Annual Financial Report
June 30, 2016 and 2015

PHEAA conducts its student loan servicing operations commercially
as American Education Services and for federally-owned loans as FedLoan
Servicing.

Ernst & Young LLP
621 East Pratt Street
Baltimore, MD 21202
Tel: +1 410 539 7940
Fax: +1 410 783 3832
ey.com

Report of Independent Auditors

Management and the Board of Directors
Pennsylvania Higher Education Assistance Agency

Report on the Financial Statements

We have audited the accompanying financial statements of the Pennsylvania Higher Education Assistance Agency (PHEAA), a component unit of the Commonwealth of Pennsylvania, as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise PHEAA's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's 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. 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 auditor's 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of PHEAA as of June 30, 2016 and 2015, and the changes in its financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Required Supplementary Information

U.S. generally accepted accounting principles require that Management's Discussion and Analysis, the required schedules of PHEAA's proportionate share of the net pension liability and PHEAA's contributions on pages 4 through 39 and 85 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 which 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, 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.

Ernst & Young LLP

September 22, 2016

The Pennsylvania Higher Education Assistance Agency's ("PHEAA") Management's Discussion and Analysis ("MD&A") is presented as required supplementary information. The MD&A introduces the basic financial statements and provides an analytical overview of our financial activities. Please read it in conjunction with the Basic Financial Statements that follow this discussion.

About PHEAA

Our mission is to improve higher education opportunities for Pennsylvanians. We are a public corporation and government instrumentality created by the Pennsylvania General Assembly. We serve students and schools nationally through our state grant, guaranty, servicing, and financial aid processing systems.

We administer the Pennsylvania State Grant program, as well as other grant programs, on behalf of the Commonwealth of Pennsylvania ("Commonwealth") each year without taxpayer support. We use our business earnings to fund the administration of these programs ensuring that every appropriated dollar goes directly to students.

We are governed by a Board of Directors and administered by a President/Chief Executive Officer and staff. We have approximately 3,600 employees and contractors and our principal offices are located in Harrisburg, Pennsylvania, with four regional offices located throughout Pennsylvania.

Our business activities are subject to audit by the Pennsylvania Department of Auditor General and we are required to make an annual report to the Governor of Pennsylvania ("Governor") and the legislature showing our financial condition at the end of the Commonwealth's fiscal year.

Public Service Benefits

The following table highlights the public service benefits and the operating expenses incurred by us in operating state and federal programs as well as public service activities.

(Dollars in thousands)

For the years ended June 30,		**2016**	2015	2014
Self-funded				
Pennsylvania State Grant Program	$	**125,000**	75,000	75,000
Costs of operating state and federal governmental programs		**15,313**	15,399	13,482
Pennsylvania Distance Education Program, net of refunds		**10,323**	7,313	5,750
Pennsylvania Targeted Industry Cluster Certificate Scholarship Program , net of refunds		**4,886**	4,373	5,146
Other public service activities and outreach		**2,910**	2,684	2,690
		158,432	104,769	102,068
Financial support funded by our business partners				
Keystone loan program origination fees and benefits paid on behalf of borrowers		**4**	9	16
	$	**158,436**	104,778	102,084

- On June 16, 2016, the Board of Directors approved that the President/Chief Executive Officer be given the authority to allocate funds to the following programs for fiscal year 2016-17:

  - Pennsylvania State Grant Program - Up to $125.0 million;
  - Pennsylvania Distance Education Program - $10.0 million; and
  - Pennsylvania Targeted Industry Cluster Certificate Scholarship Program - $6.0 million.

- On July 12, 2016, the Commonwealth's Enacted Budget for fiscal year 2016-17 (Senate Bill No. 1073, printer's number 2009) ("Enacted Budget") became law (Act 16A). The Enacted Budget allocates funding levels to the following programs for fiscal year 2016-17:

  - Pennsylvania State Grant Program - $272.9 million;
  - Institutional Assistance Grant Program - $25.7 million;
  - Matching Funds Grant Program - $12.5 million;
  - Pennsylvania Ready to Succeed Scholarship Program - $5.0 million;
  - Higher Education for the Disadvantaged Program - $2.2 million;
  - Cheyney University Keystone Academy Program - $1.8 million;
  - Horace Mann Bond-Leslie Pickney Hill Scholarship for outreach and recruitment activities at Lincoln and Cheyney Universities Program - $697 thousand;
  - Pennsylvania Internships Program Grants - $350 thousand; and
  - Higher Education of Blind or Deaf Program - $47 thousand.

We administer various programs to help students pursue higher education with the most significant Commonwealth programs as follows:

- The Pennsylvania State Grant Program is the largest of the Commonwealth supported student aid programs with approximately 154 thousand recipients and the maximum award is $4,340 for the 2015-2016 award year. As of June 30, 2016, we transferred $125.0 million to the Pennsylvania State Grant Program. As of June 30, 2016, we transferred $10.0 million to the Pennsylvania Distance Education Program and an additional $1.3 million from the Pennsylvania State Grant Program to the Pennsylvania Distance Education Program, and disbursed $10.3 million, net of refunds, from the program. As of June 30, 2016, we transferred $6.0 million to the Pennsylvania Targeted Industry Cluster Certificate Scholarship Program, and disbursed $4.9 million, net of refunds, from the program.

  During the 2014-2015 award year, the Pennsylvania State Grant Program supported approximately 174 thousand recipients and the maximum award is $4,011. During the 2014-2015 award year, the Board of Directors approved and PHEAA supplemented a $75.0 million allocation to the Pennsylvania State Grant Program Supplement, a $10.0 million allocation to the Pennsylvania Distance Education Program and a $6.0 million allocation to the Pennsylvania Targeted Industry Cluster Certificate Scholarship Program.

  During the 2013-2014 award year, the Pennsylvania State Grant Program supported approximately 179 thousand recipients and the maximum award was $4,363. During the 2013-2014 award year, the Board of Directors approved and PHEAA supplemented a $75.0 million allocation to the Pennsylvania State Grant Program Supplement, a $10.0 million allocation to the Pennsylvania Distance Education Program and a $5.0 million allocation to the Pennsylvania Targeted Industry Cluster Certificate Scholarship Program.

- The Institutional Assistance Grants ("IAG") Program serves as an integral part of the Commonwealth's commitment to the development and preservation of a planned system of postsecondary education. The IAG program goals are fulfilled through formula grants, which help non-profit independent, postsecondary institutions to maintain enrollment levels and stabilize costs.

- The Matching Funds Program provides financial assistance to higher education institutions to assist them in capturing federal funds that require a state or local match as part of the federal grant award. It also provides matching grants to scholarship awards made by selected non-profit foundations.

- The Pennsylvania National Guard Education Assistance Program ("EAP") is for members of the Pennsylvania National Guard. This program provides tuition assistance for students who enter into a service commitment with the Pennsylvania National Guard, typically for a period of six years. The maximum EAP award for full-time students (undergraduates) is the lesser of the actual tuition charged for the full-time course of study, or 100% of the tuition charged to a Pennsylvania resident at a state-owned university.

- The Postsecondary Educational Gratuity Program ("PEGP") assists birth or adoptive children of Pennsylvania police officers, firefighters, rescue and ambulance squad members, corrections employees and National Guard members who died in the line of duty since January 1, 1976. The program also includes the birth and adoptive children of Pennsylvania sheriffs, deputy sheriffs and certain other individuals who were on federal or state active military duty who died in the line of duty since September 11, 2001. The PEGP covers all institutional charges for tuition, fees, room and board not covered by other grants and scholarships for students attending public colleges and universities in Pennsylvania.

- The Ready To Succeed Scholarship Program ("RTSS") provides awards to high achieving students whose annual family income does not exceed $110,000. Students must be nominated by their post-secondary institution for participation in the program and the awards from the RTSS can be used to cover tuition, books, fees, supplies, and living expenses.

Finally, we fund other public service and outreach initiatives to ensure students are aware of the financial aid opportunities available to them and to avert student loan defaults.

Operations

To serve Pennsylvanians effectively, we operate both inside and outside Pennsylvania and our primary operations involve servicing activities, student loan holdings and guaranty activities. In the table that follows, we present total assets managed.

(Dollars in thousands)

As of June 30,		**2016**	2015	2014
Commercial Servicing:				
Client-owned student loans	$	**40,378,802**	45,013,515	46,283,711
PHEAA and PHEAA Student Loan Trust owned student loans		**5,947,255**	6,944,630	7,223,471
Total commercial servicing		**46,326,057**	51,958,145	53,507,182
Federal Servicing		**264,640,157**	226,418,604	185,212,708
Remote Servicing:				
Federal Servicing		**34,189,955**	34,117,746	37,949,856
Commercial Servicing		**13,291,354**	10,893,034	10,370,374
Total remote servicing		**47,481,309**	45,010,780	48,320,230
Total servicing		**358,447,523**	323,387,529	287,040,120
Guaranty:				
Original principal outstanding		**29,013,133**	31,898,600	35,274,795
Inventory of defaulted loans		**4,741,697**	5,023,164	4,862,600
Total guaranty		**33,754,830**	36,921,764	40,137,395
Total assets managed	$	**392,202,353**	360,309,293	327,177,515

Servicing Activities

We use our proprietary COMPASS system for servicing student loans that we own and loans owned by third parties through our Commercial Servicing, FedLoan Servicing ("FLS"), and Remote Servicing lines of business. COMPASS is a mainframe-based decision support tool that is utilized by our personnel, as well as multiple clients that include lending institutions, academic institutions and other higher education servicing agencies. Each client's data is logically tagged, secured, and monitored with strict access controls.

Our Commercial Servicing line of business services student loans owned by us and loans owned by third parties, which were originated under the Federal Family Education Loan ("FFEL") program, prior to July 1, 2010, and various alternative loan programs.

Our FLS line of business services FFEL and William D. Ford ("Direct Loan") program loans, which are owned by the United States Department of Education ("ED"). We are one of four primary servicers that were awarded a contract to service Title IV loans owned by ED and our contract expires on June 16, 2019.

Previously, ED allocated separately new student loan volume to the four primary servicers and to the Not-for-Profit ("NFP") servicers based on certain performance metrics established by ED. On December 18, 2015, President Obama signed H.R. 2029 ("Consolidated Appropriations Act, 2016") into law, which states that the Secretary shall, no later than March 1, 2016, allocate new student loan borrower accounts to eligible student loan servicers on the basis of their performance compared to all student loan servicers utilizing established common metrics, and on the basis of the capacity of each servicer to process new and existing accounts.

For the quarter ended May 31, 2016, ED released the "Explanation of Allocation and Performance Measure Methodology" document, which explains the allocation and performance methodology for each of ED's federal loan servicers. The Explanation of Allocation and Performance Measure Methodology states that ED compiles quarterly customer satisfaction survey scores and default prevention statistics for the members of the federal loan servicer team every six months to determine each servicer's allocation of loan volume. In addition, the Consolidated Appropriations Act, 2016, included a provision related to the allocation of new student loan borrower accounts to federal loan servicers.

The new statutory requirement under the Consolidated Appropriations Act, 2016, prohibits ED from using the contractually established common metrics as used prior to March 1, 2016; that is, by comparing the performance of the Title IV Additional Servicers ("TIVAS") and NFP servicers within their separate performance pools. Instead, the Consolidated Appropriations Act, 2016, requires ED to use an established common metrics to compare servicer performance among "all loan servicers," without regard to their status as a TIVAS or NFP servicer.

To meet the statutory deadline, ED implemented the new allocation percentages for all servicers on March 1, 2016. The new allocation percentages reflect the results of a comparison of performance scores across all servicers using an established metrics. Details regarding the March 1, 2016 allocation are available on the Federal Student Aid's website (www.studentaid.ed.gov) under About Us/Data Center/Business Information Resources/Federal Student Aid Contracts/Loan Servicing Contracts/Service Performance Metrics Allocations (12312015).

On April 4, 2016, ED released the "Solicitation and Statement of Objectives for Phase I of the Federal Aid Servicing Solution". ED conducted Phase I of a two-phase solicitation to acquire a single servicing solution to support the management of Title IV and Title VII financial aid, post loan and grant disbursement. The scope of the potential contract includes but is not limited to loan servicing, loan discharge, loan consolidation, financial reporting, default management, and default collections. On June 30, 2016, ED selected PHEAA to participate in Phase II. ED has stated that it expects to award a contract by December 31, 2016. Although the single servicing solution provider will provide all servicing functions including a customer service contact center, additional vendors, referred to in this solicitation as customer service providers, may be added later, via a separate procurement action to be defined in a future procurement action that is anticipated to begin within 12 months after award of this solicitation.

Our Remote Servicing line of business provides our system to guarantors, other servicers, and NFP servicers to use in their internal servicing operations.

Student Loan Holdings

The Student Aid and Fiscal Responsibility Act ("SAFRA") terminated our authority to originate new loans under the FFEL program after June 30, 2010, and currently, all new Stafford, Parent Loan for Undergraduate Students ("PLUS") and Consolidation student loans are originated under the Direct Loan program. We purchase student loans originated under the FFEL program from banks and other lenders from time to time.

We earn interest subsidies and special allowance payments on certain FFEL program student loans within our student loan portfolio. ED makes interest subsidy payments to holders of qualifying FFEL program loans under the Higher Education Act of 1965, as amended, on subsidized Stafford loans and qualifying Consolidation loans, while the student is a qualified student, during a qualifying grace period and during periods of deferment. ED pays the interest subsidy payments based on the amount of interest accruing on the unpaid balance, prior to the commencement of repayment or during the deferment period. We record the interest subsidy payments as "Student Loan Interest Revenue".

ED makes special allowance payments to holders of qualifying insured loans and guaranteed loans, subject to certain requirements under the Higher Education Act of 1965, as amended. ED makes the payments during any quarter in which the special allowance calculation is a positive number. For loans first disbursed between April 1, 2006 and June 30, 2010, ED will collect excess interest for quarters in which the interest rate on the loan exceeds the special allowance support level, commonly referred to as negative special allowance. We record the special allowance payments as a reduction to "Student Loan Interest Revenue".

Special allowance rates vary according to the type of loan, the date of the loan disbursement, the loan period and the loan status. ED calculates the special allowance rates using the following factors:

- The average of the bond equivalent rates on the quotes of the 3-month financial commercial paper rates in effect for each of the days in such quarter as reported by the Federal Reserve in Publication H-15 (or its successor) for such 3-month period;
- The average of the bond equivalent rates of the quotes of the 1-month London Inter-Bank Offered Rate ("LIBOR") in effect for each of the days in such quarter as compiled and released by the British Bankers Association;
- The average bond equivalent rate of the 91-day Treasury bills as published by the Department of Treasury; and
- A factor prescribed by law for each category of loans. This factor is added to or subtracted from the applicable 3-month financial commercial paper rate, 1-month LIBOR or 91-day Treasury bill rate.

In addition, we are required to pay ED a monthly Consolidation Loan Rebate Fee as a holder of Federal Consolidation loans. The Consolidation Loan Rebate Fee is equal to 0.0875% of the unpaid principal balance and the accrued interest on all Federal Consolidation Loans disbursed after October 1, 1993, and held by the lender on the last day of the month. This is equal to an annualized rate of 1.05%. Except for loans based on applications received during the period from October 1, 1998 and January 31, 1999, for which the rebate is equal to 0.05167% on a monthly basis or 0.62% on an annual basis.

Guaranty Activities

We manage the Federal Student Loan Reserve Fund ("Federal Fund") for ED. We facilitate the guarantee of at least 97% of the principal and accrued interest on Stafford, PLUS, Supplemental Loans for Students ("SLS") and Consolidation loans made by a lender prior to July 1, 2010, in which the lender is party to a guarantee agreement with us.

We have a federal reinsurance agreement and a supplemental guarantee agreement with ED in which ED will reimburse the Federal Fund for at least 75%, and as much as 100%, of amounts expended resulting from defaulted loans, depending on the default rates of our portfolio of guaranteed loans for that fiscal year and the disbursement date of the loan. In addition, we have agreements with ED in which ED will reimburse us for 100% of the amounts expended by us resulting from the bankruptcy, death or disability of the borrower. Prior to December 1, 2015, the reinsurance rates, based on loan disbursement dates, were as follows:

▪ Before October 1, 1993	80% - 100%
▪ Between October 1, 1993 and September 30, 1998	78% - 98%
▪ Between October 1, 1998 and June 30, 2010	75% - 95%

On December 18, 2015, the Consolidated Appropriations Act, 2016, was signed into law and amended the maximum reinsurance rate within Section 428(c)(1) of the Higher Education Act by striking 95% and inserting 100%. This change was effective for all claims paid by the guarantor on or after December 1, 2015.

We have established a loan rehabilitation program for all borrowers with an enforceable promissory note. However, the following circumstances will exclude a borrower from the loan rehabilitation program:

- For any student loan that was rehabilitated on or after August 14, 2008, the borrower cannot rehabilitate the student loan again if the student loan returns to default status following the rehabilitation;
- A judgment has been obtained on the loan;
- Default claims were filed on the loan under the Code of Federal Regulations, Title 34, Chapter VI, Sec. 682.412 (Consequences of the failure of a borrower or a student to establish eligibility); and
- The borrower has been convicted of, or has pled nolo contendere or guilty to, a crime involving fraud in obtaining Title IV, Higher Education Act program assistance.

A borrower must meet the following requirements for us to consider the loan rehabilitated:

- The borrower has made nine of the ten payments required under a monthly repayment agreement;
- Nine payments have been received by us within a ten month period; and
- The loan is sold to an eligible lender.

In order to facilitate the sale of the rehabilitated student loans to eligible lenders, we purchase and sell rehabilitated student loans to eligible lenders.

Once the borrower meets the above program requirements, the borrower regains all benefits of the loan program, including any remaining deferment eligibility.

For the year ended June 30, 2016, the average original principal balance outstanding of student loans we guaranteed was $30.5 billion compared to $33.6 billion in 2015 and $36.9 billion in 2014. For more information on the Federal Fund, see the section titled "Federal Student Loan Reserve Fund (Federal Fund)" within the MD&A.

Cohort Default Rate

On October 28, 2009, ED published in the Federal Register the regulations that govern the calculation of the 3-year cohort default rates beginning with the fiscal year 2009 cohort year. Under the provisions, ED calculates a guaranty agency's cohort default rate as the percentage of borrowers in certain FFEL program loans in the cohort who default before the end of the second fiscal year following the fiscal year in which the borrowers entered repayment. This extends the length of time in which a student can default from two to three years. Each year ED publishes cohort default rates based on the percentage of a lender's or guarantor's student borrowers who enter repayment on FFEL program loans during a federal fiscal year (October 1–December 31) and default before the end of the next fiscal year. Our 3-year cohort default rate for fiscal year 2012, the most recent year available, was 8.8%, which was better than the national industry average of 11.8%. Our 3-year cohort default rates for fiscal years 2011 and 2010 were 9.3% and 9.8%, respectively, which were better than the national industry average of 13.7% and 14.7%, respectively.

Description of the Basic Financial Statements

We follow the accounting and financial reporting guidance issued by the Governmental Accounting Standards Board ("GASB"). The Statements of Revenues, Expenses and Changes in Net Position and Statements of Net Position are prepared using the economic resources measurement focus and accrual basis of accounting.

The Statements of Revenues, Expenses and Changes in Net Position report our revenues and expenses. These statements measure the results of our operations over a period of time.

The Statements of Net Position include recorded assets, deferred outflows of resources, liabilities, deferred inflows of resources and net position. Assets are resources with present service capacity that we presently control. Deferred outflows of resources are the consumption of net position that is applicable to a future reporting period. Liabilities are present obligations to sacrifice resources that we have little or no discretion to avoid. Deferred inflows of resources are the acquisition of net position that is applicable to a future reporting period. Net position remains after assets plus deferred outflows of resources, less liabilities and deferred inflows of resources. These statements report our assets, deferred outflows of resources, liabilities, deferred inflows of resources and net position at a point in time.

The Statements of Cash Flows supplement these statements by providing relevant information about cash receipts and payments over a period of time.

The notes to the financial statements are an integral part of the financial statements and contain important information necessary to get a complete view of our finances.

Condensed Financial Information

Statements of Revenues, Expenses and Changes in Net Position

(Dollars in thousands)

For the years ended June 30,		**2016**	2015	2014
Student loan interest revenue	$	**147,512**	154,985	154,029
Investment interest revenue		**6,615**	5,679	13,419
Interest expense on student loan financings		**(37,324)**	(42,058)	(53,300)
Interest expense on other financings		**(502)**	(580)	(1,994)
Net interest revenue		**116,301**	118,026	112,154
Provision for loan losses		**(6,741)**	(7,152)	(8,064)
Net interest revenue after provision for loan losses		**109,560**	110,874	104,090
Total noninterest revenue		**515,981**	458,337	536,079
Operating revenues		**625,541**	569,211	640,169
Total operating expenses		**(528,615)**	(458,286)	(418,225)
Operating income		**96,926**	110,925	221,944
Non-operating (losses) gains		**(114)**	(232)	175
Income before grants and financial aid		**96,812**	110,693	222,119
Total grants and financial aid, net of refunds		**(149,121)**	(65,345)	(86,620)
Change in net position		**(52,309)**	45,348	135,499
Net position, beginning of period		**804,020**	758,672	893,204
Net position, end of period	$	**751,711**	804,020	1,028,703

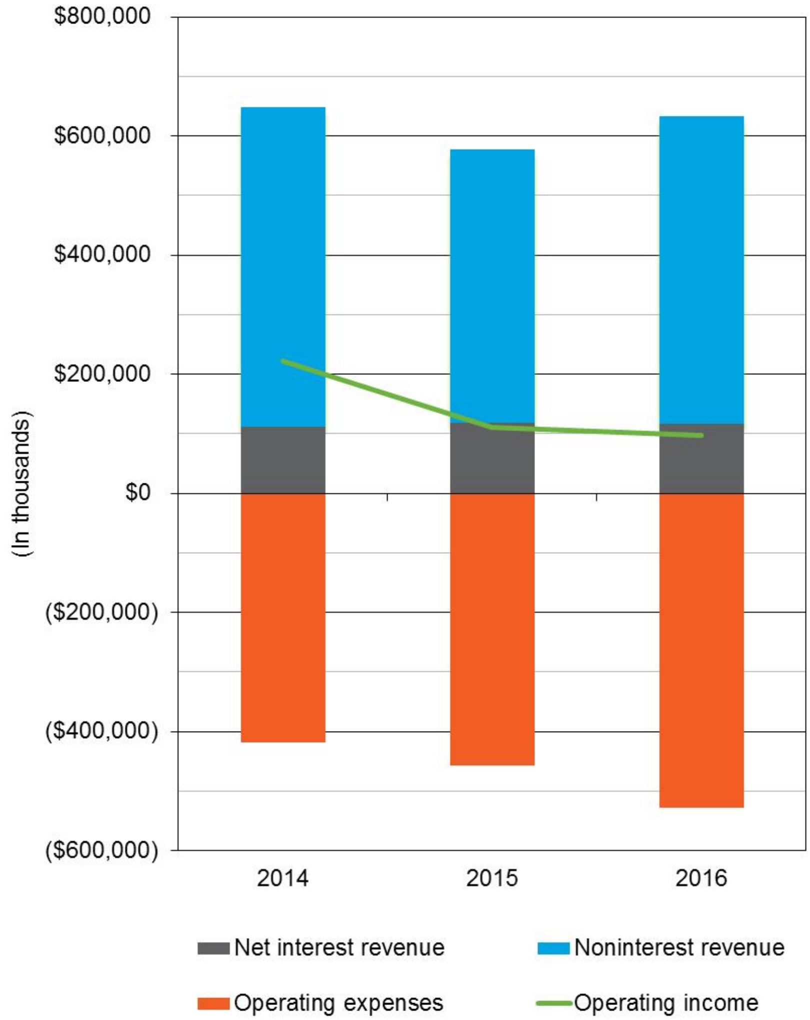
Statements of Net Position

(Dollars in thousands)

