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STATE BOARD OF ACCOUNTS
302 WEST WASHINGTON STREET
ROOM E418
INDIANAPOLIS, INDIANA 46204-2765

Telephone: (317) 232-2513
Fax: (317) 232-4711
Web Site: www.in.gov/sboa

August 22, 2016

Linae Devaisher, CFO
Indiana Secondary Market for Education Loans, Inc.
11595 North Meridian Street, Suite 200
Carmel, IN 46032

We have reviewed the audit report prepared by Katz, Sapper & Miller, LLP, Independent Public Accountants, for the period July 1, 2013 to June 30, 2014. In our opinion, the audit report was prepared in accordance with the guidelines established by the State Board of Accounts. Per the Independent Public Accountants' opinion, the financial statements included in the report present fairly the financial condition of the Indiana Secondary Market for Education Loans, Inc., as of June 30, 2014, and the results of its operations for the period then ended, on the basis of accounting described in the report.

The Independent Public Accountants' report is filed with this letter in our office as a matter of public record.

Paul D. Joyce

Paul D. Joyce, CPA
State Examiner

Indiana Secondary Market for Education Loans, Inc.

Financial Statements and Supplemental Information for the Years Ended June 30, 2014 and 2013, and Independent Auditors' Report

INDIANA SECONDARY MARKET FOR EDUCATION LOANS, INC.

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Independent Auditors' Report

Board of Directors
Indiana Secondary Market for Education Loans, Inc.

Report on the Financial Statements

We have audited the accompanying financial statements of Indiana Secondary Market for Education Loans, Inc. (ISM), a component unit of the State of Indiana, which comprise the statements of net position as of June 30, 2014 and 2013, and the related statements of revenues, expenses and changes in net position and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider 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.

Katz, Sapper & Miller, LLP
Certified Public Accountants

800 East 96th Street, Suite 500
Indianapolis, IN 46240

Tel 317.580.2000
Web ksmcpa.com

An Affiliate of
KSM Business Services, Inc.

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 net position of Indiana Secondary Market for Education Loans, Inc. as of June 30, 2014 and 2013, and the changes in its net position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States.

Report on Required Supplementary Information

Accounting principles generally accepted in the United States require that the management's discussion and analysis on pages 3 through 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States, 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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 16, 2014, on our consideration of ISM's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering ISM's internal control over financial reporting and compliance.

Katz, Sapper & Miller, LLP

Indianapolis, Indiana
October 16, 2014

MANAGEMENT’S DISCUSSION AND ANALYSIS (UNAUDITED)

INDIANA SECONDARY MARKET FOR EDUCATION LOANS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)

The financial discussion, analysis, and overview of Indiana Secondary Market for Education Loans, Inc. (ISM) is required supplementary information. Among other things, it provides an analytical overview of ISM's condensed financial information and should be read in conjunction with the financial statements and related notes that follow.

Overview of Indiana Secondary Market for Education Loans, Inc.

ISM was established pursuant to Public Law No. 154 of the 1980 Indiana General Assembly and is a public benefit corporation organized exclusively for education purposes. ISM serves as the State of Indiana's designated secondary market for education loans and acts as an eligible lender under the Higher Education Act, as amended. ISM's enabling statute was amended effective April 30, 2013 with the signing of SB 532. SB 532 permits ISM to become a direct lender of non-federal, post-secondary education supplemental loans for the purpose of attending both Indiana and non-Indiana colleges and universities. SB 532 also mandates that ISM engage in financial literacy activities.

ISM is currently governed by a nine member Board of Directors who are appointed by the Governor of the State of Indiana. Taxable bonds and existing cash balances are the primary sources of funding for ISM's programs. The Health Care and Education Reconciliation Act of 2010 ("HCEARA") eliminated the origination of new FFELP loans after June 30, 2010. This did not impact the terms of existing FFELP loans. ISM continues to administer a program for the servicing of loans guaranteed and reinsured by the United States Department of Education ("US DOED"). In addition, ISM has a teaming arrangement for servicing loans originated under the Federal Direct Student Loan Program working with the Higher Education Loan Authority of the State of Missouri.

With the change to its enabling statue, ISM is focusing on loan programs designed to facilitate access for all Indiana residents to educational funding at the lowest possible cost. In addition, ISM continues to expand its support for Indiana resident's pursuit of access by providing informational presentations and distributing educational materials related to education funding.

ISM's financial statements consist of the following: the statements of net position, the statements of revenues, expenses and changes in net position and the statements of cash flows. These financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as promulgated by the Governmental Accounting Standards Board. The statements of net position present the financial position of ISM at the end of the fiscal year and include all assets, liabilities and net position of ISM. The statements of revenues, expenses and changes in net position present ISM's changes in financial position for the years ended June 30, 2014 and 2013. The statements of cash flows provide information about the sources and uses of ISM's cash resources for the years ended June 30, 2014 and 2013.

