



Financial Statements

Nellie Mae Education Foundation, Inc.

December 31, 2008 and 2007

NELLIE MAE EDUCATION FOUNDATION, INC.

Financial Statements

Table of Contents

Financial Statements:

Independent Auditors' Report	1
Statements of Financial Position	2
Statements of Activities and Changes in Net Assets	3
Statements of Cash Flows	4
Notes to Financial Statements	5 – 12



Mayer Hoffman McCann P.C.

An Independent CPA Firm

Tofias New England Division

350 Massachusetts Avenue

Cambridge, MA 02139

Tel: 617.761.0703 Fax: 617.761.0601

www.mhm-pc.com

Independent Auditors' Report

Board of Directors
Nellie Mae Education Foundation, Inc.
Quincy, Massachusetts

We have audited the accompanying statement of financial position of Nellie Mae Education Foundation, Inc. (the "Foundation") as of December 31, 2008 and the related statements of activities and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of Nellie Mae Education Foundation, Inc. as of December 31, 2007 were audited by other auditors, Tofias P.C., whose shareholders became shareholders of Mayer Hoffman McCann P.C. as of December 31, 2008, and whose report dated February 20, 2008 expressed an unqualified opinion on those statements.

We conducted our audit in accordance with U.S. generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit 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 the 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 financial statements referred to above present fairly, in all material respects, the financial position of Nellie Mae Education Foundation, Inc. as of December 31, 2008 and the changes in its net assets and its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

Mayer Hoffman McCann P.C.

March 16, 2009
Cambridge, Massachusetts

NELLIE MAE EDUCATION FOUNDATION, INC.

Statements of Financial Position

December 31,
2008 *2007*
(in thousands)

Assets

Cash and cash equivalents	\$	4,566	\$	4,518
Investments, at fair value		339,432		474,095
Student loans receivable, net		27,904		36,066
Accrued investment income		540		589
Accrued student loan interest		273		394
Other assets		104		104
		<u> </u>		<u> </u>
Total assets	\$	<u>372,819</u>	\$	<u>515,766</u>

Liabilities and Net Assets

Accounts payable and accrued expenses	\$	549	\$	848
Grants payable		4,006		1,004
		<u> </u>		<u> </u>
Total liabilities		4,555		1,852
Net assets:				
Unrestricted net assets		<u>368,264</u>		<u>513,914</u>
Total liabilities and net assets	\$	<u>372,819</u>	\$	<u>515,766</u>

NELLIE MAE EDUCATION FOUNDATION, INC.

Statements of Activities and Changes in Net Assets

	<i>Years Ended December 31,</i>	
	<i>2008</i>	<i>2007</i>
	<i>(in thousands)</i>	
Revenues:		
Investment income, net	\$ 7,057	\$ 7,994
Net realized gains (losses)	(5,737)	22,997
Net unrealized gains (losses) on investments	(129,686)	6,967
Interest income on student loans	2,568	4,273
	<u> </u>	<u> </u>
Total revenues	(125,798)	42,231
Expenses:		
Grants awarded, net	14,735	10,810
Program support expenses	2,420	1,967
Administrative expenses	1,659	1,538
Depreciation and amortization	49	62
Student loan expenses:		
Loan servicing	329	346
Increase in uncollectible loans	660	118
	<u> </u>	<u> </u>
Total expenses	19,852	14,841
Increase (decrease) in net assets	(145,650)	27,390
Net assets, beginning	<u>513,914</u>	<u>486,524</u>
Net assets, ending	\$ <u>368,264</u>	\$ <u>513,914</u>

NELLIE MAE EDUCATION FOUNDATION, INC.

