directly by DOE on a quarterly basis. For loans disbursed on or after April 1, 2006, MHEAC and ESF earn

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**NOTES TO COMBINED FINANCIAL STATEMENTS
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NOTE 4 - STUDENT LOANS RECEIVABLE - CONTINUED:

interest at the SAP rate, as any interest earned at the loan rate that exceeds the interest earned at the SAP rate is required to be refunded to DOE on a quarterly basis. The SAP rate is related to the average of 91-day Treasury bill rates or 3-month commercial paper rates during each quarter. The SAP rate for certain loans that are related to tax-exempt obligations issued before October 1, 1993 is fixed at 9.5%.

MHEAC is required to pay DOE a monthly fee at an annualized rate of 1.05% of the principal amount of, and accrued interest on, its Consolidation loans.

Substantially all of the student loans are pledged to the repayment of bonds and notes. Concentrations of credit risk with respect to student loans are limited due to a large number of borrowers and the guarantee. Student loans are guaranteed by various guarantors, which are reinsured by the Federal government. The guarantors guarantee 98% of principal and accrued interest for loans disbursed prior to July 1, 2006, and 97% for loans disbursed on or after July 1, 2006. As of December 31, 2011 and 2010, approximately 73% and 73%, respectively, of the loans were subject to the 98% guarantee, with the remainder subject to the 97% guarantee.

At December 31, 2011 and 2010, student loans consisted of:

	<u>2011</u>	<u>2010</u>
Student loans receivable	\$ 889,204,302	979,556,485
Unamortized premiums and origination costs	<u>18,740,271</u>	<u>23,742,093</u>
	907,944,573	1,003,298,578
Provision for loan losses	<u>(1,009,565)</u>	<u>(1,108,511)</u>
	<u>\$ 906,935,008</u>	<u>1,002,190,067</u>

At December 31, 2011 and 2010, approximately 74% and 74%, respectively, of the student loans were Consolidation loans and approximately 72% and 68%, respectively, of the student loans were in repayment. During the years ended December 31, 2011 and 2010, the average annual yield on student loans was approximately 1.85% and 1.88%, respectively.

NOTE 5 - OTHER ASSETS

At December 31, 2011 and 2010, other assets consisted of:

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**NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

NOTE 5 - OTHER ASSETS - CONTINUED:

	<u>2011</u>	<u>2010</u>
Equipment, furniture and software	\$ 1,477,366	1,573,752
Accumulated depreciation	<u>(1,269,110)</u>	<u>(1,497,435)</u>
Net book value	208,256	76,317
Prepaid bond and note fees	107,842	215,680
Miscellaneous	<u>114,554</u>	<u>195,693</u>
	<u><u>\$ 430,652</u></u>	<u><u>487,690</u></u>

NOTE 6 - EXCESS INTEREST AND REBATE PAYABLE

MHEAC records a liability for its estimate of excess interest earnings on student loans financed with proceeds of certain tax-exempt bond issues. The liability must be settled through cash payments to the Federal government beginning ten years after the applicable bond issue date or through reducing the yield on student loans by forgiving student loans. In addition, a rebate payable is recorded for MHEAC's estimate of excess earnings on certain investments made with proceeds of tax-exempt bond issues. The rebate payable must be settled through cash payments to the Federal government beginning five years after the applicable bond issue date. The liability for excess interest and rebate payable is computed in accordance with current Treasury Regulations and is funded with cash deposits. This liability is subject to review and possible adjustment by the Treasury.

During the years ended December 31, 2011 and 2010, MHEAC settled approximately \$3,080,000 and \$513,000, respectively, of its excess interest liability through the forgiveness of student loan principal and accrued interest. During the years ended December 31, 2011 and 2010, MHEAC settled approximately \$132,000 and \$341,000, respectively, of its rebate liability through cash payments to the Federal government.