Condensed Financial Information (in thousands)

Statement of Net Position as of June 30,	2014	2013	2012
Cash and investments	$ 146,724	$ 165,028	$ 176,951
Student loans receivable—net	157,072	168,251	1,357,518
Other assets	4,400	4,573	37,453
Total assets	$ 308,196	$ 337,852	$ 1,571,922
Taxable bonds payable	$ 168,650	$ 189,381	$ 1,270,831
Tax-exempt bonds payable		750	183,000
Other liabilities	1,204	9,558	10,035
Total liabilities	169,854	199,689	1,463,866
Total net position	138,342	138,163	108,056
Total liabilities and net position	$ 308,196	$ 337,852	$ 1,571,922

INDIANA SECONDARY MARKET FOR EDUCATION LOANS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED, UNAUDITED)

Condensed Financial Information (in thousands)

Operating Results Years Ended June 30,	**2014**	**2013**	**2012**
Interest on student loans, including subsidy	$ 6,018	$ 43,399	$ 51,230
Special allowance on student loans	(3,658)	(24,812)	(28,204)
Loss on sale of student loans		(23,796)	
Gain on repurchase of bonds payable	674	69,717	
Net gain on investments	234		
Other income	506	794	9,186
Total operating revenues	3,774	65,302	32,212
Interest expense	2,070	17,139	17,035
Fees and debt issuance costs	154	933	965
Loan servicing and administration	1,371	7,256	5,871
Distribution to State of Indiana		10,000	
Arbitrage rebate (recovery) provision		(133)	259
Total operating expenses	3,595	35,195	24,130
Change in net position	179	30,107	8,082
Net Position - Beginning of Year	138,163	108,056	99,974
Net Position - End of year	$ 138,342	$ 138,163	$ 108,056

Financial Analysis

In June 2013, ISM sold loan and accrued interest receivables totaling $1,032 million. ISM received total proceeds of approximately $1,021 million resulting in a loss on sale of $24 million. ISM used the proceeds from the sale to repurchase outstanding bonds payable of $1,244 million at a discount resulting in a gain of $70 million.

Statement of Net Position

As of June 30, 2014, total assets decreased $29.7 million and combined with a decrease in liabilities of $29.8 million, resulted in an increase to ISM's net position of $179 thousand or .13%. This increase was due to the results of repurchasing outstanding bonds at a discount to face value and controlling operating expenses. This compares to an increase of 28% in 2013 as a result of the loan sale proceeds being used to repurchase outstanding bonds at a discount.

Cash and investments decreased 11% to $147 million as compared to a balance of $165 million in fiscal 2013. The decrease in cash and investments is the result of bond purchases throughout the year, payment of a tax exempt arbitrage VCAP settlement, as well as the normal use of cash to pay operating and debt service expenses.

Student loans receivable decreased 7% from $168 million in fiscal 2013 to $157 million in fiscal 2014, as compared to an 88% decrease from $1,358 million in fiscal 2012 to $168 million in fiscal 2013 due to a loan sale in June 2013. Effective March 30, 2010, the Health Care and Education Reconciliation Act of 2010 prohibited origination of any new loans after June 2010 under the Federal Family Education Loan Program (FFELP).

The change in student loans receivable for 2014 was due to decreases in existing loan principal through borrower consolidation, claims and payment activity. As of June 30, 2014, the student loan portfolio held by ISM was made up of approximately 87% Consolidation Loans and 13% Stafford and PLUS Loans. There was also a decrease in the allowance for loan loss due to the decrease in the size of the loan portfolio and an evaluation by management of past experience, trends in student loan claims rejected by guarantors, and other economic factors.

Other assets decreased 4% from $4.6 million in fiscal 2013 to $4.4 million in fiscal 2014, as compared to an 88% decrease from $37.5 million in fiscal 2012 to $4.6 million in fiscal 2013. This decrease relates directly to reductions in borrower interest receivable.

Liabilities decreased 15% from $200 million in fiscal 2013 to $170 million in fiscal 2014, as compared to an 86% decrease from $1,464 million in fiscal 2012 to $200 million in fiscal 2013. This decrease was generally due to a decrease in outstanding debt due to repurchases. In addition accrued payables decreased from the previous year due to expenses accrued for June 2013 transaction of loan sale and debt reduction. During this fiscal year, tax exempt arbitrage liabilities were reduced due to the VCAP settlement and the extinguishment of all tax-exempt debt.

Total net position at June 30, 2014 was $138.3 million, representing an increase from $138.2 million at June 30, 2013. This compared to a 28% increase in fiscal year 2013.

Operating Results

ISM's net position increased $179 thousand on operating revenues of $3.8 million for the fiscal year ended June 30, 2014, compared to an increase in net position of $30 million from operating revenues of $65.3 million for the prior fiscal year. The current year change in net position was primarily due to below par bond repurchases resulting in a gain of $674 thousand and an increase in investment earnings, as well as reductions in operating expenses. The market for ISM's student loan auction securities continued to be disrupted for the fiscal year, with auctions initially failing on or around February 14, 2008, and bond interest reverting to the Maximum Auction Rate. This disruption has continued throughout all of fiscal years 2014 and 2013.

Total operating revenues decreased 94%, to $3.8 million for the fiscal year ended June 30, 2014, from $65 million for the fiscal year ended June 30, 2013. Total operating revenues increased 103%, to $65 million for the fiscal year ended June 30, 2013, from $32 million for the fiscal year ended June 30, 2012. Interest income on student loans decreased 86% during the fiscal year ended June 30, 2014, due to the loan portfolio sale in June 2013. The special allowance on student loans decreased during fiscal year 2013 due to reduced loan balances. The special allowance index changed from three-month commercial paper rate to one-month LIBOR, effective April 1, 2012, reducing interest rate basis risk. Gain on extinguishment of debt has decreased dramatically from 2013 due to less bond repurchase activity.

