# MAINE EDUCATIONAL LOAN AUTHORITY

## Annual Report

2012

MELA[SM]

131 Presumpscot Street, Portland, ME 04103 ♦ 207-791-3600 ♦ 1-800-922-6352 ♦ fax 207-791-3616 ♦ www.mela.net

April 26, 2013

Governor Paul R. LePage
State of Maine
Office of the Governor
1 State House Station
Augusta, ME 04333-0001

Dear Governor LePage:

Pursuant to 20-A M.R.S.A., Chapter 417-A, Section 11427, enclosed is a copy of the Maine Educational Loan Authority's (MELA) annual report for the fiscal year January 1, 2012 through December 31, 2012.

MELA's annual report includes the following sections: introduction and background information; program administration (loan origination and servicing); application volume and distribution; loan volume; borrower distribution; financial counseling and literacy; summary; charts and graphs to illustrate the narrative contained within the report; and basic financial statements with management discussion and analysis.

MELA was established in 1988 to assist Maine students and their families in achieving their higher education goals by providing a supplemental or alternative student loan program. MELA's supplemental student loan program currently consists of The Maine Loan® and The Maine Medical Loan℠. The Maine Loan, MELA's primary student loan product, exists to bridge the gap between the full cost of undergraduate and graduate higher education and other traditional financial aid resources such as scholarships, grants, and the Federal education loan programs. The Maine Medical Loan was created in 1998 to assist Maine students pursuing a Doctor of Medicine (MD) or Doctor of Osteopathic Medicine (DO) degree. MELA expanded the scope of its medical loan program in 2002 to include other degrees such as dentistry, chiropractic, and veterinary medicine. This loan program is available to eligible medical students to borrow funds up to the full cost of a medical degree less other financial aid.

Students attending Maine's public and private institutions of higher education continue to be the greatest beneficiaries of MELA loans. MELA's loan volume in 2012 was approximately $8,045,000 in originations, which is a decrease of 23% when compared with the approximate $10,481,000 originated in fiscal year 2011.

Several factors have contributed to the decrease in loan volume for MELA and many other lenders with alternative education loan programs. The most significant factors include: 1) Federal legislation regarding the use of preferred lender lists by schools; 2) the requirement for interest only payments during in-school periods for MELA loans; 3) increased utilization of all Federal loans (including the PLUS Loans to supplement financial aid packages); and 4) low variable rate products available to students who have co-signers with



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exceptional credit. It is expected that there will be a continuing demand for supplemental student loans for a number of reasons, including the impact of the prolonged difficult economic conditions on state funding for higher education, employment opportunities, and individual wealth. In addition, the rising cost of attendance at higher education institutions requires increased borrowing by students and their families.

On June 14, 2012, MELA issued $12,685,000 in tax-exempt student loan revenue bonds. MELA's 2012 bond issue enabled the Authority to offer a lower fixed interest rate and to provide the continuity of funding to continue offering its student loan program. MELA offers the only fixed rate alternative loan program in Maine, where all approved borrowers receive the same interest rate. Most variable rate products have tiered rates based on credit scores, presence of a co-signer, and which repayment option is selected.

Baker Newman and Noyes LLC, an independent certified public accounting firm, recently completed MELA's financial audit for the 2012 fiscal year. In reviewing the financial statements, it is clear that the funds MELA has acquired with proceeds from tax-exempt bonds or obligations are being solely utilized for its alternative student loan program.

In summary, MELA looks forward to continuing to fulfill its mission of providing affordable supplemental education financing to assist Maine students and families in achieving their higher education goals. MELA considers it to be a privilege to continue to partner with the State of Maine in making a college education more accessible and affordable for its residents.

Your continued interest in and support of MELA is greatly appreciated.

Sincerely,

Shirley M. Erickson, Ph.D.
Executive Director

cc: President of the Senate
Speaker of the House
Members of the Joint Standing Committee on Education and Cultural Affairs
Members of the Maine Educational Loan Authority



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MAINE EDUCATIONAL LOAN AUTHORITY

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# Authority Members

**John C. Atkinson, *Chair***
*Retired*

**Anthony M. Payne, *Vice Chair***
*Director of Business Development* ~ Clark Insurance

**Barbara Campbell Harvey, *Secretary/Treasurer***
*Circulation/Technical Services Assistant* ~ Bowdoin College

**Daniel J. O'Halloran**
*Consultant* ~ Blue Point Financial

**Christopher Bell**
*Director of Financial Aid* ~ University of Maine at Presque Isle

**Betsy H. Libby**
*Dean of Student Services* ~ Central Maine Community College

**Neria R. Douglass**
*Treasurer* ~ State of Maine, Ex-Officio

# Mela Staff

**Shirley M. Erickson, Ph.D.**
***Executive Director***



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# 2012 Program Highlights

## I. Introduction and Background Information

The Maine Educational Loan Authority (MELA) is a quasi-governmental agency that was created and established by Maine legislation in April of 1988 (20-A M.R.S.A., Section 11414). MELA functions as an administratively independent authority within the current organizational structure of State government, and receives no appropriation from the Legislature for its operation. MELA is governed by a seven-member board appointed by the Governor and confirmed by the Legislature, except for the State Treasurer who serves as an ex-officio member.

MELA was established to assist students and their families in achieving their higher education goals by providing a supplemental or alternative student loan program. Alternative student loans exist to bridge the gap between the full cost of a higher education and traditional financial aid resources.

MELA's alternative student loan programs currently consist of The Maine Loan® and The Maine Medical Loan℠. The Maine Loan allows borrowers to borrow up to the full cost of an undergraduate or graduate education less other financial aid. This loan is available to Maine residents attending approved schools in the United States and Canada, and out-of-state students attending approved schools in Maine.

In 1998, MELA introduced The Maine Medical Loan, designed to assist Maine students pursuing a Doctor of Medicine or Doctor of Osteopathic Medicine Degree. On June 1, 2002 MELA expanded its medical loan program to include these additional degrees: Doctor of Chiropractic (DC), Doctor of Dental Medicine (DMD), Doctor of Optometry (OD), Doctor of Podiatric Medicine (DPM), Doctor of Veterinary Medicine (DVM) and Doctor of Dental Surgery or Doctor of Dental Science (DDS). The Maine Medical Loan allows borrowers to borrow up to the full cost of a medical program of study less other financial aid. This loan is available to Maine residents attending approved medical schools in the United States and Canada, and out-of-state students attending approved medical schools in Maine.

The Maine Loan and The Maine Medical Loan are available to students and their parents based on the credit-worthiness of the applicant(s). MELA's loan programs have many attractive features including a low fixed interest rate (currently 7.25% for The Maine Loan and The Maine Medical Loan), a low guarantee fee, no annual or aggregate borrowing limits, flexible repayment terms up to fifteen years, the ability to apply online, and personalized customer service based in Maine.

All MELA loans have historically been funded with the proceeds of tax-exempt bonds or obligations, and no State monies are allocated to fund the program. MELA secured its initial funds through a $35 million tax-exempt bond issue in July of 1988. In May of 1992, MELA refunded its initial offering and issued $60 million worth of tax-exempt bonds. An additional $12.5 million, $10 million, $14 million, and $10 million of tax-exempt bonds were issued in June of 1996, July of 1997, January of 1999, and September 2000, respectively. In November of 2002, MELA issued $26.9 million worth of tax-exempt bonds, including $16.9 million in refunding debt and $10 million in new money. MELA issued an additional $30 million worth of tax-exempt bonds in 2005 and an additional $50 million was issued in 2007.



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# 2012 Program Highlights

The wide spread turbulence in the capital markets adversely impacted MELA's ability to issue a bond in 2008. MELA had historically funded the origination of its student loans through debt issuances in the capital markets in the form of Auction Rate Securities (ARS). The ARS markets have closed down due to the volatility of the capital markets and movement of investors to safer investments.

In order to fund 2008-2009 academic year disbursements, MELA secured interim financing in the form of a $20 million tax-exempt line of credit with TD Bank, N.A. This interim financing required changes to the terms of MELA's loan programs, with the most significant change being the elimination of full principal and interest deferment for The Maine Loan borrowers. Principal payments continue to be deferred while the student is enrolled at least half-time, but interest payments are now required while the student is in school. This change was a nationwide shift in the student loan industry and is in the best interest of the student to reduce the overall cost of repaying their loans.

MELA issued $210 million in tax-exempt fixed-rate bonds in May 2009. The proceeds from the 2009 bond issue were used to refund $136,500,000 of ARS and $15,750,000 outstanding on the tax-exempt line of credit, as well as provide additional funds for new loan disbursements and reserves. MELA's 2009 bond issue was the first tax-exempt bond issue secured solely by alternative loans since the fall of 2008.

On July 29, 2010, MELA issued $15,460,000 in tax-exempt student loan revenue bonds. MELA's 2010 bond issue provided the Authority with the continuity of funding to continue its student loan program and to begin offering fixed interest rate student loans. Unlike the variable rate loan products offered by some national student loan providers, MELA's fixed rate loans offer borrowers more stability regarding their interest rate and payment amount during uncertain economic times.

MELA did not issue any tax-exempt bonds in 2011. In lieu of a 2011 bond issue, MELA received approval from its bond insurer to use recycling payments received on loans funded with the 2009 and 2010 bond proceeds to fund new loans for the 2011-2012 academic year. MELA found that the pricing for a new bond issue would have been significantly higher than in 2010 due primarily to weaker bond markets and the expiration of the Alternative Minimum Tax holiday for tax-exempt Private Activity Bonds. The increased financing costs would have translated into a higher interest rate on MELA's loans for Maine students and families. This recycling option allowed MELA to continue to offer the same interest rate and loan terms for the 2011-2012 academic year that were available in 2010-2011.

On June 14, 2012, MELA issued $12,685,000 in tax-exempt student loan revenue bonds. MELA's 2012 bond issue enabled the Authority to offer a lower fixed interest rate and to provide the continuity of funding to continue offering its student loan program. MELA offers the only fixed rate alternative loan program in Maine, where all approved borrowers receive the same interest rate. Most variable rate products have tiered rates based on credit scores, presence of a co-signer, and which repayment option is selected.

MELA has disbursed alternative student loans totaling over $281.7 million (Table 1) since the Authority was established in 1988.



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# 2012 Program Highlights

## II. PROGRAM ADMINISTRATION: LOAN ORIGINATION AND SERVICING

The Maine Educational Loan Authority (MELA) currently has two primary contractual relationships for the administration of its programs and services. MELA contracts with Maine Education Services (MES) for personnel, administrative and marketing services. MES, an independent, private non-profit corporation located in Portland, Maine, provides opportunities and resources for people to achieve higher education. In addition, MELA contracts with Firstmark Services, LLC, a wholly-owned subsidiary of Nelnet, for servicing of all MELA loans since 1996. Firstmark specializes in the servicing of alternative loans and has offices in Woodbury, Minnesota and Lincoln, Nebraska.

MES performs customer service and all responsibilities associated with the loan origination process including inquiry, application, approval or denial, and disbursement stages. In addition, MES manages all aspects of the existing loan servicing contracts including compliance with due diligence strategies, fulfillment of monetary contractual obligations, and monitoring the quality of customer service. MES provides administrative oversight to or directly performs the duties required of MELA in connection with the existing tax-exempt bonds and the issuance of new bonds. General financial advisory and support services are also provided to MELA by MES.

MELA recognizes that its borrowers are its most valuable asset. MELA's goal is to provide the best supplemental loan program in the country, and quality customer service is one of the most important components of any loan program. Monitoring the level of customer service provided to its borrowers has been of the utmost importance to MELA.