NOTE 7 - BONDS AND NOTES PAYABLE

At December 31, 2011, MHEAC bonds and notes payable consisted of:

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**NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

NOTE 7 - BONDS AND NOTES PAYABLE - CONTINUED:

<u>Series</u>	<u>Indenture</u>	<u>Amount</u>	<u>Maturity</u>	<u>Status</u>	<u>Rate</u>
1996	1996	\$ 61,000,000	10/1/26	Taxable	1.53%
1996-A	1993	23,100,000	9/1/16	Exempt	.25
1998-B	1993	41,700,000	9/1/33	Exempt	.23
1999-A-1	1999	26,500,000	8/1/29	Exempt	.18
1999-A-3	1999	14,000,000	8/1/29	Taxable	1.79
1999-B-1	1999	8,500,000	8/1/29	Exempt	.18
2000	1996	40,900,000	7/1/30	Taxable	1.51
2000-A-1	1999	58,600,000	9/1/30	Taxable	1.79
2000-B-1	1999	8,100,000	9/1/30	Taxable	1.93
2000-A-2	1999	12,300,000	9/1/30	Exempt	.21
2000-A-3	1999	46,600,000	9/1/30	Taxable	1.78
2000-B-2	1999	12,000,000	9/1/30	Exempt	.21
2000-A-4	1999	7,100,000	9/1/30	Exempt	.19
2001-A-1	1999	6,400,000	9/1/31	Exempt	.19
2003-A-1	1999	51,300,000	9/1/33	Taxable	1.79
2003-A-2	1999	22,000,000	9/1/33	Taxable	1.79
2003-B-1	1999	15,000,000	9/1/33	Taxable	1.93
2003-A-3	1999	12,400,000	9/1/33	Taxable	1.78
2004-A-1	2004	45,000,000	3/1/34	Exempt	.19
2004-B-1	2004	5,000,000	3/1/34	Exempt	.29
2004-A-2	1999	41,900,000	9/1/34	Taxable	1.79
2004-A-3	1999	2,000,000	9/1/34	Taxable	1.78
2004-A-4	1999	25,700,000	9/1/34	Taxable	1.78
2005-A-1	1999	68,700,000	9/1/35	Exempt	.21
2005-A-2	1999	5,000,000	9/1/35	Exempt	.21
2005-B-1	1999	18,800,000	9/1/35	Exempt	.21
2005-A-3	1999	29,300,000	9/1/35	Taxable	1.79
2005-A-4	1999	34,500,000	9/1/35	Taxable	1.78
2005-A-5	1999	5,500,000	9/1/35	Taxable	1.78
2006-A-1	1999	85,700,000	9/1/36	Exempt	.18
2006-A-2	1999	19,000,000	9/1/36	Exempt	.21
2006-B-1	1999	14,300,000	9/1/36	Exempt	.18
2007-A-1	2004	61,150,000	3/1/37	Exempt	.21
2007-A-2	2004	20,900,000	3/1/37	Exempt	.18
2007-B-1	2004	12,300,000	3/1/37	Exempt	.32

\$ 962,250,000

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**NOTES TO COMBINED FINANCIAL STATEMENTS
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NOTE 7 - BONDS AND NOTES PAYABLE - CONTINUED:

At December 31, 2011, remaining maturities and sinking fund redemptions of bonds and notes are as follows:

2012 - 2015	\$ -
2016	23,100,000
2026 - 2037	<u>939,150,000</u>
	<u>\$ 962,250,000</u>

All of MHEAC's bonds and notes outstanding are auction rate securities that are subject to auction primarily at 28-day and 35-day intervals. Since mid-February 2008, the normal functioning of the auction market for certain types of auction rate securities in the U.S. has been severely disrupted. This disruption has affected issuers of auction rate securities across broad sectors of the credit markets. Substantially all of MHEAC's auctions occurring since February 11, 2008 have failed to clear, resulting in the interest rates for those auction rate securities being calculated at the maximum rate.