Statements of Cash Flows

Years Ended December 31,
2008 **2007**
(in thousands)

Cash flows from operating activities:

Increase (decrease) in unrestricted net assets	\$ (145,650)	\$ 27,390
Adjustments to reconcile increase (decrease) in net assets to net cash used in operating activities:		
Realized losses (gains)	5,737	(22,997)
Unrealized losses (gains) on investments	129,686	(6,967)
Interest on student loans added to principal	(88)	(180)
Depreciation and amortization	49	62
Amortization of student loan origination fees	31	31
Increase for uncollectible student loans	660	118
Changes in operating assets and liabilities:		
Accrued investment income	49	(285)
Accrued student loan interest	121	117
Accounts payable, accrued expenses and other	(349)	(83)
Grants payable	3,002	705

Net cash used in operating activities

	<u>(6,752)</u>	<u>(2,089)</u>
--	-----------------------	-----------------------

Cash flows from investing activities:

Principal collected on student loans	7,560	11,153
Purchase of equipment	-	(8)
Purchases of investments	(236,349)	(294,614)
Proceeds from sale of investments	235,589	286,946

Net cash provided by investing activities

	<u>6,800</u>	<u>3,477</u>
--	---------------------	---------------------

Net increase in cash and cash equivalents

	48	1,388
--	-----------	--------------

Cash and cash equivalents, beginning

	<u>4,518</u>	<u>3,130</u>
--	--------------	--------------

Cash and cash equivalents, ending

	<u>\$ 4,566</u>	<u>\$ 4,518</u>
--	------------------------	------------------------

NELLIE MAE EDUCATION FOUNDATION, INC.

Notes to Financial Statements (in thousands)

Note 1 - Nature of Operations and Summary of Significant Accounting Policies

Nellie Mae Education Foundation, Inc. (the “Foundation”) is a Massachusetts not-for-profit corporation. The mission of the Foundation is to stimulate transformative change of public education systems across New England by growing a greater variety of higher quality educational opportunities that enable all learners, especially and essentially underserved learners, to obtain the skills, knowledge and supports necessary to become civically engaged, economically self-sufficient life-long learners.

A summary of significant accounting policies consistently applied in the preparation of the financial statements follows:

Use of Estimates and Assumptions

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the 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 vary from those estimates and assumptions.

Financial Statement Presentation

The accompanying financial statements of the Foundation have been prepared on the accrual basis of accounting.

Net assets, revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions in accordance with not-for-profit accounting. Unrestricted net assets are those not subject to restrictions by donor or by law. Unrestricted net assets may be designated for specific purposes by action of the Board or may otherwise be limited by contractual agreements with outside parties. All net assets of the Foundation for the years ending December 31, 2008 and 2007 were unrestricted.

Grant Awards

Grant awards are expensed when the grant is awarded and all significant conditions are met.

Cash and Cash Equivalents

The Foundation considers cash equivalents to include highly liquid investments that have a maturity of ninety days or less when purchased. The Foundation utilizes an overnight sweep account with its depository which invests in US Treasury investments which are valued at cost, which approximates fair value. The Foundation has not experienced any losses in these accounts. The Foundation maintains its cash in non-interest bearing bank deposit accounts which are fully insured by the FDIC up to December 31, 2009.

NELLIE MAE EDUCATION FOUNDATION, INC.

Notes to Financial Statements *(in thousands)*

Note 1 - Nature of Operations and Summary of Significant Accounting Policies (Continued)

Investments

Investments are reported at estimated fair value. In September 2006, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards (“SFAS”) No. 157, “Fair Value Measurements.” This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Foundation adopted Fair Value Measurements (“FAS 157”) as of the beginning of 2008. FAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosure about fair value measurements. FAS 157 establishes a three-tier hierarchy to classify fair value measurements for disclosure purposes.

Fair Value Measurement is based on the lowest level of input that is significant to the fair value of the instrument. Investments are classified as follows:

- Level 1: Quoted prices in active markets for identical investments that the reporting entity has the ability to access at the measurement date. The types of financial instruments included in Level 1 are highly liquid investments with quoted prices.
- Level 2: Investments are valued using other significant observable inputs (e.g. quoted prices for similar investments, interest rates, yield curves, credit risk, etc.) or inputs that are derived from other observable market data. Inputs other than quoted prices in active markets are used to model fair value.
- Level 3: Investments are valued using significant unobservable inputs, including internal assumptions. Inputs are developed based on the best information available.

The investment portfolio includes marketable and nonmarketable securities. The values of publicly traded fixed income and equity securities are based upon quoted market prices. Securities and other vehicles for which there is no quotation available are valued using current estimates of fair value determined by management based on information obtained from the general partner or external investment manager for the respective funds.