MELA has a very low annual default rate of approximately 1.0% as a percentage of loans in repayment. The MELA default rate has been historically low.

Customers continue to have access to their loan information by calling the toll free number 1-800-922-6352 or via MELA's website at www.mela.net.

## III. APPLICATION VOLUME AND DISTRIBUTION

MELA processed 1,300 loan applications for the 2012 calendar year (Table 2). The application information and materials are mailed to current and prospective borrowers each spring. It is important that students and their families are provided with application materials as early as possible so that they can have maximum latitude in determining their funding resources.

Since 1996, borrowers have been able to apply for loans directly online. The majority of borrowers are utilizing the online application process. MELA's loan approval rate has ranged between 47%-63% for applications received (Table 2), with an average approval rate of 52% for the most recent five year period. For 2012 the approval rate was 51%, a decrease from the 53% approval rate in 2011.



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# 2012 Program Highlights

## IV. LOAN VOLUME

MELA's loan volume decreased from the previous year with disbursements of approximately $8 million for 2012 compared with $10.4 million for 2011 (Table 3). During 2012, MELA made 1,308 loan disbursements resulting in an average disbursement size of $6,150.

Students attending Maine's public and private colleges and universities continue to be the greatest beneficiaries of MELA loans with fifty-four percent (54%) of all MELA funds disbursed in 2012 (Table 3).

Fifty-eight percent (58%) of MELA funds disbursed for this calendar year went to private schools (Table 4) compared to 60% in 2011. The average percentage of funds disbursed to private schools for the most recent five year period is 61%.

Table 5 reflects the cumulative percentage of funds disbursed between all public and private schools from 1988 to 2012. This breakdown, showing 38% of funds being used for public schools and 62% of funds for private schools is largely a reflection of the cost of attendance being higher for private institutions as compared to public institutions.

## V. BORROWER DISTRIBUTION

In the 2012 calendar year, as in the past, the majority of MELA disbursements (54%) have been made to Maine schools (Table 6). This calendar year shows MELA is serving more private than public schools inside Maine (Table 7). For out-of-state schools (Table 8), the percentage of disbursements to private and public schools has remained relatively consistent from the prior year.

## V. FINANCIAL COUNSELING AND LITERACY

MELA recognizes that with the increasing cost of higher education and challenging economic environment, many Maine families are faced with difficult financial challenges. With more reliance on student loans to pay for tuition and other educational costs, the need for students to understand the costs, risks, and benefits of the loans they use is critical for their future financial success.

MELA's dedicated certified financial counselors understand the daily challenges many customers face as they add student loan payments to their daily expenses. The Authority understands that default is avoidable and as such works hard to help borrowers avoid delinquency and default on their student loans.

In an effort to assist students in understanding the consequences of overborrowing, MELA has incorporated the Student Loan Game Plan℠ as a required part of all online student loan applications. This proactive step was taken to help students avoid situations where delinquency and default are more likely.

This interactive tool works to reduce student indebtedness by educating applicants and cosigners about responsible borrowing decisions and uses several methods to help borrowers avoid the dangers of the "borrow now and worry about it later" type of mentality. Utilizing customized estimated salary information based on the borrower's major and sample monthly budget numbers based on the borrower's anticipated starting salary and national-average expenses, the program allows students to review potential loan debt-to-income ratios.



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# 2012 Program Highlights

The Student Loan Game Plan highlights everyday challenges often caused by overborrowing and provides solutions to real risks. The program allows potential borrowers to reduce their requested loan amount before proceeding with the application and offers the ability to create and print a targeted action plan to reduce overall borrowing.

By educating students on how to borrow only what they can afford to repay, MELA encourages responsible borrowing during college, which is key to a sound financial future after graduation.

In December 2012, 43% of applicants reduced their loan amount an average of $4,658 after going through the module and 89% of applicants felt the information in the Student Loan Game Plan increased their understanding of how borrowing money today can affect their future.

## VI. SUMMARY

For the past 24 years, the Maine Educational Loan Authority (MELA) has provided over $281.7 million dollars in student loan disbursements primarily through The Maine Loan and The Maine Medical Loan programs.

By offering a high-quality alternative education loan program, MELA has assisted thousands of Maine students to achieve their goal of a higher education. As the State of Maine continues to work to increase the percentage of its residents possessing college degrees, MELA's student loan program will remain an important educational financing resource for Maine students and their families.

MELA looks forward to continuing to partner with the State of Maine and the higher education community to ensure that a college education is both accessible and affordable for Maine residents.



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# Charts and Graphs





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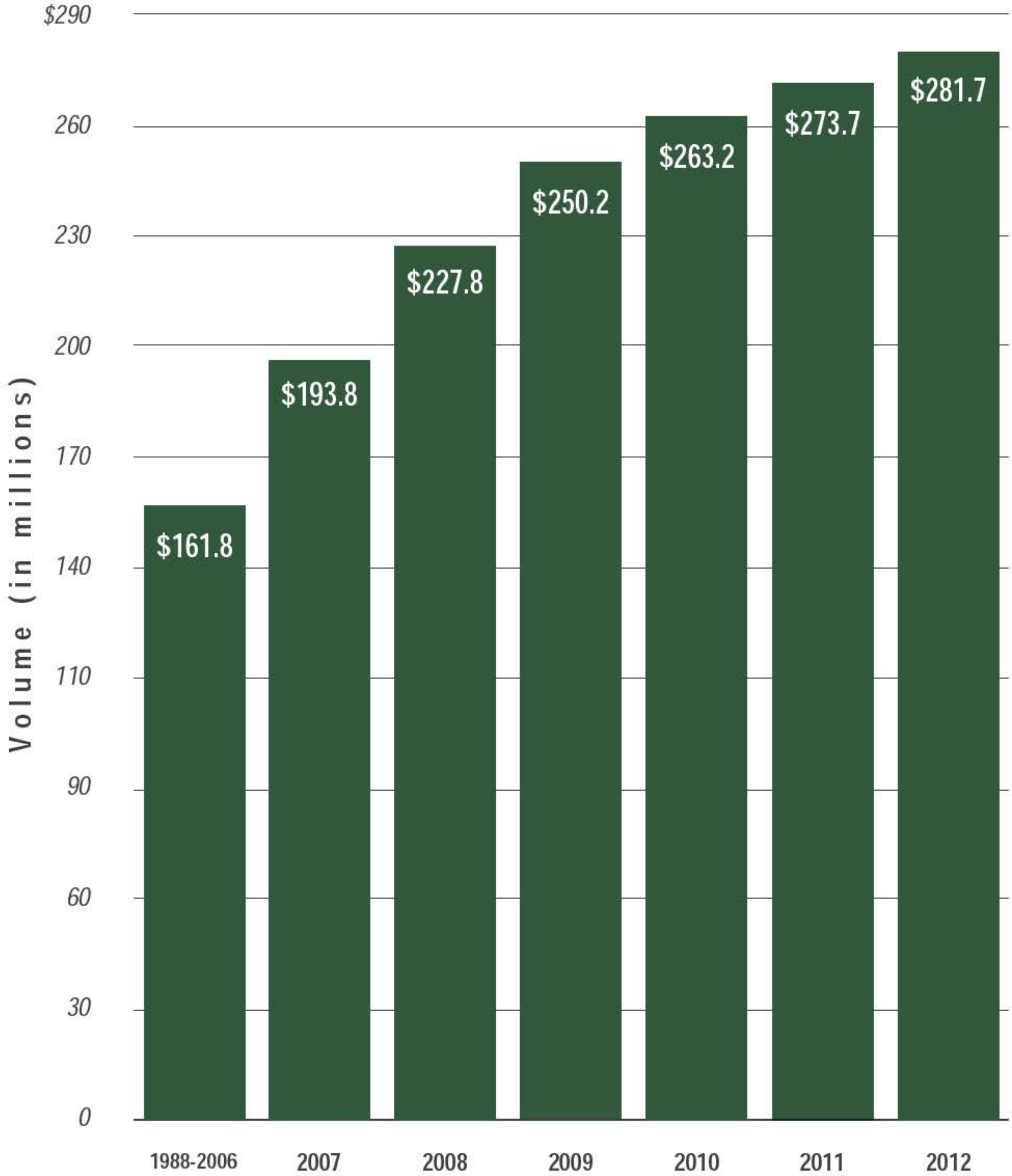
## Table 1 Total Loan Volume (1988-2012)



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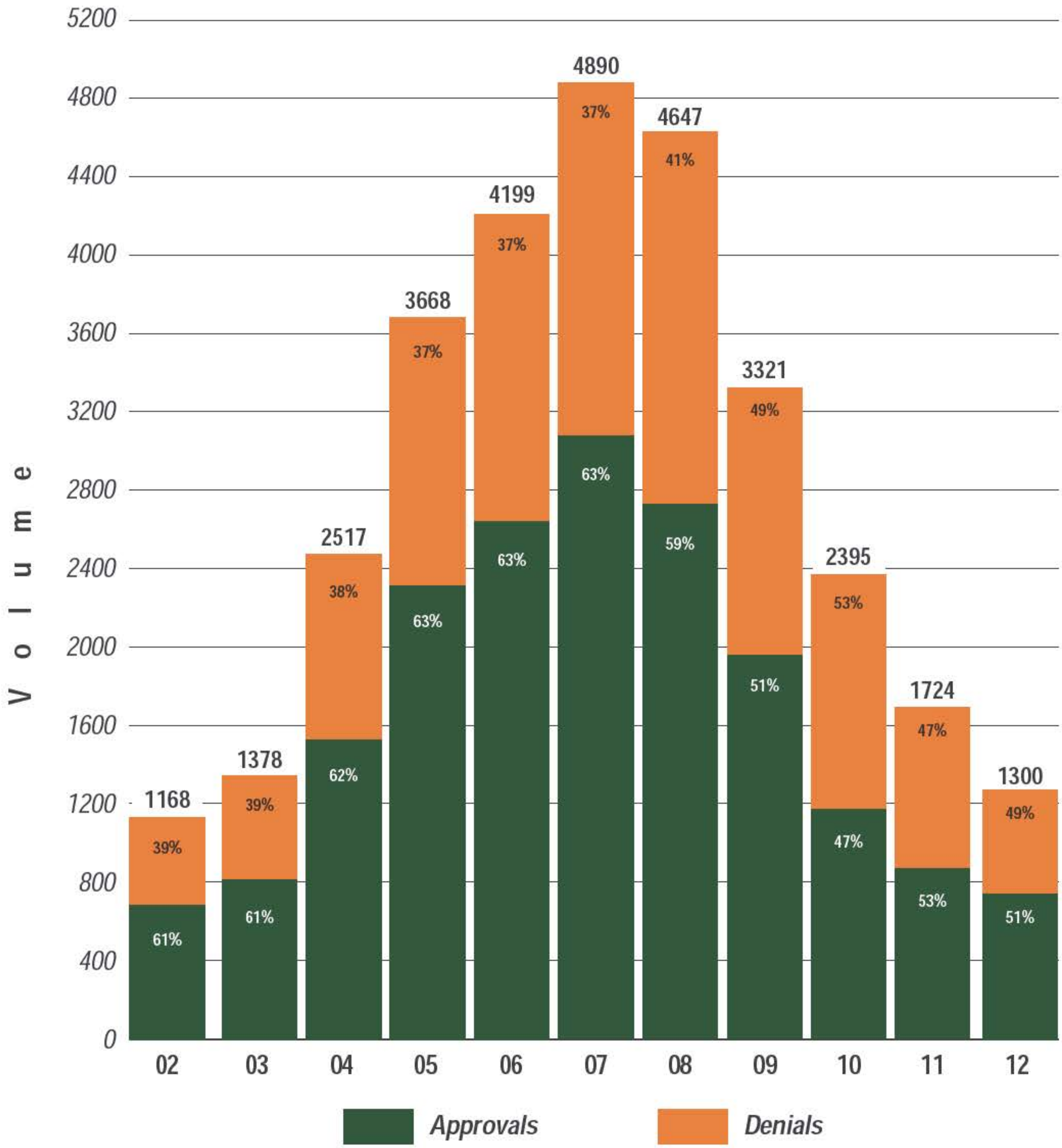
# Table 2 Application Volume By Loan Period (2002-2012)