For taxable notes, MHEAC accrues and pays interest at the lower of the maximum rate and the net loan rate for each interest period. The net loan rate is computed periodically in accordance with the terms of the related indentures. If the maximum rate exceeds the net loan rate for an interest period, then carry-over is calculated. Carry-over is calculated by determining the amount of interest that would have been accrued for the interest period if the maximum rate had been used, less the amount of interest that was accrued for the period using the net loan rate. The payment, if any, of cumulative carry-over amounts is governed by the related indentures. At December 31, 2011 and 2010, MHEAC determined that the cumulative amount of carry-over was approximately \$6,156,000 and \$4,849,000, respectively. MHEAC does not expect any indenture carry-over payment events to occur and, accordingly, cumulative carry-over amounts are not reflected in the statement of financial position. During the years ended December 31, 2011 and 2010, the average annual expense rate for bonds and notes was approximately 1.10% and 1.28%, respectively.

NOTE 8 - SUPPLEMENTAL INFORMATION ON NONCASH OPERATING, INVESTING, AND FINANCING ACTIVITIES

MHEAC and ESF have capitalized certain amounts of accrued interest income on student loans and included the amounts in student loans receivable. For the years ended December 31, 2011 and 2010, capitalized interest was approximately \$15,718,000 and \$16,608,000, respectively.

During the years ended December 31, 2011 and 2010, MHEAC settled approximately \$3,080,000 and \$513,000, respectively, of its excess interest liability through the forgiveness of student loan principal and accrued interest.

**MISSISSIPPI HIGHER EDUCATION ASSISTANCE CORPORATION
AND EDUCATION SERVICES FOUNDATION**

**NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

NOTE 9 - RETIREMENT PLAN

ESF has a 403(b) deferred compensation plan that covers substantially all employees. Participating employees may contribute up to the maximum dollar amount permitted by law. ESF's board of directors annually determines the amount of an employee's contributions that ESF will match. For the years ended December 31, 2011 and 2010, the first 6% of an employee's eligible compensation contributed by the employee was matched by ESF at 100%. For 2011 and 2010, ESF's match was \$82,072 and \$125,113, respectively.

NOTE 10 - COMMITMENTS AND CONTINGENCIES

ESF had contracts with clients to provide origination and servicing of loans in the FFELP prior to July 1, 2010. The loans serviced by ESF were for borrowers that had not begun repayment. Under the servicing agreements, ESF generally agreed to reimburse clients for any claims or losses that arose out of or related to ESF's acts or omissions with respect to services provided under such agreements.

In the normal course of business, MHEAC and ESF are subject to consumer credit disputes and potential litigation. Management is not aware of any consumer credit disputes or potential litigation which it believes is likely to have a material adverse effect on MHEAC and ESF.

NOTE 11 - GAINS ON EXTINGUISHMENT OF DEBT

During the years ended December 31, 2011 and 2010, MHEAC used available cash to retire bonds and notes for less than their carrying value, resulting in gains net of expenses of \$10,953,602 and \$6,115,918, respectively.

NOTE 12 - SUBSEQUENT EVENTS

From January 1, 2012 through March 28, 2012, MHEAC used available cash to retire bonds and notes for less than their carrying value, resulting in a gain net of expenses of approximately \$943,000.

Except as disclosed above, MHEAC and ESF had no subsequent events of a material nature requiring disclosure in the financial statements through March 28, 2012, the date the financial statements were approved by MHEAC's and ESF's management and thereby available to be issued.