As of June 30,		2016	2015	2014
Current assets:				
Cash, cash equivalents, and investments (restricted and unrestricted)	$	**950,524**	1,014,822	1,024,895
Student loans receivable		**962,917**	1,095,033	947,152
Other assets		**237,157**	280,832	332,743
Total current assets		**2,150,598**	2,390,687	2,304,790
Long-term assets:				
Student loans receivable, net		**4,955,122**	5,819,102	6,245,917
Other assets		**79,087**	75,959	61,639
Total long-term assets		**5,034,209**	5,895,061	6,307,556
Total assets		**7,184,807**	8,285,748	8,612,346
Total deferred outflow of resources		**128,125**	41,961	2,728
Current liabilities:				
Student loan financings		**938,213**	903,779	444,140
Other liabilities		**242,884**	217,216	269,546
Total current liabilities		**1,181,097**	1,120,995	713,686
Long-term liabilities:				
Student loan financings, net		**4,751,841**	5,852,233	6,621,556
Net pension liability		**440,673**	323,866	-
Other liabilities		**52,316**	56,297	58,177
Total long-term liabilities		**5,244,830**	6,232,396	6,679,733
Total liabilities		**6,425,927**	7,353,391	7,393,419
Total deferred inflow of resources		**135,294**	170,298	192,952
Net position:				
Net investment in capital assets		**79,087**	75,959	61,639
Restricted for debt service		**310,324**	263,381	216,916
Restricted for financial aid grant programs		**52,079**	61,478	41,110
Unrestricted		**310,221**	403,202	709,038
Total net position	$	**751,711**	804,020	1,028,703

Results of Operations

Years ended June 30

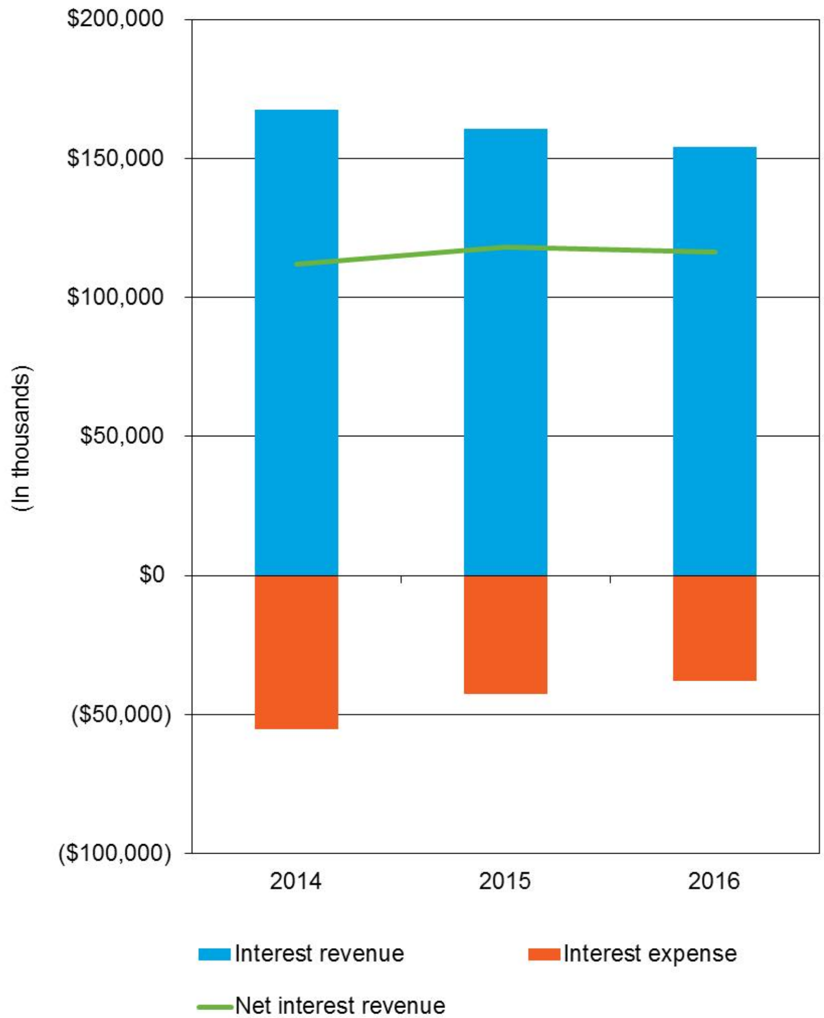


Operating income for the year ended June 30, 2016, was $96.9 million, a 12.6% decrease from $110.9 million in 2015. Operating revenues were $625.5 million in 2016, a 9.9% increase from $569.2 million in 2015. Net interest revenue was $116.3 million in 2016, a 1.4% decrease from $118.0 million in 2015. Noninterest revenue was $516.0 million in 2016, a 12.6% increase from $458.3 million in 2015. Operating expenses were $528.6 million in 2016, a 15.3% increase from $458.3 million in 2015.

Operating income for the year ended June 30, 2015, was $110.9 million, a 50.0% decrease from $221.9 million in 2014. Operating revenues were $569.2 million in 2015, an 11.1% decrease from $640.2 million in 2014. Net interest revenue was $118.0 million in 2015, a 5.2% increase from $112.2 million in 2014. Noninterest revenue was $458.3 million in 2015, a 14.5% decrease from $536.1 million in 2014. Operating expenses were $458.3 million in 2015, a 9.6% increase from $418.2 million in 2014.

A more detailed explanation of the results of operations follows.

Net Interest Revenue
Years ended June 30



Net interest revenue results primarily from the interest rate margin in our portfolio of student loans, although we have investments and debt not related to those student loans that can also create net interest revenue.

For the year ended June 30, 2016, net interest revenue was $116.3 million, a 1.4% decrease from $118.0 million in 2015. The decrease in net interest revenue was mainly due to a decrease in student loan interest revenue, which was offset by a decrease in interest expense on student loan financings.

For the year ended June 30, 2015, net interest revenue was $118.0 million, a 5.2% increase from $112.2 million in 2014. The increase in net interest revenue was due to a decrease in interest expense on student loan financings and other financings, which was offset by a decrease in investment income.

A more detailed explanation of the changes in net interest revenue follows.

Rate and Volume Analysis

The amounts we earn as student loan interest revenue are based on fixed and variable rate student loans, and involve interpreting, and complying with complicated regulations issued by ED. ED makes special allowance payments, which are included in student loan interest revenue. ED calculates special allowance payments based on the type of loan, the date of the loan disbursement, the loan period, the loan status and a factor prescribed by law. ED calculates the special allowance rates using factors such as the 3-month financial commercial paper rate, 1-month LIBOR and 91-day Treasury bill rate.

As of June 30, 2016, the 91-day U.S. Treasury Bill rate was used to calculate special allowance for 3% of the student loan portfolio, the 3-month financial commercial paper rate was used to calculate special allowance for 14% of the student loan portfolio, and the 1-month LIBOR was used to calculate special allowance for 83% of the student loan portfolio.

The following rate and volume analysis shows the relative contribution of changes in interest rates and changes in volumes to changes in net interest revenue.

(Dollars in thousands)	**2016 vs. 2015 Increase (decrease) attributable to change in**			2015 vs. 2014 Increase (decrease) attributable to change in		
For the years ended June 30	**Increase (decrease)**	**Rate**	**Volume**	Increase (decrease)	Rate	Volume
Student loan interest revenue	**$ (7,473)**	**3,909**	**(11,382)**	$ 956	5,751	(4,795)
Investment interest revenue:						
Investment income	**989**	**949**	**40**	445	(268)	713
Fair value adjustments	**(53)**	**(70)**	**17**	(8,185)	(10,168)	1,983
	(6,537)	**4,788**	**(11,325)**	(6,784)	(4,685)	(2,099)
Student loan financings interest expense	**(4,734)**	**(267)**	**(4,467)**	(11,242)	(8,778)	(2,464)
Other financings interest expense	**(78)**	**(16)**	**(62)**	(1,414)	(1,206)	(208)
	(4,812)	**(283)**	**(4,529)**	(12,656)	(9,984)	(2,672)
Net interest revenue	**$ (1,725)**	**5,071**	**(6,796)**	$ 5,872	5,299	573

2016 vs. 2015 – Changes in Rate and Volume

For the year ended June 30, 2016, the increase in the rate of our student loan interest revenue was due to an increase in student loan yields, because of a decrease in the negative special allowance payments and the consolidation loan rebate fees paid by PHEAA. The decrease in the volume of our student loan interest revenue was due to a decreasing student loan portfolio resulting from borrower payments.

For the year ended June 30, 2016, the increase in the rate of our investment income interest revenue was due to an increase in the returns earned on our investments at the Commonwealth of Pennsylvania Treasury.

For the year ended June 30, 2016, the decrease in volume of our student loan interest expense was due to payments made on our student loan financing debt.

2015 vs. 2014 – Changes in Rate and Volume

For the year ended June 30, 2015, the increase in the rate of our student loan interest revenue was due to a decrease in the payment of consolidation loan rebate fees and the decrease in the amortization of student loan purchase premium. The decrease in the volume of our student loan interest revenue was due to a decreasing student loan portfolio resulting from borrower payments.

For the year ended June 30, 2015, the decrease in the rate of our fair value adjustments associated with the interest revenue was due to the decrease in the returns earned on our investments at the Commonwealth of Pennsylvania Treasury. The increase in the volume of our fair value adjustments associated with the investment interest revenue was due to the timing of funds transferred into investments at the Commonwealth of Pennsylvania Treasury.

For the year ended June 30, 2015, the decrease in the rate of our student loan financings interest expense was due to the refunding of auction rate security bonds with floating rate notes issued by the PHEAA Student Loan Trusts.

For more details on our debt financing activity, see the debt financing activity table within the section titled "Debt Activity and Capital Assets" of the MD&A.

Net Interest Margin

The following table shows the net interest margin on student loans.

For the years ended June 30,	**2016**	2015	2014
Student loan yields	**3.11%**	3.08%	3.08%
Consolidation loan rebate fees	**(0.82)**	(0.83)	(0.85)
Premium amortization	**(0.03)**	(0.05)	(0.11)
Student loan interest revenue	**2.26%**	2.20%	2.12%
Student loan financings interest expense	**(0.60)**	(0.60)	(0.73)
Net interest margin on student loans	**1.66%**	1.60%	1.39%

For the year ended June 30, 2016, the increase in the student loan yields was due to an increase in the Treasury Bill rates associated with the variable rate FFELP loans in our student loan portfolio. The increase in the rate on student loan yields was mainly due to a decrease in the negative special allowance payments and the consolidation loan rebate fees paid by PHEAA. The negative special allowance payments and the consolidation loan rebate fees paid are reductions to student loan interest income. The decrease in the rate of the premium amortization was due to the scheduled amortization.

Noninterest Revenue

The following table displays the categories of noninterest revenue.

(Dollars in thousands)

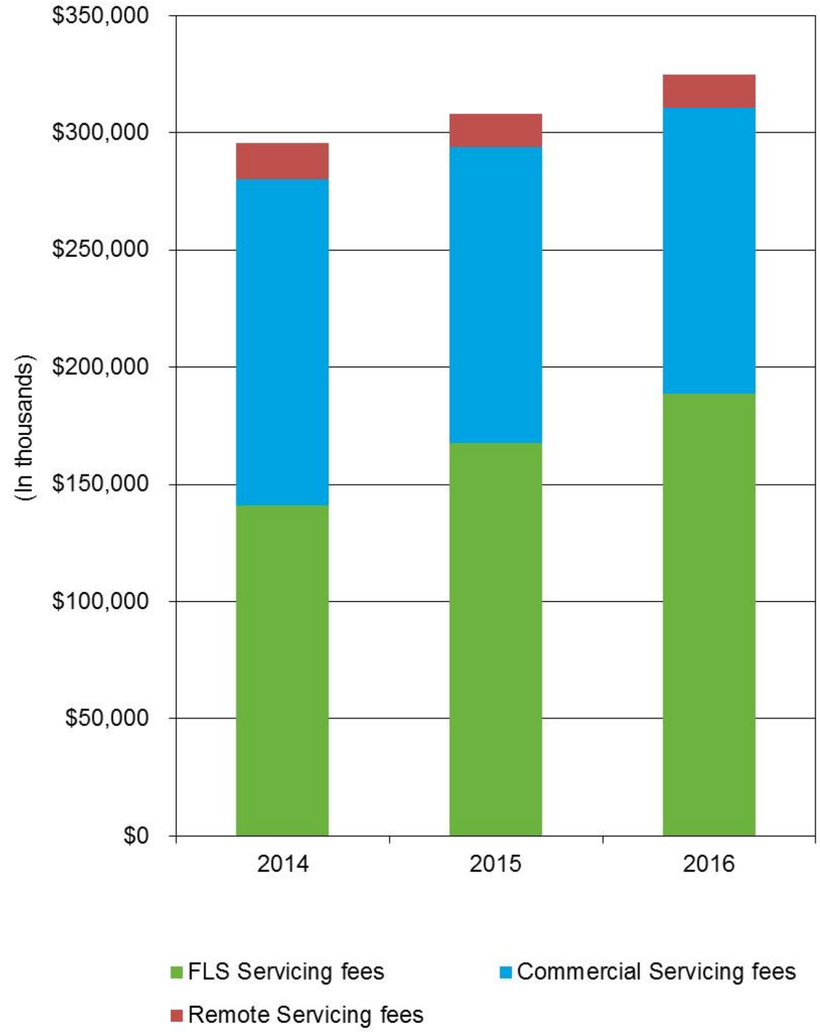
For the years ended June 30,		2016	2015	2014
Servicing fees	$	**324,664**	307,922	295,537
Retention of collections on defaulted loans, net		**170,809**	130,975	207,688
Federal fees		**18,922**	20,634	22,567
Other		**1,586**	(1,194)	10,287
Total noninterest revenue	$	**515,981**	458,337	536,079

For the year ended June 30, 2016, total noninterest revenue was $516.0 million, a 12.6% increase from $458.3 million in 2015. For the year ended June 30, 2015, total noninterest revenue was $458.3 million, a 14.5% decrease from $536.1 million in 2014.

In the sections that follow, we provide a more detailed explanation of the changes in total noninterest revenue.

Servicing Fees

Years ended June 30



We earn servicing fee revenue by servicing student loans owned by third parties. We categorize revenue earned from loans owned by ED as "FLS Servicing"; whereas we categorize revenue earned from loans owned by financial institutions and secondary markets as "Commercial Servicing". Our Remote Servicing line of business provides our system to guarantors and other servicers to use, as well as to NFP servicers who were awarded servicing contracts by ED.

Total Servicing Fees

For the year ended June 30, 2016, total servicing fees were $324.7 million, a 5.5% increase from $307.9 million in 2015. For the year ended June 30, 2016, the average third party loans serviced on our systems were $336.0 billion, a 12.5% increase from $298.7 billion in 2015.
For the year ended June 30, 2015, total servicing fees were $307.9 million, a 4.2% increase from $295.5 million in 2014. For the year ended June 30, 2015, the average third party loans serviced on our systems were $298.7 billion, a 12.3% increase from $266.1 billion in 2014.

In the sections that follow, we discuss the changes in total servicing fees.

FLS Servicing Fees

For the year ended June 30, 2016, FLS Servicing fees were $188.5 million, a 12.5% increase from $167.6 million in 2015. For the year ended June 30, 2016, the average FLS servicing portfolio of loans was $246.8 billion, an 18.8% increase from $207.8 billion in 2015. For the year ended June 30, 2016, the average number of total unique borrowers in the FLS servicing portfolio was 7.5 million, a 4.2% increase from 7.2 million in 2015.

For the year ended June 30, 2015, FLS Servicing fees were $167.6 million, an 18.8% increase from $141.1 million in 2014. For the year ended June 30, 2015, the average FLS servicing portfolio of loans was $207.8 billion, a 24.2% increase from $167.3 billion in 2014. For the year ended June 30, 2015, the average number of total unique borrowers in the FLS servicing portfolio was 7.2 million, a 7.5% increase from 6.7 million in 2014.

For the years ended June 30, 2016 and 2015, the increase in FLS Servicing fees was due to an increase in the portfolio of loans serviced by us for ED and an increase in the average fee per borrower in the FLS servicing portfolio, as student loans mature and move into higher paying statuses.

Commercial Servicing Fees

For the year ended June 30, 2016, Commercial Servicing fees were $122.0 million, a 3.4% decrease from $126.3 million in 2015. For the year ended June 30, 2016, the average Commercial Servicing portfolio of loans (excluding PHEAA owned loans) was $42.7 billion, a 4.3% decrease from $44.6 billion in 2015.

For the year ended June 30, 2016, the decrease in Commercial Servicing fees was primarily due to a decrease in the volume of our FFEL servicing portfolio, which was offset by an increase the volume of our alternative servicing portfolio. For the year ended June 30, 2016, the average FFEL servicing portfolio (excluding PHEAA owned loans) was $27.3 billion, an 11.1% decrease from $30.7 billion in 2015. For the year ended June 30, 2016, the average alternative servicing portfolio (excluding PHEAA owned loans) was $15.4 billion, a 10.8% increase from $13.9 billion in 2015.

For the year ended June 30, 2015, Commercial Servicing fees were $126.3 million, a 9.2% decrease from $139.1 million in 2014. For the year ended June 30, 2015, the average Commercial Servicing portfolio of loans (excluding PHEAA owned loans) was $44.6 billion, a 9.3% decrease from $49.2 billion in 2014.

For the year ended June 30, 2015, the decrease in Commercial Servicing fees was primarily due to decreases in the volume of our FFEL and alternative servicing portfolios. For the year ended June 30, 2015, the average FFEL servicing portfolio (excluding PHEAA owned loans) was $30.7 billion, 12.0% decrease from $34.9 billion in 2014. For the year ended June 30, 2015, the average alternative servicing portfolio (excluding PHEAA owned loans) was $13.9 billion, a 2.8% decrease from $14.3 billion in 2014.

Remote Servicing Fees

For the year ended June 30, 2016, Remote Servicing fees were $14.2 million, a 1.4% increase from $14.0 million in 2015. For the year ended June 30, 2016, the average Remote Servicing portfolio of loans, excluding the NFP Servicers, was $12.4 billion, an 18.1% increase from $10.5 billion in 2015. For the year ended June 30, 2016, the average portfolio of loans related to the NFP Servicers was $34.1 billion, a 4.7% decrease from $35.8 billion for the same period ended 2015.

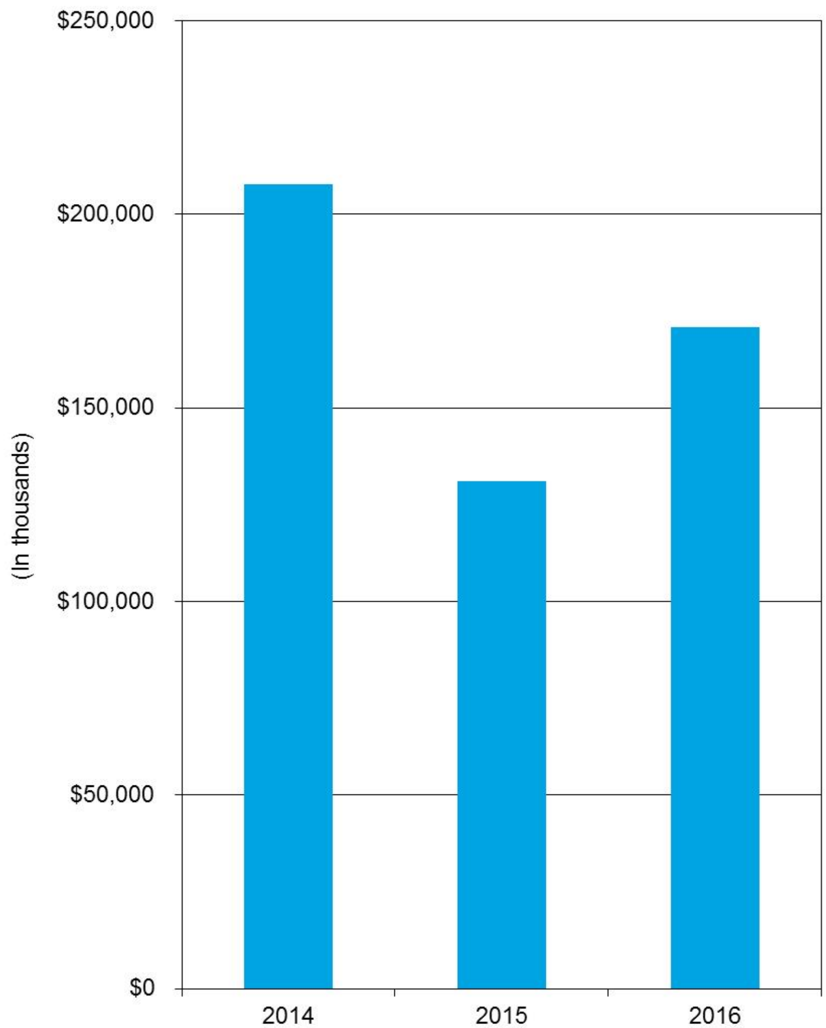
For the year ended June 30, 2016, the increase in Remote Servicing fees was primarily due to an increase in the volume of our Remote Servicers student loan servicing portfolio, excluding NFP Servicers, and one-time fees, which was offset by a decrease in the volume of our NFP Servicers student loan servicing portfolio.

For the year ended June 30, 2015, Remote Servicing fees were $14.0 million, an 8.5% decrease from $15.3 million in 2014. For the year ended June 30, 2015 the average Remote Servicing portfolio of loans, excluding the NFP Servicers, was $10.5 billion, a 1.0% increase from $10.4 billion in 2014. For the year ended June 30, 2015, the average portfolio of loans related to the NFP Servicers was $35.8 billion, an 8.9% decrease from $39.3 billion for the same period ended 2014.

For the year ended June 30, 2015, the decrease in Remote Servicing fees was primarily due to a decrease in the portfolio of student loans held on our system for NFP Servicers.

Retention of Collections on Defaulted Loans, net

Years ended June 30



As a guarantor, we facilitate the guarantee of 97% - 100% of the borrower's outstanding loan balance depending on the disbursement date of the borrower's loan. The federal government reinsures the Federal Fund, which pays any claims on defaulted loan balances, based upon default rates of the portfolio of guaranteed loans and the disbursement date of the loan.

After a loan defaults and the Federal Fund pays a claim, we continue to try to collect on the loan and we earn revenue on the collection of defaulted loans. The Bipartisan Budget Act of 2013 (the "2013 Budget"), Section 501, reduced the amount that PHEAA and other guaranty agencies are permitted to retain on rehabilitated defaulted student loans. For rehabilitated loan sales on and after July 1, 2014, the 2013 Budget requires that we pay ED 100% of the principal balance of the loan at the time of sale (multiplied by the reinsurance percentage in effect when payment under the guaranty agreement was made with respect to the loan). In addition, we can retain collection costs and accrued interest. Collection costs charged to the borrower may not exceed 16% of the outstanding principal and interest at the time of the loan sale. Previously, guaranty agencies were required to repay ED 81.5% of the amount of the principal balance outstanding at the time of sale (multiplied by the reinsurance percentage in effect when payment under the guaranty agreement was made with respect to the loan) and could retain the other 18.5% of principal. In addition, guaranty agencies retained collection costs and accrued interest, but the collection costs charged to the borrower could not exceed 18.5% of the principal balance and accrued interest at the time of loan sale.

For the year ended June 30, 2016, the retention of collections on defaulted loans, net, was $170.8 million, a 30.4% increase from $131.0 million in 2015. For the year ended June 30, 2016, total collections on defaulted loans was $1.2 billion, a 22.6% increase from $978.5 million in 2015. For the year ended June 30, 2016, the increase in the collections on defaulted loans, net, was due to an increase in the collections of rehabilitation loans, which was offset by a decrease in the collections on direct consolidation loans and an increase in the discounts offered to eligible lenders for purchasing rehabilitation loans.

For the year ended June 30, 2015, the retention of collections on defaulted loans, net, was $131.0 million, a 36.9% decrease from $207.7 million in 2014. For the year ended June 30, 2015, total collections on defaulted loans was $978.5 million, an 11.0% decrease from $1.1 billion in 2014. For the year ended June 30, 2015, the decrease in the collections on defaulted loans, net, was due to the change in the retention of collections pricing under the Bipartisan Budget Act of 2013, a decrease in the collections on direct consolidation loans and an increase in the discounts offered to eligible lenders for purchasing rehabilitation loans.

Collections on Rehabilitation Loans

For the year ended June 30, 2016, total rehabilitation collections were $803.3 million, a 56.7% increase from $512.5 million in 2015.For the year ended June 30, 2016, our share of collections on rehabilitation loans was $171.7 million, a 78.5% increase from $96.2 million in 2015. For the year ended June 30, 2016, the increase in the collections on rehabilitation loans was due to an increase in the volume of loans being rehabilitated as a result of an increase in the volume of income driven repayment applications.

