SOUTH TEXAS HIGHER EDUCATION AUTHORITY, INC.

Report of Independent Auditor and
Basic Financial Statements with
Accompanying Information

As of November 30, 2017

PMB Helin Donovan

SOUTH TEXAS HIGHER EDUCATION AUTHORITY, INC.
Basic Financial Statements with Accompanying Information

Table of Contents

PMB Helin Donovan

14090 SW Freeway
Suite 300
Sugar Land, TX 77478
pmbhd.com

T 832.301.3000
F 832.301.3010

Report of Independent Auditor

To the Board of Directors
South Texas Higher Education Authority, Inc.

Report on the Financial Statements

We have audited the accompanying financial statements of South Texas Higher Education Authority, Inc. as of and for the year ended November 30, 2017, and the related notes to the financial statements, which collectively comprise South Texas Higher Education Authority, Inc.'s statement of net position as of November 30, 2017, and the statement of revenues, expenses, and changes in net position, and statement of cash flows for the year then ended.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America 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 auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of South Texas Higher Education Authority, Inc. as of November 30, 2017, and the changes in its financial position and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

In February 2018, South Texas Higher Education Authority Inc, transferred substantially all of its remaining portfolio of investments in student loans as well as related bonds making up the 2012-1 and 2013-1 bond trusts. The Board of Directors is currently considering the use of its remaining net assets for charitable purposes in the future.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3-6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise South Texas Higher Education Authority, Inc.'s basic financial statements. The combining fund supplemental schedules on pages 19-21 are presented for purposes of additional analysis and are not a required part of the basic financial statements. The supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combining fund supplemental schedules are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated May 15, 2018 on our consideration of the 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 the 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 the Project's internal control over financial reporting and compliance.

PMB HELIN DONOVAN, LLP

PMB Helin Donovan, LLP

May 15, 2018

This section of the South Texas Higher Education Authority, Inc.'s (the "Authority") basic financial statements with accompanying information presents management's discussion and analysis of the Authority's financial performance during the year ended November 30, 2017. This section of the report should be read in conjunction with the basic financial statements.

FINANCIAL HIGHLIGHTS

- The Authority's total net position increased $754.7 thousand or 2% over the prior year period ending November 30, 2016. The principal balance outstanding on the Authority's student loan portfolio was approximately $209.9 million at November 30, 2017, compared to $235.2 million at November 30, 2016.
- Claims receivable (a part of student loans receivable), which are reinsured by the U.S. Department of Education (DOE), decreased by 62.33% to $526.6 thousand at November 30, 2017, with a 4.53% average claim paid rate.
- The Authority's total operating revenue decreased by $1.02 million, or a decrease of 8%, over the prior year ending November 30, 2016.
- The Authority's operating expenses decreased by $397.7 thousand, or a decrease of 4%, over the prior year ending November 30, 2016.

OVERVIEW OF THE FINANCIAL STATEMENTS

The Authority is considered a governmental affiliate for accounting, financial reporting, and auditing purposes. Organizations are classified as governmental if officials of one or more state or local governments appoint or approve the controlling majority of the organization's governing body and have the ability to directly issue tax-exempt debt. The Authority exercises powers enumerated in Section 53.47 of the Texas Education Code for and on behalf of the City of Edinburg. These powers include the issuance of tax-exempt revenue bonds to purchase or make student loans. The City of Edinburg's governing body appoints directors to fill vacancies on the board of directors of the Authority from nominations made by the remaining members of the board.

As a special purpose governmental organization engaged in business type activities, the basic financial statements of the Authority are presented similarly to an enterprise fund as defined by the Governmental Accounting Standards Board. Enterprise funds are accounted for using the flow of economic resources measurement focus and accrual basis of accounting. Accordingly, revenues are recognized when earned and expenses are recognized when the liability is incurred regardless of the timing of the related cash flow.

This report consists of three parts - *management's discussion and analysis* (this section), *basic financial statements*, and *notes to financial statements.*

The basic financial statements include:

- Statement of Net Position includes all of the Authority's assets, deferrals, and liabilities. The difference between the Authority's assets, deferrals, and liabilities is its net position. Net position is presented in two components – restricted and unrestricted.
- Statement of Revenues, Expenses and Changes in Net Position report all of the Authority's revenues and expenses. The statement measures the results of the Authority's operations.

- The Statement of Cash Flows supplements the Statement of Net Position and Statement of Revenues, Expenses and Changes in Net Position by providing relevant information about cash receipts and payments of the Authority.
- The Notes to the Financial Statements present information essential for the fair presentation of the financial statements that is not displayed on the face of the financial statements. The notes are an integral part of the basic financial statements.

FINANCIAL ANALYSIS OF THE AUTHORITY

The Authority's total net position increased $754.8 thousand or 2% to $44.5 million from the prior year period ending November 30, 2016, primarily due to an improved mix of student loan notes which resulted in a higher overall yield and reduced operating expenses. Restricted net position increased by 4% to $27.9 million while unrestricted net position decreased by -2% to $16.6 million. As of November 30, 2017, the Authority continues to have a strong current ratio of current assets over current liabilities.