The Foundation believes that the carrying amount of its nonmarketable investments is a reasonable estimate of fair value as of December 31, 2008 and 2007. Because these investments are not readily marketable, the estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market for the investments existed; such differences could be material. The Foundation may have exposure to derivative financial instruments through its investments in limited liability funds. Management believes that the risk associated with derivatives is not material to the Foundation at December 31, 2008 and 2007.

Investment securities are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is possible that changes in values of investment securities could occur in the near term and that such change could materially affect investment balances and activity included in the financial statements. Realized gains and losses are determined using the average cost basis. Purchases and sales of securities are accounted for using the trade date. Investment income is presented net of investment management and custodial fees.

NELLIE MAE EDUCATION FOUNDATION, INC.

Notes to Financial Statements *(in thousands)*

Note 1 - Nature of Operations and Summary of Significant Accounting Policies (Continued)

Student Loans

Student loans are presented at their estimated net realizable value including unpaid principal balances, capitalized interest receivable, loan loss allowance and unamortized premiums. Interest on student loans is recognized as it is earned. Additions to principal presented in the statement of cash flows represents interest earned on the student loans which has been capitalized as student loans receivable in accordance with the student loan agreements.

Student Loan Origination Costs

Loan origination costs are amortized over the expected life of the loan portfolio. Accumulated amortization at December 31, 2008 and 2007 was \$1,342 and \$1,310, respectively. Amortization expense is included as a reduction of interest income on student loans in the statement of activities and changes in net assets.

Student Loan Loss Allowance

The loan loss allowance is established to provide for potential student loan losses resulting from credit risk, origination error and defective servicing. The allowance is based on the type of loan made and expected loss rates. Management believes the allowance levels are adequate, but because of the inherent uncertainty of the assumptions and the estimation process, the allowance levels may differ significantly from actual losses and the differences could be material.

Fixed Assets

Fixed assets are recorded at cost less accumulated depreciation. Depreciation of business, equipment, furniture and fixtures, and software is computed on the straight-line method over the estimated useful life of each asset type, which ranges from five to seven years. Leasehold improvements are amortized over the term of the lease or useful life as described in the range above, whichever is shorter.

Income Taxes

The Foundation is organized and operated as an organization exempt from taxation under IRC Section 501(c)(3). It is not a private foundation because it is a supporting organization as described in IRC Section 509(a)(3).

Pursuant to its Articles of Organization, the Foundation operates exclusively for the benefit of, and to promote the charitable and education purposes of, educational organizations, including universities, colleges, secondary schools, elementary schools, and other educational organizations which are described in IRC Section 501(c)(3) and which are not private foundations as described in IRC Section 509(a). The Foundation's activities include making grants to the public charities it supports and providing services to those organizations. A majority of the Foundation's directors are representatives of organizations that would be eligible to receive support from the Foundation. In addition, the committee that nominates board members is composed entirely of directors who are also officers, directors, key employees or persons serving in a leadership role in public charities that would be eligible to receive support from the Foundation.

NELLIE MAE EDUCATION FOUNDATION, INC.

Notes to Financial Statements (in thousands)

Note 1 - Nature of Operations and Summary of Significant Accounting Policies (Continued)

Accounting for Uncertain Tax Positions

The uncertainties of any tax positions were accounted for under the guidance in SFAS No. 5, *Accounting for Contingencies*. Under this approach, disclosure is not required of a loss contingency involving an unasserted claim or assessment unless it is considered probable that a claim will be asserted and there is a reasonable possibility that the outcome will be unfavorable. In June 2006, the Financial Accounting Standards Board (FASB) released FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*—an interpretation of FASB Statement 109 (FIN 48). FIN 48 provides guidance for how uncertain tax positions should be recognized, measured, presented and disclosed in the financial statements. FIN 48 requires the evaluation of tax positions taken in the course of preparing the Foundation’s tax returns to determine whether tax positions are “more likely than not” of being sustained by the applicable tax authority. On December 30, 2008, the FASB Staff issued FASB Staff Position (FSP) FIN 48-3, *Effective Date of FASB Interpretation No. 48 for Certain Nonpublic Enterprises*, which defers the adoption of the provisions of FIN 48 for the Foundation until fiscal 2009. At this time, the Foundation’s management is evaluating the implications of FIN 48, however management does not believe this standard will have a material effect on its financial statements.

