

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
(formerly The Education Financing Foundation of California)

CONSOLIDATED FINANCIAL STATEMENTS

for the year ended December 31, 2007

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
(formerly The Education Financing Foundation of California)

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REPORT OF INDEPENDENT AUDITORS

The Board of Directors
College Access Foundation of California

We have audited the accompanying consolidated statement of financial position of College Access Foundation of California, formerly The Education Financing Foundation of California, (the Foundation) as of December 31, 2007, and the related consolidated statement of activities and changes in net assets and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. We were not engaged to perform an audit of internal control over financial reporting. Our audit included consideration of internal controls over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Foundation's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Foundation at December 31, 2007, and the consolidated results of its changes in net assets and its cash flows for the year then ended, in conformity with accounting principles accepted in the United States of America.

Burr Pilger & Mayer LLP

San Francisco, California
June 27, 2008

Member of The Leading Edge Alliance

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
(formerly The Education Financing Foundation of California)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

December 31, 2007

(in thousands)

ASSETS

Cash and cash equivalents	\$ 1,904
Interest and dividends receivable	579
Investments	471,575
Student loans receivable, net	8,595
Restricted assets	305
Other assets	<u>2,225</u>
 Total assets	 <u>\$485,183</u>

LIABILITIES AND NET ASSETS

Liabilities:	
Accounts payable and accrued liabilities	\$ 3,224
Grants payable, net	7,415
Bond payable	<u>9,435</u>
 Total liabilities	 20,074
 Net assets	 <u>465,109</u>
 Total liabilities and net assets	 <u>\$485,183</u>

The accompanying notes are an integral
part of these financial statements.

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
(formerly The Education Financing Foundation of California)

CONSOLIDATED STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS

for the year ended December 31, 2007

(in thousands)

Revenues:	
Investment income, net	<u>\$ 49,169</u>
Student loan related revenues (repayment):	
Interest	799
Special allowance payment repayment, net (Note 6E)	(3,920)
Other	<u>1,104</u>
Net student loan related revenues (repayment)	<u>(2,017)</u>
Other income	<u>123</u>
Total revenues	<u>47,275</u>
Expenses:	
Grants	10,065
Student loan related expenses	1,420
Salaries and benefits	1,492
General and administrative	<u>3,044</u>
Total expenses	<u>16,021</u>
Increase in net assets	31,254
Net assets, beginning of year	<u>433,855</u>
Net assets, end of year	<u>\$ 465,109</u>

The accompanying notes are an integral
part of these financial statements.

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
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CONSOLIDATED STATEMENT OF CASH FLOWS

for the year ended December 31, 2007

(in thousands)

Cash flows from operating activities:	
Increase in net assets	\$ 31,254
Adjustments to reconcile increase in net assets to net cash used in operating activities:	
Depreciation of fixed assets	73
Net realized and unrealized gains on investments	(36,682)
Provision for loan losses	254
Discount for grants payable	(166)
Changes in operating assets and liabilities:	
Net increase in interest and dividends receivable	(242)
Net decrease in student loan receivable	2,892
Net decrease in restricted assets	52
Net decrease in other assets	(368)
Net decrease in accounts payable and accrued liabilities	(3,961)
Net increase in grants payable	<u>5,004</u>
Net cash used in operating activities	<u>(1,890)</u>
Cash flows from investing activities:	
Proceeds from sale of investments	71,635
Purchases of investments	(84,681)
Purchases of property and equipment	(113)
Proceeds from sale of property and equipment	<u>5</u>
Net cash used in investing activities	<u>(13,154)</u>
Cash flows from financing activities—repayment of bonds payable	
Net cash used in financing activities	<u>(1,710)</u>
Net decrease in cash and cash equivalents	(16,754)
Cash and cash equivalents, beginning of year	<u>18,658</u>
Cash and cash equivalents, end of year	<u>\$ 1,904</u>
Supplemental disclosure of cash flow information—interest paid	<u>\$ 589</u>

The accompanying notes are an integral
part of these financial statements.