Table A-1
Net Position

Description	2017	2016	Change	Percentage Change
Current assets	$ 53,067,190	$ 59,594,677	$ (6,527,487)	-11%
Noncurrent assets and deferrals	180,473,626	201,045,102	(20,571,476)	-10%
Total assets	233,540,816	260,639,779	(27,098,963)	-10%
Current liabilities	1,209,949	1,283,365	(73,416)	-6%
Noncurrent liabilities and deferrals	188,573,612	215,638,444	(27,064,832)	-13%
Total liabilities and deferrals	189,783,561	216,921,809	(27,138,248)	-13%
Net Position				
Restricted	27,916,369	26,823,850	1,092,519	4%
Unrestricted	16,556,361	16,894,120	(337,759)	-2%
Total net position	$ 44,472,730	$ 43,717,970	$ 754,760	2%

The Authority's operating revenues decreased by 8% to $11.10 million primarily due to a decrease in the principal outstanding on student loans which decreased 11% from the prior year ending November 30, 2016. Approximately 99.7% of the Authority's operating revenue generated is interest from its student loan portfolio. The Authority's investment income increased by $47.1 thousand or 129% from the prior year ending November 30, 2016, primarily due to higher yield on investments resulting from improved market conditions.

Table A-2
Changes in Net Assets

Description	2017	2016	Change	Percentage Change
Operating revenues:				
Student loan operations	$ 10,998,505	$ 12,080,073	$ (1,081,567)	-9%
Investment Income	83,762	36,633	47,129	129%
Other	9,616	12	9,604	N/A
Total operating revenues	11,091,883	12,116,718	(1,024,834)	-8%
Operating expenses:				
Student loan operations	6,454,646	7,517,968	(1,063,322)	-14%
Bond interest expense	3,829,543	3,123,506	706,037	23%
Other expense	52,934	93,369	(40,435)	-43%
Total operating expenses	10,337,123	10,734,843	(397,720)	-4%
Changes in net position	754,760	1,381,875	(627,115)	-45%
Net position at beginning of year	43,717,972	42,336,097	1,381,875	3%
Net position at end of the year	$ 44,472,730	$ 43,717,972	$ 754,760	2%

The Authority's student loan operating expenses decreased $397.7 thousand from the prior year ending November 30, 2016. Excess interest recapture arises when the calculated special allowance rate is lower than the interest rate on the loan and the difference becomes the recapture of interest by the U.S. Department of Education (DOE). The cost of student loan operations, which includes headquarters and administrative fees and loan servicing and collection fees, decreased 11% from $2.2 million to $1.9 million.

The Authority's 2012-1 and 2013-1 Series bonds are floating rate notes tied to LIBOR plus 50 to 85 and 60 basis points, respectively. The increase in bond interest expense of $706 thousand, or an increase of 22.60%, from the prior year is primarily due to an increase in the bond interest rate. The Authority is currently paying 1.84% to 2.18% on its bonds as of November 30, 2017 compared to 1.13% to 1.69% from prior year ending November 30, 2016.

Currently, the Authority has no rebate liability or excess interest liability. Management does not anticipate the Authority incurring excess interest in the near term because the Authority has no tax-exempt bonds outstanding. Excess interest is defined as the amount by which the yield on for-purpose investment, such as student loans, made with the proceeds of tax-exempt bonds is in excess of allowable yields. Such excess interest must be distributed upon the maturity of the bond series through forgiveness of student loan notes or rebated to the U.S. Treasury. When necessary, a third party calculates the amount of excess interest and rebatable arbitrage payable and the resulting expense annually.

LONG-TERM DEBT ACTIVITY

The principal funding need for the Authority is securing capital to finance the purchase or acquisition of student loans. The Authority has used a number of sources to raise this capital including access to bond markets and arrangements with banks. Although the Authority's ability to raise tax-exempt debt is limited under Texas legislation to approximately $28 million a year, the Authority has the ability to raise capital through taxable revenue bonds. Due to the elimination of the Federal Family Education Loan (FFEL) program, the Authority has had no need for seeking additional capital. See Notes 6 and 7 to the financial statements for more detailed information about the Authority's long-term liabilities.

The following table shows the Authority's outstanding long-term debt balance of $188.57 million as of November 30, 2017:

Table A-5
Long-Term Debt (in 000,000's)
Balances as of November 30,

Description	Stated Maturity	Type	Rate	Original Amount	2017	2016	Percent Change
2012-1 A-1 Series	October 2020	Taxable	Variable	$ 129.40	$ -	$ 4.47	-100%
2012-1 A-2 Series	October 2024	Taxable	Variable	64.73	50.22	64.73	-22%
2012-1 A-3 Series	October 2045	Taxable	Variable	81.82	81.82	81.82	0%
2013-1 Series	December 2029	Taxable	Variable	104.30	56.53	65.47	-14%
				$ 380.25	$ 188.57	$ 216.49	-13%

CURRENTLY KNOWN FACTS, DECISIONS, OR CONDITIONS

Management conducts frequent environmental scans and is closely monitoring changing regulatory rules, audits, sanctions and legislative language as conducted and/or introduced by the Consumer Finance Protection Bureau, Internal Revenue Service, Congress and the Department of Education (DOE). Consumer friendly regulations and FFEL program portfolio decreases are creating audit, security and system risks as well as servicing inefficiencies both for the servicer and on the Authority's portfolio.

STHEA's Credit Rating Agency released on January 26, 2017 and November 20, 2017 for Series 2013-1 and Series 2012-1, respectively, a statement that each bond series rating outlook remained stable. Both bond series are categorized as "AAAsf". Subsequent to year end, STHEA sold the investment portfolio. The Board of Director is considering future use of the funds.