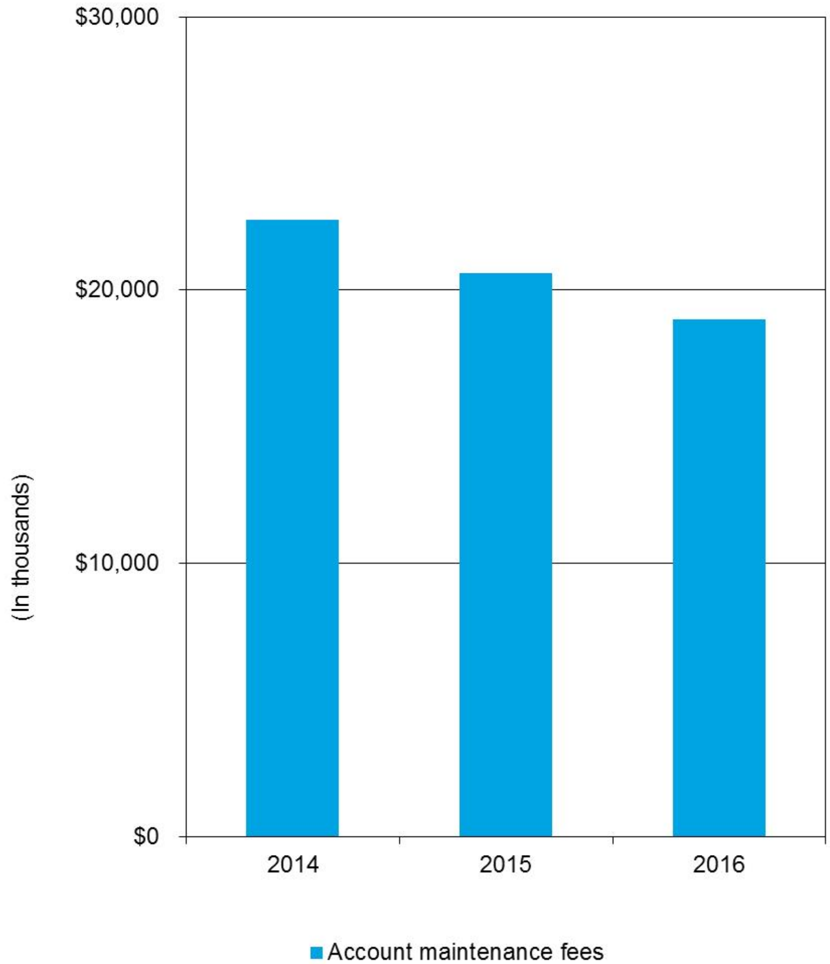
For the year ended June 30, 2015, total rehabilitation collections were $512.5 million, a 6.4% increase from $481.5 million in 2014. For the year ended June 30, 2015, our share of collections on rehabilitation loans was $96.2 million, a 38.5% decrease from $156.5 million in 2014. For the year ended June 30, 2015, the decrease in the collections on rehabilitation loans was due to the change in the retention of collections pricing under the Bipartisan Budget Act of 2013.

Discounts on Rehabilitation Loans

For the year ended June 30, 2016, the discount offered to eligible lenders for purchasing rehabilitation loans was $36.5 million, an increase from $6.0 million in 2015. For the year ended June 30, 2015, the discount offered to eligible lenders for purchasing rehabilitation loans was $6.0 million, an increase from $2.5 million in 2014.

For the years ended June 30, 2016 and 2015, the increase in the discount offered to eligible lenders for purchasing rehabilitation loans was due to an increase in the volume of rehabilitation loans sold at a discount.

Federal Fees
Years ended June 30



We earn account maintenance fees, which we classify as federal fees, from operating the guaranty agency. ED pays us an annual account maintenance fee that is 0.06% of the original principal amount of outstanding loans guaranteed as long as the guarantee remains in force.

For the year ended June 30, 2016, federal fees were $18.9 million, an 8.3% decrease from $20.6 million in 2015. For the year ended June 30, 2016, the average original principal balance of outstanding loans guaranteed was $30.5 billion, a 9.2% decrease from $33.6 billion in 2015. For the year ended June 30, 2016, the decrease in federal fees was mainly due to the decrease in the average original principal balance of outstanding loans guaranteed.

For the year ended June 30, 2015, federal fees were $20.6 million, an 8.8% decrease from $22.6 million in 2014. For the year ended June 30, 2015, the average original principal balance of outstanding loans guaranteed was $33.6 billion, an 8.9% decrease from $36.9 billion in 2014. For the year ended June 30, 2015, the decrease in federal fees was mainly due to the decrease in the average original principal balance of outstanding loans guaranteed.

Operating Expenses

The following tables display our major categories of operating expenses.

(Dollars in thousands)

For the years ended June 30,		**2016**			2015			2014	
Personnel and benefits	$	**305,489**	**57.8%**	$	257,450	56.2%	$	204,071	48.8%
Professional services		**97,073**	**18.4%**		58,698	12.8%		55,552	13.3%
Information technology		**50,828**	**9.6%**		43,930	9.6%		36,933	8.9%
Mail services		**32,588**	**6.2%**		35,148	7.7%		35,531	8.5%
Depreciation		**13,770**	**2.6%**		11,789	2.5%		9,827	2.3%
Other		**28,867**	**5.4%**		51,271	11.2%		76,311	18.2%
Total operating expenses	$	**528,615**	**100.0%**	$	458,286	100.0%	$	418,225	100.0%

For the year ended June 30, 2016, operating expenses were $528.6 million, a 15.3% increase from $458.3 million in 2015. For the year ended June 30, 2015, operating expenses were $458.3 million, a 9.6% increase from $418.2 million in 2014. In the sections that follow, we discuss changes in personnel and benefits, professional services, information technology and other expenses.

Personnel and Benefits

The following tables display personnel and benefits expenses:

(Dollars in thousands)

For the years ended June 30,		**2016**			2015			2014	
Personnel and Benefits									
Compensation	$	**171,333**	**56.1%**	$	156,024	60.6%	$	138,419	67.8%
Pension expense		**65,807**	**21.5%**		41,662	16.2%		18,709	9.2%
Healthcare benefits for employees and retirees		**42,440**	**13.9%**		35,933	14.0%		27,992	13.7%
Independent contractor fees		**16,019**	**5.2%**		15,849	6.2%		11,663	5.7%
Employer's share of Social Security		**12,487**	**4.1%**		11,296	4.4%		10,152	5.0%
Capitalized software development costs		**(4,301)**	**(1.4%)**		(4,551)	(1.8%)		(4,229)	(2.1%)
Other		**1,704**	**0.6%**		1,237	0.4%		1,365	0.7%
Total personnel and benefits	$	**305,489**	**100.0%**	$	257,450	100.0%	$	204,071	100.0%

For the year ended June 30, 2016, personnel and benefits costs were $305.5 million, an 18.6% increase from $257.5 million in 2015. For the year ended June 30, 2015, personnel and benefits costs were $257.5 million, a 26.2% increase from $204.1 million in 2014. A discussion on the changes in personnel and benefit costs follows.

Compensation

For the year ended June 30, 2016, compensation costs were $171.3 million, a 9.8% increase from $156.0 million in 2015. For the year ended June 30, 2016, our average FTE count was 3,604, an 8.1% increase from 3,335 in 2015.

For the year ended June 30, 2015, compensation costs were $156.0 million, a 12.7% increase from $138.4 million in 2014. For the year ended June 30, 2015, our average FTE count was 3,335, a 12.1% increase from 2,975 in 2014.

For the years ended June 30, 2016 and 2015, the increases in compensation costs were due to an increase in FTE count and union pay increases.

Pension expense

For the year ended June 30, 2016, pension expense was $65.8 million, a 57.8% increase from $41.7 million in 2015. For the year ended June 30, 2015, pension expense was $41.7 million, an increase from $18.7 million in 2014. For the years ended June 30, 2016 and 2015, the increases in pension expense were due to an increase in our statutorily required contributions and an increase in our proportionate share of collective pension expense.

GASB Statement No. 68 – *Accounting and Financial Reporting for Pensions* ("GASB 68") replaced the requirements of GASB Statement No. 27 – *Accounting for Pensions by State and Local Governmental Employers* ("GASB 27") and required cost-sharing employers to record their proportionate share of collective pension expense. Previously, GASB 27 required cost-sharing employers to record only their statutorily required contributions.

See **Note 9 – Retirement and Other Postemployment Benefits** for more details.

In the sections that follow is a more detailed discussion on our proportionate share of collective pension expense and our statutorily required contributions.

Proportionate share of collective pension expense

For the year ended June 30, 2016, our proportionate share of collective pension expense was $65.8 million, a 57.8% increase from $41.7 million in 2015. The increase in our proportionate share of collective pension expense was due to an increase in our allocation percentage as a result of an increase in our projected funding payroll for fiscal year 2016-17. It should be noted that the pension plan as a whole experienced an overall increase in the collective pension expense. As of and for the year ended June 30, 2016, our allocation percentage was 2.42% compared to 2.14% as of and for the year ended June 30, 2015.

For the year ended June 30, 2015, our proportionate share of collective pension expense was $41.7 million compared to zero in 2014. The increase in our proportionate share of collective pension expense was due to the adoption and implementation of GASB 68.

Statutorily required contributions

For the year ended June 30, 2016, our statutorily required contributions were $36.1 million, a 35.2% increase from $26.7 million in 2015. The increase in our statutorily required contributions was due to an increase in the employer contribution rates. For the year ended June 30, 2016, the employer's contribution rate for the "AA" Class of Service employees was 24.86%, a 24.8% increase from 19.92% in 2015, and the employer's contribution rate for the "A-3" and "A-4" Class of Service employees was 17.18%, a 24.8% increase from 13.77% in 2015. The majority of our employees fall under the AA, A-3 and A-4 Class of Service.

For the year ended June 30, 2015, pension expense was $26.7 million, a 42.8% increase from $18.7 million in 2014. The increase in our statutorily required contributions was due to an increase in the employer contribution rates. For the year ended June 30, 2015, the employer's contribution rate for the "AA" Class of Service employees was 19.92%, a 31.7% increase from 15.12% in 2015, and the employer's contribution rate for the "A-3" and "A-4" Class of Service employees was 13.77%, a 31.6% increase from 10.46% in 2014. The majority of our employees fall under the AA, A-3 and A-4 Class of Service.

Healthcare Benefits for Employees and Retirees

For the year ended June 30, 2016, healthcare benefits for employees and retirees were $42.4 million, an 18.1% increase from $35.9 million in 2015. For the year ended June 30, 2015, healthcare benefits for employees and retirees were $35.9 million, a 28.2% increase from $28.0 million in 2014.

For the years ended June 30, 2016, the increases in healthcare benefits for employees and retirees was due to an increase in personnel, as discussed previously under the section titled "*Compensation*", and an increase in the employer's share of healthcare costs for wage employees. In order to comply with the Affordable Care Act ("ACA"), on January 1, 2015, we offered healthcare benefits to wage employees. Our share of healthcare costs for wage employees was $266 per wage employee per pay period.

Professional Services

The following tables display professional services expenses:

(Dollars in thousands)

For the years ended June 30,		**2016**			2015			2014	
Professional Services									
Collection agency fees	$	**46,066**	**47.5%**	$	33,601	57.2%	$	39,248	70.6%
Consulting fees		**20,215**	**20.8%**		2,011	3.5%		1,604	2.9%
Legal fees		**11,916**	**12.3%**		14,106	24.0%		7,045	12.7%
Default aversion outsourcing fees		**8,380**	**8.6%**		3,667	6.2%		3,755	6.7%
Data entry services		**6,148**	**6.3%**		849	1.4%		-	-
Audit fees		**2,153**	**2.2%**		2,438	4.2%		2,090	3.8%
Other professional services		**2,195**	**2.3%**		2,026	3.5%		1,810	3.3%
Total professional services	$	**97,073**	**100.0%**	$	58,698	100.0%	$	55,552	100.0%

For the year ended June 30, 2016, professional services were $97.1 million, a 65.4% increase from $58.7 million in 2015. For the year ended June 30, 2016, the increase in professional services was mainly due to an increase in collection agency fees, an increase in consulting fees, an increase in default aversion outsourcing fees and an increase in data entry services, which were partially offset by a decrease in legal fees.

The increase in collection agency fees was due to an increase in the total volume collected on defaulted loans by third party vendors. The increase in consulting fees was due to an increase in information technology consultants. The increase in default aversion outsourcing fees was due to a higher success rate on collections by our third party collection vendor. The increase in the data entry services was due to us outsourcing certain processing functions to third party vendors. The decrease in legal fees was due to legal fees recorded in the prior period for the PHEAA SLT 2014-3 bond refunding. For the year ended June 30, 2016, we did not have legal fees associated with bond refundings.

For the year ended June 30, 2015, professional services were $58.7 million, a 5.6% increase from $55.6 million in 2015. For the year ended June 30, 2015, the increase in professional services was mainly due to an increase in legal fees, which was offset by a decrease in collection agency fees.

The increase in legal fees was due to the preparation of legal documents in connection with the September 18, 2014 and April 22, 2015 bond refundings, the execution of various borrowing requests on our warehouse lines of credit and on-going legal matters. The decrease in collection agency fees was due to a decrease in the total volume collected on defaulted loans by third party vendors.

Information Technology

The following tables display information technology expenses:

(Dollars in thousands)

For the years ended June 30,	**2016**		2015		2014	
Information Technology						
Equipment purchases, rentals and maintenance	**$ 22,603**	**44.5%**	$ 16,169	36.8%	$ 15,094	40.9%
PC software, licenses and rentals	**20,824**	**41.0%**	21,329	48.6%	15,857	42.9%
Other information technology	**7,401**	**14.5%**	6,432	14.6%	5,982	16.2%
Total information technology	**$ 50,828**	**100.0%**	$ 43,930	100.0%	$ 36,933	100.0%

For the year ended June 30, 2016, information technology was $50.8 million, a 15.7% increase from $43.9 million in 2015. For the year ended June 30, 2016, the increase in information technology was mainly due to an increase in equipment purchases and software maintenance.

For the year ended June 30, 2015, information technology was $43.9 million, a 19.0% increase from $36.9 million in 2015. For the year ended June 30, 2015, the increase in information technology was mainly due to an increase in equipment purchases, software licenses and rentals.

Other

The following tables display other expenses:

(Dollars in thousands)

For the years ended June 30,	**2016**		2015		2014	
Other expenses						
Telephone	**$ 8,007**	**27.7%**	$ 6,506	12.7%	$ 5,908	7.7%
Buildings and grounds	**6,646**	**23.0%**	7,093	13.8%	6,333	8.3%
Bond issuance costs and bank fees	**5,538**	**19.2%**	12,916	25.2%	22,747	29.8%
Printing expense	**2,771**	**9.6%**	3,345	6.5%	3,356	4.4%
Third party guarantor expense	**2,015**	**7.0%**	2,052	4.0%	2,703	3.5%
Net realizable value adjustment in amounts due from the Federal Fund	**(3,614)**	**(12.5%)**	14,289	27.9%	24,202	31.7%
Other G&A	**7,504**	**26.0%**	5,070	9.9%	11,062	14.6%
Total other expenses	**$ 28,867**	**100.0%**	$ 51,271	100.0%	$ 76,311	100.0%

For the year ended June 30, 2016, other expenses were $28.9 million, a 43.7% decrease from $51.3 million in 2015. For the year ended June 30, 2016, the decrease in other expenses was due to a decrease in bond issuance costs and bank fees and a decrease in the net realizable value adjustment in amounts due from the Federal Fund.

For the year ended June 30, 2015, other expenses were $51.3 million, a 32.8% decrease from $76.3 million in 2014. For the year ended June 30, 2015, the decrease in other expenses was due to a decrease in bond issuance costs and bank fees and a decrease in the net realizable value adjustment in amounts due from the Federal Fund.

A discussion on the changes in other expenses follows.

Bond issuance costs and bank fees

For the year ended June 30, 2016, bond issuance costs and bank fees were $5.5 million, a 57.4% decrease from $12.9 million in 2015. For the year ended June 30, 2016, the decrease in bond issuance costs and bank fees was mainly due a decrease in bond issuance fees. For the year ended June 30, 2016, we did not incur bond issuance fees associated with a current year bond refunding, but we did incur $2.1 million of costs associated with the maintenance of our warehouse lines of credit that are used to help facilitate a bond refunding; however, during the year ended June 30, 2015, we incurred $9.1 million of bond issuance costs associated with bond refundings that took place on September 18, 2014 and April 22, 2015.

For the year ended June 30, 2015, bond issuance costs and bank fees were $12.9 million, a 43.2% decrease from $22.7 million in 2014. For the year ended June 30, 2015, the decrease in bond issuance and bank fees was mainly due to a decrease in bond issuance fees. For the year ended June 30, 2015, we incurred $9.1 million of bond issuance fees associated with bond refundings that took place on September 18, 2014 and April 22, 2015. For the year ended June 30, 2014, we incurred $17.1 million of bond issuance fees associated with bond refundings that took place on July 30, 2013, November 20, 2013, March 14, 2014 and June 17, 2014.

Net Realizable Value Adjustment in Amounts due from the Federal Fund

For the year ended June 30, 2016, the net realizable value ("NRV") adjustment in amounts due from the Federal Fund was ($3.6) million, a decrease from $14.3 million in 2015. For the year ended June 30, 2016, the decrease in the NRV adjustment in amounts due from the Federal Fund resulted from the reversal of $4.0 million of NRV allowance during the year ended June 30, 2016, since we believe that amounts due to us from the Fed Fund are collectible. Previously, the maximum default claim reimbursement rate for guaranty agencies was 95%; however, that amount was increased to 100% during December 2015 due to the passage of the Consolidated Appropriations Act, 2016. As a result, the Federal Fund does not have to withhold amounts due to PHEAA in order to pay future claims.

For the year ended June 30, 2015, the NRV adjustment in amounts due from the Federal Fund was $14.3 million, a 40.9% decrease from $24.2 million in 2014. For the year ended June 30, 2015, the decrease in the NRV adjustment in amounts due from the Federal Fund was due to a change in the amounts due to PHEAA from the Federal Fund compared to the adjusted net position (total assets less accounts payable and accrued expenses) of the Federal Fund.

See **Note 4 – Federal Student Loan Reserve Fund (Federal Fund) and Assets held for the U.S. Department of Education** for the details on the net position held by us for ED in the Federal Fund.

Changes in Net Position

The following table shows the changes in net position:

(Dollars in thousands)

For the years ended June 30,		**2016**	2015	2014
Income before grants and financial aid	$	**96,812**	110,693	222,119
Commonwealth of Pennsylvania grants		**365,359**	403,616	397,293
Federal grants		**1,587**	1,572	1,876
Grants and other financial aid, net of refunds		**(466,439)**	(470,533)	(485,789)
Grant funds returned to the Commonwealth		**(49,628)**	-	-
Total grants and financial aid, net of refunds		**(149,121)**	(65,345)	(86,620)
Changes in net position	$	**(52,309)**	45,348	135,499

Commonwealth of Pennsylvania Grants

For the year ended June 30, 2016, Commonwealth of Pennsylvania grants were $365.4 million, a 9.5% decrease from $403.6 million in 2015. For the year ended June 30, 2016, the decrease in the Commonwealth of Pennsylvania grants was mainly due to the Commonwealth allocating fewer funds to the Pennsylvania State Grant program and requiring PHEAA to make up for the shortfall in the Commonwealth's allocation for the current fiscal year. For the year ended June 30, 2016, the Commonwealth allocated $266.2 million to the Pennsylvania State Grant program, a 22.8% decrease from $344.9 million in 2015. For the year ended June 30, 2016, we contributed $125.0 million to the Pennsylvania State Grant program, a 66.7% increase from $75.0 million in 2015

For the year ended June 30, 2015, Commonwealth of Pennsylvania grants were $403.6 million, a 1.6% increase from $397.3 million in 2015. For the year ended June 30, 2015, the increase in the Commonwealth of Pennsylvania grants was due to $5.0 million of funding related to the Ready to Succeed Scholarship program that was not appropriated or funded by the Commonwealth in the previous year.

Grants and Other Financial Aid Activity, net of refunds

The following table shows the changes within "Grants and other financial aid activity, net of refunds".

(Dollars in thousands)

For the years ended June 30,		2016	2015	2014
Pennsylvania State Grant Program, net of refunds	$	**392,902**	401,339	424,612
Institutional Assistance Grant Program, net of refunds		**24,495**	24,643	24,332
Pennsylvania National Guard Education Assistance Program, net of refunds		**12,488**	11,828	10,779
Matching Funds Grant Program, net of refunds		**11,566**	11,914	11,241
Pennsylvania Distance Education Program, net of refunds		**10,323**	7,313	5,750
Pennsylvania Ready to Succeed Scholarship Program, net of refunds		**5,019**	4,806	-
Pennsylvania Targeted Industry Cluster Certificate Scholarship Program, net of refunds		**4,886**	4,373	5,146
Higher Education for the Disadvantaged Program, net of refunds		**2,283**	2,537	2,002
Other Programs, net of refunds		**2,477**	1,780	1,927
Total grants and other financial aid, net of refunds	$	**466,439**	470,533	485,789

For the year ended June 30, 2016, grants and other financial aid, net of refunds, were $466.4 million, a 0.9% decrease from $470.5 million during 2015.

For the year ended June 30, 2015, grants and other financial aid, net of refunds, were $470.5 million, a 3.1% decrease from $485.8 million during 2014.

For the years ended June 30, 2016 and 2015, the decreases in grants and other financial aid, net of refunds, were primarily due to the timing of funds disbursed from various grant programs.

Grants Funds Returned to the Commonwealth

For the year ended June 30, 2016, grant funds returned to the Commonwealth was $49.6 million compared to zero in 2015. The increase in grant funds returned to the Commonwealth was due to PHEAA transferring $10.6 million of grant funds during March 2016 and $39.0 million of grant funds during April.

The $10.6 million of grant funds returned to the Commonwealth during March 2016 was due to the Commonwealth's annual budget process in which the General Assembly lapses unused funds from programs that are administered by the various Commonwealth Agencies. There were four programs administered by PHEAA that were de-funded and they are no longer in operation. The unused funds from these programs were returned to the Commonwealth and the Commonwealth can reallocate these funds to other priorities, as mandated by the General Assembly.

The $39.0 million of grant funds returned to the Commonwealth during April 2016 was due to a reduction in the amounts allocated by the Commonwealth to the Pennsylvania State Grant program, which was contingent upon PHEAA contributing an additional $39.0 million to the Pennsylvania State Grant program. On December 29, 2015, the Commonwealth passed a partial budget that originally allocated $305.2 million to the Pennsylvania State Grant Program. On March 28, 2016, the Commonwealth's budget for 2015-16 (House Bill 1801) was approved without the Governor's signature and became law, and House Bill 1801 reduced the original allocation from $305.2 million to $266.2. Additionally, House Bill 1801, section 2105, stated that the appropriation of $266.2 million was contingent on PHEAA committing, encumbering and expending $39.0 million of its earnings for the Pennsylvania State Grant program.

Student Loan Receivables, net

In the table below, we present our student loan receivables net.

(Dollars in thousands)

As of June 30,		2016	2015	2014
FFEL student loans:				
Consolidation	$	**4,705,793**	5,396,113	5,654,677
Stafford		**1,074,457**	1,325,486	1,325,199
PLUS		**104,978**	142,308	145,295
Supplemental Loans for Students (SLS)		**987**	1,293	1,092
Total FFEL student loans		**5,886,215**	6,865,200	7,126,263
Private		**28,789**	34,355	38,482
HEAL		**27,974**	37,689	50,785
Unamortized premium on student loan purchases		**8,203**	10,434	8,304
Unamortized discount on student loan purchases		**(11,913)**	(12,672)	(11,053)
		5,939,268	6,935,006	7,212,781
Allowance for loan losses		**(21,229)**	(20,871)	(19,712)
Student loan receivables, net	$	**5,918,039**	6,914,135	7,193,069

As of June 30, 2016, student loan receivables, net, were $5.9 billion, a 14.5% decrease from $6.9 billion in 2015. As of June 30, 2016, the decrease in student loan receivables, net, was mainly due to borrower payments.

As of June 30, 2015, student loan receivables, net, were $6.9 billion, a 4.2% decrease from $7.2 billion 2014. As of June 30, 2015, the decrease in student loan receivables, net, was due to borrower payments, which was offset by purchases of student loans from third party financial institutions.

A discussion on the student loan delinquency trends and the allowance for loan losses follows.