Note 2 - Investments

Investments consisted of the following as of December 31:

		<i>2008</i>		
	<i>Cost</i>	<i>Fair Value Level 1</i>	<i>Fair Value Level 3</i>	<i>Total Fair Value</i>
Cash equivalents	\$ 3,519	\$ 3,519	\$ -	\$ 3,519
Domestic equities and funds	149,503	97,892	21,044	118,936
Fixed income and funds	102,246	94,976	-	94,976
Alternative strategies	75,060	7,602	53,438	61,040
Foreign equities	81,454	60,961	-	60,961
	<u>\$ 411,782</u>	<u>\$ 264,950</u>	<u>\$ 74,482</u>	<u>\$ 339,432</u>

NELLIE MAE EDUCATION FOUNDATION, INC.

Notes to Financial Statements
(in thousands)

Note 2 - Investments (Continued)

	<i>Cost</i>	<i>2007</i> <i>Fair Value</i>
Cash equivalents	\$ 2,387	\$ 2,387
Domestic equities and funds	157,704	188,663
Fixed income and funds	97,607	98,617
Alternative strategies	64,331	73,487
Foreign equities	80,731	96,941
Trades pending settlement	<u>14,000</u>	<u>14,000</u>
	<u>\$ 416,760</u>	<u>\$ 474,095</u>

Investment activity was as follows for the years ended December 31:

	<i>2008</i>	<i>2007</i>
Investments, at beginning of year	\$ <u>474,095</u>	\$ <u>436,462</u>
Investment return:		
Interest and dividends collected	8,552	8,748
Net unrealized gains (losses)	(129,686)	6,967
Net realized gains (losses)	<u>(5,737)</u>	<u>22,997</u>
Reinvested income and gains (losses)	<u>(126,871)</u>	<u>38,712</u>
Transfer to operations	<u>(6,415)</u>	<u>-</u>
Management fees and other deductions	<u>(1,377)</u>	<u>(1,079)</u>
Investments	<u>\$ 339,432</u>	<u>\$ 474,095</u>

Alternative strategies include investments in hedge funds and in limited liability partnerships. Unfunded commitments related to these investments were approximately \$11.72 and \$7.35 million at December 31, 2008 and 2007, respectively.

Under Nellie Mae's policy, the annual distribution for grants and support of operations will fall between 4.0% and 4.5% of a 12 quarter trailing net asset average. The grant distribution level will not fall below the three-year trailing average of 85% of net income. Net income includes the sum of interest income, net student loan income, dividend income and short-term capital gains. Cash flows from student loan collections and interest earned along with the transfer of \$6.4 million of investment funds allowed for the distribution in 2008, while in 2007 distributions were funded without a withdrawal from invested funds.

NELLIE MAE EDUCATION FOUNDATION, INC.

Notes to Financial Statements (in thousands)

Note 2 - Investments (Continued)

The categorization of an investment within the hierarchy (Level 3) is based upon the pricing transparency of the investment and does not necessarily correspond to the Foundation's perceived risk of that investment. Certain investments, including alternative strategy investments and one equity manager, have been classified within Level 3 as they have unobservable inputs and they trade anonymously, infrequently or not at all. The table below presents reconciliation for all assets measured at fair value using significant unobservable inputs (Level 3).

Level 3 investment activity was as follows for the years ended December 31:

	<i>2008</i>	<i>2007</i>
Level 3		
Investments, at beginning of year	\$ <u>98,542</u>	\$ <u>56,559</u>
Investment return:		
Interest and dividends collected	6	-
Net unrealized gains (losses)	(27,597)	7,033
Net realized gains	<u>5,243</u>	<u>-</u>
Reinvested income and gains (losses)	<u>(22,348)</u>	<u>7,033</u>
Purchases/sales (net)	<u>(1,705)</u>	<u>34,950</u>
Management fees and other deductions	<u>(7)</u>	<u>-</u>
Investments	<u>\$ 74,482</u>	<u>\$ 98,542</u>

Note 3 - Student Loans

The Foundation had a student loan portfolio of approximately \$28 and \$36 million at December 31, 2008 and 2007, respectively. Prior to April 7, 2008, approximately one half of the portfolio was guaranteed by The Education Resources Institute, Inc. ("TERI"). Under the guarantee, TERI was obligated to pay claims on any defaulted, TERI guaranteed loans in excess of a deductible assuming compliance with certain loan origination, due diligence and loan service procedures as stipulated by TERI.