SUPPLEMENTAL INFORMATION

**MISSISSIPPI HIGHER EDUCATION ASSISTANCE CORPORATION (MHEAC)
AND EDUCATION SERVICES FOUNDATION (ESF)**

**COMBINING STATEMENT OF FINANCIAL POSITION
DECEMBER 31, 2011**

	<u>MHEAC</u>	<u>ESF</u>	<u>Eliminations</u>	<u>Total</u>
<u>ASSETS</u>				
Cash and cash equivalents	\$ 131,804,412	7,447,259	-	139,251,671
Investments	54,269,140	-	-	54,269,140
Student loans receivable	907,712,215	-	(777,207)	906,935,008
Interest and special allowance receivable	15,370,170	-	-	15,370,170
Deferred costs of issuance less accumulated amortization	4,735,653	-	-	4,735,653
Other assets	<u>116,849</u>	<u>886,325</u>	<u>(572,522)</u>	<u>430,652</u>
Total assets	\$ <u>1,114,008,439</u>	<u>8,333,584</u>	<u>(1,349,729)</u>	<u>1,120,992,294</u>
<u>LIABILITIES AND UN- RESTRICTED NET ASSETS</u>				
LIABILITIES:				
Accounts payable and accrued expenses	\$ 1,362,964	817,963	(572,522)	1,608,405
Accrued interest payable	766,054	-	-	766,054
Excess interest and rebate payable	10,918,601	-	-	10,918,601
Bonds and notes payable	<u>962,250,000</u>	<u>-</u>	<u>-</u>	<u>962,250,000</u>
Total liabilities	<u>975,297,619</u>	<u>817,963</u>	<u>(572,522)</u>	<u>975,543,060</u>
UNRESTRICTED NET ASSETS:				
Bond and note funds	112,097,446	-	(777,207)	111,320,239
General fund	<u>26,613,374</u>	<u>7,515,621</u>	<u>-</u>	<u>34,128,995</u>
Total unrestricted net assets	<u>138,710,820</u>	<u>7,515,621</u>	<u>(777,207)</u>	<u>145,449,234</u>
Total liabilities and unrestricted net assets	\$ <u>1,114,008,439</u>	<u>8,333,584</u>	<u>(1,349,729)</u>	<u>1,120,992,294</u>

**MISSISSIPPI HIGHER EDUCATION ASSISTANCE CORPORATION (MHEAC)
AND EDUCATION SERVICES FOUNDATION (ESF)**

**COMBINING STATEMENT OF ACTIVITIES AND
CHANGES IN UNRESTRICTED NET ASSETS
FOR THE YEAR ENDED DECEMBER 31, 2011**

	<u>MHEAC</u>	<u>ESF</u>	<u>Eliminations</u>	<u>Total</u>
INTEREST INCOME:				
Interest on student loans	\$ 20,241,762	-	318,437	20,560,199
Interest subsidy	5,315,680	-	-	5,315,680
Special allowance	(8,242,820)	76	-	(8,242,744)
Late fees	<u>305,199</u>	<u>-</u>	<u>-</u>	<u>305,199</u>
Student loans	17,619,821	76	318,437	17,938,334
Interest on investments	<u>525,754</u>	<u>11,573</u>	<u>-</u>	<u>537,327</u>
Total interest income	<u>18,145,575</u>	<u>11,649</u>	<u>318,437</u>	<u>18,475,661</u>
INTEREST COST:				
Interest expense	10,792,052	-	-	10,792,052
Bond and note fees	605,310	-	-	605,310
Amortization of deferred costs of issuance	<u>251,502</u>	<u>-</u>	<u>-</u>	<u>251,502</u>
Total interest cost	<u>11,648,864</u>	<u>-</u>	<u>-</u>	<u>11,648,864</u>
Net interest revenue	6,496,711	11,649	318,437	6,826,797
PROVISION FOR LOAN LOSSES	<u>170,708</u>	<u>-</u>	<u>-</u>	<u>170,708</u>
Net interest revenue after provision for loan losses	<u>6,326,003</u>	<u>11,649</u>	<u>318,437</u>	<u>6,656,089</u>
OTHER REVENUE (EXPENSE):				
Program services revenue	-	8,442,844	(8,361,577)	81,267
Program services expense	(6,013,117)	(5,146,929)	7,040,612	(4,119,434)
Support services expense	<u>(2,348,460)</u>	<u>(1,189,395)</u>	<u>1,320,965</u>	<u>(2,216,890)</u>
Total other revenue (expense)	<u>(8,361,577)</u>	<u>2,106,520</u>	<u>-</u>	<u>(6,255,057)</u>
INCREASE (DECREASE) IN UNRESTRICTED NET ASSETS BEFORE GAINS ON EXTINGUISHMENT OF DEBT	(2,035,574)	2,118,169	318,437	401,032
Gains on extinguishment of debt	<u>10,953,602</u>	<u>-</u>	<u>-</u>	<u>10,953,602</u>
INCREASE IN UNRESTRICTED NET NET ASSETS	8,918,028	2,118,169	318,437	11,354,634
UNRESTRICTED NET ASSETS, BEGINNING OF PERIOD	<u>129,792,792</u>	<u>5,397,452</u>	<u>(1,095,644)</u>	<u>134,094,600</u>
UNRESTRICTED NET ASSETS, END OF PERIOD	<u>\$ 138,710,820</u>	<u>7,515,621</u>	<u>(777,207)</u>	<u>145,449,234</u>