Delinquencies have the potential to adversely affect earnings through increased collection costs and charge-offs. The June 30, 2016 table below presents our student loan delinquency trends on FFEL and non-FFEL student loans, but does not include $6.5 million of student loans categorized as non-performing, $8.4 million of student loans categorized as uninsured and $72 thousand of student loans with credit balances.

(Dollars in thousands)

As of June 30, 2016	FFEL		Non-FFEL		Total	
Loans in-school/in-grace	$ 7,814		$ 67		$ 7,881	
Loans in deferment and forbearance:						
Deferment	428,490		1,336		429,826	
Forbearance	589,672		683		590,355	
Total loans in-school/in-grace, and deferment and forbearance	$ 1,025,976		$ 2,086		$ 1,028,062	
Loans in repayment:						
Current	$ 4,281,724	88.2%	$ 47,558	92.2%	$ 4,329,282	88.3%
31 – 60 days	180,416	3.7%	1,231	2.4%	181,647	3.7%
61 – 90 days	107,048	2.2%	313	0.6%	107,361	2.2%
91 – 120 days	63,476	1.3%	168	0.3%	63,644	1.3%
121 – 180 days	97,769	2.0%	74	0.1%	97,843	2.0%
181 – 270 days	84,285	1.7%	57	0.1%	84,342	1.7%
271 days or greater	27,962	0.6%	887	1.7%	28,849	0.6%
Claims filed not paid	10,140	0.3%	1,292	2.6%	11,432	0.2%
Total loans in repayment	$ 4,852,820	100.0%	$ 51,580	100.0%	$ 4,904,400	100.0%

The June 30, 2015 table below presents our student loan delinquency trends on FFEL and non-FFEL student loans, but does not include $8.9 million of student loans categorized as non-performing, $9.9 million of student loans categorized as uninsured and $139 thousand of student loans with credit balances.

(Dollars in thousands)

As of June 30, 2015	FFEL		Non-FFEL		Total	
Loans in-school/in-grace	$ 14,484		$ 117		$ 14,601	
Loans in deferment and forbearance:						
Deferment	569,441		1,870		571,311	
Forbearance	727,397		553		727,950	
Total loans in-school/in-grace, and deferment and forbearance	$ 1,311,322		$ 2,540		$ 1,313,862	
Loans in repayment:						
Current	$ 4,802,280	86.6%	$ 60,748	92.3%	$ 4,863,028	86.7%
31 – 60 days	232,167	4.2%	1,064	1.6%	233,231	4.2%
61 – 90 days	126,067	2.3%	242	0.4%	126,309	2.3%
91 – 120 days	74,596	1.3%	278	0.4%	74,874	1.3%
121 – 180 days	128,978	2.3%	219	0.3%	129,197	2.3%
181 – 270 days	115,456	2.1%	83	0.1%	115,539	2.1%
271 days or greater	45,317	0.8%	674	1.0%	45,991	0.8%
Claims filed not paid	21,533	0.4%	2,474	3.9%	24,007	0.3%
Total loans in repayment	$ 5,546,394	100.0%	$ 65,782	100.0%	$ 5,612,176	100.0%

Allowance for Loan Losses

FFEL Program Loans

The allowance for loan losses-FFEL program loans represents our estimate of the costs related to the risk sharing on FFEL program loans only. This allowance does not include the risk associated with non-FFEL program loans. We record a provision for loan losses on "FFEL program loans" as follows:

- FFEL program loans - The allowance for loan losses represents our estimate of the costs related to the risk sharing on the FFEL program loans and it is a weighted average calculation based upon the following guarantee rates:
    - 100% of the unpaid principal balance of each loan disbursed before October 1, 1993;
    - Not more than 98% of the unpaid principal balance of each loan disbursed on or after October 1, 1993 and before July 1, 2006; and
    - Not more than 97% of the unpaid principal balance of each loan disbursed on or after July 1, 2006 and before July 1, 2010. Student loans were no longer originated under the FFEL program on or after July 1, 2010.
- Cure loans – We consider a loan to be in "cure" status when a due diligence violation has occurred on a PHEAA owned loan and the servicer is attempting to correct or "cure" the loan. When a student loan enters a cure status, the guarantor will not guarantee the student loan and reimburse the lender for the outstanding principal and interest of the loan if the borrower defaults on the student loan while in a cure status. A loan can become incurable after three years of unsuccessfully trying to cure the loan, if a loan does not pay-off within the defined terms (i.e. 120 months for a 10 year Stafford loan), or due to an origination error. We

record a provision for loan losses on any loans that have been in a cure status for greater than 24 months, and any loans considered incurable.

This allowance along with the allowance for loan losses-other program loans (Non-FFEL) are included in the section titled "Allowance for loan losses" in **Note 6 – Student Loans Receivable, net**.

When a student loan defaults, the guarantor reimburses the lender based on the disbursement date of the student loan. We record a charge-off for the difference between the ending balance of the student loan and the guarantee rate.

We report the allowance for loan losses-FFEL program loans in the table that follows along with the allowance for loan losses-other program loans (Non-FFEL) in "Student loans receivable, net" in the Statements of Net Position. The provision for loan losses on FFEL student loans in the table that follows along with the provision for loan losses on non-FFEL program loans are included in the "provision for losses" in the Statements of Revenues, Expenses and Changes in Net Position.

(Dollars in thousands)

As of June 30,		**2016**	2015	2014
Balance at beginning of period	$	**15,100**	14,557	12,621
Provision for losses		**7,882**	6,536	7,384
Charge-offs		**(6,383)**	(5,993)	(5,448)
Balance at end of period	$	**16,599**	15,100	14,557
Ending balance of FFEL student loans	$	**5,886,215**	6,865,200	7,126,263
Allowance as a percentage of ending balance of student loans		**0.28%**	0.22%	0.20%

As of June 30, 2016, we believe the allowance for loan losses is adequate to cover the inherent losses on our FFEL student loan portfolio.

For the year ended June 30, 2016, the increase in the provision for loan losses was due to an increase in claim payments.

Other Program Loans (Non-FFEL)

The allowance for loan losses-other program loans (Non-FFEL) represents our estimate of the risk associated with non-FFEL program loans, such as private and cure loans. We record a provision for loan losses on "other program loans" as follows:

- Private loans – We record a provision for loan losses on private loans when the student loan payment status is no longer current (payments are more than 120 days past due) and/or non-performing.
    - The student loans formerly guaranteed by The Education Resource Institute, Inc. (TERI) are included with the private loans. We record a provision on 100% of the TERI student loan balances that have a payment delinquency status of 121 days and greater, and those loans classified as "claims filed but not paid".
    - The student loans associated with Pennsylvania nursing schools and the Health Education Assistance Loan ("HEAL") supplemental student loans are included with the private loans. The Pennsylvania nursing school student loans are self- insured by us and the HEAL supplemental student loans are private student loans without a guarantee. We record a provision for loan losses for these programs when the student loans are greater than 120 days delinquent and student loans that have a claim filed or are non-performing.

These allowances along with allowance for losses on FFEL program loans are included in the section titled "Allowance for loan losses" in **Note 6 – Student Loans Receivable, net**.

We report the allowance for loan losses-other program loans (Non-FFEL) in the table that follows along with the allowance for loan losses-FFEL program loans within "Student loans receivable, net" within the Statements of Net Position. The provision for loan losses on non-FFEL student loans in the table that follows along with the provision for loan losses on FFEL program loans are included in the "provision for losses" in the Statements of Revenues, Expenses and Changes in Net Position.

(Dollars in thousands)

As of June 30,		2016	2015	2014
Balance at beginning of period	$	**5,771**	5,155	4,463
Provision for losses		**(1,141)**	616	680
Recoveries		**-**	-	12
Balance at end of period	$	**4,630**	5,771	5,155
Ending balance of non-FFEL student loans	$	**56,763**	72,045	89,267
Allowance as a percentage of ending balance of student loans		**8.16%**	8.01%	5.77%

As of June 30, 2016, we believe the allowance for loan losses is adequate to cover the inherent losses on our non-FFEL student loan portfolio.

Debt Activity and Capital Assets

Debt Activity

The schedule that follows contains select information from the Statements of Net Position, which relate to our debt activity.

(Dollars in thousands)

As of June 30,		2016	2015	2014
Deferred outflow of resources:				
Deferred loss on bond refundings	$	**1,299**	2,013	2,728
Current liabilities:				
Student loan financings	$	**938,213**	903,779	444,140
Other financings		**3,895**	3,745	3,660
Long-term liabilities:				
Student loan financings, net	$	**4,751,841**	5,852,233	6,621,556
Other financings, net		**30,734**	35,290	39,772
Deferred inflow of resources:				
Deferred gain on bond refundings	$	**134,067**	168,779	192,404

Our enabling legislation imposes a debt limit, which states that the aggregate principal amount of bonds, notes and similar evidences of indebtedness of the Agency ("PHEAA") shall not exceed twenty percent (20%) of the total of loans purchased, made or guaranteed by PHEAA.

As of June 30, 2016, our outstanding debt, excluding our blended component units, the deferred gain and loss on bond refundings, premiums and discounts on bonds, amounted to $1.2 billion, which was below the 20% threshold mentioned above. The blended component units are excluded from this threshold, because their debt was not issued by PHEAA. As of June 30, 2016, the outstanding debt of our blended component units was $4.6 billion, which was related to the student loan trusts. See **Note 12 – Blended Component Units** for more details on the student loan trusts.

As of June 30, 2015, our outstanding debt, excluding our blended component units, the deferred gain and loss on bond refundings, premiums and discounts on bonds, amounted to $1.4 billion, which was below the 20% threshold mentioned above. The blended component units are excluded from this threshold, because their debt was not issued by PHEAA. As of June 30, 2015, the outstanding debt of our blended component units was $5.5 billion, which was related to the student loan trusts.

As of June 30, 2014, our outstanding debt, excluding our blended component units, the deferred gain on bond refundings, premiums and discounts on bonds, amounted to $2.8 billion, which was below the 20% threshold mentioned above. The blended component units are excluded from this threshold, because their debt was not issued by PHEAA. As of June 30, 2014, the outstanding debt of our blended component units was $4.3 billion, which was related to the student loan trusts.

The following tables show the financing (bond market and financial institutions) of our debt activity.

(Dollars in thousands)

For the years ended June 30,		2016	2015	2014
Capital market activity				
Proceeds from issuing student loan floating rate notes	$	**-**	1,279,519	2,022,952
Repayment of student loan floating rate notes		**(853,142)**	(838,030)	(589,022)
Repayment of student loan auction rate security bonds		**(50,200)**	(1,412,800)	(835,500)
Student loan financing activity				
Proceeds from student loan financings	$	**-**	1,649,158	891,266
Repayment of student loan financings		**(165,566)**	(989,519)	(1,566,087)
Repayment of student loan variable rate funding notes		**-**	-	(319,006)
Capital financing activity				
Repayment of capital lease obligations	$	**-**	-	(76)
Other financing activity				
Repayment of term and other financings	$	**-**	-	(4,827)
Repayment of capital acquisition refunding bonds		**(3,745)**	(3,660)	(3,635)

2016 Debt Activity

Capital Market Activity & Student Loan Financing Activity

For the year ended June 30, 2016, the $903.3 million in the capital market activity repayments was due to required debt payments.

For the year ended June 30, 2016, the $165.6 million in the student loan financing activity repayments was due to the repayment of funds on our warehouse lines of credit.

Other Financing Activity

For the year ended June 30, 2016, the $3.7 million in other financing activity repayments was due to required principal and interest payments on the Capital Acquisition Refunding Bonds, Series of 2012.

See **Note 8 – Notes and Bonds Payable and Other Financings** for more details on the above debt activity.

2015 Debt Activity

Capital Market Activity & Student Loan Financing Activity

For the year ended June 30, 2015, the $1.3 billion in the capital market activity proceeds was due to the PHEAA Student Loan Trust 2014-3 bond issuance on September 18, 2014 and the PHEAA Student Loan Trust 2015-1 bond issuance on April 22, 2015. The $2.3 billion in the capital market activity repayments was due to the refunding of the 1997 Master Trust and scheduled debt payments.

For the year ended June 30, 2015, the $1.6 billion in the student loan financing activity proceeds was due to the execution of various borrowing notices through our warehouse lines of credit. The funds from the warehouse lines of credit were used in the bond refunding of the 1997 Master Trust. The $989.5 million in the student loan financing activity repayments was due to the repayment of funds on our warehouse lines of credit and scheduled debt payments.

Other Financing Activity

For the year ended June 30, 2015, the $3.7 million in other financing activity repayments was due to required principal and interest payments on the Capital Acquisition Refunding Bonds, Series of 2012.

Capital Assets

The following table shows our capital assets, net of accumulated depreciation and amortization, except for land, which is a non-depreciable asset.

(Dollars in thousands)

As of June 30,		**2016**	2015	2014
Land	$	**8,038**	8,038	2,946
Buildings and improvements, net		**33,082**	33,371	32,811
Purchased software, net		**11,410**	8,806	4,441
IT equipment, net		**9,824**	8,663	7,056
Software development, net		**9,617**	9,305	8,400
Other, net		**7,116**	7,776	5,985
	$	**79,087**	75,959	61,639

As of June 30, 2016, capital assets, net of accumulated depreciation and amortization, were $79.1 million, a 4.1% increase from $76.0 million as of June 30, 2015. The increase in capital assets, net of accumulated depreciation and amortization, was mainly due to purchased software.

As of June 30, 2015, capital assets, net of accumulated depreciation and amortization, were $76.0 million, a 23.4% increase from $61.6 million as of June 30, 2014. The increase in capital assets, net of accumulated depreciation and amortization, was mainly due to the purchase of land, software and IT equipment. The land purchase was used for additional parking at our headquarters site.

Net Position

The following table shows our net position (restricted and unrestricted).

(Dollars in thousands)

As of June 30,		**2016**	2015	2014
Net investment in capital assets	$	**79,087**	75,959	61,639
Restricted for debt service		**310,324**	263,381	216,916
Restricted for financial aid grant programs		**52,079**	61,478	41,110
Unrestricted		**310,221**	403,202	709,038
	$	**751,711**	804,020	1,028,703

Net investment in capital assets

Capital assets includes land, buildings and improvements, software development, purchased software, information technology equipment, and other tangible assets that are used in our operations and that have initial useful lives extending beyond a single reporting period. These capital assets are net of accumulated depreciation and amortization, and reduced by the outstanding balances of any bonds, notes or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

As of June 30, 2016, the net investment in capital assets was $79.1 million, a 4.1% increase from $76.0 million as of June 30, 2015. The increase in net investment in capital assets was mainly due to purchased software.

As of June 30, 2015, the net investment in capital assets was $76.0 million, a 23.4% increase from $61.6 million as of June 30, 2014. The increase in net investment in capital assets was mainly due to the purchase of land, software and IT equipment.

Restricted for debt service

We have net position restricted for debt service that is held under various indentures related to financing our student loan portfolios.

As of June 30, 2016, we had net position restricted for debt service of $310.3 million, a 17.8% increase from $263.4 million as of June 30, 2015. The increase in net position restricted for debt service was due to $64.2 million of operating income restricted for debt service, which was offset by $17.2 million of transfers to unrestricted net position. See **Note 11 - Segment Information** for more details.

As of June 30, 2015, we had net position restricted for debt service of $263.4 million, a 21.4% increase from $216.9 million as of June 30, 2014. The increase in net position restricted for debt service was due to $55.7 million of operating income restricted for debt service, which was offset by $9.2 million of transfers to unrestricted net position.

Restricted for financial aid grant programs

We have net position restricted for financial aid grant programs, because of the Commonwealth of Pennsylvania grants and federal grants that relate to specific programs. This net position is restricted until we disburse program-related grants.

As of June 30, 2016, we had net position restricted for financial aid grant programs of $52.1 million, a 15.3% decrease from $61.5 million as of June 30, 2015. The decrease in net position restricted for financial aid grant programs was mainly due to $902.5 thousand of operating income restricted for financial aid grant programs, $366.9 million of grant funding, $125.0 million of transfers from the Pennsylvania State Grant Fund (unrestricted), which was offset by $451.1 million of grant disbursements, net of refunds, $49.6 million of grant funds returned to the Commonwealth, $1.3 million of transfers to the Pennsylvania Distance Education Program fund (unrestricted) and $228 thousand of transfers from the Pennsylvania Higher Education Foundation fund to PHEAA's Discretionary Fund (unrestricted).

As of June 30, 2015, we had net position restricted for financial aid grant programs of $61.5 million, a 49.6% increase from $41.1 million as of June 30, 2014. The increase in net position restricted for financial aid grant programs was mainly due to $632.7 thousand of operating income restricted for financial aid grant programs, $405.2 million of grant funding, and $75.0 million in transfers from the Pennsylvania State Grant Program Supplement fund (unrestricted), which were offset by $458.7 million of grant disbursements, net of refunds, $1.0 million of transfers to the Pennsylvania Distance Education Program fund (unrestricted) and $771 thousand of transfers from the Pennsylvania Higher Education Foundation (restricted for financial aid grant programs) to the PHEAA Discretionary Fund (unrestricted).

Unrestricted

Under Commonwealth law, our statutory purpose is to increase higher education opportunities for Pennsylvania residents. Net position that we report as unrestricted is statutorily restricted to our purpose. The Higher Education Act Amendments of 1998 also restrict our use of net position related to FFEL guaranty activities to fulfilling our guaranty responsibilities and other student financial aid related activities selected by us. Because that restriction is consistent with our statutory purpose, we consider net position related to those activities to be unrestricted.

As of June 30, 2016, we had unrestricted net position of $310.2 million, a 23.1% decrease from $403.2 million as of June 30, 2015. The decrease in unrestricted net position was due to unrestricted operating income of $31.8 million, $17.2 million of funds transferred from net position restricted for debt service, $1.3 million of funds transferred from the Pennsylvania State Grant Program (restricted for financial aid grant programs) to the Pennsylvania Distance Education Program fund, $228 thousand of funds transferred from the Pennsylvania Higher Education Foundation (restricted for financial aid grant programs) to the PHEAA Discretionary Fund, which was offset by $125.0 million of funds transferred to the Pennsylvania State Grant program, $15.3 million of net grant disbursements and $3.2 million of funds transferred to net investment in capital assets.

As of June 30, 2015, we had unrestricted net position of $403.2 million, a 43.1% decrease from $709.0 million as of June 30, 2014. The decrease in unrestricted net position was due to unrestricted operating income of $54.3 million, $9.2 million of funds transferred from net position restricted for debt service, $1.0 million of funds transferred from the Pennsylvania State Grant Program (restricted for financial aid grant programs) to the Pennsylvania Distance Education Program supplemental fund, $771 thousand of funds transferred from the Pennsylvania Higher Education Foundation (restricted for financial aid grant programs) to PHEAA's Discretionary Fund, which was offset by the $270.0 million cumulative effect of changing to a new accounting principle with the adoption and implementation of GASB Statements No. 68 and 71, $75.0 million of funds transferred to the Pennsylvania State Grant program, $11.8 million of net grant disbursements and $14.3 million of funds transferred to net investment in capital assets.

Federal Student Loan Reserve Fund (Federal Fund)

We manage the Federal Fund solely for our activities as a guarantor under the FFEL program. We pay claims on defaulted loans out of the Federal Fund, which belongs to the federal government. The assets of the Federal Fund and the earnings on those assets are, at all times, the property of the United States government. We must exercise the level of care required of a fiduciary charged with the duty of protecting, investing, and administering the money of others.

The following table shows the changes in net position in the Federal Fund.

(Dollars in thousands)

For the years ended June 30,		**2016**	2015	2014
Additions				
Collections on defaulted loans	$	**1,023,342**	765,731	764,407
Reinsurance from the U.S. Department of Education		**1,010,666**	1,139,315	1,266,444
Transfers of guarantee reserves		**-**	(3)	(95)
Net appreciation in fair value of investments		**79**	36	24
Total additions		**2,034,087**	1,905,079	2,030,780
Deductions				
Purchases of defaulted loans from lenders		**1,023,336**	1,181,082	1,313,693
Reimbursement to U.S. Department of Education for federal share of defaulted loans collections		**779,537**	603,212	533,417
Reimbursement to PHEAA for our retention of defaulted loans collections		**207,316**	96,456	204,175
Default aversion fees, net		**9,579**	9,306	10,591
Total deductions		**2,019,768**	1,890,056	2,061,876
Net increase (decrease)		**14,319**	15,023	(31,096)
Net liabilities, beginning of period		**(186,818)**	(201,841)	(170,745)
Net liabilities, end of period	$	**(172,499)**	(186,818)	(201,841)

For the year ended June 30, 2016, collections on defaulted loans were $1.0 billion, a 30.6% increase from $765.7 million in 2015. For the year ended June 30, 2015, collections on defaulted loans were $765.7 million, a 0.2% increase from $764.4 million in 2014.

For the year ended June 30, 2016, purchases of defaulted loans were $1.0 billion, a 16.7% decrease from $1.2 billion in 2015. For the year ended June 30, 2015, purchases of defaulted loans were $1.2 billion, a 7.7% decrease from $1.3 billion in 2014.

Under the Higher Education Act of 1965, as amended, Section 428(c)(9)(A), we are required to maintain a current minimum reserve level of at least 0.25% of the total attributable amount of all outstanding loans guaranteed. Historically, ED has calculated this ratio at September 30, which is the close of the federal fiscal year, based upon regulatory reports that we file with ED.

On December 10, 2014, Federal Student Aid, an office of ED, issued a letter informing Guaranty Agencies of the changes ED is making to certain reporting requirements for federal fiscal year 2015. One of the changes was to the methodology for calculating the minimum Federal Reserve Ratio, because the previous methodology did not meet statutory goals. Beginning with federal fiscal year 2015, the minimum Federal Reserve Ratio is calculated without adding allowances and other non-cash charges back to the Federal Fund. The minimum Federal Reserve Ratio is calculated as follows: Federal Fund Balance (Form 2000 AR26) divided by Original Principal Outstanding.

The table that follows displays our calculation of the Federal Reserve Ratio. The gain contingencies included in the following table reflects the projected future cash receipts to the Federal Fund based on current claims paid to date, which cannot be recognized under generally accepted accounting principles. The gain contingencies and adjustments displayed in the following table were agreed to in a management plan approved by ED on May 22, 2007.

(Dollars in thousands)		**As of June 30, 2016**	As of September 30, 2015
Generally accepted accounting principles – net position	$	**(172,499)**	(188,747)
Gain contingency – default aversion fee rebate payable from PHEAA to the Federal Fund		**5,085**	3,349
Gain contingency – collections complement on future default collections		**82,787**	109,072
Default aversion fees payable to PHEAA, but not transferred from the Federal Fund to PHEAA		**191,761**	186,035
Federal Fund balance	$	**107,134**	109,709
Original principal outstanding	$	**29,013,133**	31,175,068
Federal reserve ratio		**0.37%**	0.35%

See **Note 4 – Federal Student Loan Reserve Fund (Federal Fund) and Assets Held for the U.S. Department of Education** for more details on the net position held by us for ED in the Federal Fund.

Contacting Us

If you have questions about this report, please contact our Financial Management Division at 1200 N. 7th Street, Harrisburg, PA 17102.

Phone – (717) 720-7890
Fax – (717) 720-3923
Email – finrptg@pheaa.org

September 22, 2016

Statements of Revenues, Expenses and Changes in Net Position
For the years ended June 30,
(Dollars in thousands)

		2016	2015
Operating revenues and expenses			
Interest revenue			
Student loans	$	**147,512**	154,985
Investments		**6,615**	5,679
Total interest revenue		**154,127**	160,664
Interest expense			
Student loan financings		**37,324**	42,058
Other financings		**502**	580
Total interest expense		**37,826**	42,638
Net interest revenue		**116,301**	118,026
Provision for loan losses		**(6,741)**	(7,152)
Net interest revenue after provision for loan losses		**109,560**	110,874
Noninterest revenue			
Servicing fees		**324,664**	307,922
Retention of collections on defaulted loans, net		**170,809**	130,975
Federal fees		**18,922**	20,634
Other		**1,586**	(1,194)
Total noninterest revenue		**515,981**	458,337
Operating revenues		**625,541**	569,211
Operating expenses			
Personnel and benefits		**305,489**	257,450
Professional services		**97,073**	58,698
Information technology		**50,828**	43,930
Mail services		**32,588**	35,148
Depreciation		**13,770**	11,789
Other		**28,867**	51,271
Total operating expenses		**528,615**	458,286
Operating income		**96,926**	110,925
Non-operating losses			
Loss on sale of capital assets		**(114)**	(232)
Income before grants and financial aid		**96,812**	110,693
Grants and financial aid			
Commonwealth of Pennsylvania grants		**365,359**	403,616
Federal grants		**1,587**	1,572
Grants and other financial aid, net of refunds		**(466,439)**	(470,533)
Grant funds returned to the Commonwealth of Pennsylvania		**(49,628)**	-
Total grants and financial aid, net of refunds		**(149,121)**	(65,345)
Changes in net position		**(52,309)**	45,348
Net position, beginning of period		**804,020**	758,672
Net position, end of period	$	**751,711**	804,020

See accompanying notes to financial statements.