On April 7, 2008, TERI filed a voluntary petition for relief (TERI Reorganization) under Chapter 11 of the United States Bankruptcy Code (Bankruptcy Code) in the United States Bankruptcy Court for the District of Massachusetts (Bankruptcy Court). According to the filing, TERI intends to operate its business as "debtor-in-possession" under the jurisdiction of the Bankruptcy Court and in accordance with the applicable provisions of the Bankruptcy Code and orders of the Bankruptcy Court.

The Foundation outsources certain aspects of the servicing of the loans to SLM Corporation ("Sallie Mae"). Sallie Mae is liable for certain losses incurred by the Foundation due to servicing errors. Service fees to Sallie Mae approximated \$278 and \$292 during 2008 and 2007, respectively, including accrued services fees of approximately \$16 and \$23 at December 31, 2008 and 2007, respectively. These expenses are included in the caption loan servicing on the statement of activities and changes in net assets.

NELLIE MAE EDUCATION FOUNDATION, INC.

Notes to Financial Statements
(in thousands)

Note 3 - Student Loans (Continued)

Loan Loss Allowance

The Foundation has established an allowance to cover estimated losses on loans. This allowance for uncollectible student loans is netted against student loans on the statement of financial position and is summarized as follows:

	<i>2008</i>	<i>2007</i>
Balance at beginning of year	\$ 492	\$ 614
Additions:		
Increase in uncollectible student loans	660	118
Recoveries	337	500
Funds from recourse agreements	(3)	5
Deductions:		
Loan write-offs	(312)	(745)
Total	\$ <u>1,174</u>	\$ <u>492</u>

Note 4 - Other Assets

Other assets consist primarily of fixed assets and prepaid expenses.

Fixed assets consisted of the following at December 31:

	<i>2008</i>	<i>2007</i>
Business equipment and software	\$ 151	\$ 151
Furniture and fixtures	384	384
Leasehold improvements	39	39
	<u>574</u>	<u>574</u>
Less accumulated depreciation and amortization	(568)	(519)
Total	\$ <u>6</u>	\$ <u>55</u>

Depreciation expense totaled approximately \$49 and \$62 for the years ended December 31, 2008 and 2007, respectively.

NELLIE MAE EDUCATION FOUNDATION, INC.

Notes to Financial Statements *(in thousands)*

Note 5 - Commitments

Grants

The Foundation from time to time makes grants to certain organizations that will be paid in the future. Grant payments that are expected to be made beyond the next year have been recorded at their net present value. All grants payable as of December 31, 2008 and 2007 were scheduled for payment within the next fiscal year.

Office Lease

The Foundation leases office space under an operating lease and on October 10, 2008 signed a ten-year “First Amendment” to the lease, with rental rates to be effective January 1, 2009. The lease payments are subject to annual escalations for increase in real estate taxes and operating expenses. Total rent expense amounts to approximately \$226 and \$283 for the years ended December 31, 2008 and 2007, respectively. Future minimum rental commitments under the lease are as follows:

2009	\$	264
2010		270
2011		276
2012		282
2013		289
Thereafter		1,565
	\$	<u>2,946</u>

Note 6 - Retirement Plans

The Foundation operates a pension plan and a 401(k) savings plan (the “Plans”) for its employees. The Plans are defined contribution plans and are designed to be qualified plans under the Internal Revenue Code. Employees are eligible to participate in the plans upon meeting criteria of age, service and, in the case of the pension plan, minimum hours of work, among other criteria. The Plans vest over a five year period. Substantially all employees are eligible to participate in these Plans. The pension plan provides for a contribution of eight percent (8%) of eligible wages plus additional amounts under certain circumstances, while the 401(k) plan provides for a 100% matching contribution up to six percent (6%) of eligible wages. The Foundation’s policy is to fund all costs on a current basis. Expenses incurred related to the Plans for the years ended December 31, 2008 and 2007 were \$197 and \$174, respectively.