Total operating expenses decreased 90% from $35.2 million for the fiscal year ended June 30, 2013, to $3.6 million for the fiscal year ended June 30, 2014. Total operating expenses increased 46% from $24.1 million for the fiscal year ended June 30, 2012, to $35.2 million for the fiscal year ended June 30, 2013. This decrease is due to the decrease in portfolio size resulting in reduced interest expense as well as reduced servicing fees. General administrative costs were reduced as well over the fiscal year. In addition, the provision for loan loss decreased in this fiscal year due to the reduction in the loan portfolio and a review by management.

Loan Servicing and ISM's Loan Programs

ISM utilizes American Education Services, Xerox Education Services, LLC, and Great Lakes Education Loan Servicing to service its student loan portfolio. Additional contract compliance, loan servicing support and quality control functions are performed in ISM's Indianapolis location for the existing FFELP portfolio.

ISM has a contract with Aspire Resources, Inc. and First Merchants Bank, an Indiana chartered bank, to originate private student loans under the Hoosier Education Loan Partnership (HELP).

Recent Developments

As of June 30, 2014, ISM's portfolio of auction rate securities remain in failed auction mode. ISM continues to seek opportunities to re-finance and tender these securities with excess revenues and recoveries of loan principal. As of June 30, 2014, $1,754 million of securities have been retired as part of ISM's tender and repurchase programs. As of July 25, 2013, ISM had no remaining tax-exempt or subordinate debt.

Requests of Information

This financial report is designed to provide a general overview of ISM's finances for all those with an interest in ISM's finances. Questions concerning any of the information should be addressed to Indiana Secondary Market for Education Loans, Inc., 251 North Illinois Street, Suite 400, Indianapolis, Indiana 46204.

FINANCIAL STATEMENTS

INDIANA SECONDARY MARKET FOR EDUCATION LOANS, INC.

STATEMENTS OF NET POSITION
AS OF JUNE 30, 2014 AND 2013
(In thousands)

	2014	2013
ASSETS		
CURRENT ASSETS:		
Cash and equivalents:		
Unrestricted	$ 126,393	$ 121,772
Designated		2,022
Total cash and equivalents	126,393	123,794
Short-term investments:		
Unrestricted	9,128	24,091
Restricted	2,000	2,000
Student loans receivable — net	11,309	14,115
Accrued interest receivable — student loans receivable	4,129	4,307
Accrued interest receivable — cash and short-term investments	24	40
Prepaids and other assets	139	65
Total current assets	153,122	168,412
NON-CURRENT ASSETS:		
Investments	9,203	15,143
Student loans receivable — net	145,763	154,136
Capital assets — net	108	161
Total non-current assets	155,074	169,440
TOTAL	$ 308,196	$ 337,852
LIABILITIES AND NET POSITION		
CURRENT LIABILITIES:		
Accounts payable and accrued expenses	$ 1,162	$ 7,486
Accrued interest payable	42	50
Current portion of bonds payable		750
Total current liabilities	1,204	8,286
NON-CURRENT LIABILITIES:		
Bonds payable	168,650	189,381
Arbitrage rebate payable		2,022
Total non-current liabilities	168,650	191,403
Total liabilities	169,854	199,689
NET POSITION:		
Net investment in capital assets	108	161
Unrestricted	136,234	133,980
Restricted	2,000	4,022
Total net position	138,342	138,163
TOTAL	$ 308,196	$ 337,852

See notes to financial statements.

INDIANA SECONDARY MARKET FOR EDUCATION LOANS, INC.

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
YEARS ENDED JUNE 30, 2014 AND 2013
(In thousands)

	2014	2013
OPERATING REVENUES:		
Interest on student loans	$ 5,422	$ 38,279
U.S. Secretary of Education:		
Special allowance	(3,658)	(24,812)
Interest subsidy	596	5,120
Loss on sales of student loans and accrued interest		(23,796)
Gain on repurchase of bonds payable	674	69,717
Net gain on investments	234	
Other income	506	794
Total operating revenues	3,774	65,302
OPERATING EXPENSES:		
Interest expense	2,070	17,139
Fees	154	933
Loan servicing and administration	1,371	7,256
Distribution to State of Indiana		10,000
Arbitrage rebate recovery		(133)
Total operating expenses	3,595	35,195
CHANGE IN NET POSITION	179	30,107
NET POSITION — Beginning of year	138,163	108,056
NET POSITION — End of year	$ 138,342	$ 138,163

See notes to financial statements.

INDIANA SECONDARY MARKET FOR EDUCATION LOANS, INC.

STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2014 AND 2013
(In thousands)

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES:		
Student loan interest net of special allowance payments received	$ (1,395)	$ 27,163
Proceeds from sales of student loans and accrued interest		1,051,459
Purchase of student loans	(8,103)	
Principal receipts on student loans	20,700	136,621
Distribution to State of Indiana		(10,000)
Cash received for other operating activities	1,204	819
Cash payments for employees and vendors	(6,550)	(6,624)
Net cash provided by operating activities	5,856	1,199,438
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net maturity of certificates of deposit	16,355	2,835
Net sale (purchase) of short-term investments	3,281	(3,826)
Net cash provided (used) by investing activities	19,636	(991)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
Repayment and redemption of bonds	(20,807)	(1,193,984)
Interest paid on bonds	(2,078)	(17,360)
Net cash used by noncapital financing activities	(22,885)	(1,211,344)
CASH FLOWS FROM CAPITAL ACTIVITIES:		
Purchase of capital assets, net	(8)	(17)
Net cash used by capital activities	(8)	(17)
CHANGE IN CASH AND EQUIVALENTS	2,599	(12,914)
CASH AND EQUIVALENTS — Beginning of year	123,794	136,708
CASH AND EQUIVALENTS — End of year	$ 126,393	$ 123,794

See notes to financial statements.

INDIANA SECONDARY MARKET FOR EDUCATION LOANS, INC.

STATEMENTS OF CASH FLOWS (CONTINUED)
YEARS ENDED JUNE 30, 2014 AND 2013
(In thousands)

	2014	2013
RECONCILIATION OF CHANGE IN NET POSITION TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Change in net position	$ 179	$ 30,107
Adjustments to reconcile change in net position to net cash provided by operating activities:		
Depreciation expense	59	82
Loss on sales of student loans and accrued interest		23,796
Gain on bond repurchase	(718)	(69,717)
Interest expense	2,070	17,139
Provision for allowance for loan losses, net of write-offs and recoveries	2,165	112
Arbitrage rebate recovery	(2,022)	(133)
Interest on student loans recapitalized	(2,990)	(594)
Change in assets and liabilities:		
Decrease in student loans receivable	13,345	1,165,583
Decrease in accrued interest receivable	194	31,916
(Increase) decrease in prepaids and other assets	(74)	1,491
Decrease in market value	(20)	
Decrease in other liabilities	(6,332)	(344)
Net cash provided by operating activities	$ 5,856	$ 1,199,438

See notes to financial statements.

1. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business — Indiana Secondary Market for Education Loans, Inc. (ISM) is an Indiana public benefit corporation formed to purchase and originate student loans under the Federal Family Education Loan Program (FFELP) provided for by the Higher Education Act (the Act). Effective March 30, 2010, the Health Care and Education Reconciliation Act of 2010 prohibited origination of any new loans after June 2010 under FFELP. Outstanding bonds are payable as specified in the resolutions authorizing the related sale of the bonds, are not payable by funds received from taxation, and are not debts of the State of Indiana or any of its political subdivisions. ISM is a discretely presented proprietary component unit of the State of Indiana.

ISM's bonds payable mature between 2038 and 2047. ISM's ability to meet its long-term obligations is dependent on borrowing costs, U.S. Department of Education (US DOED) subsidies and the ability to control operating expenses. Management has determined that obligations will be paid as due.

Basis of Presentation and Accounting — ISM's financial statements have been prepared on the basis of the governmental enterprise fund concept which pertains to financial activities that operate similarly to a private business enterprise. The assets of each fund are restricted pursuant to the bond resolutions. For financial statement presentation purposes, the funds have been aggregated into one proprietary fund type. ISM's funds are accounted for on the flow of economic resources measurement focus and use the accrual basis of accounting. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental and financial reporting principles. ISM follows GASB pronouncements as codified under GASB Statement No. 62.

Student Loans Receivable — Student loans receivable are stated at the principal amounts outstanding adjusted for an estimated allowance for loan losses, and unamortized purchase premiums or discounts. The related interest income generated from student loans is offset by premium amortization. ISM amortizes loan premiums and loan discounts over the estimated average life of the loan on a straight-line basis over 10 years, which approximates the effective interest method.

Interest on student loans is accrued based upon the actual principal amount outstanding. The U.S. Secretary of Education makes quarterly interest subsidy payments until the student is required, under the provisions of the Act, to begin repayment. Repayment must begin generally within six months after the student completes their course of study, leaves school, or ceases to carry at least one-half the normal full-time academic load as determined by the participating institution.

1. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The US DOED provides a special allowance to lenders participating in the FFELP. For loans first disbursed prior to January 1, 2000, the special allowance amount is the result of applying a percentage, based upon the average bond equivalent rates of 91-day United States Treasury bills, to the average daily unpaid principal balance and capitalized interest of student loans held by ISM. For loans first disbursed from January 1, 2000 through June 30, 2006, the special allowance amount is the result of applying a percentage, based upon the average bond equivalent rates of the three-month financial Commercial Paper ("CP") rate, to the average daily unpaid principal balance and capitalized interest of student loans held by ISM. If a special allowance amount is a negative number on a loan first disbursed prior to April 1, 2006, special allowance will not be paid for that loan type for that quarter. If a special allowance amount is a negative number on a loan first disbursed after April 1, 2006, the lender must remit the excess interest ("negative SAP") to the US DOED. The special allowance amount for a loan first disbursed on or after October 1, 2007, has additional provisions for lenders qualified as an eligible not-for-profit holder. Those eligible as not-for-profit lenders earn a 15 basis point higher yield. The special allowance is accrued as earned. Effective April 1, 2012, the index used to calculate special allowance for loans disbursed after January 1, 2000 is based on one-month LIBOR.