Statements of Net Position
As of June 30,
(Dollars in thousands)

		2016	2015
Current assets:			
Cash and cash equivalents	$	**72,713**	70,238
Restricted cash and cash equivalents		**223,188**	257,751
Restricted cash and cash equivalents – due to customers		**72,256**	64,470
Investments		**531,706**	562,145
Restricted investments		**50,661**	60,218
Student loans receivable		**962,917**	1,095,033
Interest income receivable		**77,964**	94,657
Due from Federal Student Loan Reserve Fund, net		**37,074**	69,349
Federal Student Loan Reserve Fund assets held for U.S. Dept. of Ed., net		**55,533**	69,349
Other assets		**66,586**	47,477
Total current assets		**2,150,598**	2,390,687
Long-term assets:			
Student loans receivable, net		**4,955,122**	5,819,102
Capital assets, net		**79,087**	75,959
Total long-term assets		**5,034,209**	5,895,061
Total assets		**7,184,807**	8,285,748
Deferred outflow of resources:			
Deferred outflows of resources related to pensions		**126,826**	39,948
Deferred loss on bond refundings		**1,299**	2,013
Total deferred outflow of resources		**128,125**	41,961
Current liabilities:			
Accounts payable and accrued expenses		**183,456**	144,122
Student loan financings		**938,213**	903,779
Amounts related to the Federal Student Loan Reserve Fund		**55,533**	69,349
Other financings		**3,895**	3,745
Total current liabilities		**1,181,097**	1,120,995
Long-term liabilities:			
Student loan financings, net		**4,751,841**	5,852,233
Net pension liability		**440,673**	323,866
Other financings, net		**30,734**	35,290
Accrued expenses		**21,582**	21,007
Total long-term liabilities		**5,244,830**	6,232,396
Total liabilities		**6,425,927**	7,353,391
Deferred inflow of resources:			
Deferred gain on bond refundings		**134,067**	168,779
Deferred inflows of resources related to pensions		**872**	1,068
Deferred gain on sales leaseback		**355**	451
Total deferred inflow of resources		**135,294**	170,298
Net position:			
Net investment in capital assets		**79,087**	75,959
Restricted for debt service		**310,324**	263,381
Restricted for financial aid grant programs		**52,079**	61,478
Unrestricted		**310,221**	403,202
Total net position	$	**751,711**	804,020

See accompanying notes to financial statements.

(Dollars in thousands)

		2016	2015
Cash flows from operating activities			
Interest received on student loans	$	**70,111**	62,104
Principal received on student loans		**1,124,014**	1,138,959
Student loan purchases		**(847,994)**	(955,589)
Student loan sales, including net gains and losses		**808,344**	191,621
Servicing fees		**307,621**	306,941
Retention of collections on defaulted loans		**203,887**	152,393
Federal fees		**19,355**	21,166
Default aversion fee rebates		**(902)**	(4,865)
Other		**829**	1,187
Payment of operating expenses		**(452,869)**	(453,805)
Net cash provided by operating activities		**1,232,396**	460,112
Cash flows from noncapital financing activities			
Proceeds from the issuance of noncapital debt		**-**	2,928,677
Principal paid on noncapital debt		**(1,072,653)**	(3,244,009)
Interest paid on noncapital debt		**(70,081)**	(66,948)
Bond issuance costs		**(2,066)**	(9,141)
Commonwealth of Pennsylvania grants received		**365,359**	403,616
Federal grants received		**1,587**	1,572
Grants and financial aid paid		**(466,439)**	(470,533)
Grant funds returned to the Commonwealth of Pennsylvania		**(49,628)**	-
Net cash used for noncapital financing activities		**(1,293,921)**	(456,766)
Cash flows from capital and related financing activities			
Purchases of capital assets and development of software, net of disposals		**(17,109)**	(26,438)
Net cash used for capital and related financing activities		**(17,109)**	(26,438)
Cash flows from investing activities			
Proceeds from sales and maturities of investments		**832,104**	853,293
Purchases of investments		**(790,474)**	(958,169)
Interest received on investments		**4,916**	3,994
Net cash provided by (used for) investing activities		**46,546**	(100,882)
Net change in cash and cash equivalents (including restricted cash)		**(32,088)**	(123,974)
Cash and cash equivalents (including restricted cash), beginning of period		**327,989**	451,963
Cash and cash equivalents (including restricted cash), end of period	$	**295,901**	327,989

(continued)

(Dollars in thousands)

		2016	2015
Reconciliation of operating income to net cash provided by operating activities			
Operating income	$	**96,926**	110,925
Adjustments to reconcile operating income to net cash provided by operating activities:			
Depreciation		**13,770**	11,789
Interest paid on noncapital debt		**70,081**	66,948
Investment interest		**(6,615)**	(5,679)
Bond issuance costs		**2,066**	9,141
Pension expense valuation adjustment		**29,733**	14,956
Amortization of premium on loan purchases		**2,229**	3,310
Amortization of deferred gain on bond refunding		**(33,998)**	(22,910)
Amortization of deferred discount on bonds payable		**2,950**	1,987
Amortization of deferred premium on other financings		**(661)**	(737)
Changes in assets and liabilities:			
Decrease in interest income receivable		**16,759**	9,651
Decrease in student loans receivable		**993,867**	275,624
Decrease in amounts due from Federal Student Loan Reserve Fund		**32,275**	21,419
Increase in other assets		**(19,109)**	(579)
Increase (decrease) in accounts payable and accrued expenses		**32,123**	(35,733)
Total adjustments		**1,135,470**	349,187
Net cash provided by operating activities	$	**1,232,396**	460,112

See accompanying notes to financial statements.

Note 1 – About PHEAA

Organization

The Pennsylvania Higher Education Assistance Agency ("PHEAA"), doing business as American Education Services ("AES") and FedLoan Servicing ("FLS"), is a public corporation and government instrumentality created by the Pennsylvania General Assembly on August 7, 1963. Our mission is to improve higher education opportunities for Pennsylvanians.

The Commonwealth of Pennsylvania ("Commonwealth") presents our financial information as a discretely presented component unit in their Comprehensive Annual Financial Report ("CAFR"). Discretely presented component units are legally separate organizations for which the elected officials of the primary government ("Commonwealth") are financially accountable. In addition, discretely presented component units can be other organizations of which the nature and significance of their relationship with the Commonwealth is such that exclusion of these organizations from the Commonwealth's financial statements would be misleading.

We are a discretely presented component unit of the Commonwealth, because the Commonwealth appoints all twenty voting board members; a significant financial burden exists on the Commonwealth to subsidize the Pennsylvania State Grant Program; the Governor of Pennsylvania must approve our debt issuances; and although, the Commonwealth is not obligated for our debt, the Commonwealth has indicated it could take certain actions to satisfy debt holders.

Blended Component Units

PHEAA Student Loan Foundation, Inc.

We formed the PHEAA Student Loan Foundation, Inc. ("Foundation") on August 6, 2002. The Foundation is exempt from federal income tax under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3). Its charitable purpose is to carry out student loan securitization transactions for our benefit. The Foundation is a component unit, because we appoint a majority of the Foundation's board of directors and we can impose our will on the Foundation. The Foundation is a blended component unit of PHEAA, because it provides services entirely to us. As a blended component unit, the financial results of the Foundation are consolidated with the financial results of PHEAA.

PHEAA Student Loan Trust I

On January 15, 2003, the Foundation entered into a trust agreement with a financial institution, which created the PHEAA Student Loan Trust I (the "Trust"), a statutory trust. The Trust was formed under the laws of the State of Delaware and its principal purpose is to securitize student loans and related assets and to acquire student loans from the Foundation and issue promissory notes secured by a pledge of such assets. The assets of the Trust generally include student loans, collections and other payments on the student loans, and funds in trust accounts held by an indenture trustee. The student loans are pledged to an indenture trustee under an indenture agreement, and the student loans provide collateral for a bond issuance. The bonds are payable solely from and secured solely by the trust estate. Principal payments are generally funded from available funds and the principal payments are made to noteholders pro rata on each distribution date in an amount generally equal to the principal distribution amount for that distribution date.

We determined that the Trust should be treated as a component unit in order to keep our financial reports from being misleading due to the material relationship of the Trust with the Foundation. In addition, the Trust is a blended component unit of the Foundation, because the Trust provides services entirely to the Foundation. As a blended component unit, the financial results of the Trust are consolidated with the financial results of the Foundation.

PHEAA Student Loan Trust 2011-1

On April 7, 2011, the Foundation entered into a trust agreement with a financial institution, which created the PHEAA Student Loan Trust 2011-1 (“2011-1 Trust”), a statutory trust. The 2011-1 Trust was formed under the laws of the State of Delaware and its principal purpose is to securitize student loans and related assets, and to acquire student loans from the Foundation and issue promissory notes secured by a pledge of such assets. The assets of the 2011-1 Trust generally include student loans, collections and other payments on the student loans, and funds in trust accounts held by an indenture trustee. The student loans are pledged to an indenture trustee under an indenture agreement, and the student loans provide collateral for a bond issuance. The bonds are payable solely from and secured solely by the trust estate. Principal payments are generally funded from available funds and the principal payments are made to noteholders pro rata on each distribution date in an amount generally equal to the principal distribution amount for that distribution date. The 2011-1 Trust is legally separate and fiscally independent from the Foundation. However, we determined that the 2011-1 Trust should be a component unit in order to keep our financial reports from being misleading due to the material relationship of the 2011-1 Trust with the Foundation. In addition, the 2011-1 Trust is a blended component unit of the Foundation, because the 2011-1 Trust provides services entirely to the Foundation. As a blended component unit, the financial results of the 2011-1 Trust are consolidated with the financial results of the Foundation.

PHEAA Student Loan Trust 2012-1

On October 11, 2012, the Foundation entered into a trust agreement with a financial institution, which created the PHEAA Student Loan Trust 2012-1 (“2012-1 Trust”), a statutory trust. The 2012-1 Trust was formed under the laws of the State of Delaware and its principal purpose is to securitize student loans and related assets, and to acquire student loans from the Foundation and issue promissory notes secured by a pledge of such assets. The assets of the 2012-1 Trust generally include student loans, collections and other payments on the student loans, and funds in trust accounts held by an indenture trustee. The student loans are pledged to an indenture trustee under an indenture agreement, and the student loans provide collateral for a bond issuance. The bonds are payable solely from and secured solely by the trust estate. Principal payments are generally funded from available funds and the principal payments are made to noteholders pro rata on each distribution date in an amount generally equal to the principal distribution amount for that distribution date. The 2012-1 Trust is legally separate and fiscally independent from the Foundation. However, we determined that the 2012-1 Trust should be a component unit in order to keep our financial reports from being misleading due to the material relationship of the 2012-1 Trust with the Foundation. In addition, the 2012-1 Trust is a blended component unit of the Foundation, because the 2012-1 Trust provides services entirely to the Foundation. As a blended component unit, the financial results of the 2012-1 Trust are consolidated with the financial results of the Foundation.

PHEAA Student Loan Trust 2013-1

On March 18, 2013, the Foundation entered into a trust agreement with a financial institution, which created the PHEAA Student Loan Trust 2013-1 (“2013-1 Trust”), a statutory trust. The 2013-1 Trust was formed under the laws of the State of Delaware and its principal purpose is to securitize student loans and related assets, and to acquire student loans from the Foundation and issue promissory notes secured by a pledge of such assets. The assets of the 2013-1 Trust generally include student loans, collections and other payments on the student loans, and funds in trust accounts held by an indenture trustee. The student loans are pledged to an indenture trustee under an indenture agreement, and the student loans provide collateral for a bond issuance. The bonds are payable solely from and secured solely by the trust estate. Principal payments are generally funded from available funds and the principal payments are made to noteholders pro rata on each distribution date in an amount generally equal to the principal distribution amount for that distribution date. The 2013-1 Trust is legally separate and fiscally independent from the Foundation. However, we determined that the 2013-1 Trust should be a component unit in order to keep our financial reports from being misleading due to the material relationship of the 2013-1 Trust with the Foundation. In addition, the 2013-1 Trust is a blended component unit of the Foundation, because the 2013-1 Trust provides services entirely to the Foundation. As a blended component unit, the financial results of the 2013-1 Trust are consolidated with the financial results of the Foundation.

PHEAA Student Loan Trust 2013-2

On March 18, 2013, the Foundation entered into a trust agreement with a financial institution, which created the PHEAA Student Loan Trust 2013-2 (“2013-2 Trust”), a statutory trust. The 2013-2 Trust was formed under the laws of the State of Delaware and its principal purpose is to securitize student loans and related assets, and to acquire student loans from the Foundation and issue promissory notes secured by a pledge of such assets. The assets of the 2013-2 Trust generally include student loans, collections and other payments on the student loans, and funds in trust accounts held by an indenture trustee. The student loans are pledged to an indenture trustee under an indenture agreement, and the student loans provide collateral for a bond issuance. The bonds are payable solely from and secured solely by the trust estate. Principal payments are generally funded from available funds and the principal payments are made to noteholders pro rata on each distribution date in an amount generally equal to the principal distribution amount for that distribution date. The 2013-2 Trust is legally separate and fiscally independent from the Foundation. However, we determined that the 2013-2 Trust should be a component unit in order to keep our financial reports from being misleading due to the material relationship of the 2013-2 Trust with the Foundation. In addition, the 2013-2 Trust is a blended component unit of the Foundation, because the 2013-2 Trust provides services entirely to the Foundation. As a blended component unit, the financial results of the 2013-2 Trust are consolidated with the financial results of the Foundation.

PHEAA Warehouse Facility Trust 2013-1

On April 8, 2013, the Foundation entered into a trust agreement creating the PHEAA Warehouse Facility Trust 2013-1 (“Warehouse Trust 2013-1”) as a statutory trust. The Warehouse Trust 2013-1 was formed under the laws of the State of Delaware and its principal purpose is to securitize student loans and student loan related assets and to acquire student loans from the Foundation and issue a note secured by a pledge of assets. The assets of the Warehouse Trust 2013-1 generally include student loans, collections and other payments on the student loans, and funds in trust accounts held by an indenture trustee. The student loans are pledged to an indenture trustee under an indenture agreement, and the student loans provide collateral for a bond issuance. The bonds are payable solely from and secured solely by the trust estate. Principal payments are generally funded from available funds and the principal payments are made to noteholders pro rata on each distribution date in an amount generally equal to the principal distribution amount for that distribution date. The Warehouse Trust 2013-1 is legally separate and fiscally independent from the Foundation. However, we determined that the Warehouse Trust 2013-1 should be a component unit in order to keep our financial reports from being misleading due to the material relationship of the Warehouse Trust 2013-1with the Foundation. In addition, the Warehouse Trust 2013-1 is a blended component unit of the Foundation, because the Warehouse Trust 2013-1 provides services entirely to the Foundation. As a blended component unit, the financial results of the Warehouse Trust 2013-1 are consolidated with the financial results of the Foundation.

PHEAA Student Loan Trust 2013-3

On October 3, 2013, the Foundation entered into a trust agreement with a financial institution, which created the PHEAA Student Loan Trust 2013-3 (“2013-3 Trust”), a statutory trust. The 2013-3 Trust was formed under the laws of the State of Delaware and its principal purpose is to securitize student loans and related assets, and to acquire student loans from the Foundation and issue promissory notes secured by a pledge of such assets. The assets of the 2013-3 Trust generally include student loans, collections and other payments on the student loans, and funds in trust accounts held by an indenture trustee. The student loans are pledged to an indenture trustee under an indenture agreement, and the student loans provide collateral for a bond issuance. The bonds are payable solely from and secured solely by the trust estate. Principal payments are generally funded from available funds and the principal payments are made to noteholders pro rata on each distribution date in an amount generally equal to the principal distribution amount for that distribution date. The 2013-3 Trust is legally separate and fiscally independent from the Foundation. However, we determined that the 2013-3 Trust should be a component unit in order to keep our financial reports from being misleading due to the material relationship of the 2013-3 Trust with the Foundation. In addition, the 2013-3 Trust is a blended component unit of the Foundation, because the 2013-3 Trust provides services entirely to the Foundation. As a blended component unit, the financial results of the 2013-3 Trust are consolidated with the financial results of the Foundation.

PHEAA Student Loan Trust 2014-1

On October 3, 2013, the Foundation entered into a trust agreement with a financial institution, which created the PHEAA Student Loan Trust 2013-4, a statutory trust under the laws of the State of Delaware. On January 29, 2014, the Foundation and the owner trustee entered into a "First Amendment to the Trust Agreement" ("First Amendment") to modify the legal name of the PHEAA Student Loan Trust 2013-4 to the PHEAA Student Loan Trust 2014-1 ("2014-1 Trust"). On the same date, upon execution of the First Amendment, a "Second Amended and Restated Certificate of Trust" was filed to register the new legal name of the 2014-1 Trust with the Delaware Secretary of State.

The principal purpose of the 2014-1 Trust is to securitize student loans and related assets, and to acquire student loans from the Foundation and issue promissory notes secured by a pledge of such assets. The assets of the 2014-1 Trust generally include student loans, collections and other payments on the student loans, and funds in trust accounts held by an indenture trustee. The student loans are pledged to an indenture trustee under an indenture agreement, and the student loans provide collateral for a bond issuance. The bonds are payable solely from and secured solely by the trust estate. Principal payments are generally funded from available funds and the principal payments are made to noteholders pro rata on each distribution date in an amount generally equal to the principal distribution amount for that distribution date. The 2014-1 Trust is legally separate and fiscally independent from the Foundation. However, we determined that the 2014-1 Trust should be a component unit in order to keep our financial reports from being misleading due to the material relationship of the 2014-1 Trust with the Foundation. In addition, the 2014-1 Trust is a blended component unit of the Foundation, because the 2014-1 Trust provides services entirely to the Foundation. As a blended component unit, the financial results of the 2014-1 Trust are consolidated with the financial results of the Foundation.

PHEAA Student Loan Trust 2014-2

On April 16, 2014, the Foundation entered into a trust agreement with a financial institution, which created the PHEAA Student Loan Trust 2014-2 ("2014-2 Trust"), a statutory trust under the laws of the State of Delaware. The principal purpose of the 2014-2 Trust is to securitize student loans and related assets, and to acquire student loans from the Foundation and issue promissory notes secured by a pledge of such assets. The assets of the 2014-2 Trust generally include student loans, collections and other payments on the student loans, and funds in trust accounts held by an indenture trustee. The student loans are pledged to an indenture trustee under an indenture agreement, and the student loans provide collateral for a bond issuance. The bonds are payable solely from and secured solely by the trust estate. Principal payments are generally funded from available funds and the principal payments are made to noteholders pro rata on each distribution date in an amount generally equal to the principal distribution amount for that distribution date. The 2014-2 Trust is legally separate and fiscally independent from the Foundation. However, we determined that the 2014-2 Trust should be a component unit in order to keep our financial reports from being misleading due to the material relationship of the 2014-2 Trust with the Foundation. In addition, the 2014-2 Trust is a blended component unit of the Foundation, because the 2014-2 Trust provides services entirely to the Foundation. As a blended component unit, the financial results of the 2014-2 Trust are consolidated with the financial results of the Foundation.

PHEAA Student Loan Trust 2014-3

On August 8, 2014, the Foundation entered into a trust agreement with a financial institution, which created the PHEAA Student Loan Trust 2014-3 ("2014-3 Trust"), a statutory trust under the laws of the State of Delaware. The principal purpose of the 2014-3 Trust is to securitize student loans and related assets, and to acquire student loans from the Foundation and issue promissory notes secured by a pledge of such assets. The assets of the 2014-3 Trust generally include student loans, collections and other payments on the student loans, and funds in trust accounts held by an indenture trustee. The student loans are pledged to an indenture trustee under an indenture agreement, and the student loans provide collateral for a bond issuance. The bonds are payable solely from and secured solely by the trust estate. Principal payments are generally funded from available funds and the principal payments are made to noteholders pro rata on each distribution date in an amount generally equal to the principal distribution amount for that distribution date. The 2014-3 Trust is legally separate and fiscally independent from the Foundation. However, we determined that the 2014-3 Trust should be a component unit in order to keep our financial reports from being misleading due to the material relationship of the 2014-3 Trust with the Foundation. In addition, the 2014-3 Trust is a blended component unit of the Foundation, because the 2014-3 Trust provides services entirely to the Foundation. As a blended component unit, the financial results of the 2014-3 Trust are consolidated with the financial results of the Foundation.

PHEAA Student Loan Trust 2015-1

On January 15, 2015, the Foundation entered into a trust agreement with a financial institution, which created the PHEAA Student Loan Trust 2015-1 ("2015-1 Trust"), a statutory trust under the laws of the State of Delaware. The principal purpose of the 2015-1 Trust is to securitize student loans and related assets, and to acquire student loans from the Foundation and issue promissory notes secured by a pledge of such assets. The assets of the 2015-1 Trust generally include student loans, collections and other payments on the student loans, and funds in trust accounts held by an indenture trustee. The student loans are pledged to an indenture trustee under an indenture agreement, and the student loans provide collateral for a bond issuance. The bonds are payable solely from and secured solely by the trust estate. Principal payments are generally funded from available funds and the principal payments are made to noteholders pro rata on each distribution date in an amount generally equal to the principal distribution amount for that distribution date. The 2015-1 Trust is legally separate and fiscally independent from the Foundation. However, we determined that the 2015-1 Trust should be a component unit in order to keep our financial reports from being misleading due to the material relationship of the 2015-1 Trust with the Foundation. In addition, the 2015-1 Trust is a blended component unit of the Foundation, because the 2015-1 Trust provides services entirely to the Foundation. As a blended component unit, the financial results of the 2015-1 Trust are consolidated with the financial results of the Foundation.

The Pennsylvania Higher Education Foundation, Inc.

We supported the formation of the Pennsylvania Higher Education Foundation, Inc. ("PHEF"), which is tax-exempt under Section 501(c)(3) of the Internal Revenue Code. Its charitable purposes include, but are not limited to, activities intended to improve or enhance postsecondary education opportunities for students in Pennsylvania and elsewhere. PHEF is considered a component unit of PHEAA, because PHEAA appointed a voting majority of the PHEF's governing board, and PHEAA has the ability to impose its will on PHEF. PHEF is considered a blended component unit, because PHEF no longer provided services to outside third parties in the form of grants and scholarships used to promote nursing education, but rather provided services entirely to us. As a blended component unit, the financial results of PHEF are consolidated with the financial results of PHEAA.

On March 18, 2015, the Board of Directors authorized the dissolution of PHEF. As part of the dissolution of PHEF, all of the PHEF assets and all funds in its possession that have not been paid or set aside for PHEF's obligations are to be paid to the PHEAA, for its public purposes. On June 8, 2015, PHEF entered into an "Assignment of Rights Incident to Dissolution Agreement" with PHEAA. On October 29, 2015 the "Articles of Dissolution" were received by the PA Department of State Bureau of Corporations and Charitable Organizations, and PHEF was officially dissolved.

Note 2 – Summary of Significant Accounting Policies

Basis of Presentation and Accounting

The basic financial statements have been prepared in conformity with generally accepted accounting principles ("GAAP") in the United States applicable to governments. The Governmental Accounting Standards Board ("GASB") establishes accounting and financial reporting requirements for governments. We prepared our financial statements based on the governmental proprietary fund (enterprise fund) reporting concept, which follows the economic resources measurement focus and accrual basis of accounting. The proprietary fund financial reporting concept focuses on the determination of operating income, changes in net position (or cost recovery), financial position, and cash flows.

Use of Estimates

The preparation of our financial statements in conformity with GAAP requires management to make estimates and assumptions that influence the reported assets, deferred outflow of resources, liabilities, deferred inflow of resources, net position, revenues, and expenses during the reporting periods. Actual results could differ significantly from those estimates.

Cash Equivalents

Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and so near their maturity that they present insignificant risk of changes in value because of changes in interest rates. Cash equivalents include amounts in money market funds, federal agency discount notes, and commercial paper with original maturities at acquisition of three months or less. We report money market funds, commercial paper and federal agency discount notes at fair value.

