CONNECTICUT HIGHER EDUCATION SUPPLEMENTAL LOAN AUTHORITY

Financial Statements

June 30, 2006 and 2005

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
CONNECTICUT HIGHER EDUCATION SUPPLEMENTAL LOAN AUTHORITY
West Hartford, Connecticut

We have audited the accompanying basic financial statements of the Connecticut Higher Education Supplemental Loan Authority ("Authority"), a component unit of the State of Connecticut, as of and for the years ended June 30, 2006 and 2005, as listed in the table of contents. These basic financial statements are the responsibility of the Authority's management. Our responsibility is to express opinions on these basic financial statements based on our audits.

We conducted our audits 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 of the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic 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 audits provide a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the Connecticut Higher Education Supplemental Loan Authority as of June 30, 2006 and 2005, and the respective changes in financial position and cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards,* we have also issued a report dated September 9, 2006 on our consideration of the Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, 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* and should be considered in assessing the results of our audits.

The Management's Discussion and Analysis as listed in the table of contents is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Rocky Hill, Connecticut
September 9, 2006

CONNECTICUT HIGHER EDUCATION SUPPLEMENTAL LOAN AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS

The Connecticut Higher Education Supplemental Loan Authority (CHESLA) is a public instrumentality and political subdivision of the State of Connecticut (the "State"). CHESLA provides financial assistance in the form of education loans to students in or from the State, their parents or others responsible for the cost of their education and provides an alternative method to enable institutions of higher education in the State to assist qualified students to attend such institutions. CHESLA is authorized to issue tax-exempt bonds, the proceeds of which are used to fund education loans to applicants meeting certain eligibility requirements. The repayments of such loans service the debt on CHESLA bonds. CHELSA, in connection with the issuance of its bonds, has made certain covenants with respect to such loans, including a covenant to do or cause to be done all such acts and things necessary to receive and collect all revenues due with respect to such loans. CHESLA bonds are further secured by a special capital reserve fund.

The following Management's Discussion and Analysis (MD&A) of the State of Connecticut Higher Education Supplemental Loan Authority ("the Authority") activities and financial performance provides an introduction to the audited financial statements for the fiscal year ended June 30, 2006 as compared to June 30, 2005. Following the MD&A are the basic financial statements of the Authority together with the notes thereto, which are essential to a full understanding of the data contained in the financial statements.

CONNECTICUT HIGHER EDUCATION
SUPPLEMENTAL LOAN AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS

FINANCIAL POSITION SUMMARY

The Authority's fiscal year 2006 assets decreased by $14 million or 9.8% over fiscal year 2005 and liabilities decreased by $15.4 million or 11.5% over fiscal year 2005. Total assets exceeded liabilities by $10.1 million in 2006 as compared to $8.8 million for 2005, or a net increase of $1.3 million.

BALANCE SHEETS
(In Thousands)

	2006	2005
ASSETS:		
Current unrestricted assets	$ 15,788	$ 19,309
Current restricted assets	32,102	45,493
Total Current Assets:	47,890	64,802
Non-Current assets:		
Restricted Investments	7,000	7,000
Loans receivable, net of current portion	72,040	68,799
Bond issuance costs, net	2,091	2,445
Total Non-Current Assets	81,131	78,244
TOTAL ASSETS	$ 129,021	$ 143,046
LIABILITIES:		
Current liabilities	$ 7,037	$ 6,899
Long-term liabilities	111,911	127,396
TOTAL LIABILITIES	118,948	134,295
NET ASSETS:		
Unrestricted	10,072	8,751
TOTAL LIABILITIES AND NET ASSETS	$ 129,021	$ 143,046

FINANCIAL HIGHLIGHTS

The following is an overview of significant changes within the Balance Sheets during the past fiscal year:

Assets

Current unrestricted assets decreased by $3.5 million or 18.2%. This was due primarily to the decrease of the current portion of loans receivable which resulted from collections received in 2006 offset by existing loans becoming more current.

FINANCIAL HIGHLIGHTS (Continued)

Current restricted assets decreased by $13.4 million or 29.4%. This decrease was primarily the result of a decrease in investments of $11.7 million due to the disbursement of loans in FY 2006.