**MISSISSIPPI HIGHER ASSISTANCE CORPORATION (MHEAC)
AND EDUCATION SERVICES FOUNDATION (ESF)**

**COMBINING STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2011**

	<u>MHEAC</u>	<u>ESF</u>	<u>Eliminations</u>	<u>Total</u>
RECEIPTS (DISBURSEMENTS) IN CASH AND CASH EQUIVALENTS:				
Cash flows from operating activities:				
Interest on student loans	\$ 11,414,359	-	-	11,414,359
Interest subsidy	5,594,021	450	-	5,594,471
Special allowance	(8,377,957)	76	-	(8,377,881)
Late fees	305,199	-	-	305,199
Interest on investments	664,540	11,718	-	676,258
Other program services revenue	-	8,464,776	(8,382,640)	82,136
Interest expense	(11,285,003)	-	-	(11,285,003)
Program and support services	(8,421,819)	(6,549,302)	8,382,640	(6,588,481)
Bond and note fees	<u>(405,973)</u>	<u>(1,334)</u>	<u>-</u>	<u>(407,307)</u>
Net cash provided (used) by operating activities	<u>(10,512,633)</u>	<u>1,926,384</u>	<u>-</u>	<u>(8,586,249)</u>
Cash flows from investing activities:				
Additions to equipment	-	(229,778)	-	(229,778)
Collection of student loan principal	107,396,888	-	-	107,396,888
Purchases of student loan principal	(4,451,786)	-	-	(4,451,786)
Investments matured/redeemed	<u>11,966,682</u>	<u>-</u>	<u>-</u>	<u>11,966,682</u>
Net cash provided (used) by investing activities	<u>114,911,784</u>	<u>(229,778)</u>	<u>-</u>	<u>114,682,006</u>
Cash flows from financing activities:				
Collection of excess and rebate interest liability	1,327,036	-	-	1,327,036
Payment of rebate interest	(131,859)	-	-	(131,859)
Payments to redeem bonds and notes	<u>(159,363,014)</u>	<u>-</u>	<u>-</u>	<u>(159,363,014)</u>
Net cash provided (used) by financing activities	<u>(158,167,837)</u>	<u>-</u>	<u>-</u>	<u>(158,167,837)</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(53,768,686)	1,696,606	-	(52,072,080)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	<u>185,573,098</u>	<u>5,750,653</u>	<u>-</u>	<u>191,323,751</u>
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ <u>131,804,412</u>	<u>7,447,259</u>	<u>-</u>	<u>139,251,671</u>

**MISSISSIPPI HIGHER ASSISTANCE CORPORATION (MHEAC)
AND EDUCATION SERVICES FOUNDATION (ESF)**

**COMBINING STATEMENT OF CASH FLOWS - CONTINUED:
FOR THE YEAR ENDED DECEMBER 31, 2011**

	<u>MHEAC</u>	<u>ESF</u>	<u>Eliminations</u>	<u>Total</u>
RECONCILIATION OF INCREASE IN UNRESTRICTED NET ASSETS TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:				
Increase in unrestricted net assets	\$ <u>8,918,028</u>	<u>2,118,169</u>	<u>318,437</u>	<u>11,354,634</u>
Adjustments to reconcile increase in unrestricted net assets to net cash provided (used) by operating activities:				
Amortization and depreciation	5,571,761	96,970	(318,437)	5,350,294
Capitalized interest on student loans	(15,717,953)	-	-	(15,717,953)
Provision for loan losses	170,708	-	-	170,708
Gains on extinguishment of debt	(10,953,602)	-	-	(10,953,602)
Decrease in interest and special allowance receivable	1,852,281	594	-	1,852,875
Decrease in other assets	124,097	86,812	-	210,909
Increase (decrease) in accounts payable	14,999	(376,161)	-	(361,162)
Decrease in accrued interest payable	<u>(492,952)</u>	<u>-</u>	<u>-</u>	<u>(492,952)</u>
Total adjustments	<u>(19,430,661)</u>	<u>(191,785)</u>	<u>(318,437)</u>	<u>(19,940,883)</u>
Net cash provided (used) by operating activities	\$ <u>(10,512,633)</u>	<u>1,926,384</u>	<u>-</u>	<u>(8,586,249)</u>