Restricted Cash and Investments

Restricted cash and investments include cash received from financial institutions pending disbursement for student loans, cash received for the benefit of servicing customers, and cash and investments of bond proceeds held by a trustee and restricted by the provision of the bond indentures and financing agreements. We consider these amounts restricted and they cannot be disbursed for any other purpose.

Investments

Investments include amounts in the Commonwealth’s Treasury Department Bureau of Cash Management and Investments (“Treasury Department”) State Treasury Investment Pool (“STIP”), Pools 998 and 999, within the Commonwealth Investment Program (“CIP”). The CIP is an internal investment pool in which a number of Commonwealth agencies participate.

Pools 998 and 999 each has its own distinct investment strategies, goals, and holdings that reflect the differing needs of Commonwealth funds for income, cash flows, and risk tolerance. Pool 998 is a less liquid vehicle that allows for investment in assets that offer potentially higher returns with commensurate risk. Pool 999 is a highly liquid vehicle that consists of short-term fixed income securities and cash, which provide a high degree of liquidity and security but only modest returns. The Treasury Department provides us information on the net asset value for Pools 998 and 999 and we report the amounts invested in these pools at fair value.

Student Loans Receivable, net

We report student loans in the Statements of Net Position at their unpaid principal balances net of an allowance for inherent losses within our student loan portfolio. Allowances for potential losses on our student loans can result from deficient servicing, risk sharing on defaults and uninsured loans. These allowances are based upon our ongoing evaluation of the loan portfolios, past and anticipated loss experience and the amount and quality of the loans. We maintain the allowances at a level that we believe is adequate to absorb estimated incurred losses, but our evaluation is inherently subjective and the required allowances may significantly change in the future. We report expenses related to risk sharing on defaults in the provision for loan losses, and we include the expenses related to servicing deficiencies in “Other” operating expenses.

Capital Assets, net

We report capital assets at cost net of depreciation and estimated impairment, if any. We report assets held under capital leases at the present value of minimum lease payments net of amortization. We calculate depreciation based on the straight-line method over the estimated useful life of the asset. We amortize assets held under capital leases and leasehold improvements based on the straight-line method over the shorter of the lease term or the estimated useful life of the asset.

We capitalize purchased computer software if the per unit costs, based on per license fee, is $10,000 or more. We capitalize improvements or additions to existing software that constitute a capital outlay or increase the value or life of the asset by 25% of the original cost or life as a betterment and we record it as an addition of value to the existing asset. We calculate amortization based on the straight-line method over the estimated useful life of the purchased software.

Software development involves three phases: preliminary project phase, application development phase and post-implementation/operation phase. We expense the cost associated with the preliminary project and the post-implementation/operating phase. We capitalize internal and external costs associated with the application development phase. The capitalization of costs begins when the preliminary project phase is complete and management has implicitly authorized or commits to funding the software project with the intent it will be completed and used to perform its planned functions. Capitalization will cease no later than at the time when substantial testing is complete and the software is ready for its intended purpose or rendered into service. Upgrades and enhancements are modifications to existing internal-use software that result in additional functionality, that is, modifications to enable the software to perform tasks that it was previously incapable of performing. Upgrades and enhancements normally require new software specifications and may require a change to all or part of the existing software specifications. We capitalize upgrades and enhancements, as defined above. We report software development at cost net of amortization. We calculate amortization based on the straight-line method over the estimated useful life of the software developed.

We capitalize assets that cost $10,000 or more; amounts under that threshold are expensed. The following estimated useful lives are used for significant asset categories:

- Buildings and improvements 7 – 40 years
- Furniture, furnishings and equipment 5 – 10 years
- Software (purchased and development) 3 – 5 years

Deferred Gain (Loss) on Bond Refundings

In a current refunding resulting in the defeasance of debt, the difference between the reacquisition price and the net carrying amount of the old debt is reported as a deferred outflow of resources (deferred loss on bond refundings) or a deferred inflow of resources (deferred gain on bond refundings) and recognized as a component of “Student loan financings” interest expense in a systematic and rational manner over the remaining life of the old debt or the life of the new debt, whichever is shorter.

Compensated Absences

Employees earn annual leave based upon years of service and may carry forward up to 45 days of unused annual leave at the end of each calendar year. We pay employees for accumulated annual leave at termination or retirement. Employees earn sick leave and may carry forward up to 300 days of unused sick leave at the end of each calendar year. We pay employees a portion of accumulated sick leave at retirement based upon a formula. We include in accrued expenses on the Statements of Net Position the estimated amounts payable under these arrangements.

Revenue Recognition

Student loan income

We recognize student loan income as it is earned, net of consolidation rebate fees, government interest, special allowance interest, amortization of student loan purchase premiums and discounts, and write offs and recoveries.

We are required to pay the United States Department of Education ("ED") a monthly Consolidation Loan Rebate Fee as a holder of Federal Consolidation loans. The Consolidation Loan Rebate Fee is equal to 0.0875% of the unpaid principal balance and the accrued interest on all Federal Consolidation Loans disbursed after October 1, 1993, and held by the lender on the last day of the month. This is equal to an annualized rate of 1.05%. Except for loans based on applications received during the period from October 1, 1998 and January 31, 1999, for which the rebate is equal to 0.05167% on a monthly basis or 0.62% on an annual basis. We record the payment of Consolidation Loan Rebate Fees as an offset to student loan income.

We earn interest subsidies and special allowance payments on certain FFEL program student loans within our student loan portfolio. ED makes interest subsidy payments to holders of qualifying FFEL program loans under the Higher Education Act of 1965, as amended, on subsidized Stafford loans and qualifying Consolidation loans, while the student is a qualified student, during a qualifying grace period and during periods of deferment. ED pays the interest subsidy payments based on the amount of interest accruing on the unpaid balance, prior to the commencement of repayment or during the deferment period. We record the interest subsidy payments as student loan income.

ED makes special allowance payments to holders of qualifying insured loans and guaranteed loans, subject to certain requirements under the Higher Education Act of 1965, as amended. ED makes the payments during any quarter in which the special allowance calculation is a positive number. For loans first disbursed between April 1, 2006 and June 30, 2010, ED will collect excess interest for quarters in which the interest rate on the loan exceeds the special allowance support level, commonly referred to as negative special allowance. We record the special allowance payments as student loan income.

The premium or discount on student loans purchases are calculated based on the difference between carrying value and the purchase price of the student loans at the time of purchase. The premium or discount of student loans is amortized over the estimated life of the student loan portfolio. We record the amortization of the student loan purchase premium or discount as student loan income.

Servicing fees

We earn servicing fee revenue by servicing student loans owned by third parties. We recognize servicing fees when we provide the contractual services and we record the unbilled amounts as accounts receivable. We categorize revenue earned from loans owned by ED as "FLS Servicing"; whereas, we categorize revenue earned from loans owned by financial institutions and secondary markets as "Commercial Servicing". Our Remote Servicing line of business provides our system to guarantors and other servicers to use.

Retention of Collections on Defaulted Loans

As a guarantor, we facilitate the guarantee of 97% - 100% of the borrower's outstanding loan balance depending on the disbursement date of the borrower's loan. The federal government reimburses the Federal Fund based upon default rates of the portfolio of guaranteed loans and the disbursement date of the loan. Retention of collections on defaulted loan rates are based upon the Higher Education Act, as amended, and revenue is earned when collected.

Federal Fees

We earn account maintenance fees, which we classify as federal fees, from operating the guaranty agency. ED pays us an annual account maintenance fee that is 0.06% of the original principal amount of outstanding loans guaranteed as long as the guarantee remains in force.

Operating Revenues and Expenses

Operating revenues include net interest revenue earned on student loans and investments and fees earned from providing services. Operating expenses include the costs of providing services and operating all programs. We do not report as a component of operating income the grants we receive and the grants and financial aid we disburse.

Advertising

We incur advertising expenses to make sure Pennsylvanians are aware of postsecondary education opportunities and default prevention initiatives. As we incur advertising expenses, we expense them.

Commonwealth of Pennsylvania and Federal Grant Revenues

Commonwealth and federal grants are non-exchange transactions. We use the receipts as a source of funds to disburse grants and financial aid. Our agreements contain restrictions requiring us to spend the money in accordance with the legislation or grant agreement, but generally do not refer to specific time requirements. Accordingly, we recognize the entire amount as revenue when we receive it.

When an expense is incurred for the purposes of which both restricted and unrestricted net position are available, we first apply restricted resources and then unrestricted resources.

Elimination of Intra-Entity Activity

The Trust I, 2011-1 Trust, 2012-1 Trust, 2013-1 Trust, 2013-2 Trust, 2013-3 Trust, 2014-1 Trust, 2014-2 Trust, 2014-3 Trust, 2015-1 Trust and Warehouse Trust 2013-1 are blended component units of the Foundation, and the Foundation is a blended component unit of PHEAA. In addition, PHEF is a blended component unit of PHEAA. We consider the resource flows between PHEAA and the blended component units as intra-entity, because PHEAA is the administrator and servicer for the blended component units. We eliminate the intra-entity activity in the Statements of Net Position, the Statements of Revenues, Expenses and Changes in Net Position and the Statements of Cash Flows.

Note 3 – Recently Issued GASB Pronouncements

During 2015, the GASB issued Statement No. 72 – *Fair Value Measurement and Application* (“GASB 72”). This Statement addresses accounting and financial reporting issues related to fair value measurements. The definition of fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. This Statement is effective for periods beginning after June 15, 2015. On July 1, 2015, we adopted and implemented GASB 72, and as of June 30, 2016, there was no material impact to the financial results of adopting and implementing GASB 72.

During 2015, the GASB issued Statement No. 75 – *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* (“GASB 75”). This Statement replaces the requirements of GASB Statements No. 45 - *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57 - *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, for OPEB.

Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, establishes new accounting and financial reporting requirements for OPEB plans.

The scope of this Statement addresses accounting and financial reporting for OPEB that is provided to the employees of state and local governmental employers. This Statement establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. For defined benefit OPEB, this Statement identifies the methods and assumptions that are required to be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Note disclosure and required supplementary information requirements about defined benefit OPEB also are addressed. This Statement is effective for fiscal years beginning after June 15, 2017, and earlier application is encouraged. Currently, we are evaluating the impact of this Statement on our financial statements.

During 2015, the GASB issued Statement No. 76 - *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments* (“GASB 76”). The objective of this Statement is to identify—in the context of the current governmental financial reporting environment—the hierarchy of generally accepted accounting principles (GAAP). The “GAAP hierarchy” consists of the sources of accounting principles used to prepare financial statements of state and local governmental entities in conformity with GAAP and the framework for selecting those principles. This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and non-authoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. This Statement supersedes GASB Statement No. 55 - *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The requirements of this Statement are effective for financial statements for periods beginning after June 15, 2015, and should be applied retroactively. Earlier application is permitted. On July 1, 2015, we adopted and implemented GASB 76 and as of June 30, 2016, there was no impact to the financial results of adopting and implementing GASB 76.

During 2016, the GASB issued Statement No. 82 - *Pension Issues an amendment of GASB Statements No. 67, No. 68, and No. 73* (“GASB 82”). The objective of this Statement is to address certain issues that have been raised with respect to Statements No. 67, *Financial Reporting for Pension Plans*, No. 68, *Accounting and Financial Reporting for Pensions*, and No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. Specifically, this Statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. The requirements of this Statement are effective for reporting periods beginning after June 15, 2016. Earlier application is encouraged. Currently, we are evaluating the impact of this Statement on our financial statements.

Note 4 – Federal Student Loan Reserve Fund (Federal Fund) and Assets Held for the U.S. Department of Education

The following table shows the detail of the net position held by us for ED in the Federal Fund.

(Dollars in thousands)

As of June 30,		**2016**	2015
Assets			
Cash	$	**38,301**	24,506
Receivable from the U.S. Department of Education		**36,935**	52,544
Other receivables		**219**	134
Total assets		**75,455**	77,184
Liabilities			
Accounts payable and accrued expenses		**1,997**	7,835
Payable to USDE		**17,925**	-
Amounts payable to PHEAA		**228,032**	256,167
Total liabilities		**247,954**	264,002
Net liabilities	$	**(172,499)**	(186,818)

Under the Higher Education Act of 1965, as amended, (HEA) we are to act as a fiduciary in managing the assets of the Federal Fund. Under HEA, Section 428(c)(9)(A), we are required to maintain a current minimum reserve level of at least 0.25% of the total attributable amount of all outstanding loans guaranteed. Historically, ED has calculated this ratio at September 30, which is the close of the federal fiscal year, based upon regulatory reports that we file with ED.

As of June 30, 2016, we have managed the cash flow of the Federal Fund in a manner to assure our customers that sufficient funds are available to continue to pay default claims by not transferring default aversion fees that are due to us. In addition to paying default claims, we pay our share of retention on defaulted loan collections from the Federal Fund.

As of June 30, 2016 and 2015, we reported $55.5 million and $69.3 million, respectively, in the line item “Federal Student Loan Reserve Fund assets held for the U.S. Department of Education, net” in the Statements of Net Position, which is the difference between the Federal Fund’s total assets, accounts payable and accrued expenses and amounts payable to USDE, excluding amounts payable to PHEAA.

Note 5 – Cash, Cash Equivalents and Investments

Overview

We manage our portfolio in such a manner that assures that funds are available as needed to meet the immediate and/or future operating requirements. This is accomplished by structuring the portfolio so that securities mature concurrent with cash needs to meet anticipated demands. At maturity or liquidation, such monies shall be reinvested according to our investment guidelines and the prudent person rule described below.

Restricted cash and cash equivalents include amounts restricted under bond indentures and financing agreements, which are held by a trustee and managed under the provisions of the agreements. Restricted cash and cash equivalents also include amounts due to customers.

General Investment Objectives

The primary objectives, in priority order, of our investment activities are safety, liquidity, and yield.

Safety of principal is the foremost objective of our investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. Investment transactions must be designed to keep capital losses at a minimum, whether they are from securities defaults or erosion of market value. To further mitigate risk, our investment portfolio shall be diversified by the type of investment, issuer, and maturity date.

The liquidity of our portfolio shall be managed in such a manner that assures that funds are available as needed to meet the immediate and/or future operating requirements. Furthermore, since all possible cash demands cannot be anticipated, the portfolio should consist largely of securities with active secondary or resale markets. Also, a portion of the portfolio may be placed in money market mutual funds, which offer same-day liquidity for short-term funds.

The yield of the investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account the investment risk constraints and liquidity needs. Return on investment is of secondary importance compared to the safety and liquidity objectives described above. The core of the investments is limited to relatively low risk securities in anticipation of earning a fair return relative to the risk being assumed. Securities will not be sold prior to maturity with the following exceptions:

- A security with declining credit may be sold early to minimize loss of principal;
- A security swap would improve the quality, yield, or target duration in the portfolio; and
- Liquidity needs of the portfolio require that the security be sold.

Standards of Care

The board of directors authorized the investments guidelines and we govern our investments by using the "prudent person" rule under our investment policy. Generally, our investments are limited to U.S. Government securities, U.S. Government agency securities, federal instrumentalities sponsored by U.S. agencies, high-grade commercial paper, repurchase agreements collateralized by U.S. Treasury obligations, certificates of deposit, bankers' acceptances eligible for purchase by the Federal Reserve System, and other investments approved by the board of directors from time to time.

The standard of prudence used in our investment portfolio shall be the "prudent person" standard and shall be applied in the context of managing an overall portfolio. The prudent person rule requires the contractor to exercise: the judgment, care, skill, prudence and diligence under the circumstances then prevailing, which persons of prudence, discretion and intelligence, acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims by diversifying the investments of the funds, so as to minimize the risk, considering the probable income as well as the probable safety of their capital.

The following table shows the carrying value of cash and cash equivalents (unrestricted and restricted), investments (unrestricted and restricted), and cash on deposit.

(Dollars in thousands)

As of June 30,		2016	2015
Cash and cash equivalents	$	**72,713**	70,238
Restricted cash and cash equivalents		**223,188**	257,751
Restricted cash and cash equivalents – due to customers		**72,256**	64,470
Investments		**531,706**	562,145
Restricted investments		**50,661**	60,218
Carrying value	$	**950,524**	1,014,822

Fair Value Measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is a market-based measurement, not an entity-specific measurement. For some assets and liabilities, observable market transactions or market information might be available; for others, it might not be available. However, the objective of a fair value measurement in both cases is the same—that is, to determine the price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions. Fair value is an exit price at the measurement date from the perspective of a market participant that controls the asset or is obligated for the liability.

The fair value hierarchy categorizes the inputs to valuation techniques used to measure fair value into three levels. Level 1 inputs are quoted prices (unadjusted) for identical assets or liabilities in active markets that a government can access at the measurement date. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for an asset or liability, either directly or indirectly. Level 3 inputs are unobservable inputs for an asset or liability. The fair value hierarchy gives the highest priority to Level 1 inputs and the lowest priority to Level 3 inputs.

The following table shows the fair value and the fair value measurements for our cash equivalents and investments.

(Dollars in thousands)

As of June 30, 2016		Fair Value	Level 1	Level 2	Level 3
Cash equivalents					
Money market funds:					
Federated money market funds	$	**214,961**	**214,961**	**-**	**-**
PFM Funds Prime Series – Institutional Shares		**64,576**	**-**	**64,576**	**-**
Federal agency discount notes		**61,721**	**-**	**61,721**	**-**
Commercial paper		**9,674**	**-**	**9,674**	**-**
Total cash equivalents	$	**350,932**	**214,961**	**135,971**	**-**
Investments					
State Treasury investment pool:					
Pool 998	$	**135,339**	**-**	**-**	**135,339**
Pool 999		**447,028**	**-**	**-**	**447,028**
Total investments		**582,367**	**-**	**-**	**582,367**
Total cash equivalents and investments	$	**933,299**	**214,961**	**135,971**	**582,367**

(Dollars in thousands)

As of June 30, 2015		Fair Value	Level 1	Level 2	Level 3
Cash equivalents					
Money market funds:					
Federated money market funds	$	251,015	251,015	-	-
PFM Funds Prime Series – Institutional Shares		67,470	-	67,470	-
Federal agency discount notes		61,251	-	61,251	-
Commercial paper		21,694	-	21,694	-
Total cash equivalents	$	401,430	251,015	150,415	-
Investments					
State Treasury investment pool:					
Pool 998	$	131,220	-	-	131,220
Pool 999		491,143	-	-	491,143
Total investments		622,363	-	-	622,363
Total cash equivalents and investments	$	1,023,793	251,015	150,415	622,363

Cash Equivalents

Money Market Funds

Federated Money Market Funds – As of June 30, 2016 and 2015, we held positions in various Federated money market funds and the fair values of those funds were $215.0 million and $251.0 million, respectively. The fair values of the Federated money market funds were valued using quoted market prices (Level 1).

PFM Funds Prime Series – As of June 30, 2016 and 2015, we held positions in PFM Funds Prime Series and the fair values were $64.6 million and $67.5 million, respectively. The fair values of the PFM Funds Prime Series were valued based on the published net asset value per share by PFM, which were not obtained from a quoted price in an active market (Level 2).

Federal Agency Discount Notes

As of June 30, 2016 and 2015, we held positions in federal agency discounted notes and the fair values were $61.7 million and $61.3 million, respectively. The fair values of the federal agency discount notes were based on a market approach using quoted prices by a third party for markets that are not active (Level 2).

Commercial Paper

As of June 30, 2016 and 2015, we held positions in commercial paper and the fair values were $9.7 million and $21.7 million, respectively. The fair values of the commercial paper were based on a market approach using quoted prices by a third party for markets that are not active (Level 2).

Investments

State Treasury Investment Pool

Investment Pools 998 and 999

The Commonwealth of Pennsylvania Treasury Department's Bureau of Cash Management and Investments maintain the State Treasury investment pool for the benefit of all Commonwealth funds, which is governed by the provisions of the State Treasury investment policy. The Treasury Department created two separate pools, Pools 998 and 999, within the Commonwealth Investment Program (CIP), each with its own distinctive investment strategies, goals, and holdings that reflect the differing needs of Commonwealth funds for income, cash flows, and investment risk tolerance. The CIP does not have any restrictive terms and conditions upon which a participant may redeem their investments in Pools 998 and 999.

Pool 998

Pool 998 operates much like a mutual fund: depending on market conditions, an account owner who makes a withdrawal may realize a gain or a loss. Shares in Pool 998 are priced at the most recent net asset value (NAV) per share, which fluctuates daily. Consequently, if a participant's average cost per share (based on its own history of purchases and redemptions) is less than the share price on the day of redemption, the participant will realize a capital gain in the shares redeemed. Conversely, if a participant's average cost per share exceeds the share price on the day of redemption, the participant will realize a capital loss on the shares redeemed. Pool 998 gains and losses are distributed periodically to participants in the form of reduced or increased share totals.

According to the Pennsylvania Treasury Annual Investment Report for the fiscal year ending June 30, 2015 (most recent annual report available), Pool 998's asset allocations were 75% invested in fixed income (including cash and cash equivalents) and 25% invested in equities and alternative assets. Pool 998 is benchmarked against a blended index of the Standard & Poor's 500 Index, the MCSI ACWI ex U.S. Index, the Barclay's Capital U.S. Aggregate Bond Index and the Merrill Lynch 6-Month U.S. Treasury Bill Index. For the equity portion of Pool 998's investments, a weighting of 75% is measured against the Standard & Poor's 500 Index and 25% is measured against the MCSI ACWI ex US Index. For the fixed income portion of Pool 998's investments, a weighting of 83% is measured against the Barclay's Capital U.S. Aggregate Bond Index and 17% is measured against the Merrill Lynch 6-Month U.S. Treasury Bill Index. As of June 30, 2016 and 2015, our investments in Pool 998 were $135.3 million and $131.2 million, respectively. The fair values of Pool 998 were based on unobservable inputs (Level 3), which primarily included our own data and market participant assumptions particular to PHEAA.

Pool 999

Pool 999 maintains a stable NAV of $1 per share by investing exclusively in high quality fixed-income securities, primarily of short duration. Pool 999 is designed to generate income while minimizing investment volatility, which protects principal and ensures ready access to account balances through investments with easy liquidity. Pool 999's permitted investments include U.S. Treasury securities, federal agency securities, certificates of deposit, commercial paper, money market funds, repurchase agreements, and similar short-term fixed income instruments. According to the Pennsylvania Treasury Annual Investment Report for the fiscal year ending June 30, 2015 (most recent annual report available), Pool 999's asset allocations were 100% invested in fixed income (including cash and cash equivalents).

The value of a share in Pool 999 is calculated daily, incorporating all realized and unrealized gains and losses, and any cash returned from investments. All gains and losses are distributed to participants monthly to re-set the value to $1 per share. Pool 999's performance is benchmarked against the Merrill Lynch 3-Month U.S. Treasury Bill Index. As of June 30, 2016 and 2015, our investments in Pool 999 were $447.0 million and $491.1 million, respectively. The fair values for Pools 999 were based on unobservable inputs (Level 3), which primarily included our own data and market participant assumptions particular to PHEAA.

As of and for the period ended June 30, 2016, there were no transfers between the fair value hierarchy levels for the previously mentioned cash equivalents and investments.

For more information on Pools 998 and 999, see the Pennsylvania Treasury "Annual Investment Report for Fiscal Year Ended June 30, 2015", which can be found at www.patreasury.gov/reports/investments.html.

Deposits and investments have certain risks that have the potential to result in losses, and those risks are described in the following sections.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. We manage our exposure to interest rate risk by structuring our investment portfolio so that investments mature to meet cash requirements for ongoing operations and investing operating funds primarily in shorter-term investments.

As of June 30, 2016 and 2015, $350.9 million and $401.4 million, respectively, of our cash equivalents have maturities of less than one year. As of June 30, 2016 and 2015, $582.4 million and $622.4 million, respectively, of our investments in the State Treasury Investment Pool have maturities of less than one year.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. We minimize our credit risk by limiting investments to authorized investments that have a higher credit rating and diversifying the investment portfolio so potential losses on individual investments will be minimized. This risk is measured by the assignment of a rating by a nationally recognized statistical rating organization.

As of June 30, 2016, all of our investments in commercial paper were rated A-1 and higher. As of June 30, 2016, all of our investments in money market funds were rated AAAm. As of June 30, 2016, $582.4 million was invested in the State Treasury investment pool, and the investment pool was not rated.

As of June 30, 2015, all of our investments in commercial paper were rated A-1 and higher. As of June 30, 2015, all of our investments in money market funds were rated AAAm. As of June 30, 2015, $622.4 million was invested in the State Treasury investment pool, and the investment pool was not rated.