CONTACTING THE AUTHORITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our customers, business partners and creditors with a general overview of the Authority's finances. If you have questions about this report or need additional financial information, please contact the Authority's Assistant Treasurer at 200 South 10th Street, Suite 502, McAllen, Texas 78501 or call (956) 682-6371.

SOUTH TEXAS HIGHER EDUCATION AUTHORITY, INC.
Statement of Net Position
November 30, 2017

Assets	
Current assets:	
Cash and cash equivalents	$ 16,959,918
Student loan interest receivable	6,423,820
Student loan notes receivable, current portion, net of allowance	29,146,628
Due from servicing agent	523,988
Other current assets	12,836
Total current assets	53,067,190
Noncurrent assets:	
Student loan notes receivable, net of current portion and allowance	180,440,028
Other assets	33,598
Total noncurrent assets	180,473,626
Total assets	233,540,816
Liabilities	
Current liabilities:	
Accrued interest payable	567,619
Special allowance payable	221,102
Accounts payable	415,228
Total current liabilities	1,203,949
Noncurrent liabilities:	
Bonds payable	188,573,612
Total noncurrent liabilities	188,573,612
Total liabilities	189,777,561
Deferred Inflows of Resources	
Deferred debit on refunding	(709,475)
Total liabilities and deferrals	189,068,086
Net position	
Restricted for debt service	27,916,369
Unrestricted	16,556,361
Total net position	$ 44,472,730

See accompanying notes and report of independent auditor.

SOUTH TEXAS HIGHER EDUCATION AUTHORITY, INC.

Statement of Revenues, Expenses, and Changes in Net Position

Year Ended November 30, 2017

Operating revenues:	
Interest on student loan notes	$ 10,998,505
Investment income	93,378
Total operating revenues	11,091,883
Operating expenses:	
Headquarters and administrative fees	936,638
Loan servicing and collection fees	1,026,132
Trustee fees	40,340
Professional fees	550,818
Provision for uncollectible receivables	282,051
Consolidation rebate fees	1,511,040
Directors and officers insurance	7,908
Special allowance payments	1,959,594
Bond interest expense	3,829,543
Other	193,059
Total operating expenses	10,337,123
Change in net position	754,760
Net position at beginning of year	43,717,970
Net position at end of year	$ 44,472,730

See accompanying notes and report of independent auditor.

SOUTH TEXAS HIGHER EDUCATION AUTHORITY, INC.
Statement of Cash Flows
Year Ended November 30, 2017

Cash flows from operating activities	
Receipt of student loan interest	$ 12,614,635
Payments for special allowance	(2,189,134)
Collection of principal on student loans	32,659,504
Claim repurchases, write offs, and capitalized interest	(7,442,330)
Receipt of investment income	84,754
Payment of bond interest	(3,740,820)
Payments to suppliers	(4,179,759)
Net cash provided by operating activities	27,806,850
Cash flows from noncapital financing activities	
Payment on bonds payable, net	(27,914,430)
Net cash used in noncapital financing activities	(27,914,430)
Cash flows from investing activities	-
Net decrease in cash and cash equivalents	(107,580)
Cash and cash equivalents at beginning of year	17,067,498
Cash and cash equivalents at end of year	$ 16,959,918
Reconciliation of change in net position to net cash provided by operating activities:	
Change in net position	$ 754,760
Adjustments to reconcile change in net position to net cash provided by operating activities:	
Provision for uncollectible receivables	282,051
Amortized gains (losses) on bonds issued	140,122
Changes in assets and liabilities:	
Decrease (increase) in student loan interest receivable	1,616,130
Decrease (increase) in student loan notes receivable	24,995,741
Decrease (increase) in due from servicing agents	101,858
Decrease (increase) in other assets	(4,395)
Increase (decrease) in accrued interest payable	88,723
Increase (decrease) in special allowance payable	(229,540)
Increase (decrease) in accounts payable	61,400
Net cash provided by operating activities	$ 27,806,850

See accompanying notes and report of independent auditor.

(1) Reporting Entity and Summary of Significant Accounting Policies

Reporting Entity

The South Texas Higher Education Authority, Inc. (the Authority) is a Texas not-for-profit corporation incorporated under the laws of the State of Texas at the request of the City of Edinburg, Texas in July 1973 for the purpose of providing funds for the acquisition and servicing of guaranteed student loans, which are insured by the U.S. Government, Texas Guaranteed Student Loan Corporation or other national guarantors under the FFEL program as provided for in the Higher Education Authority Act of 1965, as amended. To maintain such insurance and guarantee of student loans, the Authority must comply with servicing, collecting, accounting, and reporting requirements of the FFEL program.

The Authority exercises powers enumerated in Section 53.47 of the Texas Education Code for and on behalf of the City of Edinburg. These powers include the issuance of tax-exempt revenue bonds to purchase or make student loans. The City of Edinburg's governing body appoints directors to fill vacancies on the board of directors of the Authority from nominations made by the remaining members of the board.

Through the year ended November 30, 2017, the Authority had an agreement with the Council for South Texas Economic Progress (COSTEP) whereby COSTEP provides the Authority with facilities and administrative support and the servicing of its student loan portfolio. COSTEP further sub-contracts with Panhandle-Plains Management and Servicing Corporation (PPMSC) to provide due diligence, collecting, and reporting functions to maintain compliance with the requirements of FFEL program. The agreements, in general, provide for a fee, subject to annual predetermination, and additional payments based upon the number of loans and services performed related to such loans and for other payments as approved by the Authority. As further discussed in Note 10, this agreement was terminated in February 2018, upon the sale and transfer of the Authority's student loan portfolio.