Non-current assets increased by $2.9 million or 3.7%. This was primarily due to:

- Loans receivable increased by $3.2 million because of new loans associated with the 2005 bond offering having a greater non-current portion offset by existing loans becoming more current.

Liabilities

Current liabilities increased by $0.1 million or 1.4% as compared to June 30, 2005, due primarily to the current payment obligations of bonds payable offset by a decrease in accrued interest payable.

Long-term liabilities decreased by $15.5 million or 12.2% as compared to June 30, 2005, due to scheduled principal payments and mandatory redemptions on outstanding bonds payable.

SUMMARY OF OPERATIONS AND CHANGES IN NET ASSETS

A summary of operations and changes in net assets for the fiscal year ended June 30, 2006, and the amount and percentage of change in relation to prior fiscal year amount is as follows:

STATEMENTS OF REVENUES, EXPENSES
AND CHANGES IN NET ASSETS
(In Thousands)
Fiscal Years Ending June 30,

	2006	2005
Operating revenues	$ 9,113	$ 10,139
Operating expenses	7,792	7,915
Increase in Net Assets	$ 1,322	$ 2,224

Operating revenues decreased in fiscal year 2006 by $1.0 million or 10.1% over fiscal year 2005, due primarily to the decrease in interest earning on loans receivable due to newer loans outstanding having lower interest rates.

SUMMARY OF OPERATIONS AND CHANGES IN NET ASSETS (Continued)

Operating expenses also decreased during fiscal year 2006 by $163,000 or 2.1% compared to fiscal year 2005. This was primarily due to a decrease in loan collection fees, a decrease in professional fees, offsetting an increase in interest expense.

SUMMARY OF REVENUE

A summary of revenues for the fiscal year ended June 30, 2006, and the amount and percentage of change in relation to prior fiscal year amounts is as follows:

	2006	Percent of Total	2005	Increase/ (decrease) from 2005	Percent Increase/ (decrease)
Operating:					
Interest income on loans receivable	$ 6,406	70.3%	$ 7,986	$ (1,580)	-19.8%
Interest income on investments	1,951	21.4%	1,455	495	34.0%
Administrative fees	741	8.1%	698	43	6.2%
Other operating income	16	0.2%	-	16	100.0%
Total operating revenues	9,113	100.0%	10,139	(1,026)	
TOTAL REVENUES	$ 9,113	100.0%	$ 10,139	$ (1,026)	-10.1%

The following discusses the major changes in operating revenues of the Authority:

- Interest income on loans receivable, which represents interest income from educational loans, decreased by 19.8% or $1.6 million due to lower rates on outstanding loans.

- Interest income on investments, increased by $495,303 or 34% from fiscal year 2005. The increase is due to higher rates of return on investment balances in 2006.

- Administrative fees increased by $43,035 or 6.2%. These fees are based on Authority income from a percentage of originations and principal outstanding from the various bond deals. The increase is due to the addition of the 2005 bond series for a full year in 2006.

CONNECTICUT HIGHER EDUCATION SUPPLEMENTAL LOAN AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS

SUMMARY OF EXPENSES

A summary of expenses for the fiscal year ended June 30, 2006, and the amount and percentage of change in relation to prior fiscal year amounts is as follows:

	2006	Percent of Total	2005	Increase/ (decrease) from 2005	Percent Increase/ (decrease)
Operating:					
Interest expense	$ 5,648	72.5%	$ 5,593	$ 55	1.0%
Administrative fees	741	9.5%	698	43	6.2%
Loan collection fees	593	7.6%	756	(163)	-21.6%
General and administrative expenses	269	3.4%	327	(59)	-17.9%
Amortization of bond issuance costs	354	4.5%	340	14	4.2%
Professional fees	154	2.0%	204	(50)	-24.3%
Provision for loan losses	(230)	-3.0%	(300)	70	-23.3%
Salaries	108	1.4%	99	9	9.3%
Trustee fees	38	0.5%	44	(6)	-13.7%
Arbitrage rebate expense	117	1.5%	154	(37)	-23.9%
TOTAL OPERATING EXPENSES	$ 7,792	100.0%	$ 7,914	$ (123)	-1.5%

The Authority's expenses decreased from fiscal year 2005 to 2006 by $123,000 or 1.5% in total. Notable differences between the years include:

- Interest expense increased by $55,311 or 1% due to the 2005 bond deal.
- Administrative fees increased by $43,035 or 6.2% primarily due to the 2005 bond deal.
- Arbitrage rebate expense decreased by $36,838 due to the decrease in the 2% yield liability as compared to June 30, 2005 and the refunding of a prior bond issue.
- Professional fees decreased by $49,618 due primarily to the services of a Financial Advisor, which were not utilized as no new bond series were issued during the year.
- Provision for loan losses increased by $70,000 or 23.3% primarily due to historical collection results, CHESLA's reduction in write offs and its increase in recoveries in recent years which support a reduction in the overall allowance for loan losses.
- Loan collection fees decreased largely due to Firstmark being the loan servicer for CHESLA during the whole of FY 2006.

SUMMARY OF CASH FLOW ACTIVITIES

The following is a summary of the major sources and uses of cash and cash equivalents for the two most recent fiscal years. Cash equivalents are considered cash-on-hand, bank deposits and highly liquid investments with an original maturity of three months or less.

STATEMENTS OF CASH FLOWS
(In Thousands)
Fiscal Years Ending June 30,

	2006	2005
Cash flows from operating activities	$ 1,773	$ 2,616
Cash flows from investing activities	11,667	(27,900)
Cash flows from non-capital financing activities	(14,830)	14,161
Net decrease in cash and cash equivalents	(1,389)	(11,123)
Cash and cash equivalents:		
Beginning of year	8,423	19,546
End of year	$ 7,034	$ 8,423

The Authority's available cash and cash equivalents decreased $1.4 million from $8.4 million at the end of fiscal year 2005 to $7 million at the end of fiscal year 2006 due to:

- Cash flows from operating activities, which represent the net difference between cash received for loan payments and interest and loans disbursed to borrowers and cash paid to employees and vendors for goods and services. For fiscal year 2006, this net source of cash was $0.8 million less than fiscal year 2005 and was mainly due to a decrease in the rate of originations and collections in 2006.

- Cash flows from investing activities, which represent the net difference between proceeds from maturing investments versus the purchase of investment securities. For fiscal year 2006, this net source of cash was $39.6 million more than fiscal year 2005 and was mainly due to significant sales of investments in the current year whereas 2005 included significant purchases from the 2005 bond deal.

- Cash flows from non-capital financing activities, which represent the net difference between total proceeds from bond issuances, versus the costs of issuance and scheduled payments on bond principal. For fiscal year 2006, this net use of cash was $29 million higher than fiscal year 2005 and was mainly due to principal payments on outstanding bonds with no new proceeds from bond issuances in 2006.

CONNECTICUT HIGHER EDUCATION SUPPLEMENTAL LOAN AUTHORITY

BALANCE SHEETS

June 30, 2006 and 2005

ASSETS	2006	2005
CURRENT ASSETS		
Unrestricted assets:		
Cash and cash equivalents	$ 1,880,511	$ 1,545,601
Current portion of loans receivable, net of allowances for loan losses of $2,070,000 in 2006 and $2,300,000 in 2005	13,360,451	16,957,639
Interest receivable on investments	226,112	435,210
Interest receivable on loans receivable	321,408	370,818
Total Unrestricted Assets	15,788,482	19,309,268
Restricted assets:		
Cash and cash equivalents	5,153,906	6,878,006
Investments	26,945,628	38,613,093
Connecticut Higher Education Trust	2,154	2,085
Total Restricted Assets	32,101,688	45,493,184
Total Current Assets	47,890,170	64,802,452
NON-CURRENT ASSETS		
Restricted investments	7,000,000	7,000,000
Loans receivable, net of current portion	72,040,403	68,798,981
Bond issuance costs, net of accumulated amortization of $3,140,823 in 2006 and $2,786,922 in 2005	2,090,683	2,444,584
Total Non-Current Assets	81,131,086	78,243,565
Total Assets	$ 129,021,256	$ 143,046,017

See notes to financial statements.