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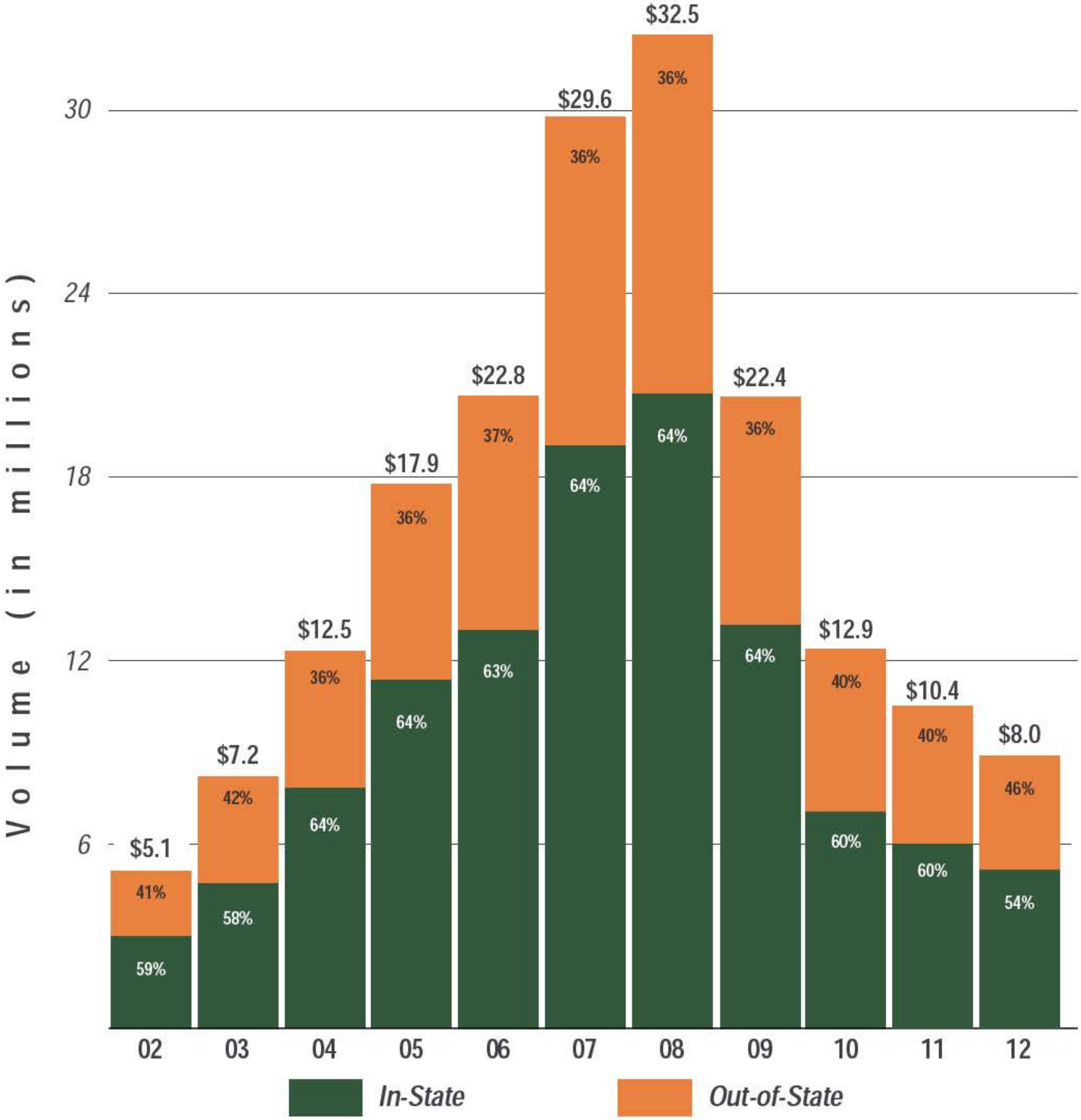
## Table 3

## Percentage of Funds Disbursed to In-State/Out-of-State Schools (2002-2012)




Note: MELA Private Consolidation volume of $928,047 in 2006, $2,356,830 in 2007, and $1,537,963 in 2008 is excluded.



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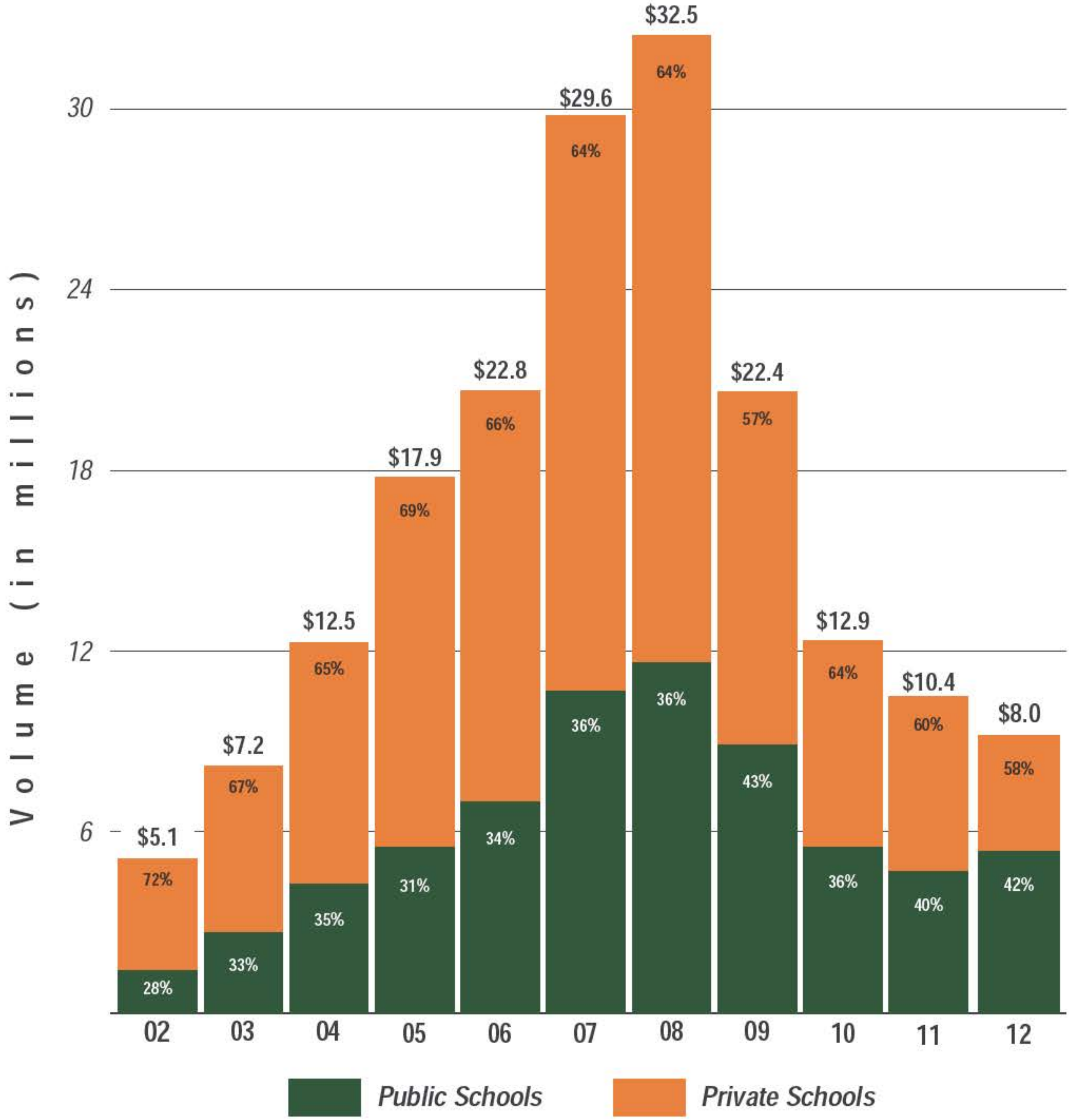
## Table 4

## Percentage of Funds Disbursed to Public/Private Schools (2002-2012)




Note: MELA Private Consolidation volume of $928,047 in 2006, $2,356,830 in 2007, and $1,537,963 in 2008 is excluded.



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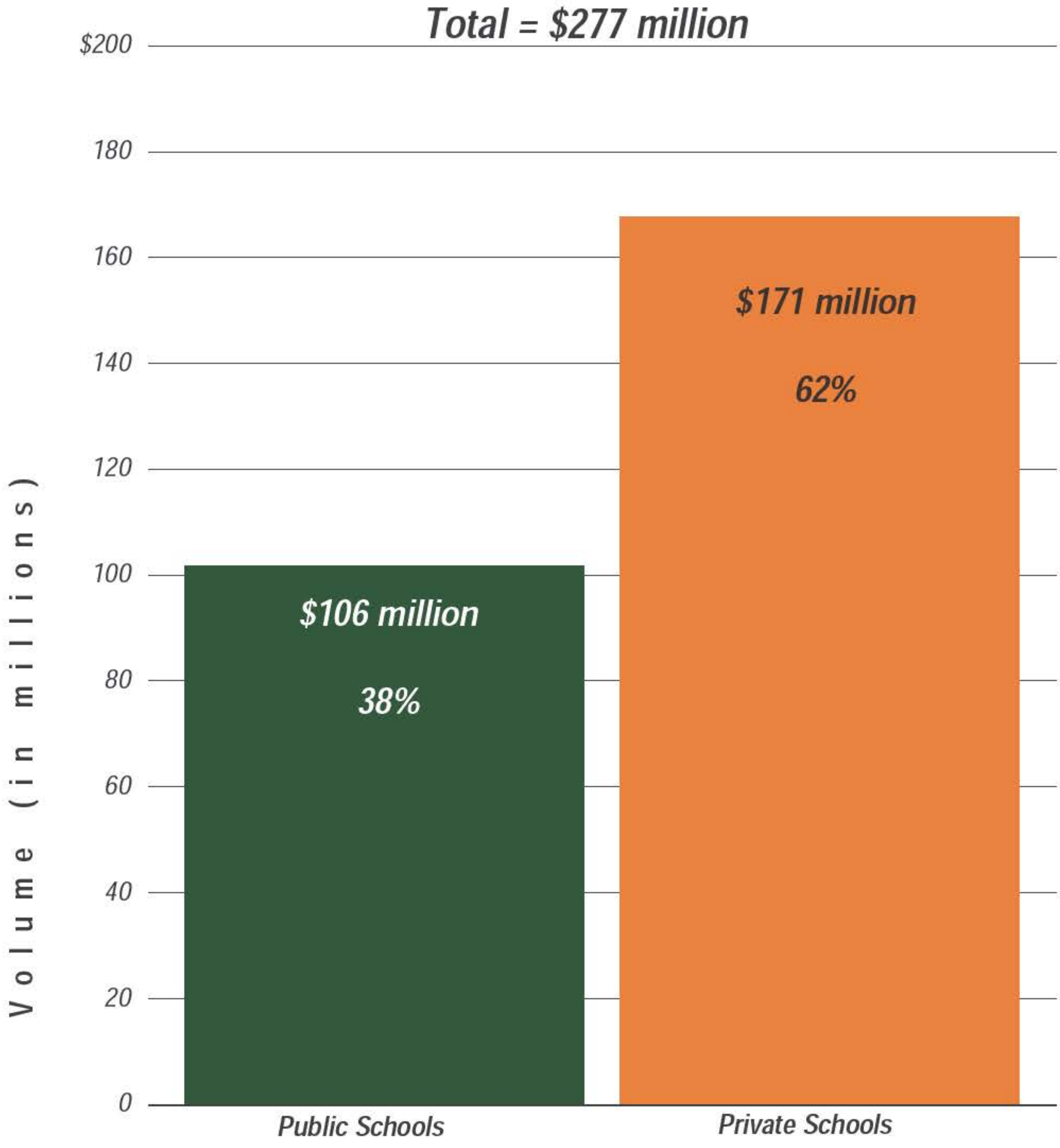
## Table 5 Cumulative Percentage of Funds Disbursed to Public/Private Schools (1988-2012)




Note: MELA Private Consolidation Loan volume of $4,822,840 is excluded.