Summary of Significant Accounting Policies

(a) Basis of Accounting

The Authority meets the definition of a governmental entity as set forth in the AICPA Audit and Accounting Guide, *Audits of State and Local Governmental Units*. As a special purpose governmental entity engaged in business type activities, the financial statements of the Authority are prepared similarly to an enterprise fund as defined by the Governmental Accounting Standards Board (GASB).

Enterprise funds are used to account for operations that are financed and operated in a manner similar to private business enterprises and are accounted for on the flow of economic resources measurement focus and use the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

(b) Cash and Cash Equivalents

For purposes of the Statement of Cash Flows, the Authority considers money market accounts, certificates of deposit, and other investments with original purchase maturities of three months or less from the date of acquisition to be cash equivalents.

(c) Allowance for Losses

Student loan notes receivable are stated net of an allowance for losses. A calculation is made to determine STHEA's exposure on current claims, uninsured loans, and future defaulted loans by using the average of the actual claims paid for the past three years. As of November 30, 2017, the allowance for losses was $351,238.

(d) Investments

The Authority invests funds not invested in student loans in accordance with its investment policy, bond indentures, and the Texas Public Funds Investment Act. Investments are carried at fair value. Fair value is defined as the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The fair value is determined typically by quoted market prices.

(e) Income Taxes

The Authority is a not-for-profit corporation, which is exempt from federal income taxes under the provisions of Section 501(c)(3) of the Internal Revenue Code. As a qualified political subdivision, the Authority is further exempt from filing state and federal tax returns. As such, no provision for federal or state income taxes has been made in the accompanying financial statements.

(f) Restricted Assets

A substantial portion of the Authority's assets are restricted by virtue of bond indenture provisions (see Note 3).

(g) Deferred Debits on Refunding

When advance refundings resulting in defeasance of bonds occur, the difference between the reacquisition price (i.e. principal, call premium, miscellaneous costs of reacquisition, etc.) and the net carrying amount of the old debt is deferred and amortized as a component of interest expense in a systematic and rational manner over the remaining life of the old debt or the life of the new debt, whichever is shorter. The Authority elected to amortize these costs under the straight-line method which approximates the effective interest method. The bond interest rate conversion costs are recorded as deferred debits on refundings.

(h) Use of Estimates

Management of the Authority has made estimates and assumptions relating to reporting of assets, liabilities, revenues, expenses, and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with generally accepted accounting principles. The most significant estimates include accrued interest and the allowances for losses on student loans. Actual results could differ from those estimates.

(i) Classification of Operating and Non-operating Revenue and Expenses

The Authority defines operating revenues and expenses as those revenues and expenses generated by a specified program offering either a good or service. Operating revenues include interest on student loan notes receivable, investment income, and other revenues related to student loan operations. Operating expenses include contractual services, special allowance payments, other expenses (such as insurance and loan consolidation costs), bond interest expense, and amortization of deferred debit on refunding.

(j) Recently Issued Accounting Pronouncements

GASB Summary of Statement No.86 was issued in May 2017 and addresses accounting and financial reporting issues related to extinguishment of debt. This statement provides guidance for transactions in which cash and other monetary assets, acquired with only existing resources, are placed in an irrevocable trust for the sole purpose of extinguishing debt. The requirements of this statement are effective for financial statements for periods beginning after June 15, 2017. The Authority is currently evaluating the effects of that the adoption of this standard will have on its financial position, results of operations, or cash flows.

GASB Summary of Statement No.87 was issued in June 2017 and addresses accounting and financial reporting issues related to leases. Under the new standard, leases are all assumed to be capital financings of the underlying assets with only a narrow range of short-term equipment and motor vehicle leases treated as operating leases. The new standard will require recognition of assets and liabilities for all leases whether or not they previously were accounted for as an operating or capital lease. The requirements of this statement are effective for financial statements for periods beginning after December 15, 2019. The Authority is currently evaluating the effects of that the adoption of this standard will have on its financial position, results of operations, or cash flows.

(2) Cash and Cash Equivalents

The composition of the Authority's cash and cash equivalents as of November 30, 2017 is as follows:

Cash in depository institutions	$ 5,336,012
Certificate of deposit	4,000,000
Money market mutual funds	7,623,906
Total cash and cash equivalents	$ 16,959,918

Credit Risk
The Authority is allowed to invest available funds in specified municipal obligations, U.S. government and certain other U.S. governmental agency obligations, SEC registered money market mutual funds, certain types of repurchase agreements, commercial paper, banker acceptances, and interest-bearing time deposits of one of more banks located within the U.S. in accordance with laws governing the Authority's charter and as further restricted by the bond indentures, Public Funds Investment Act, and other financing agreements.

Custodial Credit Risk
The Authority maintains cash in banks that are insured by the Federal Deposit Insurance Corporation (FDIC). At various times throughout the year ended November 30, 2017, cash and cash equivalents on deposit may have exceeded federally insured limits; however, the Authority requires said banks to pledge collateral, in an amount that equals at least 102% of uninsured deposits in order to comply with the Public Funds Investment Act (PFIA). As of November 30, 2017, a Line of Credit from the Federal Home Loan Bank Atlanta was issued to collateralize deposits in accordance with the Authority's investment and collaterization policy.