LIABILITIES AND NET ASSETS	2006	2005
CURRENT LIABILITIES		
Current portion of bonds payable	$ 5,795,324	$ 5,225,280
Accounts payable and accrued liabilities	89,635	90,520
Current portion of arbitrage rebate payable	117,345	154,183
Accrued interest payable	649,945	1,023,187
Current portion of deferred revenue	384,846	405,384
Total Current Liabilities	7,037,095	6,898,554
LONG-TERM LIABILITIES		
Bonds payable, net of current portion	109,663,204	124,993,529
Arbitrage rebate payable, net of current portion	47,493	130,736
Deferred revenue, net of current portion	2,200,666	2,272,034
Total Long-Term Liabilities	111,911,363	127,396,299
Total Liabilities	118,948,458	134,294,853
UNRESTRICTED NET ASSETS	10,072,798	8,751,164
Total Liabilities and Net Assets	$ 129,021,256	$ 143,046,017

CONNECTICUT HIGHER EDUCATION SUPPLEMENTAL LOAN AUTHORITY

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
YEARS ENDED JUNE 30, 2006 AND 2005

	2006	2005
OPERATING REVENUES		
Interest income on investments	$ 1,950,683	$ 1,455,380
Interest income on loans receivable	6,406,133	7,985,977
Administrative fees	740,623	697,588
Other operating income	15,822	-
Total Operating Revenues	9,113,261	10,138,945
OPERATING EXPENSES		
Interest expense	5,648,244	5,592,934
Administrative fees	740,623	697,588
Loan collection fees	592,640	755,965
General and administrative expenses	268,580	327,124
Amortization of bond issuance costs	353,901	340,657
Professional fees	154,470	204,088
Arbitrage rebate expense	117,345	154,183
Salaries	107,770	98,615
Trustee fees	38,054	44,092
Provision for loan losses	(230,000)	(300,000)
Total Operating Expenses	7,791,627	7,915,246
CHANGE IN NET ASSETS	1,321,634	2,223,699
NET ASSETS, beginning	8,751,164	6,527,465
NET ASSETS, ending	$ 10,072,798	$ 8,751,164

See notes to financial statements.

CONNECTICUT HIGHER EDUCATION SUPPLEMENTAL LOAN AUTHORITY

STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2006 AND 2005

	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received for the following:		
Loan payments	$ 15,430,451	$ 18,318,094
Interest collected on loans	6,455,543	8,101,422
Interest collected on investments	2,159,781	1,158,039
Other income	756,445	697,588
Total cash received	24,802,220	28,275,143
Cash paid for the following:		
Loans disbursed	(15,007,202)	(17,917,527)
Bond Interest	(5,951,767)	(5,445,055)
Other expenses	(2,069,837)	(2,296,544)
Total cash disbursed	(23,028,806)	(25,659,126)
Net Cash Provided by Operating Activities	1,773,414	2,616,017
CASH FLOWS FROM INVESTING ACTIVITIES		
Sale of restricted investments	11,667,396	-
Purchase of restricted investments	-	(27,900,259)
Net Cash Provided by (Used in) Investing Activities	11,667,396	(27,900,259)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Issuance of bonds	-	37,355,000
Bond issuance costs	-	(1,368,623)
Payments on bond principal	(14,830,000)	(21,825,000)
Net Cash Provided by (Used in) Noncapital Financing Activities	(14,830,000)	14,161,377
Net decrease in cash and cash equivalents	(1,389,190)	(11,122,865)
CASH AND CASH EQUIVALENTS, Beginning	8,423,607	19,546,472
CASH AND CASH EQUIVALENTS, Ending	$ 7,034,417	$ 8,423,607

See notes to financial statements.

	2006	2005
RECONCILIATION OF CHANGE IN NET ASSETS TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Change in net assets	$ 1,321,634	$ 2,223,699
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Amortization of bond issuance costs	353,901	340,657
Amortization of deferred amount on refunding	88,020	111,220
Amortization of bond discount	19,869	5,795
Amortization of bond premium	(38,170)	(6,827)
Provision for loan losses	(230,000)	(300,000)
Change in assets and liabilities:		
Decrease in loans receivable	585,766	1,111,368
(Increase) decrease in interest receivable on investments	209,098	(297,341)
Decrease in interest receivable on loans receivable	49,410	115,445
Decrease in accounts payable and accrued liabilities	(885)	(14,889)
(Decrease) increase in arbitrage rebate payable	(120,081)	(960,972)
Increase (decrease) in accrued interest payable	(373,242)	330,638
Decrease in deferred revenue	(91,906)	(42,776)
Net Cash Provided by Operating Activities	$ 1,773,414	$ 2,616,017