Cash and Equivalents — Cash and equivalents may consist of United States Treasury bills, money market funds, and short-term investments with original maturities of three months or less from the date of acquisition.

Investments — Investments consist of certificates of deposit, bonds and guaranteed investment contracts ("GICs"), which are carried at fair value based on available market prices. Changes in fair value are recorded in the statement of revenues, expenses and changes in net position. ISM adopted a revised investment policy on April 17, 2014 that was approved by the Indiana Finance Authority on July 17, 2014. This policy is for all funds held outside the existing trust. ISM is restricted to investments that meet the rating requirements per the bond indenture for all funds held within the trust. All cash and investments whose proceeds are designated for the payment of arbitrage rebate liabilities are classified as designated cash and investments (see Note 2).

Allowance for Loan Losses — Guarantees on student loans originated after October 1, 1993 but before July 1, 2006, provide for a reduced recovery of 98% of loan principal and accrued interest on loans which default. Guarantees on student loans originated after July 1, 2006 provide for a reduced recovery of 97% of loan principal and accrued interest on loans which default. Accordingly, ISM provides for an allowance for the estimated loss associated with the portion not recoverable. This allowance is increased by a provision charged to operations and reduced for losses actually incurred, and is included in the financial statements as a reduction of student loans receivable. ISM utilizes two national collection agencies to attempt collection on charged off accounts. The amount attributable to expected recoveries remains in the allowance.

In completing the analysis of the adequacy of the allowance for loan losses, past collection experience, delinquency trends and size of the portfolio, economic conditions, document deficiencies, and other factors are considered. Significant changes in these factors could impact the allowance and provision for loan losses. Accordingly, the evaluation of the allowance for loan losses is inherently subjective as it requires material estimates that may be subject to change.

1. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Capital Assets — Capital assets consist of office furniture, equipment and leasehold improvements recorded at cost. Depreciation is charged to operations using the straight-line method over the estimated useful lives of the related assets or the term of the lease, which is 3 to 7 years depending on the asset class.

Net Position — $136,234,000 and $133,980,000 of ISM's net position and all related revenues were unrestricted at June 30, 2014 and 2013, respectively. ISM does, however, maintain debt and other arrangements which limit the use of assets. At June 30, 2014 and 2013, ISM's restricted net position of $2,000,000 and $2,000,000, respectively, per bond reserve requirements (see Note 4) and $0 and $2,022,000, respectively, reflect amounts restricted to fund the arbitrage rebate payable (see Note 6) and $108,000 and $161,000, respectively, reflect amounts invested in capital assets (see Note 5).

Loan Income and Related Expenses — Interest and special allowance on loans are recognized as income in the period earned, and servicing costs are charged to expense as incurred. Premiums paid for student loans are amortized using a method which approximates the effective interest method over the estimated life of the loans (10 years). At June 30, 2014 and 2013, unamortized premiums totaled $1,890,000 and $2,642,000, respectively.

In addition, loans were purchased at a discount in June 2009, and this discount is being amortized over the estimated life of the loans (10 years). At June 30, 2014 and 2013, the unamortized discount totaled $237,000 and $281,000, respectively.

Servicing Fees — As of June 30, 2014, Affiliated Computer Services, American Education Services, and Great Lakes Education Loan Servicing service ISM's student loan portfolio. Servicing fee expense amounts are included in operating expenses in the statement of revenues, expenses and changes in net position.

Risk Management — ISM is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries. Coverage for these various risks of loss is obtained through commercial insurance. There has been no significant reduction in insurance coverage from the prior year for all categories of risk. Commercial insurance is purchased in an amount that is sufficient to cover ISM's risk of loss. ISM will record an estimated loss from a claim as an expense and a liability if it meets the following requirements: (1) information available indicates that it is probable that an asset has been impaired or a liability has been incurred at the date of the financial statements and (2) the amount of the loss can be reasonably estimated.

Operating Revenues and Expenses — Bond and loan issuances are the principal source of the funds. ISM derives revenue from investments, sublease rents, servicing fee income, interest on student loans, the U.S. Secretary of Education, and gains (losses) from the sale of student loans and early redemption of bonds payable. ISM's expenses primarily consist of interest on debt arrangements and loan servicing and administration.

Income Taxes — ISM is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. Therefore, no provision or liability for income taxes has been included in the financial statements. In addition, ISM has been determined by the Internal Revenue Service not to be a private foundation within the meaning of Section 509(a) of the Internal Revenue Code. There was no unrelated business income for the years ended June 30, 2014 and 2013.

1. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Use of Estimates — The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates that are particularly susceptible to change in the near-term relate to the determination of the arbitrage rebate payable and the allowance for loan losses.

Subsequent Events — Management has evaluated the financial statements for subsequent events occurring through October 16, 2014, the date the financial statements were available to be issued.