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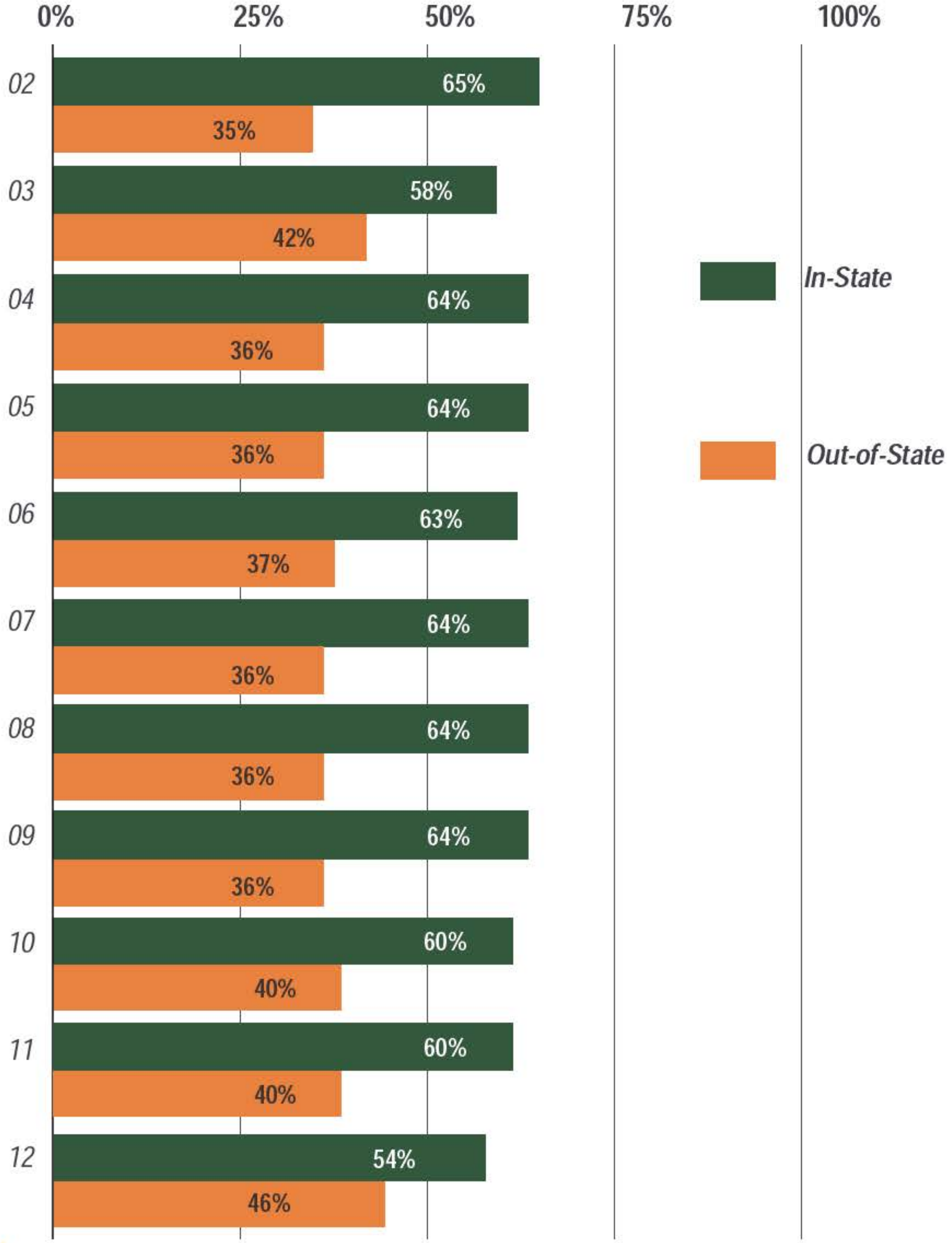
## Table 6 Percentage of Disbursements to In-State/Out-of-State Schools (2002-2012)



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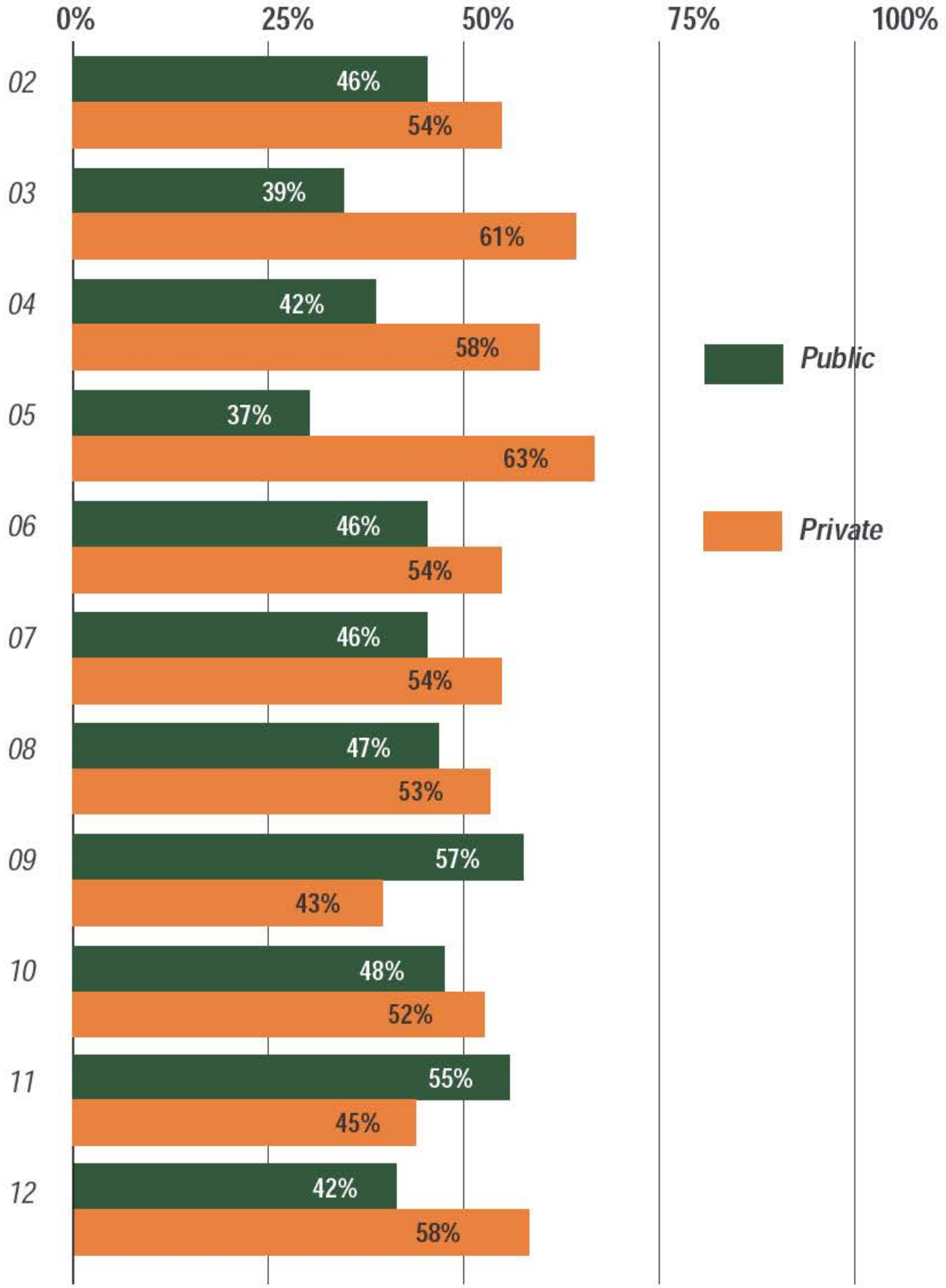
## Table 7 Percentage of Disbursements to Public/Private Maine Schools (2002-2012)



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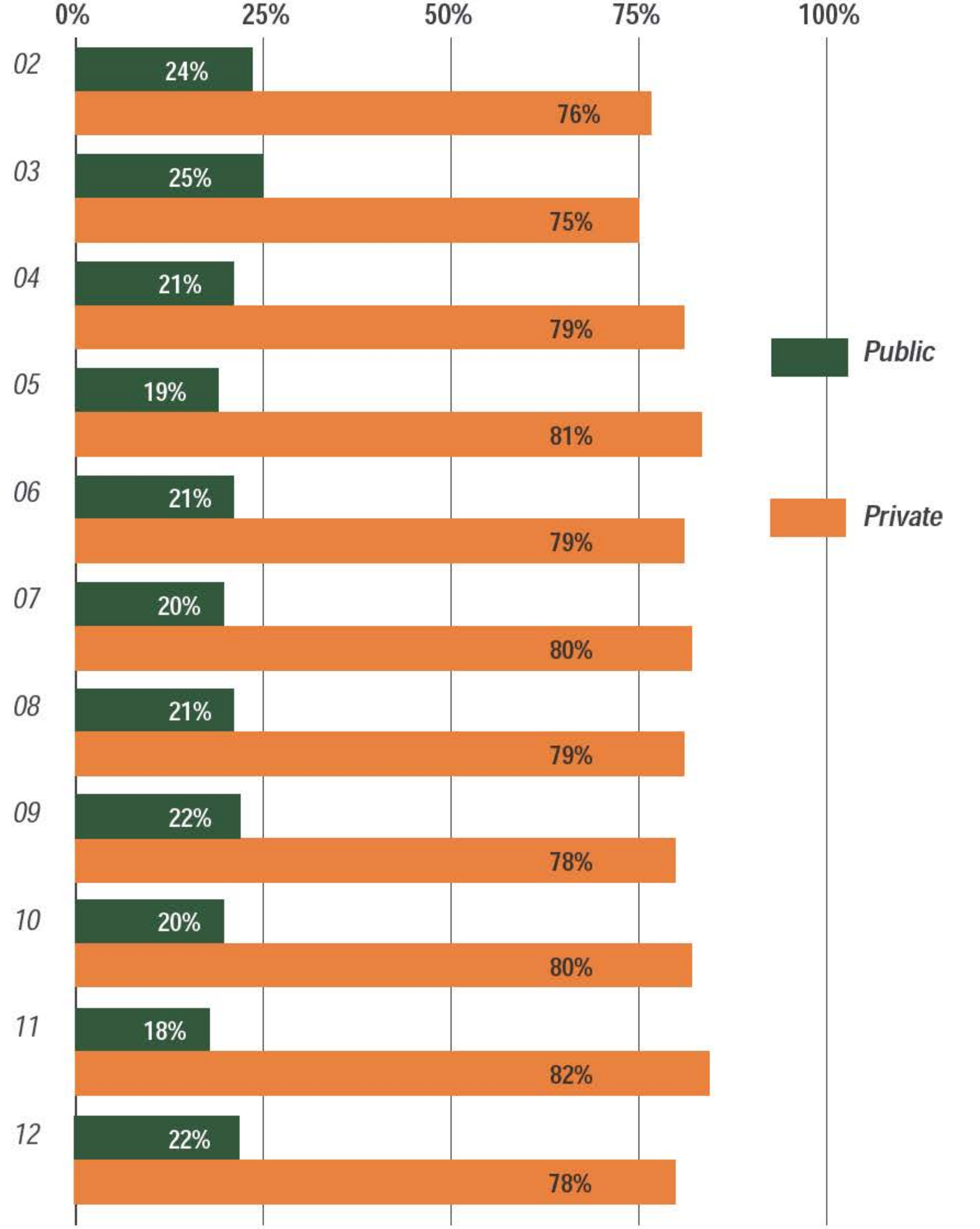
## Table 8 Percentage of Disbursements to Public/Private Out-of-State Schools (2002-2012)