MISSISSIPPI HIGHER EDUCATION ASSISTANCE CORPORATION

**COMBINING STATEMENT OF FINANCIAL POSITION
DECEMBER 31, 2011**

	<u>1993</u>	<u>1996</u>	<u>1999</u>	<u>2004</u>	<u>General</u>	<u>Eliminations</u>	<u>Total</u>
	<u>Indenture</u>	<u>Indenture</u>	<u>Indenture</u>	<u>Indenture</u>	<u>Fund</u>		
<u>ASSETS</u>							
Cash and cash equivalents	\$ 24,815,477	33,512,735	47,392,486	18,032,783	8,050,931	-	131,804,412
Investments	43,093,992	1,843,137	8,388,511	943,500	13,000,000	(13,000,000)	54,269,140
Student loans receivable	8,042,282	85,564,290	686,808,550	123,454,898	3,842,195	-	907,712,215
Interest and special allowance receivable	443,968	1,389,826	9,614,255	3,883,993	40,719	(2,591)	15,370,170
Deferred costs of issuance less accumulated amortization	283,297	499,604	3,109,697	715,041	128,014	-	4,735,653
Other assets	<u>(76,475)</u>	<u>(409,034)</u>	<u>(582,263)</u>	<u>(940,636)</u>	<u>2,125,257</u>	<u>-</u>	<u>116,849</u>
Total assets	<u>\$ 76,602,541</u>	<u>122,400,558</u>	<u>754,731,236</u>	<u>146,089,579</u>	<u>27,187,116</u>	<u>(13,002,591)</u>	<u>1,114,008,439</u>
<u>LIABILITIES AND UNRESTRICTED NET ASSETS</u>							
LIABILITIES:							
Accounts payable and accrued expenses	\$ 24,083	87,239	659,497	18,403	573,742	-	1,362,964
Accrued interest payable	57,099	78,592	502,852	130,102	-	(2,591)	766,054
Excess interest and rebate payable	4,443,601	-	6,475,000	-	-	-	10,918,601
Bonds and notes payable	<u>64,800,000</u>	<u>101,900,000</u>	<u>664,200,000</u>	<u>144,350,000</u>	<u>-</u>	<u>(13,000,000)</u>	<u>962,250,000</u>
Total liabilities	69,324,783	102,065,831	671,837,349	144,498,505	573,742	(13,002,591)	975,297,619
UNRESTRICTED NET ASSETS	<u>7,277,758</u>	<u>20,334,727</u>	<u>82,893,887</u>	<u>1,591,074</u>	<u>26,613,374</u>	<u>-</u>	<u>138,710,820</u>
Total liabilities and unrestricted net assets	<u>\$ 76,602,541</u>	<u>122,400,558</u>	<u>754,731,236</u>	<u>146,089,579</u>	<u>27,187,116</u>	<u>(13,002,591)</u>	<u>1,114,008,439</u>