Interest rate risk
In accordance with the Authority's investment and collaterization policy, the Authority's investment maturities are staggered and the average maturity of investments shall not exceed two years. The maximum stated maturity of any one investment shall not exceed five years.

(3) Restricted Assets

The Authority maintains a general fund, which at November 30, 2017 had a net position of $16.6 million, which is not restricted by bond indenture provisions. The Authority had a restricted net position of $27.9 million as of November 30, 2017, which represents the net position that is subject to bond indenture provisions.

A summary of unrestricted assets and liabilities as of November 30, 2017 is as follows:

Cash and cash equivalents	$ 9,852,236
Student loan interest receivable	242,099
Student loan notes receivable	6,583,055
Due from servicing agent	6,039
Other assets	15,523
Special allowance payable	(26,157)
Accounts payable	(116,434)
Net position – unrestricted	$ 16,556,361

(4) Fair Value

The Authority categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

The Authority has the following recurring fair value measurements as of November 30, 2017 and 2016:

Money market funds – Valued at cost plus accrued interest, which approximates fair value.
Certificate of deposit – Valued at amortized cost, which approximates fair value.

The following table presents assets that are measured at fair value on a recurring basis by level within the fair value hierarchy. Financial assets are classified in their entirety based on the lowest level of input that is significant to the fair value measurements. The following investments are included in cash and cash equivalents on the Statement of Net Position at November 30, 2017.

		Fair Value Measurements at Reporting Date Using:		
	Total November 30, 2017	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Investments, at fair value:				
Money market funds	$ 7,626,310	$ 7,626,310	$ -	$ -
Certificate of deposit	4,000,000	-	4,000,000	-
Total investments, at fair value	$ 11,626,310	$ 7,626,310	$ 4,000,000	$ -

(5) Student Loan Notes Receivable

The student loan notes receivable are recorded at amortized cost and represent loans to students and parents of students. When the loans were originated, the students were enrolled in eligible educational institutions. In general, the notes bear interest at rates ranging from 1.75% to 12% and are payable by the borrower following a specified grace period. The terms of the loans, which vary on an individual basis, generally provide for repayment in monthly installments of principal and interest.

The U.S. government pays the Authority the interest on student loans from the date of acquisition until the end of a specified grace period. In addition, for certain eligible loans, a special allowance is paid at the end of each quarter which represents supplemental interest on outstanding insured or guaranteed loans. The special allowance is calculated using an annual rate which is determined quarterly and is based on the average interest rate for 91-day U.S. Treasury Bills, 1 month LIBOR, or 3-month commercial paper rate for the quarter plus a factor determined by the loan status and when the loan was originated less the current loan rate. Additionally, all holders of consolidation loans are required to pay to the Education Department (ED) an annual 105 basis point consolidation loan rebate fee on all outstanding principal and accrued interest balances of consolidation loans purchased or originated after October 1, 1993, except for loans for which consolidation applications were received between October 1, 1998 and January 31, 1999, where the consolidation loan rebate fee is 62 basis points.

The net investment in student loan notes receivable was as follows as of November 30, 2017:

	2012-1 Series	2013-1 Series	General Fund	Total
Student loan notes receivable	$ 142,115,038	$ 60,677,976	$ 6,618,278	$ 209,411,292
Claims receivable	402,731	123,871	-	526,602
Allowance for losses	(221,615)	(94,400)	(35,223)	(351,238)
Student loan notes receivable, net	$ 142,296,154	$ 60,707,447	$ 6,583,055	$ 209,586,656

A summary of changes in student loan notes receivable for the year ended November 30, 2017 is as follows:

Student loan notes receivable - December 1, 2016	$	234,864,448
Claims, repurchases and writeoffs		946,276
Accrued interest added to principal		6,496,056
Collections		(32,659,504)
Less: FY2017 allowances for losses, net of recoveries		(60,620)
Student loan notes receivable - November 30, 2017		209,586,656
Less current portion		29,146,628
Student loan notes receivable, less current portion, net - November 30, 2017	$	180,440,028

Student loan notes purchased by the Authority have been either insured or guaranteed by the U.S. Government, Texas Guaranteed Student Loan Corporation or other national guarantors, provided that the original lender and prior servicer have met applicable program requirements with respect to such loans. The original lenders have warranted to the Authority that the student loans have met these requirements and are valid obligations of the borrowers. Student loan notes acquired by the Authority which do not conform to the terms of the purchase agreement between the Authority and the original lender may be returned to the lending institution for reimbursement of principal, interest, and costs incurred.

In circumstances where the applicable program requirements referred to above have not been met as a result of servicing deficiencies by the servicing agent, a student loan note may become uninsured or lose its guarantee. In addition, the Authority owns student loan notes which have been discharged by bankruptcy court and are not eligible for guarantee reimbursement.

An allowance has been established for student loan notes which have become uninsured for other various reasons. In addition, the allowance includes an estimated loss on claims as a component of the allowance for uncollectible student loan notes.