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
(formerly The Education Financing Foundation of California)

NOTES TO FINANCIAL STATEMENTS

1. **Organization and Business**

College Access Foundation of California (the Foundation), formerly known as The Education Financing Foundation of California through March 2007, is a public charity dedicated to promoting educational opportunities by helping qualified California students with financial need attend college. The Foundation makes grants to community-based, school-based and college-based academic support programs statewide, which use the funds to award scholarships to low-income and first generation students pursuing two-year or four-year degrees. The Foundation is also developing a “place-based” grant making strategy that will support long-term investments in selected California communities and regions with low college-going rates, to help those communities build a college-going culture.

The Foundation and its subsidiary, CEFI Corporation (CEFI), are the surviving entities after a series of corporate restructurings that are described in Note 11.

2. **Summary of Significant Accounting Policies**

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States that require management to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those and other estimates.

Under the provisions of the American Institute of Certified Public Accountants (AICPA) *Audit and Accounting Guide for Not-for-Profit Organizations* and related standards, net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. At December 31, 2007, there were no donor-imposed restrictions. Therefore, according to AICPA standards, net assets of the Foundation were unrestricted as it related to donor-imposed restrictions. However, there are restricted assets related to a bond indenture agreement disclosed in Note 6D.

The consolidated financial statements include the accounts of the Foundation and its subsidiary, CEFI Corporation, as well as the accounts of the CalEdge trust estate for the outstanding student loan revenue bond, notes, and the general operating accounts for each of the consolidated entities. All significant intercompany accounts and transactions have been eliminated. References to the Foundation in these notes to consolidated financial statements refer to or include the Foundation, its subsidiary, and their predecessors.

Cash and Cash Equivalents

Cash and cash equivalents consist of demand deposits in banks, money market funds, and other short-term investments with original maturities of 90 days or less. Certain cash equivalents are held in custodian accounts pending future calls for certain investments.

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
(formerly The Education Financing Foundation of California)

NOTES TO FINANCIAL STATEMENTS, Continued

2. **Summary of Significant Accounting Policies**, continued

Investments

Debt and equity securities with readily determinable fair values are carried at estimated fair value, based on quoted market prices. The Foundation invests in limited partnerships, private equity funds, and inflation hedging assets that may not have readily determinable fair values. Accordingly, these values are based on guidelines established by the general partners, or other governing body, of each respective investment. In addition to relying on the funds' financial reports, the Foundation uses alternate methods to confirm values and supplement the valuation process such as reviewing funds' audited financial statements, comparing investment manager statements to reports received from the Foundation's investment consultant, reviewing the investment manager valuation policies on a regular basis to insure they are reasonable and consistent with industry practices, monitoring news reported in the public domain in connection to any investment manager valuation or operational issues and scheduling conference calls and meetings with investment managers as needed. Management believes these methods provide a reasonable estimate of fair value. These values may differ significantly from values that would have been used had a readily available market existed for such investments, and the differences could be material to the change in net assets of the Foundation.

Net realized and unrealized gains or losses are reflected as increases or decreases in unrestricted net assets. Gains and losses that result from market fluctuations are recognized in the period such fluctuations occur. Realized gains or losses are calculated on an adjusted cost basis. Adjusted cost is the estimated fair value of the security at the beginning of the year, or the cost if purchased during the year. Dividend income is recorded on ex-dividend dates. Interest income from investments is recorded on an accrual basis.

Grants

Unconditional grants are recognized as grant expense and liability when the Foundation approves the grant. Unconditional grants that are expected to be paid in less than one year are measured at net settlement value. Unconditional grants that are expected to be paid in more than one year are measured at the present value of the estimated future cash flows. Conditional grants, which depend on the occurrence of a specified future and uncertain event to bind the Foundation, are recognized when the conditions on which they depend are substantially met. As of December 31, 2007, the Foundation had \$250 thousand in outstanding conditional grants payable that have not yet been recorded in the consolidated financial statements. The conditions on these grants relate to matching requirements by the grantee.

Income Taxes

The Foundation, formerly known as The Education Financing Foundation of California has maintained its IRS Code Section 501(c)(3) organization status.

As a recently created for-profit Delaware corporation, CEFI uses the liability method to account for income taxes. Under this method, deferred income tax assets and liabilities are based on the differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
(formerly The Education Financing Foundation of California)

NOTES TO FINANCIAL STATEMENTS, Continued

2. **Summary of Significant Accounting Policies**, continued

Functional Expenses

The costs of the Foundation's various activities have been summarized on a functional basis in Note 5. Expenses are allocated to program and supporting services based upon employees' time for each function, purpose of each expenditure, and services provided for each program. Costs that cannot be specifically identified with a particular program are charged to supporting services.