MISSISSIPPI HIGHER EDUCATION ASSISTANCE CORPORATION

**COMBINING STATEMENT OF ACTIVITIES AND
CHANGES IN UNRESTRICTED NET ASSETS
FOR THE YEAR ENDED DECEMBER 31, 2011**

	<u>1993</u> <u>Indenture</u>	<u>1996</u> <u>Indenture</u>	<u>1999</u> <u>Indenture</u>	<u>2004</u> <u>Indenture</u>	<u>General</u> <u>Fund</u>	<u>Eliminations</u>	<u>Total</u>
INTEREST INCOME:							
Interest on student loans	\$ (494,187)	2,510,762	13,504,421	4,691,076	29,690	-	20,241,762
Interest subsidy	70,907	436,489	3,169,942	1,630,913	7,429	-	5,315,680
Special allowance	39,924	(2,752)	(3,819,216)	(4,477,310)	16,534	-	(8,242,820)
Late fees	<u>9,921</u>	<u>47,331</u>	<u>217,801</u>	<u>28,608</u>	<u>1,538</u>	<u>-</u>	<u>305,199</u>
Student loans	(373,435)	2,991,830	13,072,948	1,873,287	55,191	-	17,619,821
Interest on investments	<u>331,548</u>	<u>29,562</u>	<u>128,436</u>	<u>2,878</u>	<u>91,701</u>	<u>(58,371)</u>	<u>525,754</u>
Total interest income	<u>(41,887)</u>	<u>3,021,392</u>	<u>13,201,384</u>	<u>1,876,165</u>	<u>146,892</u>	<u>(58,371)</u>	<u>18,145,575</u>
INTEREST COST:							
Interest expense	239,238	1,622,482	8,425,719	562,984	-	(58,371)	10,792,052
Bond and note fees	77,961	146,200	308,529	71,620	1,000	-	605,310
Amortization of deferred costs of issuance	<u>25,263</u>	<u>31,260</u>	<u>157,077</u>	<u>32,127</u>	<u>5,775</u>	<u>-</u>	<u>251,502</u>
Total interest cost	<u>342,462</u>	<u>1,799,942</u>	<u>8,891,325</u>	<u>666,731</u>	<u>6,775</u>	<u>(58,371)</u>	<u>11,648,864</u>
Net interest revenue (expense)	(384,349)	1,221,450	4,310,059	1,209,434	140,117	-	6,496,711
PROVISION FOR LOAN LOSSES	<u>(4,154)</u>	<u>23,865</u>	<u>53,246</u>	<u>97,770</u>	<u>(19)</u>	<u>-</u>	<u>170,708</u>
Net interest revenue (expense) after provision for loan losses	<u>(380,195)</u>	<u>1,197,585</u>	<u>4,256,813</u>	<u>1,111,664</u>	<u>140,136</u>	<u>-</u>	<u>6,326,003</u>
OTHER REVENUE (EXPENSE):							
Program and support services	<u>(80,986)</u>	<u>(475,859)</u>	<u>(3,547,134)</u>	<u>(881,564)</u>	<u>(3,376,034)</u>	<u>-</u>	<u>(8,361,577)</u>
Total other revenue (expense)	<u>(80,986)</u>	<u>(475,859)</u>	<u>(3,547,134)</u>	<u>(881,564)</u>	<u>(3,376,034)</u>	<u>-</u>	<u>(8,361,577)</u>
INCREASE (DECREASE) IN UN- RESTRICTED NET ASSETS BEFORE GAINS ON EXTING- UISHMENT OF DEBT	(461,181)	721,726	709,679	230,100	(3,235,898)	-	(2,035,574)
GAINS ON EXTINGUISHMENT OF DEBT	<u>180,138</u>	<u>26,031</u>	<u>8,925,665</u>	<u>1,821,768</u>	<u>-</u>	<u>-</u>	<u>10,953,602</u>
INCREASE (DECREASE) IN UN- RESTRICTED NET ASSETS	(281,043)	747,757	9,635,344	2,051,868	(3,235,898)	-	8,918,028
UNRESTRICTED NET ASSETS, BEGINNING OF PERIOD	7,558,801	19,530,485	61,746,142	(496,651)	41,454,015	-	129,792,792
TRANSFERS IN (OUT)	<u>-</u>	<u>56,485</u>	<u>11,512,401</u>	<u>35,857</u>	<u>(11,604,743)</u>	<u>-</u>	<u>-</u>
UNRESTRICTED NET ASSETS, END OF PERIOD	<u>\$ 7,277,758</u>	<u>20,334,727</u>	<u>82,893,887</u>	<u>1,591,074</u>	<u>26,613,374</u>	<u>-</u>	<u>138,710,820</u>