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# FINANCIAL INFORMATION

BAKER | NEWMAN | NOYES
Certified Public Accountants

## Maine Educational Loan Authority
(A Component Unit of the State of Maine)

Basic Financial Statements and
Management's Discussion and Analysis
and Additional Information

*Years Ended December 31, 2012 and 2011*

INTEGRITY•SERVICE•SOLUTIONS



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BAKER NEWMAN NOYES

**INDEPENDENT AUDITORS' REPORT**

Members of the Authority
Maine Educational Loan Authority

We have audited the accompanying financial statements of the Maine Educational Loan Authority (the Authority), a Component Unit of the State of Maine, which comprise the statements of net position as of December 31, 2012 and 2011, and the related statements of revenues, expenses and changes in net position, and cash flows for the years then ended and the related notes to the financial statements.

***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

***Auditors' Responsibility***

Our responsibility is to express an opinion on these 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.



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Members of the Authority
Maine Educational Loan Authority

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Maine Educational Loan Authority as of December 31, 2012 and 2011, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

***Emphasis of Matter***

As discussed in Note 1, the Authority adopted the provisions of GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, and GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, in 2012.

***Other Matters***

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

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary information in Schedule 1 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 financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Baker Newman & Noyes
Limited Liability Company

Portland, Maine
April 12, 2013

As financial management of the Maine Educational Loan Authority (the Authority), we offer readers of these financial statements this narrative overview and analysis of the financial activities of the Authority for the fiscal years ended December 31, 2012 and 2011. This discussion and analysis is designed to assist the reader in focusing on the significant financial issues and activities of the Authority and to identify any significant changes in financial position. We encourage readers to consider the information presented here in conjunction with the basic financial statements as a whole.

**Overview of the Authority**

The Authority was created in 1988 by an Act of the Maine Legislature and is a public body corporate and politic constituting a public instrumentality of the State of Maine. The Authority was established to grant educational loans primarily using funds acquired through the issuance of long-term bonds payable. For financial reporting purposes the Authority is considered a component unit of the State of Maine, however, the Authority receives no appropriations from the State legislature. The Authority periodically receives allocations of the State's tax-exempt bond cap.

**Overview of the Financial Statements**

This discussion and analysis is intended to serve as an introduction to the Authority's financial statements, which is comprised of the basic financial statements and the notes to the financial statements. Since the Authority is comprised of a single enterprise fund, no fund level financial statements are shown.

**Basic Financial Statements**

The basic financial statements are designed to provide readers with a broad overview of the Authority's finances, in a manner similar to a private-sector business.

The statements of net position present information on all of the Authority's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Authority is improving or deteriorating. Net position increases when revenues exceed expenses. Increases to assets without a corresponding increase to liabilities, result in increased net position, which indicates an improved financial position.

The statements of revenues, expenses, and changes in net position present information showing how the Authority's net position changed during the fiscal year. This statement reports all revenues and expenses, and reconciles beginning and end of year net position balances.

**Notes to the Financial Statements**

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements.

**Financial Highlights – 2012**

- Operating loss for the Authority was $180,658 for fiscal year 2012, a decrease of $293,814 from the prior year operating income of $113,156, due mainly to a decrease in interest on educational loans.

- Net position decreased in 2012 solely as a result of the operating loss. The term "net position" refers to the difference between assets and deferred loss on refinancing and liabilities. At the close of fiscal year 2012, the Authority had net position of $3,456,724, a decrease of 5.0% from the prior year.
- The Authority's debt outstanding of $149,935,000 decreased $11,855,000 as a result of Series 2009 bond redemptions and scheduled bond maturities, which were partially offset by the issuance of the Series 2012 bonds.
- Loans originated during the year totaled approximately $8,384,000, down 23% from the $10,937,000 originated in fiscal year 2011.
- As a result of the early adopting of GASB Standard Number 65, *Items Previously Reported as Assets and Liabilities*, issued in March of 2012, MELA was required to write off certain previously deferred assets and liabilities. Furthermore, MELA was required to restate all prior year amounts reflected in its Financial Statements and Management Discussion and Analysis. The details and financial impact of these restatements are discussed in the accompanying Notes to Financial Statements in Note 1, Summary of Significant Accounting Policies. Financial presentations as of December 31, 2011 and for the year then ended have been restated to reflect the effect of this new accounting standard being implemented for that year.

**Financial Analysis – 2012**

Net position may serve, over time, as a useful indicator of a government's financial position. In the case of the Authority, assets exceeded liabilities by $3,456,724 at the close of the most recent fiscal year. This represents a decrease of $180,658 (5.0%) from the previous year. The unrestricted net position was $417,938 compared to restricted net position of $3,038,786. By far, the largest portion of the Authority's net position reflects its investment in educational loans plus bond proceeds remaining in trust investments less any related debt used to acquire those assets.

The Authority's financial position and operations for the past two years are summarized below based on information included in the financial statements.

| Net Position | 2012 | Restated 2011 | Percentage Change |
|---|---|---|---|
| Cash and investments | $ 18,397,298 | $ 19,812,879 | (7.1)% |
| Educational loans, net | 129,543,010 | 138,336,811 | (6.4) |
| Other assets | 3,616,254 | 5,414,338 | (33.2) |
| Total assets | $ 151,556,562 | $ 163,564,028 | (7.3) % |
| Deferred loss on refinancing | $ 1,104,471 | $ 1,191,726 | (7.3)% |
| Bonds payable, net | $ 148,392,752 | $ 160,234,371 | (7.4)% |
| Other liabilities | 811,557 | 884,001 | (8.2) |
| Total liabilities | $ 149,204,309 | $ 161,118,372 | (7.4)% |
| Restricted net position | $ 3,038,786 | $ 3,218,662 | (5.6)% |
| Unrestricted net position | 417,938 | 418,720 | (0.2) |
| Total net position | $ 3,456,724 | $ 3,637,382 | (5.0)% |



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The decrease in the Authority's cash and investments at December 31, 2012 from the balance at December 31, 2011 was mainly attributed to the redemptions of the Series 2009 bond issue and disbursements for the origination of educational loans in excess of loan repayments and the net proceeds from the Series 2012 bonds.

The Authority's educational loans, net, decreased $8,793,801 in 2012. The Authority's total loans originated and disbursed in 2012 was $8,384,059 compared to the $10,936,588 originated in 2011. The receipt of educational loan principal payments totaling $19,451,217 increased from the 2011 level of $18,164,566 due to an increase in loans in repayment status. The Authority's allowance for loan losses of $3,137,244 at December 31, 2012, increased from 2.3% to 2.4% of total loans outstanding, due primarily to the decrease in the total loans outstanding. During 2012, the Authority provided $900,000 to the allowance for loan losses compared to $875,000 in 2011.

Bonds payable, net, decreased $11,841,619 during 2012 as a result of the redemptions and scheduled maturities for the Series 2009 bond issue, which were partially offset by the issuance of the Series 2012 bonds. For additional information refer to the Long-Term Debt Activity section of the Management's Discussion and Analysis.

Other assets decreased $1,798,084 during 2012, mainly as a result of a decrease in interest receivable on educational loans. The decline in accrued interest receivable is attributable to the decline of educational loans in interim status, whereby the interest that accrues during the deferment period is capitalized and added to the educational loan balance when the loan enters repayment status, and the decline in the balance of educational loans outstanding.

The Authority's financial position declined as net position decreased 5.0% in 2012. This decline was due primarily to the decreasing interest on educational loans.

| Changes in Net Position | 2012 | Restated 2011 | Percentage Change |
|---|---|---|---|
| Interest on educational loans | $10,966,506 | $11,485,582 | (4.5)% |
| Interest on investments | 25,260 | 8,340 | 202.9 |
| Other revenue | 372,024 | 457,616 | (18.7) |
| Total operating revenue | 11,363,790 | 11,951,538 | (4.9) |
| Financing expenses | 8,557,546 | 8,735,715 | (2.0) |
| Servicing expense | 1,355,459 | 1,456,567 | (6.9) |
| Bond administration expense | 529,834 | 541,875 | (2.2) |
| Provision for loan losses | 900,000 | 875,000 | 2.9 |
| Other operating expenses | 201,609 | 229,225 | (12.0) |
| Total operating expense | 11,544,448 | 11,838,382 | (2.5) |
| Change in net position | (180,658) | 113,156 | (259.7) |
| Net position at beginning of year | 3,637,382 | 3,524,226 | 3.2 |
| Net position at end of year | $ 3,456,724 | $ 3,637,382 | (5.0)% |



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Operating revenues are generated principally from interest earned on educational loans. In 2012, the Authority's operating revenue totaled $11,363,790. Of this amount, 96.5% was from interest on educational loans, compared to 96.1% in 2011. Interest on educational loans decreased during 2012, mainly due to lower balances of loans outstanding during the year.

Operating expenses of the Authority consist primarily of interest expense on debt incurred to fund the origination of educational loans. The total operating expense for 2012 and 2011 was $11,544,448 and $11,838,382, respectively, of which $8,557,546 (74.1%) and $8,735,715 (73.8%) was attributable to debt related financing costs. Total operating expenses decreased $293,934 (2.5%) from 2011 to 2012 mainly as a result of the decrease in financing expenses resulting from redemptions of MELA's bonds outstanding as well as the decrease in loan servicing expenses resulting from a decline in MELA's student loans outstanding.

**Long-Term Debt Activity**

The Authority is authorized to issue student loan revenue bonds to originate alternative educational loans. As of December 31, 2012, the Authority had $149,935,000 in bonds payable outstanding, a decrease of 7.3% from December 31, 2011. The Authority retired $24,540,000 of the Series 2009 and Series 2010 bonds upon scheduled maturity and mandatory redemptions. The Authority issued Series 2012 bonds totaling $12,570,835 (net of underwriter's discount). Refer to Note 4 of the financial statements for further information.