Significant Accounting Policies Associated with Student Loans

As outlined in Notes 11 and 12, there was a corporate restructuring, sale of assets and a wind-down of operations associated with student loans. Listed below are the significant accounting policies associated with the student loan assets, liabilities and operations.

A. Student Loans Receivable

Student loans held for investment are classified as portfolio loans and are carried at the principal amount outstanding net of unamortized premiums or discounts, deferred loan fees and costs and acquisition fair value adjustments, if any. Write-downs of the loans' carrying value attributable to credit quality are charged to the allowance for loan losses while write-downs attributable to interest rates are charged to noninterest income. Additionally, from time to time, certain student loans receivable that have previously been written off and deemed uncollectible are recovered.

B. Allowance for Loan Losses

The Foundation maintains an allowance for loan losses to provide for probable net losses on the uninsured portion of its federally guaranteed FFELP student loans and on the uninsured consumer education loans (CEL loans) in the CalEdge program. The allowance is maintained at a level to provide for probable losses, net of estimated recoveries, inherent in the portfolio as of the reporting date. The allowance is established through a provision charged to student loan program expenses as well as through guarantee fees associated with the certain CEL loan programs.

In evaluating the adequacy of the allowance for federally guaranteed FFELP loans, the Foundation also considers the incidence of student loan claims rejected for payment by guarantors and the amount of FFELP loans subject to risk-sharing.

Substantially all of the Foundation's FFELP loans had been sold to Nelnet Corporation (Nelnet) as of December 31, 2007, leaving approximately \$0.1 million of FFELP loans that were more than 210 days delinquent remained on the Foundation's books.

The CEL loans held in the CalEdge program were not included in the asset sale. The CEL allowance process is now administered by California Alternative Loan Marketing Association (CALMA) under the CalEdge management and administration agreement, as discussed in Note 12. The Foundation and CALMA periodically assesses the recoverability of the portfolio and calculates an allowance to provide for probable net losses on the remaining CEL loans. As of December 31, 2007, the Foundation held approximately \$9.0 million of CEL loans.

In 2007, the Foundation received approximately \$0.5 million of previously written off loans which is included in other student loan related revenue.

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
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NOTES TO FINANCIAL STATEMENTS, Continued

2. **Summary of Significant Accounting Policies**, continued

Significant Accounting Policies Associated with Student Loans, continued

C. Allowance for Investment Arbitrage Rebates

Section 148 of the Internal Revenue Code (IRC), as amended, required that the Foundation subsidiaries calculate and remit amounts deemed by the IRC to be excess yields earned on purpose (excess loan yield) and nonpurpose investments (arbitrage rebates) acquired with proceeds of tax-exempt bond or note financings. The calculation is based on the excess of investment yield over the related bond or note cost of funds. Arbitrage rebate, if any, is paid at each five-year anniversary of the underlying bond's issuance date and at bond maturity. The CalEdge bond indenture is the only remaining bond subject to this calculation, as the Foundation defeased all other bonds in the prior year. The Foundation accrued a liability for arbitrage rebate and recognized income or expense related to changes in this liability based on third-party calculations as of the balance sheet dates. The Foundation applied for a refund of overpaid arbitrage rebates in the amount of \$0.6 million which is included in other assets and other student loan related revenue for the year ended December 31, 2007.

D. Student Loan Income

Interest income on student loans includes borrower interest, government interest, and special allowance payments. Interest income is recognized based upon the interest rate and principal amount outstanding in accordance with the terms of the applicable loan agreement until the outstanding balance is paid or charged off.

E. Interest Expense and Financing Costs

Interest expense is based upon contractual interest rates adjusted for the amortization of deferred financing costs. Financing costs incurred when establishing financing arrangements are capitalized and amortized over the term of the financing arrangement as a component of interest expense. The net value of financing costs is approximately \$0.4 million at December 31, 2007 and is included in other assets on the statement of financial position. Substantially all of the capitalized interest was amortized to interest expense in conjunction with the sale of loans to Nelnet.