The following represents the components of the allowance for loan losses and interest at November 30, 2017:

Allowance for student loan notes receivable	$ 284,399
Allowance for uninsured loans	29,388
Allowance for claims receivable	37,451
Total reserve for losses on notes	$ 351,238

The following represents the changes to the allowance for loan losses and interest for the year ended November 30, 2017:

Allowance for student loan notes receivable, December 1, 2016	$ 290,618
Increase in allowance	282,051
Write-off of student loan notes	(221,431)
Allowance for student loan notes receivable, November 30, 2017	$ 351,238

(6) Change in Long-Term Liabilities

The following is a summary of changes in long-term liabilities for the year ended November 30, 2017:

	Bonds Payable	Net Deferred Debit On Refunding	Total
Balance at November 30, 2016	$ 216,488,043	$ (849,597)	$ 215,638,446
Amortization	-	140,122	140,122
Proceeds and additions	-	-	-
Payments	(27,914,431)	-	(27,914,431)
Classified as current	-	-	-
Balance at November 30, 2017	$ 188,573,612	$ (709,475)	$ 187,864,137

(7) Bonds Payable

The Authority issues revenue bonds to finance the purchase or acquisition of student loans. At November 30, 2017, the Authority had two bond issues outstanding: Series 2012-1 and Series 2013-1.

On January 26, 2012, the Authority issued Student Loan Backed Bonds, Series 2012-1 (Taxable LIBOR Floating Rate Bonds) at an aggregate par value of $276 million.

The Authority issued $129,450,000 of its Student Loan Backed Bonds, 2012-1 Series Class A-1, $64,730,000 of its Student Loan Backed Bonds, 2012-1 Series Class A-2, and $81,820,000 of its Student Loan Backed Bonds 2012-1 Series Class A-3.

The 2012-1 Series Bonds bear interest at the following rates: the Class A-1 Bonds bear interest at an annual rate equal to three-month LIBOR plus 0.50%; the Class A-2 Bonds bear interest at annual rate equal to three-month LIBOR, plus 0.85%; and the Class A-3 Bonds bear interest at annual rate equal to three-month LIBOR plus 0.85%. The initial interest accrual period for the 2012-1 Series Bonds began on the date of issuance and ended on April 1, 2012, and thereafter, the period of interest accrual continues on a quarterly basis. At November 30, 2017, the weighted average auction rate for the 2012-1 Series Bonds was 2.002%. The 2012-1 Series Bonds are subject to redemption prior to their stated maturities, as defined by the indenture.

On June 1, 2013, the Authority issued Student Loan Backed Bonds, Series 2013-1 (Taxable LIBOR Floating Rate Bonds) at an aggregate par value of $104.3 million. The 2013-1 Series Bonds bear interest at an annual rate equal to one-month LIBOR plus 0.60% after the first interest accrual period. The initial interest accrual period for the 2013-1 Series Bonds began on the date of issuance and ended on September 2, 2013, and thereafter, the period of interest accrual continues on a monthly basis. At November 30, 2017, the weighted average auction rate for the 2013-1 Series Bonds was 1.611%. The 2013-1 Series Bonds are subject to redemption prior to their stated maturities, as defined by the indenture.

The Series 2012-1 Bonds and Series 2013-1 Bonds fully refunded Series 2007 Taxable and Tax-Exempt Bonds. The Series 2013-1 Bonds were tendered at 99.028% incurring a total discount of $1 million, which is being amortized over the life of the 2013-1 bonds.

Under the 2012-1 and 2013-1 bond indentures, cash and cash equivalents held by the Authority in the amount of $7.1 million are pledged for the benefit of the applicable Senior and Subordinate bondholders as of November 30, 2017. There is approximately $9.8 million of unrestricted cash and cash equivalents in the general loan fund accounts as of November 30, 2017, for the Authority's use.

Subsequent to year end, the Authority transferred the Series 2012-1 and Series 2013-1 bonds. See Note 10 for further discussion.

The Authority's bonds outstanding as of November 30, 2017 were as follows:

Description	Maturity Date	Weighted Average Auction Rate	Amount Outstanding
2012 A-2 Series	October 1, 2024	2.002%	$ 50,213,980
2012 A-3 Series	October 1, 2046	2.002%	81,820,000
2013 Series	December 3, 2029	1.611%	56,539,632
			$ 188,573,612

The following represents the contractual maturities of the Authority's bonds as of November 30, 2017:

Year Ended	2012 A-2 Series	2012 A-3 Series	2013 Series	Total
2018	$ -	$ -	$ -	$ -
2019	-	-	-	-
2020	-	-	-	-
2021	-	-	-	-
2022	-	-	-	-
Thereafter	50,213,980	81,820,000	56,539,632	188,573,612
	$ 50,213,980	$ 81,820,000	$ 56,539,632	$188,573,612

The following represents the interest requirements to maturity of the Authority's bonds at November 30, 2017 assuming interest rates on the floating rate securities remain the same as those at November 30, 2017:

Year Ended	2012 A-2 Series	2012 A-3 Series	2013 Series	Total
2018	$ 1,005,203	$ 1,637,905	$ 910,611	$ 3,553,719
2019	1,005,203	1,637,905	910,611	3,553,719
2020	1,005,203	1,637,905	910,611	3,553,719
2021	1,005,203	1,637,905	910,611	3,553,719
2022	1,005,203	1,637,905	910,611	3,553,719
Thereafter	1,842,872	39,036,729	5,463,666	46,343,267
	$ 6,868,887	$ 47,226,254	$ 10,016,721	$ 64,111,862

(8) Commitments and Contingencies

The Authority participates in the Title IV FFEL program administered by the U.S. Department of Education. This program is subject to numerous terms and conditions as specified in the federal regulations and to audit by the U.S. Department of Education. In the opinion of management, liabilities resulting from disallowed costs, if any, will not have a material adverse effect on the financial position of the Authority.