2. DEPOSITS AND INVESTMENTS

Deposits and investments as of June 30, 2014 and 2013, consisted of the following:

	2014	2013
	(In thousands)	
Special trust accounts:		
Unrestricted:		
Loan accounts	$ 9,998	$105,578
Revenue accounts	5,308	489
Designated – rebate accounts		2,022
	15,306	108,089
Restricted:		
Reserve accounts	2,000	2,000
Operating account	6,414	22,313
Money market funds	104,678	
Certificates of deposit	17,192	32,626
Bonds	1,134	
	129,418	54,939
	$146,724	$165,028
Current portion	$137,521	$149,885
Long-term portion	$ 9,203	$ 15,143

2. DEPOSITS AND INVESTMENTS (CONTINUED)

Cash Deposits with Financial Institutions

Deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are uncollateralized or collateralized with securities held by the pledging financial institution. Deposits held in the three demand deposit accounts are carried at cost and are insured up to $250,000 per financial institution.

The carrying amount of demand deposits was $8,414,000 and bank balances were $8,430,000. ISM's maximum risk was $7,930,000 at June 30, 2014.

Investments

The investment strategy of ISM for non-trust accounts is to emphasize a balanced return of current income and growth of principal consistent with the preservation of the purchasing power. The investment policy allows for investing in a portfolio balanced between equity and fixed income securities. The permissible investments are detailed in the investment policy. Trust accounts are invested in accordance with trust indentures executed by ISM.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of the investments.

As of June 30, 2014, ISM had the following investments and cash equivalents and maturities:

Investment Type	Fair Value (In thousands)	Maturities (In Years) < 1	1–5	6–10	> 10
Guaranteed investment contracts	$ 2,000	$ 2,000		$	$
Money market funds	119,984	119,984			
U.S. Treasury	1,134		$ 1,134		
Certificates of deposit	17,192	9,374	7,818		
	$ 140,310	$ 131,358	$ 8,952	$	$

As of June 30, 2013, ISM had the following investments and cash equivalents and maturities:

Investment Type	Fair Value (In thousands)	Maturities (In Years) < 1	1–5	6–10	> 10
Guaranteed investment contracts	$ 8,607	$ 8,607		$	$
Money market funds	106,067	106,067			
Certificates of deposit	32,626	17,783	$14,843		
	$ 147,300	$ 132,457	$14,843	$	$

2. DEPOSITS AND INVESTMENTS (CONTINUED)

Custodial Credit Risk

Custodial credit risk is the risk that ISM will not be able to recover the value of its deposits, investments or collateral securities that are in the possession of an outside party if the counterparty fails. Investment securities are exposed to risk if the securities are uninsured, are not registered in the name of ISM, and are held by either the counterparty or the counterparty's trust department or agent but not in ISM's name. ISM has no custodial credit risk on investments.

Credit Risk

The following table provides information on the credit ratings associated with ISM's investments and cash equivalents as of June 30, 2014:

Investment Type	Fair Value (In thousands)	S & P	Fitch	Moody's
Guaranteed investment contracts	$ 2,000	AA+	unrated	A1
Government money market funds	15,306	AAAm	unrated	Aaa-mf
Government money market funds	104,678	unrated	unrated	unrated
U.S. Treasury	1,134	AAA	unrated	unrated
Certificates of deposit	17,192	unrated	unrated	unrated
	$ 140,310			

Concentration of Credit Risk

Concentration of credit risk is the risk of loss that may arise in the event of default by a single issuer.

The following shows investments in issuers that represents 5% or more of the total investments at June 30, 2014:

Fidelity Government Money Market	76%
Northern Institutional U.S. Gov't Select Money Market	10%

3. STUDENT LOANS RECEIVABLE — NET

Student loans receivable consist of loans made under the Act and are carried at their unpaid principal balance net of an allowance for loan losses plus unamortized purchase premiums and discounts. Student loans earn interest at various rates ranging from 1.73% to 10.00%, depending upon the type of student loan and the date the student loan was made. Substantially all of the principal and accrued interest on student loans is insured by certain guarantee agencies which are reinsured by the federal government. At June 30, 2014 and 2013, the majority of ISM's student loans were guaranteed by the Pennsylvania Higher Education Assistance Agency (61% as of June 30, 2014), Educational Credit Management Corp. (19% as of June 30, 2014), and Great Lakes Higher Education Corporation (8% as of June 30, 2014).

3. STUDENT LOANS RECEIVABLE — NET (CONTINUED)

A portfolio of student loans was sold in June 2013 (see Note 1) and this sale agreement includes certain recourse provisions where ISM is required to repurchase loans that have inaccuracies that materially and adversely affect the value of the loan. The recourse provision is in effect through the life of the student loans. ISM has 60 days to cure any identified issue prior to being required to repurchase the loan. ISM has recorded an estimated recourse liability which is included as a component of the allowance for loan losses.

Student loans receivable - net as of June 30, 2014 and 2013, consisted of the following:

	2014 (In thousands)	2013
Student loans	$ 156,419	$ 169,055
Purchase premiums and discounts — net	1,653	2,361
Less — allowance for loan losses	(1,000)	(3,165)
	$ 157,072	$ 168,251
Current portion	$ 11,309	$ 14,115

The activity for the allowance for loan losses for the years ended June 30, 2014 and 2013 is as follows:

	2014 (In thousands)	2013
Beginning of year	$ 3,165	$ 3,053
Provision for loan losses	(2,100)	298
Write-offs of loans	(65)	(187)
Recoveries		1
End of year	$ 1,000	$ 3,165

4. BONDS PAYABLE

The following table displays the aggregate changes in bonds payable for the years ended June 30, 2014 and 2013:

	2014	2013
	(In thousands)	
Bonds payable — beginning of year	$ 190,131	$ 1,453,831
Repayments	(21,481)	(1,263,700)
Bonds payable — end of year	$ 168,650	$ 190,131

Bonds payable as of June 30, 2014 and 2013, consisted of the following:

	2014	2013
Auction Rate Certificates	$ 168,650	$ 190,131

Bonds payable at June 30, 2014, include $168,650 million of taxable Auction Rate Certificates (ARCs). The ARCs mature on various dates between December 1, 2038 and December 1, 2047. Interest on the ARCs ranged from 0.00% to 1.673% and 0.00% to 2.749% during the years ended June 30, 2014 and 2013, respectively, and was payable either at each auction, which generally occurs every 28 or 35 days as stipulated in the related ARC agreement, or semiannually. The interest rates are reset via a "dutch auction." Since February 2008, the auction process to establish these rates has failed; thus the ARCs will generally pay interest to the holder at a maximum rate as defined by the indenture. This failure also resulted in auctions occurring every 7 days.

The following table displays scheduled debt maturities and contractual interest payments for bonds payable at June 30, 2014 (in thousands):

Years Ending June 30	Principal	Interest	Total
2015		$ 2,074	$ 2,074
2016		2,074	2,074
2017		2,074	2,074
2018		2,074	2,074
2019		2,074	2,074
2020-2024		10,372	10,372
2025-2029		10,372	10,372
2030-2034		10,372	10,372
2035-2039	$ 12,000	10,139	22,139
2040-2044	19,725	9,433	29,158
2045-2048	136,925	3,532	140,457
Total	$ 168,650	$ 64,590	$ 233,240

4. BONDS PAYABLE (CONTINUED)

Bonds of each series are secured by (a) the proceeds derived from the sale of the bonds, (b) eligible loans, and (c) certain accounts established by the respective bond resolutions, including monies and securities therein.

The respective bond resolutions establish the following special trust accounts for each bond series, unless otherwise indicated:

Loan Accounts — The loan accounts are used to account for the proceeds of bond issues not required to be deposited in the debt service reserve accounts. Generally, amounts in the loan accounts may be expended (a) to finance eligible student loans, (b) to pay bond issue costs, and (c) to make deposits to the revenue accounts for the purpose of paying principal and/or interest on the bonds.

Revenue Accounts — The revenue accounts are used to account for all revenues received by ISM. Generally, amounts in the revenue accounts are used (a) to make principal and/or interest payments on the bonds, (b) to fund debt service reserve accounts, (c) to pay estimated program expenses to the operating account, and (d) to reimburse the issuers of insurance guaranteeing the bonds for amounts borrowed under the terms of the policies. Excess amounts in the revenue account may be transferred to the loan accounts or to optional redemption accounts.

Operating Accounts — Amounts deposited in operating accounts are used to pay reasonable and necessary program expenses for the bond issues.

5. CAPITAL ASSETS

Capital assets activity for the year ended June 30, 2014 (in thousands) was as follows:

	Beginning Balance	Additions	Retirements	Ending Balance
Depreciable capital assets:				
Furniture and equipment	$ 593	$ 7	$ 13	$ 587
Leasehold improvements	865			865
Total depreciable capital assets	1,458	7	13	1,452
Less accumulated depreciation	1,297	59	12	1,344
Net depreciable capital assets	$ 161	$ (52)	$ 1	$ 108

5. CAPITAL ASSETS (CONTINUED)

Capital assets activity for the year ended June 30, 2013 (in thousands) was as follows:

	Beginning Balance	Additions	Retirements	Ending Balance
Depreciable capital assets:				
Furniture and equipment	$ 626	$ 17	$ 50	$ 593
Leasehold improvements	865			865
Total depreciable capital assets	1,491	17	50	1,458
Less accumulated depreciation	1,264	82	49	1,297
Net depreciable capital assets	$ 227	$ (65)	$ 1	$ 161

6. ARBITRAGE REBATE PAYABLE

In accordance with Section 148 of the Internal Revenue Code of 1986 (the Code), as amended, and the regulations promulgated thereunder, ISM is required to pay to the United States Treasury certain amounts related to the ISM tax-exempt bond issues. The amount required to be paid represents the excess of amounts earned over the interest cost of the tax-exempt borrowings as defined in the Code. Non-purpose rebate payments are due every fifth year and when the bonds are retired. Purpose rebate payments are due every tenth year and every fifth year thereafter during the life of each bond issue and when the bonds are retired. The rebate calculation utilizes various assumptions and allows for the selection of alternative calculation options under the Code. At June 30, 2014 and 2013, the estimated arbitrage rebate liability was $0 and $2,022,000, respectively, which has been provided for in the financial statements. The factors used in determining this estimate are sensitive to change in the future and the change in estimate may be material to the financial statements. However, the ultimate amount payable, if any, is dependent on the investment yields and bond rates in the future.