F. Student Loan Related Expenses

As indicated in Notes 11 and 12 the Foundation has restructured and sold off substantially all of its assets associated with student loans. Student loan related expenses include all other third-party costs directly attributable to the management of trust assets and liabilities. Such expenses include fees paid to the Department of Education (DOE), trustee fees, professional service provider fees, arbitrage rebate expenses, interest paid related to bond indenture, loan servicing fees, provisions for loan losses and asset purchase related costs.

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
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NOTES TO FINANCIAL STATEMENTS, Continued

3. Investments

On April 5, 2005, the Board of Directors of the Foundation delegated authority to the Investment Committee of the Board to develop the Foundation's investment policy and objectives, and to allocate and direct the investment of Foundation funds. The Investment Committee reports to the Board of Directors on a quarterly basis.

During 2007, the Foundation's investments consisted of guaranteed investment contracts, U.S. government debt, U.S. government agency debt, corporate debt, fixed income securities, commodity futures, real estate investments, and domestic and international equity securities. The Foundation's investments at December 31, 2007 were as follows:

	(in thousands)
Guaranteed investment contracts (CalEdge Program)	\$ 2,233
Fixed income and bond funds	86,074
Diversified inflation hedge fund	88,312
Domestic equity funds	118,446
International equity funds	104,502
Marketable alternatives	71,377
Private equity	<u>631</u>
Total investments	<u>\$471,575</u>

The guaranteed investment contracts held by the Foundation at December 31, 2007, are associated with the CalEdge student loan and bond program (see Note 6C) and mature in 2028. These guaranteed investment contracts include provisions requiring the issuer to provide collateralization in the form of U.S. government obligations. The guaranteed investment contracts held by the Foundation were issued by GE Capital Corporation.

The diversified inflation hedge funds include a wide variety of investments, such as domestic and international equities, fixed income securities, commodities futures, and real estate investments.

Investment income for the year ended December 31, 2007 was as follows:

	(in thousands)
Interest and dividends	\$12,487
Realized gains, net	16,398
Unrealized gains, net	<u>20,284</u>
Total investment income, net	<u>\$49,169</u>

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
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NOTES TO FINANCIAL STATEMENTS, Continued

4. Grants Payable

The following is a schedule of future unconditional grant payments required under current grants at December 31, 2007:

	(in thousands)
Payable in less than one year	\$5,575
Payable in one to five years	1,969
Payable in more than five years	<u>37</u>
Total unconditional grants payable	7,581
Less discounts to net present value	<u>(166)</u>
Net unconditional grants payable	<u><u>\$7,415</u></u>

5. Functional Expenses

At December 31, 2007, the Foundation's functional allocation of expenses is represented as follows:

	(in thousands)
Program expenses:	
Grant-making activities	\$10,702
Student loan activities	<u>1,420</u>
Total program expenses	12,122
Management and general expenses	<u>3,899</u>
Total expenses	<u><u>\$16,021</u></u>

6. Items Associated with Student Loans

Certain assets liabilities, income and expenses are directly tied to operations that are in a wind down phase associated with student loans. The history of the restructuring, sale of assets and wind-down of such operations is outlined in Notes 11 and 12. The consolidated financial statements of the Foundation reflect the following items associated with the student loan operations.

A. Student Loans Receivable

The following is a schedule of student loans receivable at December 31, 2007:

	(in thousands)
FFELP student loans receivable	\$ 138
Consumer education loans receivable	<u>9,026</u>
	9,164
Allowance for loan losses	<u>(569)</u>
Student loans receivable, net	<u><u>\$8,595</u></u>

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
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NOTES TO FINANCIAL STATEMENTS, Continued

6. **Items Associated with Student Loans**, continued

A. Student Loans Receivable , continued

FFELP Program

FFELP student loans receivable comprise federally guaranteed student loans with DOE-specified interest rate formulas and repayment terms. The Foundation's FFELP student loans receivable consists of loans originated under the provisions of the FFELP. The FFELP programs are the Federal Stafford Loan (Stafford) Program, the Federal Supplemental Loans for Students (SLS) Program, the Federal Parent Loan for Undergraduate Students (PLUS) Program, and the Federal Consolidation Loan Program.

CEL Program

The Foundation continues to hold the CalEdge portfolio. All other CEL loans were sold on June 8, 2006 as mentioned in Note 12. The CalEdge loans have an average time to maturity of approximately 10 years.