**Financial Highlights – 2011**

- Operating income for the Authority was $113,156 for fiscal year 2011, an increase of $2,259,168 from the prior year operating loss of $2,146,012, due mainly to decreased financing expenses.
- Net position increased in 2011 solely as a result of the operating income. The term "net position" refers to the difference between assets and deferred loss on refinancing and liabilities. At the close of fiscal year 2011, the Authority had a net position of $3,637,382, an increase of 3.2% from the prior year.
- The Authority's debt outstanding of $161,790,000 decreased $10,185,000 as a result of Series 2009 bond redemptions and scheduled bond maturities.
- Loans originated during the year totaled approximately $10,937,000, down 19% from the $13,506,000 originated in fiscal year 2010.
- As a result of the early adoption of GASB Standard Number 65, *Items Previously Reported as Assets and Liabilities*, issued in March of 2012, MELA was required to write off certain previously deferred assets and liabilities. Furthermore, MELA was required to restate all prior year amounts reflected in its Financial Statements and Management Discussion and Analysis. The details and financial impact of these restatements are discussed in the accompanying Notes to Financial Statements in Note 1, Summary of Significant Accounting Policies. Financial presentations as of December 31, 2011 and 2010 and for the years then ended have been restated to reflect the effect of this new accounting standard being implemented for those years.

**Financial Analysis – 2011**

Net position may serve, over time, as a useful indicator of a government's financial position. In the case of the Authority, assets exceeded liabilities by $3,637,382 at the close of 2011. This represents an increase of $113,156 (3.2%) from the previous year. The unrestricted net position was $418,720 compared to a restricted net position of $3,218,662. By far, the largest portion of the Authority's net position reflects its investment in educational loans plus bond proceeds remaining in trust investments less any related debt used to acquire those assets.

The Authority's financial position and operations for 2011 and 2010 are summarized below based on information included in the financial statements.

| Net Position | Restated 2011 | Restated 2010 | Percentage Change |
|---|---|---|---|
| Cash and investments | $ 19,812,879 | $ 23,687,728 | (16.4)% |
| Educational loans, net | 138,336,811 | 142,761,691 | (3.1) |
| Other assets | 5,414,338 | 6,989,064 | (22.5) |
| Total assets | $ 163,564,028 | $ 173,438,483 | (5.7)% |
| Deferred loss on refinancing | $ 1,191,726 | $ 1,282,771 | (7.1)% |
| Bonds payable, net | $ 160,234,371 | $ 170,294,118 | (5.9)% |
| Other liabilities | 884,001 | 902,910 | (2.1) |
| Total liabilities | $ 161,118,372 | $ 171,197,028 | (5.9)% |
| Restricted net position | $ 3,218,662 | $ 3,098,821 | 3.9% |
| Unrestricted net position | 418,720 | 425,405 | (1.6) |
| Total net position | $ 3,637,382 | $ 3,524,226 | 3.2% |

The decrease in the Authority's cash and investments at December 31, 2011 from the balance at December 31, 2010 was mainly attributed to the redemptions of the Series 2009 bond issue and disbursements for the origination of educational loans in excess of loan repayments.

The Authority's educational loans, net, decreased $4,424,880 in 2011. The Authority's total loans originated and disbursed in 2011 was $10,936,588 compared to the $13,506,418 originated in 2010. The receipt of educational loan principal payments totaling $18,164,566 increased from the 2010 level of $15,522,108 due to an increase in loans in repayment status. The Authority's allowance for loan losses of $3,251,703 at December 31, 2011, increased from 2.2% to 2.3% of total loans outstanding, due primarily to the decrease in the total loans outstanding. During 2011, the Authority provided $875,000 to the allowance for loan losses compared to $1,350,000 in 2010.

Bonds payable, net, decreased $10,059,747 during 2011 as a result of the redemptions and scheduled maturities for the Series 2009 bond issue. For additional information refer to the Long-Term Debt Activity section of the Management's Discussion and Analysis.

The Authority's financial position grew as net assets increased 3.2% in 2011. This growth was due primarily to the decreasing financing expenses and allowance levels.

| Changes in Net Position | Restated 2011 | Restated 2010 | Percentage Change |
|---|---|---|---|
| Interest on educational loans | $11,485,582 | $11,586,089 | (0.9)% |
| Interest on investments | 8,340 | 213,174 | (96.1) |
| Other revenue | 457,616 | 545,722 | (16.1) |
| Total operating revenue | 11,951,538 | 12,344,985 | (3.2) |
| Financing expenses | 8,735,715 | 10,747,824 | (18.7) |
| Servicing expense | 1,456,567 | 1,513,001 | (3.7) |
| Bond administration expense | 541,875 | 658,131 | (17.7) |
| Provision for loan losses | 875,000 | 1,350,000 | (35.2) |
| Other operating expenses | 229,225 | 222,041 | 3.2 |
| Total operating expense | 11,838,382 | 14,490,997 | (18.3) |
| Change in net position | 113,156 | (2,146,012) | 105.3 |
| Net position at beginning of year | 3,524,226 | 5,670,238 | (37.8) |
| Net position at end of year | $ 3,637,382 | $ 3,524,226 | 3.2% |

Operating revenues are generated principally from interest earned on educational loans. In 2011, the Authority's operating revenue totaled $11,951,538. Of this amount, 96.1% was from interest on educational loans, compared to 93.9% in 2010. Interest on educational loans decreased during 2011, mainly due to lower balances of loans outstanding during the year. The interest on investments decreased during 2011 due to the decrease in cash and investments resulting from the Series 2009 bond redemptions and the lower reinvestment rates available for the proceeds from the Series 2009 and 2010 bond issues.

Operating expenses of the Authority consist primarily of interest expense on debt incurred to fund the origination of educational loans. The total operating expense for 2011 and 2010 was $11,838,382 and $14,490,997, respectively, of which $8,735,715 (73.8%) and $10,747,824 (74.2%) was attributable to debt related financing costs. Total operating expenses decreased $2,652,615 (18.3%) from 2010 to 2011 mainly as a result of the decrease in financing expenses resulting from redemptions of MELA's bonds outstanding as well as the decrease in provision for loan losses.

**Long-Term Debt Activity**

The Authority is authorized to issue student loan revenue bonds to originate alternative educational loans. As of December 31, 2011, the Authority had $161,790,000 in bonds payable outstanding, a decrease of 5.9% from December 31, 2010. The Authority retired $10,185,000 of the Series 2009 bonds upon scheduled maturity and mandatory redemptions. Refer to note 4 of the financial statements for further information.

**Requests for Information**

This financial report is designed to provide a general overview of the Authority's finances for all those with an interest in its finances. Questions concerning any of the information provided in this report or request for additional information should be addressed to the Executive Director, Maine Educational Loan Authority, 131 Presumpscot Street, Portland, Maine 04103.

STATEMENTS OF NET POSITION

December 31, 2012 and 2011

| | 2012 | Restated 2011 (Note 1) |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents (notes 2, 4 and 6) | $ 10,016,920 | $ 19,812,879 |
| Investments (notes 2, 4 and 6) | 8,380,378 | – |
| Educational loans, net (notes 3, 4, 6 and 7) | 18,277,400 | 17,336,000 |
| Guarantee fees receivable | 173,163 | 290,688 |
| Interest receivable | 1,333,423 | 1,574,938 |
| Prepaid expenses | 25,541 | 25,171 |
| Total current assets | 38,206,825 | 39,039,676 |
| Noncurrent assets: | | |
| Educational loans, net (notes 3, 4, 6 and 7) | 111,265,610 | 121,000,811 |
| Interest receivable | 1,449,472 | 2,818,900 |
| Guarantee fees receivable | 171,478 | 227,116 |
| Prepaid expenses | 462,797 | 476,773 |
| Fixed assets, less accumulated depreciation of $2,671 and $2,299 in 2012 and 2011, respectively | 380 | 752 |
| Total noncurrent assets | 113,349,737 | 124,524,352 |
| Total assets | $ 151,556,562 | $ 163,564,028 |
| **DEFERRED OUTFLOW OF RESOURCES** | | |
| Deferred loss on refinancing (note 4) | $ 1,104,471 | $ 1,191,726 |
| **LIABILITIES** | | |
| Current liabilities: | | |
| Accounts payable (note 5) | $ 175,457 | $ 192,573 |
| Accrued interest payable | 636,100 | 691,428 |
| Bonds payable, net (notes 4 and 6) | 7,358,230 | 7,621,482 |
| Total current liabilities | 8,169,787 | 8,505,483 |
| Noncurrent liabilities: | | |
| Bonds payable, net (notes 4 and 6) | 141,034,522 | 152,612,889 |
| Total liabilities | $ 149,204,309 | $ 161,118,372 |
| Commitments and contingencies (notes 5, 7 and 8) | | |
| **NET POSITION** | | |
| Net position: | | |
| Restricted | 3,038,786 | 3,218,662 |
| Unrestricted | 417,938 | 418,720 |
| Total net position | $ 3,456,724 | $ 3,637,382 |

See accompanying notes, as they are an integral part of the financial statements.



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## STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

Years Ended December 31, 2012 and 2011

| | 2012 | Restated 2011 (Note 1) |
|---|---|---|
| Operating revenues: | | |
| Interest on educational loans | $10,966,506 | $11,485,582 |
| Interest on investments | 25,260 | 8,340 |
| Guarantee fee income | 308,867 | 400,372 |
| Other revenue | 63,157 | 57,244 |
| Total operating revenues | 11,363,790 | 11,951,538 |
| Operating expenses: | | |
| Financing expenses – interest | 8,557,546 | 8,735,715 |
| Servicing expenses (note 5) | 1,355,459 | 1,456,567 |
| Bond administration expenses | 529,834 | 541,875 |
| Provision for losses on educational loans (note 3) | 900,000 | 875,000 |
| Professional fees | 43,293 | 64,484 |
| Salaries and related benefits | 100,603 | 100,933 |
| Other operating expenses (note 5) | 57,713 | 63,808 |
| Total operating expenses | 11,544,448 | 11,838,382 |
| Operating (loss) income | (180,658) | 113,156 |
| Net position, beginning of year | 3,637,382 | 3,524,226 |
| Net position, end of year | $ 3,456,724 | $ 3,637,382 |

See accompanying notes, as they are an integral part of the financial statements.