Effective June 30, 2010, with the passage of the Health Care and Education Reconciliation Act of 2010, no subsequent loans were permitted to be made under the FFEL program. Existing loans made under the FFEL program will continue to be guaranteed against default until paid in full. However, as no future loans will be made under the FFEL program, the related loan portfolios of the Authority will continue to decrease. As such, revenues generated by the Authority related to these loans will continue to decrease. Failing to replace these revenues would have an increasingly significant negative impact to the long term operational viability of the Authority. Subsequent to year end, the Authority sold the loan portfolio as further discussed in Note 10.

(9) Related Party Transactions

The Authority conducts business with several financial institutions where members of the Authority's board hold management positions. Transactions with these institutions occurred during the normal course of business and included the acquisition of student loan notes. The Authority and Council for South Texas Economic Progress (COSTEP) share facilities and personnel.

During the year ended November 30, 2017, COSTEP charged the following fees to the Authority:

Loan servicing fees	$ 1,026,132
Headquarter and administrative fees	936,638
Total fees	$ 1,962,770

As of November 30, 2017, COSTEP owed the Authority $523,988 related to collections on student loans including principal and interest and the Authority owed COSTEP $179,861 for servicing fees.

(10) Subsequent Events

The Authority evaluates events that occur subsequent to the statement of financial position date of periodic reports, but before financial statements are issued for periods ending on such dates, for possible adjustment to such financial statements or other disclosure. This evaluation generally occurs through the date at which the Authority's financial statements are issued or available to be issued. For the financial statements as of and for the year ending November 30, 2017, this date was May 15, 2018.

On February 9, 2018, the Authority transferred its Student Loan Backed Bonds, Series 2012-1 issued under an Indenture of Trust dated January 1, 2012 and its Student Loan Backed Bonds, Series 2013-1 issued under an Indenture of Trust dated June 1, 2013 to North Texas Higher Education Authority, Inc. (North Texas), a non-profit corporation headquartered in Arlington, Texas. At the same time the Authority transferred to North Texas all student loan notes and other assets securing the 2012 Bonds and the 2013 Bonds, respectively, and North Texas has assumed the Authority's obligations under the 2012 Indenture and the 2013 Indenture, including all reporting requirements.

In conjunction with the transfer, the Master Servicer for the student loans securing the Series 2012 Bonds and Series 2013 Bonds was converted from Council for South Texas Economic Progress to Higher Education Servicing Corporation, a non-profit corporation which acts as the operational arm of North Texas. Actual servicing of the student loans securing the Series 2012 Bonds and the Series 2013 Bonds was converted from Conduent Education Services, LLC to EdFinancial Education Services, LLC, Knoxville, Tennessee.

The Authority received cash proceeds of $25,988,531 of which $19,392,888 was for the sale of the Trust Estates and $6,595,643 for the sale of the Student Loan Notes in the General Loan Fund. The General Loan Fund recorded a loss of $143,196 which was recorded in the period of the sale in accordance with GASB 48. Cash received from the transaction was transferred to the Authority's General Fund.

The purpose of the transfer is to allow the Authority to cease its operations as a corporation operated exclusively to purchase guaranteed student loans and to convert to a charitable foundation. The Board of Directors is currently considering the future charitable use of its assets.

SOUTH TEXAS HIGHER EDUCATION AUTHORITY, INC.

Supplemental Information - Combining Schedule of Net Position Information

November 30, 2017

	2012-1 Series	2013-1 Series	General Fund	Total
Assets				
Current assets:				
Cash and cash equivalents	$ 4,799,163	$ 2,308,519	$ 9,852,236	$ 16,959,918
Student loan interest receivable	4,318,816	1,862,905	242,099	6,423,820
Student loan notes receivable, current portion, net of allowance	19,206,891	9,069,064	870,673	29,146,628
Due from servicing agent	256,732	261,217	6,039	523,988
Other current assets	1,668	766	10,402	12,836
Total current assets	28,583,270	13,502,471	10,981,449	53,067,190
Noncurrent assets:				
Student loan notes receivable, net of current portion and allowances	123,089,263	51,638,383	5,712,382	180,440,028
Other assets	10,352	18,125	5,121	33,598
Total noncurrent assets	123,099,615	51,656,508	5,717,503	180,473,626
Total assets	151,682,885	65,158,979	16,698,952	233,540,816
Liabilities				
Current liabilities:				
Accrued interest payable	480,824	86,795	-	567,619
Special allowance payable	146,636	48,309	26,157	221,102
Accounts payable	191,881	106,913	116,434	415,228
Total current liabilities	819,341	242,017	142,591	1,203,949
Noncurrent liabilities:				
Bonds payable	132,033,980	56,539,632	-	188,573,612
Total noncurrent liabilities	132,033,980	56,539,632	-	188,573,612
Total liabilities	132,853,321	56,781,649	142,591	189,777,561
Deferred Inflows of Resources				
Deferred debit on refunding	(1,074,574)	365,099	-	(709,475)
Total liabilities and deferrals	131,778,747	57,146,748	142,591	189,068,086
Net position				
Restricted for debt service	19,904,138	8,012,231	-	27,916,369
Unrestricted	-	-	16,556,361	16,556,361
Total net position	$ 19,904,138	$ 8,012,231	$ 16,556,361	$ 44,472,730

See accompanying notes and report of independent auditor.