Combined FFELP and CEL Programs

At December 31, 2007, the Foundation maintained third-party servicing agreements with four corporations to act as agents for the FFELP and CEL programs to perform loan servicing, billing, accounting, reporting, and loan administrative duties. Under the terms of the servicing agreements, the service providers are held liable for losses resulting from their own negligent loan servicing. At December 31, 2007, 100% of the Foundation's loans were serviced by third-party service providers.

B. Allowance for Loan Losses

The table below summarizes the changes in the allowance for loan loss reserve for the year ended December 31, 2007:

	(in thousands)
Balance at the beginning of the year	\$ 599
Provision for possible losses	254
Charges to allowance	(393)
Recoveries	622
Decrease in allowance estimate	<u>(513)</u>
Balance at end of the year	<u>\$ 569</u>

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
(formerly The Education Financing Foundation of California)

NOTES TO FINANCIAL STATEMENTS, Continued

6. **Items Associated with Student Loans**, continued

C. Bonds Payable

The Foundation has one bond payable outstanding as of December 31, 2007 totaling \$9.4 million. This bond payable is due to California Educational Facilities Authority (CEFA) and is related to the CalEdge program (see Note 12).

The CEFA bond payable was issued in connection with a tax-exempt financing and is payable at a fixed rate of 5.55%. The bond matures in 2028. Payments of principal and interest are paid semi-annually based on a cash flow analysis performed by CALMA. Principal and interest paid totaled \$1.7 million and \$0.6 million, respectively, for the year ended December 31, 2007.

D. Restricted Assets

In accordance with the CalEdge bond indenture agreements, a ratio of trust asset collateral to bond liability or indebtedness must meet or exceed a specified distribution threshold in order for the Foundation to have the ability to transfer funds from the indenture trust accounts to the general operating account. These amounts represent restricted assets.

Asset collateral held in trusts in excess of bond and notes liability or indebtedness, but not available for distribution due to asset collateral ratio threshold restrictions, was approximately \$0.3 million at December 31, 2007.

E. Special Allowance Payment (SAP) and Interest Repayment

In 2007, one of the third party student loan service providers, ACS, informed CEFI that an audit had revealed an error in the software system that calculated average student loan balances outstanding used by the DOE to calculate SAP and government interest payments. The error produced an overstatement of SAP and government interest for a period of approximately 10 years. ACS reported that CEFI's overpayment totaled \$6.1 million. The DOE invoiced CEFI for this amount in two separate installments, \$2.1 million in April 2007, which was accrued at December 31, 2006, and \$4.0 million in September 2007. These amounts were paid in July and November 2007 respectively. The amount totaled \$4.0 million for the year ended December 31, 2007 and is reflected as a reduction of revenues on the consolidated statement of activities. Another student loan service provider, Nelnet, provided a refund of \$0.1 million which has been netted against the special allowance payment and interest repayment.

7. **Employee Benefits**

The Foundation sponsors a 403(b) plan to which eligible employees may voluntarily contribute a percentage of their compensation. The Foundation contributes a matching amount up to 6% of an employee's salary. The Foundation's plan expense was \$59 thousand for the year ended December 31, 2007.

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
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NOTES TO FINANCIAL STATEMENTS, Continued

7. **Employee Benefits**, continued

CEFI has a nonqualified deferred compensation plan (the DCP), established utilizing an irrevocable trust called a Rabbi Trust, to provide specified benefits to a select group of former CEFI management. Contribution, vesting, and benefit provisions are as outlined in the plans. In May 2005, CEFI funded the DCP using corporate-owned life insurance carried by Sun Life Assurance Company of Canada (U.S.), which is owned by the Rabbi Trust through Wilmington Trust Bank, the trustee of the plan. At December 31, 2007, the cash surrender value of this life insurance policy was \$0.8 million and is included in other assets on the statement of financial position. The deferred compensation liability was \$0.8 million, and the deferred compensation expense for 2007 was \$70 thousand. The following table sets forth the DCP status, along with amounts recognized in the Foundation's consolidated statement of financial position for the year ended December 31, 2007:

	(in thousands)
Reconciliation of DCP cost:	
Accrued DCP cost at beginning of year	\$(964)
Net periodic DCP credit	(70)
Plans' participant contributions	-
Benefits paid	<u>211</u>
Accrued DCP cost at end of year	(823)
Cash surrender value of insurance policy	<u>846</u>
Over funded/(under funded) status	<u>\$ 23</u>

8. **Income Taxes**

As a result of the restructuring discussed in Note 11, CEFI, a for-profit Delaware corporation, was created. Because CEFI incurred a taxable net loss in 2007, there is no current income tax expense.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of CEFI's deferred tax liabilities and assets at December 31, 2007, are as follows:

	(in thousands)
Deferred tax assets:	
Accrued liabilities	\$ 627
Tax loss carryforwards	7,216
Other	<u>234</u>
Net deferred tax assets	8,077
Valuation allowance	<u>(8,077)</u>
Net deferred taxes	<u>=</u>

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
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NOTES TO FINANCIAL STATEMENTS, Continued

8. **Income Taxes**, continued

CEFI has provided a full valuation allowance on the net deferred tax assets due to uncertainties regarding the realization of deferred tax assets based on CEFI's lack of earnings history and nominal projected future earnings. The change in the valuation allowance for the year ended December 31, 2007 was \$0.8 million.

As of December 31, 2007, CEFI had federal and state net operating loss carryforwards of approximately \$18.6 million and \$19.4 million, respectively. If not utilized, the net operating loss carryforwards will expire beginning in 2025 and 2010, respectively.

Utilization of net operating losses may be subject to a substantial annual limitation due to the "change of ownership" provisions of the Internal Revenue Code of 1986. The annual limitation may result in the expiration of net operating losses before utilization.

CEFI's provision for income taxes differs from the federal statutory rate. Below is a reconciliation for the year ended December 31, 2007:

Statutory federal income tax rate	34%
State income taxes, net of federal benefit	5%
Other	(1%)
Prior year true-ups	(68%)
Increase in valuation allowance	<u>30%</u>
Effective tax rate	0%

Prior year true-ups primarily relate to the true up of book-to-tax basis differences in the loans that were sold in prior years.

9. **Fair Value of Financial Instruments**

SFAS No. 107, *Disclosures About Fair Value of Financial Instruments*, requires an estimation of fair values of the Foundation's financial instruments. The following is a summary of the assumptions and methods used to estimate those values.

Cash and Equivalents

Fair value approximates carrying value based on the liquidity and short-term nature of the instruments.

Investments

Fair value for investments with short-term remaining maturities (less than three months) is approximately carrying value. The fair value of variable rate guaranteed investment contracts approximates carrying value as the underlying interest rate of these investments over the anticipated holding period approximates current market rates. The fair value of the fixed rate investment contracts is estimated using discounted cash flow analyses, using then-prevailing market interest rates. The carrying value for the remaining investments, principally debt and equity securities, approximates fair value, as taken from market prices reported in brokerage and investment manager account statements.

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
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NOTES TO FINANCIAL STATEMENTS, Continued

9. **Fair Value of Financial Instruments**, continued

Student Loans Receivable

The fair value of student loans receivable, with the exception of certain fixed rate loans, is deemed to be their carrying value. The fair value for fixed rate loans is estimated using discounted cash flow analyses, using then-prevailing market interest rates.

Bonds Payable

The fair value approximates the carrying value as bonds interest rates are principally variable rates that regularly adjust to levels consistent with prevailing market interest rates. For fixed rate bonds, the fair value is estimated using discounted cash flow analyses using then-prevailing market interest rates.

The following table summarizes the fair value of the Foundation's financial instruments as of December 31, 2007:

	Carrying Value	Fair Value
	(in thousands)	
Assets:		
Cash and equivalents	\$ 1,904	\$ 1,904
Investments	\$ 471,575	\$ 471,575
Student loan receivables*	\$ 9,265	\$ 9,175
Liabilities—bonds payable	\$ 9,435	\$ 9,636

*The carrying value for student loans receivable includes net unamortized purchase premiums and origination costs, and allowance for loan losses, but excludes accrued interest receivable.