## STATEMENTS OF CASH FLOWS

Years Ended December 31, 2012 and 2011

| | 2012 | Restated 2011 (Note 1) |
|---|---|---|
| Cash flows from operating activities: | | |
| Interest received on educational loans | $ 9,577,083 | $ 9,356,668 |
| Principal payments received on educational loans | 19,451,217 | 18,164,566 |
| Educational loans originated | (8,384,059) | (10,936,588) |
| Fees received from borrowers | 308,867 | 400,372 |
| Payments for operating expenses | (1,931,700) | (2,030,381) |
| Payments for salaries and benefits | (100,603) | (100,933) |
| Net cash provided by operating activities | 18,920,805 | 14,853,704 |
| Cash flows from non-capital financing activities: | | |
| Interest payments on bonds | (8,276,427) | (8,555,611) |
| Proceeds from sale of bonds | 12,570,835 | – |
| Redemption of bonds | (24,540,000) | (10,185,000) |
| Issuance costs paid | (121,646) | – |
| Net cash used by non-capital financing activities | (20,367,238) | (18,740,611) |
| Cash flows from investing activities: | | |
| Proceeds from investment maturities | 14,408,068 | – |
| Purchase of investment securities | (22,783,026) | – |
| Interest received on investments | 25,432 | 12,058 |
| Net cash (used) provided by investment activities | (8,349,526) | 12,058 |
| Net decrease in cash and cash equivalents | (9,795,959) | (3,874,849) |
| Cash and cash equivalents at beginning of year | 19,812,879 | 23,687,728 |
| Cash and cash equivalents at end of year | $ 10,016,920 | $ 19,812,879 |
| Reconciliation of operating (loss) income to net cash provided by operating activities: | | |
| Operating (loss) income | $ (180,658) | $ 113,156 |
| Adjustments to reconcile operating (loss) income to net cash used by operating activities: | | |
| Provision for losses on educational loans | 900,000 | 875,000 |
| Interest income on investments | (25,260) | (8,340) |
| Interest on bonds payable | 8,557,546 | 8,735,716 |
| Depreciation expense | 372 | 446 |
| Unrealized gain on investments | (5,420) | – |
| Changes in assets and liabilities: | | |
| Educational loans, net | 11,067,158 | 7,227,978 |
| Interest receivable on educational loans | (1,389,423) | (2,128,914) |
| Prepaid expenses | 13,606 | 21,378 |
| Accounts payable | (17,116) | 17,284 |
| | $ 18,920,805 | $ 14,853,704 |

Noncash activities:

The Authority capitalized interest on educational loans in the amount of \$3,000,194 and \$3,387,411 during 2012 and 2011, respectively.

See accompanying notes, as they are an integral part of the financial statements.

## 1. **Summary of Significant Accounting Policies**

*Organization*

The Maine Educational Loan Authority (MELA or the Authority) was created by the Maine Educational Loan Authority Act, Title 20-A, Chapter 417-A, of the Maine Revised Statutes, as amended, as a public body corporate and politic constituting a public instrumentality of the State of Maine. The Authority was established to grant educational loans primarily using funds acquired through the issuance of long-term bonds payable.

For financial reporting purposes under Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*, and No. 39, *Determining Whether Certain Organizations are Component Units*, the Authority is considered a component unit of the State of Maine. As such, the financial position, results of operations and cash flows of the Authority are included in the State of Maine's basic financial statements.

*Basis of Accounting*

The accounts of the Authority are maintained in accordance with the principles of "fund accounting." These principles require that resources for various purposes be classified for accounting and reporting purposes into funds that are in accordance with activities or objectives specified. The Authority only has one fund. The financial statements are prepared on the accrual method of accounting and accordingly recognize revenues as earned and expenses as incurred.

*Management Estimates*

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management of the Authority 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 these estimates.

*New Accounting Pronouncements*

In March, 2012 GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities.* This Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. This Statement also provides other financial reporting guidance related to the impact of the financial statement elements deferred outflows of resources and deferred inflows of resources, such as changes in the determination of the major fund calculations and limiting the use of the term *deferred* in financial statement presentations. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012. Earlier application is encouraged.

## 1. Summary of Significant Accounting Policies (Continued)

MELA implemented this pronouncement during the year ended December 31, 2012 resulting in a restatement of the Statement of Net Position as of December 31, 2011 and the Statements of Revenues, Expenses and Changes in Net Position and Cash Flows for the year then ended. The effects of this change on the statements were:

| | Net Position as of December 31, 2010 | Excess of Revenues Over Expenses Year Ended December 31, 2011 | Net Position as of December 31, 2011 |
|---|---|---|---|
| As originally reported | $2,800,838 | $ 218,823 | $3,019,661 |
| Restatements resulting from: | | | |
| Alternative loan fee revenue | 2,157,095 | (239,910) | 1,917,185 |
| Lender paid origination fees | (676,782) | 102,416 | (574,366) |
| Bond issuance costs | (756,925) | 31,827 | (725,098) |
| Restated amount | $3,524,226 | $ 113,156 | $3,637,382 |

Additionally, the deferred loss on refinancing has been presented as a deferred outflow on the statements of net position.

In June 2011 GASB issued Statement No. 63 *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. This Statement provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources. This Statement amends the net asset reporting requirements by incorporating deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets. The provisions of this Statement are effective for financial statements for years beginning after December 15, 2011 and earlier application is encouraged. MELA implemented this pronouncement during the year ended December 31, 2012, resulting in a retitling of the Statement of Net Assets as the Statement of Net Position.

In December 2010 GASB issued Statement No. 62 *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The objective of this Statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements:

1. Financial Accounting Standards Board (FASB) Statements and Interpretations
2. Accounting Principles Board Opinions
3. Accounting Research Bulletins of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure.

**1. Summary of Significant Accounting Policies (Continued)**

This Statement also supersedes Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, thereby eliminating the election provided in that Statement for enterprise funds and business-type activities to apply post-November 30, 1989 FASB Statements and Interpretations that do not conflict with or contradict GASB pronouncements. However, those entities can continue to apply, as other accounting literature, post-November 30, 1989 FASB pronouncements that do not conflict with or contradict GASB pronouncements, including this Statement. The requirements of this Statement are effective for financial statements for years beginning after December 15, 2011. MELA adopted this pronouncement during the year ended December 31, 2012. The adoption had no impact on the Authority's financial position or results of operations.

*Restriction on Net Position*

The restricted components of net position of the Authority are restricted by the bond indentures. Financial activities and resulting account balances that fall outside of the bond indentures are presented in the statements of net position as unrestricted. The Authority's restricted net position is restricted for the acquisition and origination of educational loans, payment of debt service and payment of program operating expenses.

*Educational Loans*

Educational loans are stated at their unpaid principal balance. Educational loans consist primarily of student loans, which are made to postsecondary students attending eligible educational institutions, and parental loans made to parents of dependent undergraduate students, graduate and professional students and independent undergraduate students attending eligible educational institutions.

For educational loans granted subsequent to June 1996, MELA retained guarantee fees in varying amounts for these loans. The guarantee fees assessed has varied between 0% and 7% of the principal amount of the loan depending on when the loan was originated and the creditworthiness of the borrowers. Beginning June 1, 2005, the guarantee fees assessed were added to the loan principal once the loan enters repayment. Beginning July 28, 2008, all new loans were assessed a guarantee fee of 4% of the loan amount added to the principal balance at the time of disbursement. The guarantee fees outstanding for loans that were originated between June 1, 2005 and July 28, 2008 and have not entered repayment at December 31, 2012 and 2011 totaled $344,641 and $517,804, respectively.

Fees and costs related to the origination of student loans, including the guarantee fees, are recognized as revenue or expense when the loans are disbursed.

Interest on educational loans is recognized as revenue in the period earned and servicing costs are charged directly to expense as incurred.



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## 1. Summary of Significant Accounting Policies (Continued)

*Allowance for Loan Losses*

Management of MELA has established an allowance for loan losses to provide for probable losses. The amount of the allowance, which is established through a provision for losses on educational loans charged to expense, is based on management's estimation of the probable losses within the portfolio. In estimating the adequacy of the allowance for loan losses, management considers such factors as the nature and volume of the portfolio, delinquency trends, specific problem loans and current economic conditions that may affect the borrowers' ability to repay. Actual results could differ from those estimates. Past due loans greater than 180 days are automatically charged off.

*Discount and Issuance Costs on Bonds and Line of Credit*

Bond discount is amortized by the effective interest method over the life of the bonds. Bond issuance costs are charged directly to expense when incurred. Amortization of bond discount is accelerated for early repayment of bonds. Unamortized bond discount related to refunded bonds are deferred and amortized over the life of the original or refunded bonds, whichever is shorter.

*Cash Equivalents*

For purposes of the statements of cash flows, cash equivalents include funds held in institutional money market funds.

*Investments*

Investment securities consist of United States Treasury obligations. Investments are carried at fair value in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. Unrealized gains and losses due to changes in fair values of investments are included in investment income.

*Depreciation*

Capital assets of MELA consist of equipment and related software. Capital assets are defined by MELA as assets with an initial individual cost of one thousand dollars or more and are depreciated under the straight-line method over the respective estimated useful lives of the assets.

*Income Taxes*

As a public entity and body politic of the State of Maine, MELA is a tax-exempt organization and, accordingly, no provision for income taxes has been made in the accompanying financial statements.



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## 2. Cash, Cash Equivalents and Investments

In accordance with the terms of its bond indentures, MELA may invest in, subject to various restrictions, direct obligations of the United States; high grade obligations of any state, public agency, political subdivision, political agencies or authorities; deposit accounts; repurchase agreements; guaranteed investment contracts; or any other investment approved by the bond indentures. The majority of investments and cash and cash equivalents are restricted for the repayment of bond obligations, and to satisfy certain reserve requirements specified by the bond indentures.

*Interest Rate Risk:* Interest rate risk is the risk that changes in interest rates of investments in debt instruments will adversely affect the fair value of an investment. As a means of limiting its exposure to fair value losses arising from rising interest rates, the Authority invests primarily in Federal Deposit Insurance Corporation (FDIC) insured deposits, highly rated money market funds, and direct obligations of the United States.

*Credit Risk:* Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. This credit risk is measured by the credit quality ratings of investments as described by nationally recognized statistical rating organizations. The Authority limits its credit risk by investing in investment securities with high credit quality and FDIC insured deposits. The Authority's investments purchased with proceeds from the various bonds must meet minimum investment criteria contained in the bond indentures.

*Custodial Credit Risk:* Custodial credit risk is the risk that, in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Authority limits the custodial credit risk by regularly monitoring the credit quality ratings of the counterparties and the adequacy of the collateral accounts.

*Cash and Cash Equivalents*

Cash and cash equivalents consisted of the following:

| | 2012 | 2011 |
|---|---|---|
| Cash | $ 192,894 | $ 209,304 |
| Money market funds | 9,824,026 | 19,603,575 |
| | $10,016,920 | $19,812,879 |



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## 2. Cash, Cash Equivalents and Investments (Continued)

At December 31, 2012 and 2011, cash accounts with bank balances of $202,768 and $239,398, respectively, were deposited at financial institutions and fully insured by the FDIC. At December 31, 2012, the money market funds were invested in the Invesco Liquid Assets Portfolio Short-Term Investors Trust. The fund normally invests in a diversified portfolio of short-term, high-credit-quality money market instruments. These instruments are US-dollar denominated obligations and primarily include commercial paper, certificates of deposit, master and promissory notes, municipal securities, and repurchase agreements. As of December 31, 2012, the fund was rated Aaa-mf by Moody's Investors Service, AAAm by Standard & Poor's, and AAAmmf by Fitch Ratings. The underlying assets were not held in the name of the Authority.

At December 31, 2011, the money market funds were invested in the Dreyfus Cash Management Institutional Fund. The fund normally invests in a diversified portfolio of high quality, short-term, dollar-denominated debt securities, including: securities issued or guaranteed as to principal and interest by the U.S. government or its agencies or instrumentalities; certificates of deposit, time deposits, bankers' acceptance and other short-term securities issued by domestic or foreign banks or thrifts or their subsidiaries or branches; repurchase agreements, including tri-party repurchase agreements; asset-backed securities; domestic and dollar-denominated foreign commercial paper and other short-term corporate obligations, including those with floating or variable rates of interest; and dollar-denominated obligations issued or guaranteed by one or more foreign governments or any of their political subdivisions or agencies. As of December 31, 2011, the fund was rated Aaa-mf by Moody's Investors Service, AAAm by Standard & Poor's, and AAAmmf by Fitch Ratings. The underlying assets were not held in the name of the Authority.