The following table displays the aggregate changes in the arbitrage rebate payable during the years ended June 30, 2014 and 2013:

	2014 (In thousands)	2013 (In thousands)
Arbitrage rebate payable — beginning of year	$ 2,022	$ 2,155
Provision		(133)
Payment	(2,022)	
Arbitrage rebate payable — end of year	$	$ 2,022

6. ARBITRAGE REBATE PAYABLE (CONTINUED)

In July 2012, ISM requested a voluntary closing agreement with the Internal Revenue Service (IRS) (the process hereinafter referred to as (VCAP). The request for a closing agreement was based on application of the settlement proposed in IRS Announcement 2012-14 to certain bond issues described in a closing agreement. The bond issues that were covered were issued as tax-exempt qualified student loan bonds described in Section 144 of the Code. The terms of the proposed closing agreement included a payment by ISM as well as other matters required to be addressed by Announcement 2012-14. The bonds were repaid during fiscal year 2014.

7. FAIR VALUE OF FINANCIAL INSTRUMENTS

The estimated fair value amounts have been determined by ISM using available market information and appropriate valuation methodologies. However, considerable judgment is required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts ISM could realize in a current market exchange. The use of different market assumptions and/or valuation methodologies may have a material effect on the estimated fair value amounts.

The estimated fair values of ISM's financial instruments as of June 30, 2014 were as follows:

	2014	
	Carrying Amount	Estimated Fair Value
	(In thousands)	
ASSETS:		
Cash and equivalents and investments	$ 147,136	$ 146,724
Student loans receivable - net	156,419	156,419
Accrued interest receivable	4,153	4,153
LIABILITIES:		
Bonds payable	168,650	165,277
Accrued interest payable	42	42

7. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

The estimated fair values of ISM's financial instruments as of June 30, 2013 were as follows:

	2013	
	Carrying Amount	Estimated Fair Value
	(In thousands)	
ASSETS:		
Cash and equivalents and investments	$ 165,028	$ 165,028
Student loans receivable — net	168,251	164,015
Accrued interest receivable	4,307	4,307
LIABILITIES:		
Bonds payable	190,131	179,674
Accrued interest payable	50	50

Cash and Equivalents — Cash and equivalents are carried at cost, which approximates fair value.

Investments – Investments in money market mutual funds, certificates of deposit, bonds and investments in United States agency obligations are valued using quoted market prices for identical instruments.

Student Loans Receivable — ***Net*** — Loans are categorized by status (in-school, grace, repayment, and delinquent). The fair value is estimated by discounting the future cash flows using current rates of return required by investors in similar assets, less an estimated allowance for credit losses.

Accrued Interest Receivable — Accrued interest receivable is carried at cost, which approximates fair value.

Bonds Payable — The estimated fair value is estimated based on quoted current market prices. They are not recorded in the financial statements at fair value but at face value.

Accrued Interest Payable — Accrued interest payable is carried at cost, which approximates fair value.

8. RETIREMENT PLANS

ISM established the Indiana Secondary Market 401(k) Retirement Plan (Plan) in July 2002. Effective March 16, 2012, this Plan was merged into the EmPower Retirement Savings Plan as part of the contract with Human Capital Concepts, LLC. The Plan is a "Safe Harbor 401(k) Plan" as described in the Code. All employees 18 or older are eligible to participate on the first day of the month following their hire date. ISM makes a safe-harbor matching contribution equal to 100% of the first 4% that each participant contributes to the Plan. ISM also may make a discretionary profit-sharing contribution to Plan for participants who are employed at the end of the Plan year. Participants are 100% vested in ISM's contributions after one year of service. ISM's contributions to the Plan during fiscal years 2014 and 2013 were approximately $30,000 and $32,000, respectively.

9. COMMITMENT

ISM leases office space under the terms of a long-term non-cancellable operating lease. Future minimum required payments under this operating lease at June 30, 2014, were as follows:

Years Ending June 30	Rental Payments
2015	$ 607,000
2016	306,000
	$ 913,000

Rent expense under this operating lease was approximately $598,000 and $476,000 for the years ended June 30, 2014 and 2013, respectively.

ISM has entered into sublease agreements for a portion of its office space. The amount of rental income received for the years ended June 30, 2014 and 2013 was approximately $178,000 and $175,000, respectively. The sublease agreements expire in January 2016. At June 30, 2014, the future sublease rental income to be received through January 2016 was as follows:

Years Ending June 30	Rental Income
2015	$ 180,583
2016	106,606
	$ 287,189

10. CONTINGENCIES

ISM is subject to various legal proceedings and claims which arise primarily in the ordinary course of conducting its business. In management's opinion, the ultimate resolution of such matters will not have a material adverse effect on ISM's financial position or its results of operations.

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OTHER REPORT

Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards

Board of Directors
Indiana Secondary Market for Education Loans, Inc.

We have audited, in accordance with the auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States, the financial statements of Indiana Secondary Market for Education Loans, Inc. (ISM), a component unit of the State of Indiana, which comprise the statement of net position as of June 30, 2014, and the related statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated October 16, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered ISM's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of ISM's internal control. Accordingly, we do not express an opinion on the effectiveness ISM's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Katz, Sapper & Miller, LLP
Certified Public Accountants
800 East 96th Street, Suite 500
Indianapolis, IN 46240
Tel 317.580.2000
Web ksmcpa.com
An Affiliate of
KSM Business Services, Inc.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether ISM's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this report is not suitable for any other purpose.

Katz, Sapper & Miller, LLP

Indianapolis, Indiana
October 16, 2014