10. **Commitments, Contingencies, and Concentrations of Risk**

Premises and Equipment Lease Commitments

The following is a schedule of future minimum rental payments required under operating leases, including the Foundation's office facilities and equipment that have remaining noncancelable terms in excess of one year at December 31, 2007:

	(in thousands)
2008	\$ 332
2009	338
2010	301
2011	244
2012	<u>40</u>
Total	<u>\$1,255</u>

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
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NOTES TO FINANCIAL STATEMENTS, Continued

10. **Commitments, Contingencies, and Concentrations of Risk**, continued

Premises and Equipment Lease Commitments, continued

In late 2006, the Foundation entered into a five year lease agreement for new office space with a commencement date of February 2007. The lease on its original office space has a termination date of July 2010. Simultaneously with its entering into the new lease, the Foundation sublet its original office space for the remainder of its term.

The total sublease income specified in the sublease agreement is as follows:

	(in thousands)
2008	\$ 114
2009	114
2010	<u>66</u>
Total	<u>\$294</u>

Total rental expense for the year ended December 31, 2007 was \$0.3 million.

Investment Commitments

As of December 31, 2007, the Foundation has commitments under various investment agreements to make additional capital contributions of \$21.4 million.

Contingencies

From time to time, the Foundation may be involved as a party to certain legal proceedings and other claims arising in the normal course of its business. While litigation and claims resolution are subject to many uncertainties and cannot be predicted with assurance, it is management's opinion that any resulting losses would not have a material effect on the Foundation's financial statements.

The Foundation is subject to significant regulations and administrative rules imposed by various regulatory bodies. These rules and regulations are subject to legislative changes and departmental interpretation that may change over time. It is possible that future legislative changes or interpretations of administrative rules and regulations may result in changes to the Foundation's financial position.

Concentrations of Risk

The Foundation maintains its cash balance in two financial institutions. The balance is insured by the Federal Deposit Insurance Corporation (FDIC) up to \$100,000. At December 31 2007, the Foundation's uninsured cash balance was \$2.1 million.

The Foundation's credit risk is inherent principally in its investments. Adverse economic conditions either nationwide or internationally may result in a reduction of the investments carrying amount. The maximum loss on the investments would be the carrying amount in the financial statements, less amounts insured by the Securities Investor Protection Corporation (SIPC). At December 31 2007, the Foundation's uninsured investment balance was \$468.8 million. Guaranteed investment contracts are held at one financial institution and are insured by the FDIC up to \$100,000. At December 31 2007, the Foundation's uninsured investment balance related to guaranteed investment contracts was \$2.1 million.

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
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NOTES TO FINANCIAL STATEMENTS, Continued

10. **Commitments, Contingencies, and Concentrations of Risk**, continued

Concentrations of Risk, continued

The Foundation's credit risk is also inherent in its student loans receivable. Adverse economic conditions either regionally or nationwide may result in an increase in student loan borrower defaults.

11. **Corporate Restructuring**

As indicated in Note 1, the Foundation and its subsidiary, CEFI Corporation (CEFI) are the surviving entities after a series of corporate restructuring beginning in 2004. In late 2004, Chela Financial Resources, Inc. (Resources) and its affiliate, Chela Inc., were nonprofit public benefit corporations organized for the purpose of assisting students in obtaining funds for their education by way of purchasing student loans in the secondary market place, offering various education loan assistance programs and providing loan servicing. Chela Inc. was incorporated on April 23, 1979 under the Internal Revenue Code (IRC) Section 501(c)(3), 150(d) and Resources was incorporated on May 11, 1994 under IRC Section 501(c)(3). Both entities were incorporated under the laws of the State of California.

Chela Inc., pursuant to the requirements of Internal Revenue Service (IRS) Code Section 150(d), was required to apply all of its net income to the acquisition of additional student loans authorized under the Higher Education Act. In addition, Chela Inc. would have been required, upon dissolution, to return its net assets to the United States government.

Recognizing the problems inherent in these restrictions, Congress enacted IRC Section 150(d)(3) which specifically authorized IRC Section 150(d) corporations to undergo a "conversion" process whereby they were allowed to transfer all of their liabilities and pledged student loan assets to a wholly owned, for-profit subsidiary, sell the assets, pay down the liabilities and transfer the residual cash to the original 150(d) corporation which was transformed into a charitable foundation. This opened the possibility for the Chela Inc. to use its assets more fully for the charitable purpose of benefiting higher education.