*Investments*

A summary of the fair values of investment securities is as follows:

| | 2012 | 2011 |
|---|---|---|
| U.S. Treasury obligations, maturing in 2013 (rated AA+) | $8,380,378 | $ - |

Investments are held by the Authority's Trustee in the Trustee's name.

## 3. Educational Loans

Educational loans earn interest at variable and fixed rates. Most of MELA's borrowers are located in the New England states, primarily the State of Maine. Educational loans are unsecured.

Educational loans are classified as being in "interim" status during the period from the date the loan is made until a student ceases to be enrolled at least on a half-time basis plus a grace period of six months, during which time no payments of principal or interest are required. Beginning in July of 2008, all new borrowers are required to make "interest only" payments during the in-school and grace period. Subsequent to this period, student loans are classified as being in "repayment" status. "Forbearance" status is a period during the life of the loan when repayment is suspended for authorized purposes.

## 3. Educational Loans (Continued)

Educational loans at December 31, 2012 and 2011 are summarized as follows:

| | 2012 | 2011 |
|---|---|---|
| **Status:** | | |
| Interim | $ 12,263,409 | $ 21,825,979 |
| Interest only | 19,321,959 | 22,249,862 |
| Repayment | 100,101,649 | 97,056,346 |
| Forbearance | 993,237 | 456,327 |
| Educational loans | 132,680,254 | 141,588,514 |
| Less allowance for loan losses | (3,137,244) | (3,251,703) |
| Total educational loans, net | 129,543,010 | 138,336,811 |
| Current portion | 18,277,400 | 17,336,000 |
| Noncurrent portion | $ 111,265,610 | $ 121,000,811 |

The educational loans are pledged to the repayment of bonds.

Transactions in the allowance for loan losses for the years ended December 31, 2012 and 2011 are as follows:

| | 2012 | 2011 |
|---|---|---|
| Balance at January 1 | $ 3,251,703 | $ 3,164,380 |
| Loans charged off | (1,265,504) | (1,024,563) |
| Recoveries on loans | 251,045 | 236,886 |
| Net loans charged-off | (1,014,459) | (787,677) |
| Provision for losses on educational loans | 900,000 | 875,000 |
| Balance at December 31 | $ 3,137,244 | $ 3,251,703 |

At December 31, 2012 and 2011, respectively, loans greater than 90 days delinquent or in claims or forbearance status approximated $2,503,000 and $1,657,000.

## 4. Bonds Payable

MELA has issued the following bonds to finance the purchase and origination of educational loans:

| Educational Loan Revenue Bonds | Amount Outstanding 2012 | 2011 |
|---|---|---|
| 2009 series due in annual installments on December 1, 2013 through 2039; interest fixed at rates ranging from 3.125% to 5.875% | $ 122,690,000 | $ 146,330,000 |
| 2010 series due in annual installments on December 1, 2013 through 2025; interest fixed at rates ranging from 1.50% to 4.45% | 14,560,000 | 15,460,000 |
| 2012 series due in annual installments on December 1, 2013 through 2027; interest fixed at rates ranging from 1.85% to 5.05% | 12,685,000 | – |
| | 149,935,000 | 161,790,000 |
| Less: | | |
| Unaccreted bond discount | 1,542,248 | 1,555,629 |
| Bonds payable, net | 148,392,752 | 160,234,371 |
| Current portion, net of discount | 7,358,230 | 7,621,482 |
| Non-current portion | $ 141,034,522 | $ 152,612,889 |
| Unaccreted deferred loss on refunding | $ 1,104,471 | $ 1,191,726 |

The Authority accreted $87,255 and $91,045 in 2012 and 2011, respectively, of the deferred loss on refunding.

To date, the bonds issued by MELA have been exempt from federal income taxes. In 2011, MELA carried forward a $16,790,000 allocation of Private Activity Bond Cap from previous years, and received an allocation of $30,000,000 for 2011 resulting in $46,790,000 of Private Activity Bond Cap being available for 2012. MELA received an allocation of $25,000,000 for 2012 and issued $12,685,000 in tax-exempt debt in 2012, resulting in $59,105,000 of Private Activity Bond Cap being available for 2013. MELA expects to continue to receive allocations of Private Activity Bond Cap in the future.

The bonds are not a debt or liability of the State of Maine but are payable solely as provided in the bond indentures. The bonds are secured by cash, cash equivalents, investments and a first lien on the educational loans originated and acquired with the proceeds.

The bonds are subject to early redemption at par, in whole or in part, from unused bond proceeds and investment income thereon, to the extent that the funds will not be used to originate eligible loans. The bonds are subject to mandatory redemption under provisions outlined in the bond indentures.

## 4. Bonds Payable (Continued)

Investments made and educational loans originated with the proceeds of the bonds, and the net revenues thereon are held in trust. As additional security for the bonds, MELA has established cash reserve funds totaling approximately \$2,383,000 and \$2,254,600 at December 31, 2012 and 2011, respectively, to be used to replenish any deficiency in funds required to pay principal or interest due on the bonds. In addition to the cash reserve funds, the Authority also has a reserve fund insurance policy ("surety bond") available in an amount up to the maximum annual debt service in any given year, less the cash reserve funds. The Authority paid a one-time premium for the surety bond of \$540,049 on the closing date of the Series 2009 bonds and a \$4,098 one-time premium on the closing date of the Series 2012 bonds. The premium for the surety bond related to the Series 2010 bonds was waived by the bond insurer.

On June 22, 2011, the State of Maine approved legislation extending the ability of the Authority to create or establish capital reserve funds which will benefit from a "moral obligation" from the State of Maine to June 30, 2017. The maximum amount of bonds that the Authority can have outstanding with a capital reserve fund which will benefit from a "moral obligation" of the State of Maine is \$225,000,000.

The debt service requirements, which are based on the interest rates at December 31, 2012, through 2017 and in five-year increments thereafter to maturity for the Authority, are as follows:

| Year(s) | Principal | Interest | Total |
|---|---|---|---|
| 2013 | \$ 7,485,000 | \$ 7,633,206 | \$ 15,118,206 |
| 2014 | 7,505,000 | 7,370,350 | 14,875,350 |
| 2015 | 7,880,000 | 7,084,250 | 14,964,250 |
| 2016 | 7,980,000 | 6,761,688 | 14,741,688 |
| 2017 | 8,155,000 | 6,418,548 | 14,573,548 |
| 2018 – 2022 | 37,360,000 | 26,575,976 | 63,935,976 |
| 2023 – 2027 | 22,380,000 | 18,075,339 | 40,455,339 |
| 2028 – 2032 | 15,360,000 | 14,134,663 | 29,494,663 |
| 2033 – 2037 | 25,600,000 | 7,517,063 | 33,117,063 |
| 2038 – 2040 | 10,230,000 | 901,519 | 11,131,519 |
| | \$ 149,935,000 | \$ 102,472,602 | \$ 252,407,602 |

The actual maturities and interest may differ due to redemption provisions or other factors.



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## 4. Bonds Payable (Continued)

The following summarizes the bond activity for the Authority for the years ended December 31, 2012 and 2011:

| | 2012 | 2011 |
|---|---|---|
| Balance at beginning of year | $ 160,234,371 | $ 170,294,118 |
| Issuance | 12,570,835 | – |
| Redemption of bonds | (24,540,000) | (10,185,000) |
| Accretion | 127,546 | 125,253 |
| Balance at end of year | $ 148,392,752 | $ 160,234,371 |

## 5. Commitments

The Authority is party to an agreement whereby Maine Education Services (MES), provides administrative services for the Authority. The current contract extends from October 1, 2009 through September 30, 2014. The current fee for these services is equal to 0.65% per annum of the aggregate principal amount of loans outstanding. The fee is further reduced to 0.60%, 0.55%, and 0.50% if the outstanding loan balance exceeds $150,000,000, $175,000,000, and $200,000,000, respectively. MELA also pays MES a 1% origination fee on all supplemental loan disbursements. The Authority recorded expense of $968,273 and $1,036,167 in 2012 and 2011, respectively, under this arrangement, which is recorded as servicing expenses.

In addition, MELA pays to MES a management and financial advisory fee of 0.05% times the par value of each new bond issue for services required to facilitate each bond or line of credit offering, and to establish the initial loan and investment portfolios and bond level financial statements, which fee amounted to $6,343 in 2012.

As a result of the various transactions described above, at December 31, 2012 and 2011, the Authority owed MES $72,876 and $79,257, respectively, which is included in accounts payable.

The Authority is party to an agreement whereby Firstmark Services provides student loan servicing for the Authority. The current agreement expires on April 30, 2017. The Authority recorded expense of $373,963 and $396,213 in 2012 and 2011, respectively, under this arrangement, which is recorded as servicing expenses.

## 6. Arbitrage

The bonds issued by MELA are subject to Internal Revenue Service regulations which limit the amount of income which may be earned on certain cash equivalents, investments and educational loans acquired with bond proceeds. Any excess earnings are to be refunded to the Federal government. There is no estimated arbitrage liability at December 31, 2012 and 2011.

## 7. Loan Commitments

At December 31, 2012 and 2011, MELA had commitments to extend credit for educational loans of approximately $2,552,000 and $3,472,000, respectively. Commitments to extend credit are agreements to lend to a borrower as long as there is no violation of any condition established in the commitment agreement. Commitments generally have fixed expiration dates or other termination clauses. MELA uses the same credit policies in making commitments as it does for educational loans receivable.

## 8. Contingencies

The Authority carries insurance to cover its exposure to various risks of loss. The Authority does not have any self-insurance programs and there were no significant uninsured losses during 2012 and 2011.

*IRS Examination of 2009 Bonds*

On March 4, 2013, the Authority received a letter, dated March 1, 2013 (the Letter), from the Internal Revenue Service (IRS) requesting information and documents for an examination of the Authority's compliance with federal tax requirements with respect to the bonds listed as 2009 Series Bonds. The 2009 Bonds were issued on May 27, 2009; certain of the 2009 Bonds have previously matured.

Portions of the Letter also request information with respect to the Authority's $26,925,000 Student Loan Revenue & Refunding Bonds (collectively, the "2002 Bonds"), as certain of the 2009 Bonds refunded certain of the 2002 Bonds. The 2002 Bonds were issued on November 15, 2002 and are no longer outstanding.

The Letter requests that documentation be provided by April 1, 2013, and the Authority has complied with this request. The Letter also notes that the IRS has no reason at this time to believe that the Authority's 2009 Bonds fail to comply with applicable federal tax requirements, but that the IRS does reserve the right to expand the examination to any aspect of the Authority's debt issuance. The fiscal year 2012 IRS Tax Exempt Bond (TEB) Work Plan included Student Loan Bonds as one of the examination categories where TEB resources would be allocated in fiscal year 2012. The Authority is unable to predict the outcome of the pending examination. The Authority intends to fully cooperate with IRS' examination of the 2009 and 2002 Bonds.

# 2012 Financial Information

## Schedule 1

SCHEDULE OF ACTIVITIES

Year Ended December 31, 2012

| Functions/ Programs | Expenses | Program Revenues: Charges for Services | Program Revenues: Program Investment Income | Program Revenues: Operating Grants and Contributions | Program Revenues: Capital Grants/ Contributions | Net Revenue (Expenses) and Changes in Net Position: Total |
|---|---|---|---|---|---|---|
| Student loan programs | $11,544,448 | $11,338,530 | $25,260 | $ – | $ – | $ (180,658) |
| | | Change in net position | | | | $ (180,658) |
| | | Net position, beginning of the year | | | | 3,637,382 |
| | | Net position, end of the year | | | | $3,456,724 |



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