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, we would not be able to recover deposits or collateral securities that are in the possession of an outside party.

As of June 30, 2016, we had $15.5 million of cash deposits with financial institutions of which $15.3 million was in excess of the federal depository insurance limits.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of our investment in a single issuer. Our investment policy does not contain requirements that limit the amount that can be invested in any one issuer.

As of June 30, 2016, our investment in federal agency discount notes (FHLB) represented 6.6% of our total cash equivalents and investments. As of June 30, 2015, our investment in FHLB represented 6.0% of our total cash equivalents and investments.

Note 6 – Student Loans Receivable, net

The following table shows our student loan holdings.

(Dollars in thousands)

As of June 30,		2016	2015
FFEL:			
Consolidation	$	**4,705,793**	5,396,113
Stafford		**1,074,457**	1,325,486
PLUS		**104,978**	142,308
Supplemental Loans for Students		**987**	1,293
		5,886,215	6,865,200
Private		**28,789**	34,355
HEAL		**27,974**	37,689
Unamortized premium on student loan purchases		**8,203**	10,434
Unamortized discount on student loan purchases		**(11,913)**	(12,672)
		5,939,268	6,935,006
Allowance for loan losses		**(21,229)**	(20,871)
Student loans receivable, net	$	**5,918,039**	6,914,135

Allowance for loan losses

We estimated and established an allowance for loan losses based upon our continuing evaluation of our student loan portfolio, past and anticipated loss experience, current operating information, and changes in economic conditions. We maintain the allowances for loan losses at a level that is adequate to absorb estimated incurred losses, but our evaluation is inherently subjective and the required allowances may significantly change in the future.

When a student loan defaults, the guarantor reimburses the lender based on the disbursement date of the student loan. We record a charge-off for the difference between the ending balance of the student loan and the reinsurance rate. In the table that follows, we report the “provision for losses – FFEL program loans” and the “provision for losses - other program loans (Non-FFEL)” as the “provision for loan losses” in the Statements of Revenues, Expenses and Changes in Net Position.

We present an analysis of our allowance for loan losses related to student loans in the following table.

(Dollars in thousands)

As of June 30,		2016	2015
Balance at beginning of period	$	**20,871**	19,712
Provision for losses – FFEL program loans		**7,882**	6,536
Provision for losses – other program loans (Non-FFEL)		**(1,141)**	616
Charge-offs		**(6,383)**	(5,993)
Balance at end of period	$	**21,229**	20,871

Note 7 – Capital Assets, net

The following tables show an analysis of the capital asset activity.

(Dollars in thousands)

As of and for the year ended June 30, 2016		Beginning Balance	Additions	Retirements	Ending Balance
Land	$	8,038	-	-	8,038
Buildings and improvements		73,762	1,714	-	75,476
Purchased software		18,715	5,714	(541)	23,888
Software development		18,823	4,301	(3,322)	19,802
Information technology equipment		17,323	3,991	(3,464)	17,850
Other equipment		16,913	1,415	(829)	17,499
Total capital assets		153,574	17,135	(8,156)	162,553
Less accumulated depreciation and amortization for:					
Buildings and improvements		(40,391)	(2,003)	-	(42,394)
Purchased software		(9,909)	(3,109)	540	(12,478)
Software development		(9,518)	(3,989)	3,322	(10,185)
Information technology equipment		(8,660)	(2,606)	3,240	(8,026)
Other equipment		(9,137)	(2,063)	817	(10,383)
Total accumulated depreciation and amortization		(77,615)	(13,770)	7,919	(83,466)
Total capital assets, net	$	75,959	3,365	(237)	79,087

(Dollars in thousands)

As of and for the year ended June 30, 2015		Beginning Balance	Additions	Retirements	Ending Balance
Land	$	2,946	5,092	-	8,038
Buildings and improvements		71,993	2,808	(1,039)	73,762
Purchased software		14,578	6,705	(2,568)	18,715
Software development		16,805	4,551	(2,533)	18,823
Information technology equipment		16,953	3,789	(3,419)	17,323
Other equipment		14,663	3,552	(1,302)	16,913
Total capital assets		137,938	26,497	(10,861)	153,574
Less accumulated depreciation and amortization for:					
Buildings and improvements		(39,182)	(1,899)	690	(40,391)
Purchased software		(10,139)	(2,340)	2,570	(9,909)
Software development		(8,405)	(3,647)	2,534	(9,518)
Information technology equipment		(9,897)	(2,143)	3,380	(8,660)
Other equipment		(8,676)	(1,762)	1,301	(9,137)
Total accumulated depreciation and amortization		(76,299)	(11,791)	10,475	(77,615)
Total capital assets, net	$	61,639	14,706	(386)	75,959

Depreciation expense for the years ended June 30, 2016 and 2015 was $13.8 million and $11.8 million, respectively.

Note 8 – Notes and Bonds Payable and Other Financings

The following tables show the activity of our student loan and other financings.

(Dollars in thousands) As of and for the year ended June 30, 2016		Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due within One Year
Student loan financings:						
Student loan floating rate notes, due 2027 - 2046, at weighted-average rates of 1.17% as of June 30, 2016 and 0.87% as of June 30, 2015.	$	5,398,585	-	(853,142)	4,545,443	-
Deferred gain on bond refunding of student loan floating rate notes.		168,779	-	(34,712)	134,067	-
Deferred loss on bond refunding of student loan floating rate notes.		(2,013)	-	714	(1,299)	-
Discount on student loan floating rate notes.		(14,752)	-	2,950	(11,802)	-
Student loan auction rate security bonds, due 2042 - 2044, at weighted-average rates of 1.65% as of June 30, 2016 and 1.45% as of June 30, 2015.		268,400	-	(50,200)	218,200	-
Student loan financing warehouse facilities, due 2017 - 2018, at weighted-average rates of 1.70% as of June 30, 2016 and 1.01% as of June 30, 2015.		903,779	-	(165,566)	738,213	738,213
Student loan financings, due on demand, at weighted-average rates of 1.20% as of June 30, 2016 and 0.94% as of June 30, 2015.		200,000	-	-	200,000	200,000
Total student loan financings	$	6,922,778	-	(1,099,956)	5,822,822	938,213

(Dollars in thousands)

As of and for the year ended June 30, 2016		Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due within One Year
Other financings:						
Capital acquisition refunding bonds, Series of 2012, due 2016 – 2022, at weighted- average rates of 4.15% as of June 30, 2016 and 2015.	$	29,940	-	(3,745)	26,195	3,895
Unamortized premium on capital acquisition refunding bonds		2,815	-	(661)	2,154	-
Term financings, due 2029, at zero percent interest as of June 30, 2016 and 2015.		6,280	-	-	6,280	-
Total other financings		39,035	-	(4,406)	34,629	3,895
Total student loan and other financings	$	6,961,813	-	(1,104,362)	5,857,451	942,108

The note and bond indentures, among other things, require us to comply with various covenants, such as parity ratio requirements and annual financial statement, servicing and administration audits. Student loans and investments collateralize all student loan financings. As of June 30, 2016, $5.9 billion of student loan principal and related interest receivable and $218.6 million of cash equivalents collateralized the $5.7 billion of student loan financings.

As of June 30, 2016, the student loan financings and other financings are non-recourse obligations to our unrestricted net position and to the Commonwealth, except for the $200.0 million of student loan financings and $26.2 million of Capital Acquisition Refunding Bonds, Series of 2012, which are recourse obligations to us.

Student loan financings

For the year ended June 30, 2016, the student loan financings decreased $1.1 billion due to required debt payments, scheduled amortization of deferred gains and losses on bond refundings and scheduled amortization of discounts on student loan floating rate notes.

Other financings

For the year ended June 30, 2016, the other financings decreased $4.4 million due to required debt payments and scheduled amortization of premium on capital acquisition refunding bonds.

Debt service requirements

The following table displays the debt service requirements based on estimated interest rates for the variable rate debt and the stated maturities for the student loan and other financings.

(Dollars in thousands) Fiscal Year of Maturity	Student Loan Financings Principal	Student Loan Financings Interest	Other Financings Principal	Other Financings Interest
2017	$ 938,213	70,295	$ 3,895	2,089
2018	-	57,100	4,055	833
2019	-	56,903	4,230	661
2020	-	56,903	4,415	482
2021	-	56,903	4,595	295
2022-2026	-	284,515	5,005	104
2027-2031	552,733	266,323	6,280	-
2032-2036	168,064	251,990	-	-
2037-2041	2,061,182	168,680	-	-
2042-2046	1,966,814	30,534	-	-
2047-2051	14,850	92	-	-
	$ 5,701,856	1,300,238	$ 32,475	4,464

The student loan financings are variable-rate debt, which have interest rates that reset on various dates. As of June 30, 2016, interest rates on $218.2 million reset based upon auctions every 28 days, $4.7 billion is indexed to the 1-month or 3-month LIBOR, and $738.2 million is indexed to the asset-backed commercial paper rate.

Note 9 – Retirement and Other Postemployment Benefits

Retirement Plan

Plan Description

We contribute to the Commonwealth of Pennsylvania State Employees' Retirement System ("SERS"), which the Commonwealth established under the provisions of Public Law 858, No. 331. SERS is the administrator of a cost-sharing multiple-employer defined benefit retirement plan to provide pension benefits for employees of state government and certain independent agencies.

SERS is a component unit of the Commonwealth and is included in the Commonwealth's comprehensive annual financial report (CAFR) as a pension trust fund. As a pension trust fund, SERS issues a CAFR that includes financial statements and required supplementary information. The SERS CAFR is available on-line at www.sers.state.pa.gov, select "Newsroom", select "SERS Facts" and the CAFRs are listed by year under the section titled "Comprehensive Annual Financial Reports". Written requests for the SERS CAFR should be directed to the following address: State Employees' Retirement System, 30 North Third Street, Suite 150, Harrisburg, Pennsylvania 17101-1716.

Summary of Significant Accounting Policies

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of SERS and additions to/deductions from SERS fiduciary net position have been determined on the same basis as they are reported by SERS.

Plan member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due and the employer has a legal requirement to provide the contributions. Investment purchases and sales are recorded on a trade-date basis, and reported at fair value.

Retirement Benefits

Article II of the Commonwealth of Pennsylvania's Constitution assigns the authority to establish and amend the benefit provision of the plan to the General Assembly. On November 23, 2010, the Governor signed H.B. 2497 into law as PA Act 120. This legislation preserved the benefits in place for all members prior to January 1, 2011, but mandated a number of benefit reductions for members that join SERS on or after January 1, 2011. Below is a listing of some of the benefit reductions that are included in PA Act 120:

- Creates a new A-3 and an optional A-4 Class of Service for future non-judicial employees (Class A-3 members will contribute 6.25% of their pay toward their benefit, and they will accrue benefits at 2% of their final average salary for each year of credited service. Class A-4 members will contribute 9.3% of their pay toward their benefit, and they will accrue benefits at 2.5% of their final average salary for each year of credited service);
- Increases the vesting period for Class A-3 and A-4 members to 10 years;
- Increases normal retirement age for Class A-3 and A-4 members from 60 to 65;
- Gradually increases funding through the use of collars that cap employer contribution rate increases;
- Implements a shared risk provision that introduces the possibility of higher or lower member contribution rates for future members; and
- Re-amortizes the SERS existing liabilities over 30 years through an actuarial "Fresh Start".

Prior to PA Act 120, employees who retire at age 60 with three years of service or with 35 years of service if under age 60, are entitled to a normal annual retirement benefit. Most members of SERS, and all state employees hired after June 30, 2001 and prior to January 1, 2011, are Class AA members. The multiplier for Class AA is 1.25, which translates into an annual benefit of 2.5% of the member's highest three-year average salary times years of service. Most members vest with five years of credited service.

Funding Policy

The State Employees Retirement Code (SERC), section 5507, requires the Commonwealth and other employers whose employees are SERS members to make contributions to the fund on behalf of all active members and annuitants necessary to fund the liabilities and provide the annuity reserves required to pay benefits. The SERS board of directors certifies the employer contribution rates on an annual basis, typically in April of each year to become effective the following fiscal year beginning in July. The employer rates are determined based on an independent actuarial valuation of the pension fund. The actuarial valuation assesses the pension system's current funds and determines its future expected liabilities. The employer contribution rate is set so that it can fund all retirement benefits earned by employees working during the year and pay toward any unfunded liability that may exist. In some cases, the actuarially calculated employer contribution rate has been set or adjusted by Pennsylvania law. Lastly, according to the SERC, all obligations of SERS will be assumed by the Commonwealth should SERS terminate.

PA Act 120 gradually increases funding with collars (limits) that cap employer contribution rate increases. For the year ended June 30, 2016, the employer contribution rate was 19.89% for the "A" Class of Service employees, 24.86% for the "AA" Class of Service employees and 17.18% for the "A-3" and "A-4" Class of Service employees. For the year ended June 30, 2015, the employer contribution rate was 15.94% for the "A" Class of Service employees, 19.92% for the "AA" Class of Service employees and 13.77% for the "A-3" and "A-4" Class of Service employees. On July 1, 2016, the employer contribution rates will be 23.96% for the "A" Class of Service employees, 29.95% for the "AA" Class of Service employees and 20.70% for the "A-3" and "A-4" Class of Service employees.

According to the Commonwealth of Pennsylvania SERS 2015 actuarial report, Schedule K, page 2 (Projection of Expected Contributions and Benefits – Reflecting Act 120 Collars), the blended fiscal projections indicate the employer's rate will increase to 31.5% by calendar year 2018, and remain above 27% through calendar year 2026.

For the years ended June 30, 2016, 2015 and 2014, our statutorily required contributions were $36.1 million, $26.7 million and $18.7 million, respectively, and these contributions were equal to the required contributions set by SERS.

SERS GASB 68 Valuation

On June 22, 2016, SERS released the "GASB 68 Valuation", which had a valuation date of December 31, 2015 (**measurement date**), to the cost-sharing employers of the multiple-employer defined benefit retirement plan. It should be noted that the SERS valuation measurement date of December 31, 2015 is **not** the same as PHEAA's fiscal year end date of June 30, 2016.

The information that follows on "Assumptions and Other Inputs" and the "GASB 68 Employer Schedules" were provided by SERS in the GASB 68 Valuation mentioned above. In some cases, SERS provided us with total plan-level information in which we applied our proportionate share percentage in to order to calculate the required schedules under GASB 68. As stated previously in the "Plan Description", separately issued financial statements for SERS can be obtained from SERS management at www.sers.state.pa.gov.

Assumptions and Other Inputs

Actuarial Methods and Assumptions

The GASB 68 Valuation states that every five years SERS is required to conduct an actuarial experience study to determine whether the assumptions used in its annual actuarial valuations remain accurate based on current and anticipated demographic trends and economic conditions. The 18th Investigation of Actuarial Experience study for the period 2011 – 2015 was released in March 2016. The actuary, under oversight of the SERS Board, reviewed economic assumptions (such as the assumed future investment returns and salary increases) as well as demographic assumptions (such as employee turnover, retirement, disability, and death rates). Some assumption adjustments increased projected cost and some decreased projected cost, but the overall result was a slight increase to the net pension liability.

Economic assumption recommendations resulting from the experience study included: keeping the targeted investment return rate assumption at 7.5%; keeping the inflation rate at 2.75%; keeping the general salary growth rate at 3.05%; and decreasing career salary growth rates, by varying amounts depending upon the employee's length of service at all service levels. In addition to the five-year experience study, SERS reviews its investment return assumption in light of economic conditions every year as part of its annual valuation.

Most demographic assumptions remained the same as or similar to experience over the last five years. However, the experience study did recommend changing some assumptions, which are highlighted as follows. The study recommended decreasing disability retirement rates for all active members. Additionally, it recommended adjusting superannuation separation rates, early retirement separation rates, and withdrawal rates for certain active member groupings (gender, age, years of service) in both the general and special membership classes. Furthermore, it recommended decreasing most annuitant and survivor mortality rates.

The board adopted the actuarial assumptions set forth in the 18th Investigation of Actuarial Experience at its March 2016 meeting. The study can be viewed at www.SERS.pa.gov.

The following methods and assumptions were used in the GASB 68 Valuation for the December 31, 2015 measurement date:

- Actuarial cost method – entry age
- Amortization method – straight-line amortization of investments over five years and amortization of assumption changes and noninvestment gains/losses over the average expected remaining service lives of all employees that provided benefits
- Investment rate of return – 7.50% net of expenses including inflation
- Projected salary increases – average of 5.70% with a range of 3.85% to 9.05% including inflation.
- Asset valuation method – fair market value
- Inflation – 2.75%
- Mortality rate – projected RP-2000 Mortality Tables adjusted for actual plan experience and future improvement
- Cost of living adjustment (COLA) – ad hoc

The long-term expected real rate of return on pension plan investments is determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return for each major asset class included in SERS current and target asset allocation in the GASB 68 Valuation are summarized in the following table:

Asset Class	**Target Allocation**	**Long-term Expected Real Rate of Return**
Alternative Investments	15.00%	8.50%
Global Public Equity	40.00%	5.40%
Real Assets	17.00%	4.95%
Diversifying Assets	10.00%	5.00%
Fixed Income	15.00%	1.50%
Liquidity Reserve	3.00%	- %
Total	100.00%	

Discount Rate

According to the GASB 68 Valuation, the discount rate used to measure the total pension liability was 7.50%. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the rates applicable for each member and that employer contributions will be made based on rates determined by the actuary and as set by statute. Based on those assumptions, SERS fiduciary net position was projected to be available to make all projected future benefit payments of current active and non-active SERS members. Therefore, the long-term expected rate of return on SERS investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of PHEAA's Proportionate Share of Net Pension Liability to Changes in the Discount Rate

The following table presents our proportionate share of the net pension liability calculated using the discount rate of 7.50% as well as the impact on the net pension liability if it were calculated using a discount rate that is one percentage point lower (6.50%) or one percentage point higher (8.50%) than the current rate.

(Dollars in thousands)

As of June 30,		**2016**	2015
1% decrease of the discount rate - 6.50%	$	**547,399**	414,540
Current discount rate - 7.50%	$	**440,673**	323,866
1% increase of the discount rate - 8.50%	$	**349,162**	245,900

GASB 68 Employer Schedules

Proportionate Share of Net Pension Liability

As of June 30, 2016, our proportionate share of net pension liability was $440.7 million. The net pension liability was measured as of December 31, 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. As of June 30, 2015, our proportionate share of net pension liability was $323.9 million, which the net pension liability was measured as of December 31, 2014.

The following tables present our proportionate share of net pension liability as of June 30, 2016 and 2015. As stated previously, PHEAA's proportionate share percentage was rounded to the nearest hundredth of a percent; therefore, you will not be able to recalculate "PHEAA's proportionate share of net pension liability".

(Dollars in thousands)

As of June 30,		**2016**		2015
SERS net pension liability	$	**18,183,831**	$	14,857,408
PHEAA's allocation percentage		**2.42%**		2.18%
PHEAA's proportionate share of net pension liability	$	**440,673**	$	323,866

PHEAA's Allocation Percentage Methodology

The allocation percentage assigned to PHEAA was based on a projected-contribution method. This methodology applies the most recently calculated contribution rates for the Commonwealth's 2016-2017 fiscal year, from the December 31, 2015 funding valuation, to the expected funding payroll for the allocation of the calendar year 2015 amounts.

The amounts assigned to us were our proportionate share of the net pension liability, pension expense, deferred outflows of resources and deferred inflows of resources (the collective pension amounts) determined in accordance with GASB 68.

As of June 30, 2016, our allocation percentage was 2.42%, an 11.0% increase from our allocation percentage of 2.18% as of June 30, 2015. The allocation percentages were measured as of December 31, 2015 and 2014, respectively.

In the tables below, we present our proportionate share allocation percentages, which were rounded to the nearest hundredth of a percent.

(Dollars in thousands)

As of June 30, 2016		
Projected contributions, July 1, 2016 through June 30, 2017	**$**	**44,675**
Total projected contributions, July 1, 2016 through June 30, 2017	**$**	**1,843,462**
PHEAA's allocation percentage (rounded to the nearest hundredth)		**2.42%**

(Dollars in thousands)

As of June 30, 2015		
Projected contributions, July 1, 2015 through June 30, 2016	$	32,720
Total projected contributions, July 1, 2015 through June 30, 2016	$	1,501,022
PHEAA's allocation percentage (rounded to the nearest hundredth)		2.18%

Proportionate Share of Total Deferred Outflows of Resources and Total Inflows of Resources

As of June 30, 2016, our deferred outflows of resources and deferred inflows of resources related to pensions were $107.0 million and $872 thousand, respectively. As of June 30, 2015, our deferred outflows of resources and deferred inflows of resources related to pensions were $26.4 million and $1.1 million, respectively.

The following table presents the components of our proportionate share of total deferred outflows of resources and total inflows of resources related to pensions.

(Dollars in thousands)

Deferred Outflows of Resources

As of June 30,	Differences between expected and actual experience	Net difference between projected and actual investment earnings on pension plan investments	Changes in assumptions	Changes in proportion	Contributions subsequent to the measurement date	Total Deferred Outflow of Resources
2016	**$8,923**	**44,868**	**13,092**	**40,165**	**19,778**	**$126,826**
2015	$1,758	9,358	-	15,250	13,582	$39,948

(Dollars in thousands)

Deferred Inflows of Resources

As of June 30,	Differences between PHEAA's contributions and proportionate share of contributions	Total Deferred Inflow of Resources
2016	**$872**	**$872**
2015	$1,068	$1,068

Amortization of Deferred Outflows of Resources and Deferred Inflows of Resources

The components of deferred outflows of resources and deferred inflows of resources, other than the net difference between the projected and actual investment earnings on SERS pension plan investments, are amortized into pension expense over 5.2 years. The net difference between the projected and actual investment earnings on SERS pension plan investments are amortized in pension expense over 5.0 years.

The amounts of deferred outflows of resources and deferred inflows of resources related to the items previously reported as of June 30, 2016, which will be recognized in pension expense in future periods are as follows:

(Dollars in thousands)

For the year ended June 30,		2017	2018	2019	2020	2021	Thereafter
Deferred outflows of resources	$	27,206	27,206	27,206	23,109	2,320	-
Deferred inflows of resources		241	241	241	148	2	-
Net amortization	$	26,965	26,965	26,965	22,961	2,318	-

Pension Expense

For the year ended June 30, 2016 and 2015, our proportionate share of total pension expense was $68.0 million and $41.6 million, respectively. The components of our proportionate share of total pension expense are as follows:

(Dollars in thousands)

For the year ended June 30,	PHEAA's proportionate share of allocable plan pension expense	Net amortization of the difference between PHEAA's contributions and proportionate share of contributions	Net amortization of deferred amounts from changes in proportion	Total pension expense excluding that attributable to employer-paid member contributions
2016	**$58,213**	**(241)**	**10,037**	**$68,009**
2015	$38,544	(232)	3,315	$41,627

Other Postemployment Benefits

Plan Description

The Commonwealth of Pennsylvania (Commonwealth) sponsors the Retired Employees' Health Program (REHP). We participate in the Commonwealth's REHP, a single-employer defined benefit postemployment healthcare plan administered by the Pennsylvania Employees' Benefit Trust Fund (PEBTF), acting as a third-party administrator on behalf of the Commonwealth's Office of Administration. The REHP provides health care and prescription drug plan benefits to eligible Commonwealth retirees, and their eligible dependents. The REHP's benefit provisions are established and may be amended by the Commonwealth of Pennsylvania's Office of Administration.

While the Commonwealth accounts for the REHP as a single employer plan, we account for our participation in the plan as a cost-sharing employer, because the plan is administered like a cost-sharing plan with a single actuarial valuation and the Commonwealth allocates annual OPEB costs to Commonwealth funds and component units, consistent with a pooling arrangement. Additionally, the Commonwealth structured the REHP so that employer contributions are irrevocable, plan assets are dedicated to providing benefits to retirees and their beneficiaries in accordance with the terms of the plan, and plan assets are legally protected from creditors of the employer(s) or plan administrator.

The REHP does not issue stand-alone financial statements, however the REHP note disclosures will be included in the Commonwealth's CAFR for the year ended June 30, 2016. For additional information on the REHP including the Commonwealth's total Other Post Employment Benefit (OPEB) expenses, funded status, funding progress, actuarial accrued liability, and the actuarial assumptions used to determine these amounts for the Commonwealth's REHP, a complete actuarial report is available for review at www.budget.state.pa.us (select Financial Reports and under the heading "Special Reports" select "Actuarial Valuation of the Commonwealth's Post-Retirement Medical Plan (August 2013)).