In late 2004, Chela Inc.'s management embarked on a program to take advantage of the benefits of this new legislation and initiated the organizational changes and the sale of assets to Nelnet Corporation (Nelnet) and First Marblehead Bank (First Marblehead) described more fully below:

- Substantially all of Chela Inc.'s assets and liabilities were transferred to CEFI, a newly created for-profit Delaware corporation, in exchange for CEFI's issuance of Senior Stock to Chela Inc.
- Resources merged with Chela Inc., after which all of Resources' assets liabilities, business and employees were transferred to CEFI.
- The name of Chela Inc. was changed to The Education Financing Foundation of California.
- CEFI sold substantially all (approximately \$2.2 billion) of its FFELP and private student loans.
- Profits from these sales were paid in a dividend to the Foundation, forming the asset base that allows the Foundation to carry out its mission.

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
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NOTES TO FINANCIAL STATEMENTS, Continued

11. **Corporate Restructuring**, continued

Prior to the sale of assets, the primary source of revenue for Chela, Inc. was interest on student loans. After the sale of assets, the Foundation's primary source of revenue is from interest and investment income.

12. **Sale of Assets and Wind-Down of CEFI**

On October 25, 2005, under the terms of the Asset Purchase Agreement (APA) with Nelnet Corporation (Nelnet), CEFI sold substantially all of its FFELP student loan assets, totaling approximately \$2.2 billion (not including loans more than 210 days delinquent), along with related origination, servicing operations, and intellectual property and trademarks. Then, on June 8, 2006, the Foundation consummated a sale of substantially all remaining consumer education loans (CEL loans) to First Marblehead for \$93 million. Concomitant with these sales, the bonds that financed each asset pool were redeemed and CEFI had no further obligations to the bondholders. The only remaining loans and debt retained by CEFI were related to the CalEdge program, more fully described below.

After the asset sale, the Foundation was left with delinquent FFELP loans that did not qualify for sale because they were more than 210 days delinquent. The APA provided that if any previously delinquent FFELP loans became less than 210 days delinquent, Nelnet would purchase these loans at par. As of December 31, 2007, the remaining balance of FFELP loans more than 210 days delinquent totaled \$0.1 million.

As mentioned above, the Foundation also retained CEL loans originated under the CalEdge program. The CalEdge program was initiated on April 1, 1998 as a joint program of Chela, Inc. and the California Educational Facility Authority (CEFA) whereby CEFA provided funding for student loans via a bond issue and Chela, Inc. originated the loans and provided program administration. As of December 31, 2007, these loans totaled \$9.0 million and related debt totaled \$9.4 million, respectively.

Aside from the purchase of loans and other assets as discussed above, there were a number of other contractual arrangements entered into between CEFI and Nelnet, including:

- Nelnet agreed to provide future servicing or oversight of third-party servicers for those loans retained by CEFI for a period of up to five years from the date of the agreement.
- For a period of 36 months from the date of the agreement, Nelnet may require CEFI to repurchase any of the purchased loans under a variety of specified circumstances. Generally, these circumstances relate to events or actions prior to the date Nelnet purchased the loans. Any such repurchases are to be at a comparable premium to the purchase price Nelnet had originally paid plus any incidental costs to fully compensate Nelnet. CEFI has an indemnification reserve of \$0.8 million at December 31, 2007, against potential repurchases of this nature. Repurchases through June 2008 have been negligible.

On March 27, 2006, The Foundation entered into an Administrative Services Agreement with the California Alternative Loan Marketing Association (CALMA) whereby CALMA assumed the Foundation's administrative and program duties under the 1998 Indenture and Program Administration Agreement for the CalEdge student loan program.

Continued

COLLEGE ACCESS FOUNDATION OF CALIFORNIA
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NOTES TO FINANCIAL STATEMENTS, Continued

12. **Sale of Assets and Wind-Down of CEFI**, continued

After the sale of assets to Nelnet and First Marblehead, CEFI management turned its attention to winding down the CEFI business, terminating CEFI employees and transferring management of the remaining assets to the Foundation. Most of the terminations took place during the later part of 2005 and first half of 2006. Three CEFI employees were transitioned to the Foundation.

In December 2006, CEFI management took action to terminate its 401(k) retirement plans. Employees still retain balances in the 403(b) plan, therefore termination had not yet taken place at June 2008. A recent change in the law will now enable the Foundation to terminate the plan.