SOUTH TEXAS HIGHER EDUCATION AUTHORITY, INC.

Supplemental Information - Combining Schedule of Revenues, Expenses, and Changes in Net Position Information

Year Ended November 30, 2017

	2012-1 Series	2013-1 Series	General Fund	Total
Operating revenues:				
Interest on student loan notes	$ 7,416,340	$ 3,175,352	$ 406,813	$ 10,998,505
Investment income	24,725	9,438	59,215	93,378
Total operating revenues	7,441,065	3,184,790	466,028	11,091,883
Operating expenses:				
Headquarters and administrative fees	634,903	324,853	(23,118)	936,638
Loan servicing and collection fees	667,319	328,477	30,336	1,026,132
Trustee fees	25,340	12,500	2,500	40,340
Professional fees	57,568	25,001	468,249	550,818
Provision for uncollectible receivables	179,320	89,485	13,246	282,051
Consolidation rebate fees	1,075,308	379,298	56,434	1,511,040
Directors and officers insurance	-	-	7,908	7,908
Special allowance payments	1,302,518	461,479	195,597	1,959,594
Bond interest expense	2,851,271	978,272	-	3,829,543
Other	171,434	(31,010)	52,635	193,059
Total operating expenses	6,964,981	2,568,355	803,787	10,337,123
Change in net position	476,084	616,435	(337,759)	754,760
Net position at beginning of year	19,428,054	7,395,796	16,894,120	43,717,970
Net position at end of year	$ 19,904,138	$ 8,012,231	$ 16,556,361	$ 44,472,730

See accompanying notes and report of independent auditor.

SOUTH TEXAS HIGHER EDUCATION AUTHORITY, INC.
Supplemental Information - Combining Schedule of Cash Flows Information
Year Ended November 30, 2017

	2012-1 Series	2013-1 Series	General Fund	Total
Cash flows from operating activities				
Receipt of student loan interest	$ 8,566,364	$ 3,599,873	$ 448,398	$ 12,614,635
Payments for special allowance	(1,453,779)	(529,075)	(206,280)	(2,189,134)
Collection of principal on student loans	21,417,925	10,278,327	963,252	32,659,504
Claim repurchases, write offs, and capitalized interest	(5,011,750)	(2,171,048)	(259,532)	(7,442,330)
Receipt of investment income	19,225	6,615	58,914	84,754
Payment of bond interest	(2,787,543)	(953,277)	-	(3,740,820)
Payments to suppliers	(2,360,329)	(1,281,806)	(537,624)	(4,179,759)
Net cash provided by operating activities	18,390,113	8,949,609	467,128	27,806,850
Cash flows from noncapital financing activities				
Payment on bonds payable, net	(18,980,620)	(8,933,810)	-	(27,914,430)
Net cash used in noncapital financing activities	(18,980,620)	(8,933,810)	-	(27,914,430)
Cash flows from investing activities	-	-	-	-
Net (decrease) increase in cash and cash equivalents	(590,507)	15,799	467,128	(107,580)
Cash and cash equivalents at beginning of year	5,389,670	2,292,720	9,385,108	17,067,498
Cash and cash equivalents at end of year	$ 4,799,163	$ 2,308,519	$ 9,852,236	$ 16,959,918
Reconciliation of change in net position to net cash provided by operating activities:				
Change in net position	$ 476,084	$ 616,435	$ (337,759)	$ 754,760
Adjustments to reconcile change in net position to net cash provided by operating activities:				
Provision for uncollectible receivables	179,320	89,485	13,246	282,051
Amortized gains (losses) on bonds issued	171,132	(31,010)	-	140,122
Changes in assets and liabilities:				
Decrease (increase) in student loan interest receivable	1,150,024	424,521	41,585	1,616,130
Decrease (increase) in student loan notes receivable	16,293,468	8,041,495	660,778	24,995,741
Decrease (increase) in due from servicing agents	230,635	(131,857)	3,080	101,858
Decrease (increase) in other assets	210	(517)	(4,088)	(4,395)
Increase (decrease) in accrued interest payable	63,728	24,995	-	88,723
Increase (decrease) in special allowance payable	(151,261)	(67,596)	(10,683)	(229,540)
Increase (decrease) in accounts payable	(23,227)	(16,342)	100,969	61,400
Net cash provided by operating activities	$ 18,390,113	$ 8,949,609	$ 467,128	$ 27,806,850

See accompanying notes and report of independent auditor.

PMB Helin Donovan

14090 SW Freeway
Suite 300
Sugar Land, TX 77478
pmbhd.com

T 832.301.3000
F 832.301.3010

Independent Auditor's 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

The Board of Directors
South Texas Higher Education Authority, Inc.:

We have audited, in accordance with the auditing standards generally accepted in the United States of America 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 South Texas Higher Education Authority, Inc. (the Authority), which comprise the statement of net position as of and for the year ended November 30, 2017, and the related statements of revenues, expenses, and changes in net position and cash flows for the year then ended, and the notes to the financial statements and have issued our report thereon dated May 15, 2018.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Authority'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 the Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

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 a 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 over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies. 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority'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 direct and 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 results 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 communication is not suitable for any other purpose.

PMB HELIN DONOVAN, LLP

PMB Helin Donovan, LLP

May 15, 2018