Funding Policy

The Office of Administration and the Governor's Budget Office establish REHP contribution requirements. All employing agencies and certain plan members of the Commonwealth must contribute specified amounts to the REHP.

REHP plan members with a retirement date between July 1, 2005 and June 30, 2007, must contribute 1.0% of their final annual gross salary toward the cost of REHP coverage. REHP plan members with a retirement date on or after July 1, 2007, must contribute a percentage of their final annual gross salary toward the cost of REHP coverage. The contribution rate shall be equal to the active employee contribution rate in effect at the date of retirement, which is a percentage of the employee's final annual gross salary. The contribution rate shall change thereafter in accordance with the active employee contribution.

For the years ended June 30, 2016, 2015 and 2014, our annual contribution rate was $4.7 million, $4.0 million and $3.6 million, respectively, and we have made all required contributions to the REHP as determined by the Office of Administration.

The monthly contribution rate was based on a projected per retiree cost for the related fiscal years times the estimated number of PHEAA retirees enrolled in the REHP. Effective July 1, 2016, our contribution rate will be $391 thousand per month or $4.7 million annually. This current level of funding generally represents an amount needed to fund ongoing annuitant health care costs for the current year with a smaller portion representing advance funding.

The Statements of Funded Status and Funding Progress are disclosed in the Commonwealth's CAFR, Note I – Pension and Other Postretirement Benefits for the fiscal year ended June 30, 2015. The June 30, 2015 Commonwealth's CAFR can be accessed on-line at www.budget.state.pa.us, select "Financial Reports" and select "Comprehensive Annual Financial Reports".

Note 10 – Servicing Fees

As a servicer, we are responsible for servicing, maintaining custody of, and making collections on student loans. We earn servicing fee revenue by servicing student loans owned by third parties. We categorize revenue earned from loans owned by financial institutions and secondary markets as "Commercial Servicing"; whereas, we categorize revenue earned from loans owned by ED as "FLS Servicing". We categorize revenue earned from providing our system to guarantors and other servicers to use, as well as, not-for-profit servicers who were awarded servicing contracts by ED, as "Remote Servicing".

For the years ended June 30, 2016 and 2015, total servicing revenues were $324.7 million and $307.9 million, respectively. For the years ended June 30, 2016 and 2015, we were servicing on average $289.5 billion and $252.4 billion, respectively, of loans for third party customers. For the years ended June 30, 2016 and 2015, customers using our servicing systems serviced on average $46.5 billion and $46.3 billion, respectively, of loans.

Our servicing agreements, some of which expired during the fiscal year ended June 30, 2016, have contractual terms at inception ranging from three years to life of loan. Under our servicing agreements, we generally agree to reimburse customers for any claims, losses, liabilities, or expenses that arise out of or relate to our acts or omissions with respect to services provided under such agreements. We record a provision for estimated claims under the agreements as "other" operating expenses in the financial statements.

For the year ended June 30, 2016, ED provided $188.5 million of servicing revenue, which represents 58.1% of the total servicing revenue. The next three loan-servicing customers provided $51.7 million of servicing revenue, which represents 15.9% of the total servicing revenue.

For the year ended June 30, 2015, ED provided $167.6 million of servicing revenue, which represents 54.4% of the total servicing revenue. The next three loan-servicing customers provided $55.5 million of servicing revenue, which represents 18.0% of the total servicing revenue.

Note 11 – Segment Information

Our Student Loan Trust segment generally finances student loan portfolios by issuing notes, bonds, and other financings and we pledge the earnings to support the debt. Because we pledge the revenue stream of the student loan portfolios to support the debt, we are reporting condensed financial information about the Student Loan Trust segment. The notes, bonds, and other financings related to this segment are limited obligations payable only from the pledged assets.

Statements of Revenues, Expenses and Changes in Net Position

(Dollars in thousands)

For the years ended June 30,		**2016**	2015
Interest revenue	$	**148,091**	153,343
Interest expense		**(37,324)**	(42,059)
Net interest revenue		**110,767**	111,284
Provision for loan losses		**(7,045)**	(3,202)
Net interest revenue after provision for loan losses		**103,722**	108,082
Total noninterest revenue		**919**	(706)
Total operating revenues		**104,641**	107,376
Operating expenses		**(40,487)**	(51,644)
Operating income		**64,154**	55,732
Financial aid		**-**	(2)
Income before transfers		**64,154**	55,730
Transfers to unrestricted net position		**(17,211)**	(9,265)
Changes in net position		**46,943**	46,465
Net position, beginning of period		**263,381**	216,916
Net position, end of period	$	**310,324**	263,381

Statements of Net Position

(Dollars in thousands)

As of June 30,		2016	2015
Current assets:			
Restricted cash and cash equivalents	$	**218,582**	253,339
Student loans receivable		**947,881**	1,082,224
Interest income receivable		**72,787**	89,135
Other assets		**8**	12
Total current assets		**1,239,258**	1,424,710
Long-term assets:			
Student loans receivable, net		**4,914,498**	5,782,456
Total long-term assets		**4,914,498**	5,782,456
Total assets		**6,153,756**	7,207,166
Deferred outflow of resources:			
Deferred loss on bond refundings		**1,299**	2,013
Total deferred outflow of resources		**1,299**	2,013
Current liabilities:			
Accounts payable and accrued expenses		**20,610**	21,008
Student loan financings		**938,213**	903,779
Total current liabilities		**958,823**	924,787
Long-term liabilities:			
Student loan financings, net		**4,751,841**	5,852,232
Total long-term liabilities		**4,751,841**	5,852,232
Total liabilities		**5,710,664**	6,777,019
Deferred inflow of resources:			
Deferred gain on bond refundings		**134,067**	168,779
Total deferred inflow of resources		**134,067**	168,779
Net position:			
Restricted for debt service		**310,324**	263,381
Total net position	$	**310,324**	263,381

Statements of Cash Flows

(Dollars in thousands)

For the years ended June 30,		2016	2015
Cash flows from operating activities			
Interest received on student loans	$	**65,978**	65,299
Principal received on student loans		**1,109,297**	1,126,333
Student loan purchases		**(820,992)**	(924,432)
Student loan sales, including net gains and losses		**805,864**	171,601
Other		**154**	51
Payment of operating expenses		**(38,255)**	(43,807)
Net cash provided by operating activities		**1,122,046**	395,045
Cash flows from noncapital financing activities			
Proceeds from the issuance of noncapital debt		**-**	2,928,677
Principal paid on noncapital debt		**(1,068,908)**	(3,240,349)
Interest paid on noncapital debt		**(68,879)**	(65,654)
Bond issuance costs		**(2,066)**	(9,066)
Other		**(17,211)**	(9,267)
Net cash used for noncapital financing activities		**(1,157,064)**	(395,659)
Cash flows from investing activities			
Interest received on investments		**261**	31
Net cash provided by investing activities		**261**	31
Net change in restricted cash and cash equivalents		**(34,757)**	(583)
Restricted cash and cash equivalents, beginning of period		**253,339**	253,922
Restricted cash and cash equivalents, end of period	$	**218,582**	253,339

There are eighteen separate trusts with parity ratios, a ratio of assets to liabilities. As of June 30, 2016, the trusts had parity ratios ranging from 1.023 to 1.285. Two of the eighteen trusts have minimum parity ratio requirements and as of June 30, 2016, the trusts complied with the minimum parity ratio requirements.

Note 12 – Blended Component Units

We consider the Trust, the 2011-1 Trust, the 2012-1 Trust, the 2013-1 Trust, the 2013-2 Trust, the 2013-3 Trust, the 2014-1 Trust, the 2014-2 Trust, the 2014-3 Trust, the 2015-1 Trust and the Warehouse Trust 2013-1, collectively "PHEAA SLTs", blended component units ("BCUs") of the Foundation, and the PHEF a BCU of PHEAA.

The PHEAA SLTs are legally separate entities and we consider them component units of the Foundation, because of their material relationship with the Foundation. The PHEAA SLTs are BCUs of the Foundation, because they provide services entirely for the Foundation.

The PHEF is a component unit of PHEAA, because PHEAA appointed a voting majority of the PHEF's governing board, and PHEAA has the ability to impose its will on PHEF. We consider PHEF a blended component unit of PHEAA, because PHEF no longer provided services to outside third parties in the form of grants and scholarships used to promote nursing education, but rather provided services entirely to us. On March 18, 2015, the Board of Directors authorized the dissolution of PHEF. As part of the dissolution of PHEF, all of the PHEF assets and all funds in its possession that have not been paid or set aside for PHEF's obligations were to be paid to PHEAA, for its public purposes. On June 8, 2015, PHEF entered into an "Assignment of Rights Incident to Dissolution Agreement" with PHEAA. On October 29, 2015 the "Articles of Dissolution" were received by the PA Department of State Bureau of Corporations and Charitable Organizations, and PHEF was officially dissolved.

As legally separate entities, the student loan financings, net of the BCUs are non-recourse obligations to our unrestricted net position and to the Commonwealth.

In the statements that follow, we present condensed combining information of the BCUs.

Statements of Revenues, Expenses and Changes in Net Position

(Dollars in thousands)

For the year ended June 30, 2016		PHEAA SLTs	PHEF	Total BCUs
Interest revenue	$	**118,975**	**-**	**118,975**
Interest expense		**(24,072)**	**-**	**(24,072)**
Net interest revenue		**94,903**	**-**	**94,903**
Provision for loan losses		**(4,971)**	**-**	**(4,971)**
Net interest revenue after provision for loan losses		**89,932**	**-**	**89,932**
Total noninterest revenue		**-**	**-**	**-**
Total operating revenues		**89,932**	**-**	**89,932**
Operating expenses		**(32,196)**	**(37)**	**(32,233)**
Operating income (loss)		**57,736**	**(37)**	**57,699**
Total transfers and financial aid		**(12,509)**	**(229)**	**(12,738)**
Changes in net position		**45,227**	**(266)**	**44,961**
Net position, beginning of period		**143,037**	**266**	**143,303**
Net position, end of period	$	**188,264**	**-**	**188,264**

(Dollars in thousands)

For the year ended June 30, 2015		PHEAA SLTs	PHEF	Total BCUs
Interest revenue	$	114,233	8	114,241
Interest expense		(29,659)	-	(29,659)
Net interest revenue		84,574	8	84,582
Provision for loan losses		(5,582)	-	(5,582)
Net interest revenue after provision for loan losses		78,992	8	79,000
Total noninterest revenue		(1)	-	(1)
Total operating revenues		78,991	8	78,999
Operating expenses		(41,657)	(10)	(41,667)
Operating income (loss)		37,334	(2)	37,332
Total transfers and financial aid		89,063	(771)	88,292
Changes in net position		126,397	(773)	125,624
Net position, beginning of period		16,640	1,039	17,679
Net position, end of period	$	143,037	266	143,303

Statements of Net Position

(Dollars in thousands)

As of June 30, 2016		PHEAA SLTs	PHEF	Total BCUs
Current assets:				
Restricted cash and cash equivalents	$	**121,270**	**-**	**121,270**
Restricted investments		**-**	**-**	**-**
Student loans receivable		**769,078**	**-**	**769,078**
Interest income receivable		**61,867**	**-**	**61,867**
Other assets		**8**	**-**	**8**
Total current assets		**952,223**	**-**	**952,223**
Long-term assets:				
Student loans receivable, net		**3,939,517**	**-**	**3,939,517**
Total long-term assets		**3,939,517**	**-**	**3,939,517**
Total assets		**4,891,740**	**-**	**4,891,740**
Total deferred outflow of resources		**700**	**-**	**700**
Current liabilities:				
Accounts payable and accrued expenses		**17,579**	**-**	**17,579**
Student loan financings		**531,330**	**-**	**531,330**
Total current liabilities		**548,909**	**-**	**548,909**
Long-term liabilities:				
Student loan financings, net		**4,021,200**	**-**	**4,021,200**
Total long-term liabilities		**4,021,200**	**-**	**4,021,200**
Total liabilities		**4,570,109**	**-**	**4,570,109**
Total deferred inflow of resources		**134,067**	**-**	**134,067**
Net position:				
Restricted for debt service		**188,264**	**-**	**188,264**
Restricted for financial aid grant programs		**-**	**-**	**-**
Total net position	$	**188,264**	**-**	**188,264**

(Dollars in thousands)

As of June 30, 2015		PHEAA SLTs	PHEF	Total BCUs
Current assets:				
Restricted cash and cash equivalents	$	155,758	-	155,758
Restricted investments		-	266	266
Student loans receivable		1,092,340	-	1,092,340
Interest income receivable		77,427	-	77,427
Other assets		12	-	12
Total current assets		1,325,537	266	1,325,803
Long-term assets:				
Student loans receivable, net		4,439,933	-	4,439,933
Total long-term assets		4,439,933	-	4,439,933
Total assets		5,765,470	266	5,765,736
Total deferred outflow of resources		732	-	732
Current liabilities:				
Accounts payable and accrued expenses		18,174	-	18,174
Student loan financings		465,544		465,544
Total current liabilities		483,718	-	483,718
Long-term liabilities:				
Student loan financings, net		4,970,669	-	4,970,669
Total long-term liabilities		4,970,669	-	4,970,669
Total liabilities		5,454,387	-	5,454,387
Total deferred inflow of resources		168,778	-	168,778
Net position:				
Restricted for debt service		143,037	-	143,037
Restricted for financial aid grant programs		-	266	266
Total net position	$	143,037	266	143,303

Statements of Cash Flows

(Dollars in thousands)

For the year ended June 30, 2016		PHEAA SLTs	PHEF	Total BCUs
Net cash provided by (used for) operating activities	$	**921,182**	**(37)**	**921,145**
Net cash used for noncapital financing activities		**(955,871)**	**(229)**	**(956,100)**
Net cash provided by investing activities		**201**	**266**	**467**
Net change in restricted cash and cash equivalents		**(34,488)**	**-**	**(34,488)**
Restricted cash and cash equivalents, beginning of period equivalents		**155,758**	**-**	**155,758**
Restricted cash and cash equivalents, end of period equivalents	$	**121,270**	**-**	**121,270**

(Dollars in thousands)

For the year ended June 30, 2015		PHEAA SLTs	PHEF	Total BCUs
Net cash used for operating activities	$	(1,165,394)	(10)	(1,165,404)
Net cash provided by (used for) noncapital financing activities		1,202,660	(771)	1,201,889
Net cash provided by investing activities		16	16	32
Net change in restricted cash and cash equivalents		37,282	(765)	36,517
Restricted cash and cash equivalents, beginning of period equivalents		118,476	765	119,241
Restricted cash and cash equivalents, end of period equivalents	$	155,758	-	155,758

Note 13 – Net Position

We have net investment in capital assets, which includes land, buildings and improvements, software development, purchased software, information technology equipment, and other tangible assets that are used in our operations. These capital assets are net of accumulated depreciation and amortization, and reduced by the outstanding balances of any bonds, notes or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. As of June 30, 2016, net investment in capital assets amounted to $79.1 million. As of June 30, 2015, net investment in capital assets amounted to $76.0 million.

We have net position that is restricted for debt service that is held under various indentures related to financing our student loan portfolios. As of June 30, 2016, net position restricted for debt service amounted to $310.3 million. As of June 30, 2015, net position restricted for debt service amounted to $263.4 million.

We have net position that is restricted for financial aid grant programs, because of the Commonwealth of Pennsylvania grants and federal grants that relate to specific programs. The net position is restricted until we disburse program-related grants. As of June 30, 2016, net position restricted for financial aid grant programs amounted to $52.1 million. As of June 30, 2015, net position restricted for financial aid grant programs amounted to $61.5 million.

We have net position that is unrestricted, which is the net amount of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted components of net position. Under Commonwealth law, our purpose is to increase higher education opportunities for Pennsylvania residents. Net position that we report as unrestricted are statutorily restricted to our purpose. The Higher Education Amendments of 1998 also restricts our use of net position related to FFEL guaranty activities to fulfilling our guaranty responsibilities and other student financial aid related activities selected by us. Because that restriction is consistent with our statutory purpose, we consider net position related to those activities to be unrestricted. As of June 30, 2016, unrestricted net position amounted to $310.2 million of which net position related to the guaranty activities was $156.9 million. As of June 30, 2015, unrestricted net position amounted to $403.2 million of which net position related to the guaranty activities was $184.5 million.

Note 14 – Risk Management, Contingencies, and Legal Proceedings

Risk Management and Contingencies

The current heightened regulatory environment for student and consumer lenders and servicers has resulted in significant additional governmental scrutiny, and we may be adversely impacted by the results of such additional scrutiny. The regulatory environment with respect to the student loan industry is evolving, and governmental or regulatory officials may exercise broad discretion in deciding how to interpret and apply applicable laws, rules, regulations and standards. From time to time and in the past, we have received formal and informal inquiries, subpoenas, civil investigative demands from various government regulatory and investigatory authorities about the loans we service or own, our operations, borrowers or our compliance with laws, rules, regulations or standards. We expect to continue to receive similar demands from time to time in the future and an adverse outcome in one or more of these matters could be material to our operations, financial condition, cash flows and/or reputation. Any determination that our operations or activities or the activities of our employees are not in compliance with existing laws, rules, regulations or standards, could result in payment delays, the imposition of substantial fines, a requirement of restitution, interruptions of our respective operations, the reduction or loss of supplier, vendor or other third party relationships, termination of necessary licenses or permits, or similar results, all of which could potentially harm our respective operations, financial condition, cash flows and/or reputation. Even if any reviews, inquiries or investigations do not result in these types of determinations, such reviews, inquiries and investigations could cause us to incur substantial costs, require us to change our operating or servicing practices, or create negative publicity, which could also harm our respective operations, financial condition, business relationships or reputation. To date, there has been no material supervisory or enforcement actions or findings.

Federal programs in which we participate are subject to audit in accordance with the provisions of the U.S. Office of Management and Budget's ("OMB") Uniform Guidance, which superseded OMB's Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. The provisions of the Uniform Guidance do not limit the authority of ED or other federal audit officials to perform, or contract for, audits and evaluations of federal financial assistance programs. Therefore, our operations in current and prior years are subject to audit. We believe we are in substantial compliance with applicable federal regulations and that any adjustment because of future audits will not be material.

Legal Proceedings

As previously reported, in *U.S. ex. rel. Jon H. Oberg v. Kentucky Higher Ed. Student Loan Corp., et. al.,* Dr. Jon H. Oberg, a former U.S. Department of Education employee, filed a False Claims Act ("FCA") case in the United States District Court for the Eastern District of Virginia against several public and private student loan financing entities. PHEAA was served with a copy of Oberg's First Amended Complaint on or about September 29, 2009. The First Amended Complaint alleged that the defendants submitted claims to the U.S. Department of Education for special allowance payments providing a 9.5% floor on the return on certain loans, including loans that were not eligible for such a special allowance. It further alleged that PHEAA in particular obtained approximately $92 million in unlawful payments from the Department of Education. The FCA provides for treble damages and civil penalties.

PHEAA filed a motion to dismiss the action, and an order was issued by the district court dismissing PHEAA, the Vermont Student Assistance Corporation, the Kentucky Higher Education Student Loan Corporation, and the Arkansas Student Loan Authority (the "State Defendants") on December 1, 2009. The district court held that each of the State Defendants was not a "person" subject to liability under the FCA because each was an agency of its respective state. Dr. Oberg and the United States litigated and then settled with the other (non-State) defendants remaining in the case.

Dr. Oberg appealed the December 1, 2009 order of dismissal. The Court of Appeals for the Fourth Circuit (the "Fourth Circuit") vacated the dismissal and remanded the case on the ground that the district court did not employ the proper analysis in determining whether PHEAA, among others, is a state agency subject to suit under the FCA. The Fourth Circuit concluded that a court should employ the Eleventh Amendment "arm-of-the-state" analysis in determining if an entity is properly regarded as a "person," for FCA purposes, that is subject to suit under the FCA.

On remand, Oberg filed a Fourth Amended Complaint, which PHEAA moved to dismiss, again arguing it is not a person subject to liability under the FCA. The district court granted PHEAA's motion, finding PHEAA is an arm of the Commonwealth of Pennsylvania and therefore not a "person" subject to liability under the FCA.

Dr. Oberg appealed a second time. The Fourth Circuit vacated the dismissal of the claims against PHEAA and remanded the case to the district court "to permit limited discovery on the question of whether PHEAA is 'truly subject to sufficient state control to render [it] a part of the state'."

On remand, following discovery, PHEAA moved for summary judgment, arguing that there was no genuine issue of material fact and PHEAA was entitled to judgment as a matter of law because discovery confirmed that it is an arm of the Commonwealth. The district court granted the motion on January 16, 2015.

Dr. Oberg appealed a third time. On October 21, 2015, the Fourth Circuit reversed and held that, as a matter of law, PHEAA is not an arm of the state and is a "person" subject to suit under the FCA.

On November 17, 2015, the Fourth Circuit denied PHEAA's request for a rehearing by all of the judges of the Fourth Circuit (a "rehearing *enbanc*"). On February 16, 2016, PHEAA filed a *petition for writ of certiorari* with the United States Supreme Court ("Supreme Court"). The Supreme Court has not yet decided whether it will review PHEAA's appeal. If the Supreme Court decides not to hear the appeal, the case will proceed on the merits. As of June 30, 2016, and through the date of this report, we believe it is remote that a loss contingency exists, and we will continue to contest this matter vigorously.

Lastly, we are involved in various legal matters in the normal course of business. We have considered the available information on these legal matters, and the criteria for a loss contingency, as defined by GASB, does not exist as of June 30, 2016 and through the date of this report.

Note 15 – Subsequent Events

On May 7, 2015, the Foundation entered into a trust agreement with a financial institution, which created the PHEAA Student Loan Trust 2015-2, a statutory trust under the laws of the State of Delaware. On August 5, 2016, an Amended and Restated Certificate of Trust was filed with the Delaware Secretary to modify the legal name of the PHEAA Student Loan Trust 2015-2 to the PHEAA Student Loan Trust 2016-1 (“2016-1 Trust”). The principal purpose of the 2016-1 Trust is to securitize student loans and related assets, and to acquire student loans from the Foundation and issue one or more classes of securities secured by a pledge of such assets.

On September 14, 2016, the 2016-1 Trust issued $534.0 million of original principal amount of student loan asset backed notes, Class A (“Class A Notes”), at par, and $11.6 million of original principal amount of student loan asset backed notes, Class B (“Class B Notes”), at a discount. The Class A Notes were issued with an interest rate of 1-month LIBOR plus 1.15% and a final maturity of September 25, 2065. The Class B Notes had a price to public of 84.00%, which resulted in a discount of $1.9 million. The Class B Notes were issued with an interest rate of 1-month LIBOR plus 1.50% and a final maturity date of September 25, 2065.

Required Supplementary Information

The schedules that follow are required supplementary information and are presented as of and for the year ended December 31, 2015 (**measurement date**) and as of and for the year ended June 30, 2016 (**PHEAA's fiscal year-end**):

Schedule of PHEAA's Proportionate Share of Net Pension Liability
As of and for the years ended December 31 (measurement date)
(Dollars in thousands)

Calendar year end	PHEAA's proportionate (percentage) share of collective net pension liability	PHEAA's proportionate (amount) share of collective net pension liability	PHEAA's covered employee payroll	PHEAA's proportionate share of collective net pension liability as a percentage of covered employee payroll	Fiduciary (SERS) net position as a percentage of the total pension liability
2015	**2.42%**	**$440,673**	**164,947**	**267.2%**	**58.9%**
2014	2.18%	$323,866	$141,621	228.7%	64.8%

The "Schedule of PHEAA's Proportionate Share of Net Pension Liability" presented above is to illustrate the required 10-year trend of information. However, until we can compile a full 10-year trend of information, we are presenting the information for which information was available.

Schedule of PHEAA's Contributions
As of and for the years ended June 30 (PHEAA's fiscal year-end)
(Dollars in thousands)

Fiscal year end	Required contributions	PHEAA's contributions recognized by the pension plan	Contribution excess/(deficiency)	PHEAA's covered employee payroll	PHEAA's contributions as a percentage of covered employee payroll
2016	**$36,074**	**$36,074**	**-**	**$165,650**	**21.8%**
2015	$26,027	$26,027	-	$149,629	17.4%

The "Schedule of PHEAA's Contributions" presented above is to illustrate the required 10-year trend of information. However, until we can compile a full 10-year trend of information, we are presenting the information for which information was available.