RECONCILIATION OF CASH AND CASH EQUIVALENTS TO THE STATEMENT OF NET ASSETS

	2006	2005
Cash and cash equivalents - unrestricted	1,880,511	1,545,601
Cash and cash equivalents - restricted	5,153,906	6,878,006
	$ 7,034,417	$ 8,423,607

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity – The Connecticut Higher Education Supplemental Loan Authority ("Authority") is a body politic and corporate established in 1982 pursuant to Section 4 of Connecticut Higher Education Supplemental Loan Authority Act, Public Act 82-313 of the Connecticut General Assembly (the Act). For purposes of financial reporting, the Authority is a component unit of the State of Connecticut and the Authority's financial statements are included in the State's Comprehensive Annual Financial Report. The Authority was established to assist students, their parents and institutions of higher education to finance the cost of higher education through its Bond funds.

The funds of the Authority are proprietary fund types. Proprietary funds are used to account for governmental activities that are similar to those found in the private sector where the determination of net income is necessary or useful for sound financial administration. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. Proprietary funds are accounted for on a cost of services or "capital maintenance" measurement focus. This means that all assets and all liabilities (whether current or non-current) associated with their activity are included on their balance sheet. Accounting principles generally accepted in the United States of America (GAAP) used for proprietary funds are generally those applicable to businesses in the private sector. In accordance with Governmental Accounting Standards Board (GASB) Statement No. 20, the Authority applies all GASB pronouncements and all Financial Accounting Standards Board Statements, Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins issued on or before November 30, 1989, except those that conflict with GASB pronouncements.

Authority Operating Fund – The administrative functions of the Authority are accounted for in the Authority Operating Fund. Revenues in this fund consist of interest income and administrative fees.

Bond Funds – Under the Bond Funds, the Authority issues revenue bonds, the proceeds of which are used to provide loans directly to students or other borrowers to assist in the financing of higher education. Revenue in the Bond Funds is derived from interest earned on investments and loans receivable. The 2003 Bond Fund is governed by the 2003 Master Revenue Bond Resolution, pursuant to which the 2003 and 2005 Series A and B bonds were issued. The proceeds from the 2003 Series B bonds were used to refund the 1991 Series A bonds and the 2003 Series 1 bonds. The proceeds from the 2005 Series B bonds were used to refund the 1993 and 1994 Series A bonds (see Note 4). The 2003 Series 1 bonds were issued on May 15, 2003 to refund prior obligations of the Authority scheduled to be retired by special mandatory redemption on May 15, 2003. The Pre 2003 Bond Fund is governed by the 1990 Revenue Bond Resolution, as amended, supplemented and restated, pursuant to which all outstanding bonds were issued prior to the 2003 Series A and B bonds. In accordance with the bond resolutions, the Authority internally accounts for each bond issue, which includes individual funds as defined by each bond resolution, including but not limited to combinations of some of the following:

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Bond Funds (Continued) –

Loan Fund, Revenue Fund, Debt Service Reserve Fund and the Special Capital Reserve Fund.

Prior to 1988, these loans were provided for the purpose of assisting in the financing of attendance at eligible colleges and universities in Connecticut under the Family Education Loan Program (CTFELP). In 1988, the program was expanded to include loans to Connecticut residents attending institutions outside the state.

Connecticut Higher Education Trust (CHET) – Under the CHET program, the Authority maintains trust accounts for students in the Authority's early college awareness program.

Use of Estimates – 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 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. A material estimate that is particularly susceptible to significant change relates to the determination of the allowance for loan losses. In connection with the determination of the allowance for loan losses, management has used historical loss experience to make predictions about future losses. As the loan portfolio matures, the Authority adjusts its estimate of expected default rates used to estimate loan losses

Revenue Recognition – Interest income on loans is recognized based on the rates applied to principal amounts outstanding. The accrual of interest income is generally discontinued when a loan is classified as non-performing (see Note 3). Loans are currently considered to be non-performing by management when the borrower has defaulted and not made payments for the most recent three months.

Cash and Cash Equivalents – For purposes of the statement of cash flows, the Authority considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. Cash equivalents consisted of short-term investments in the State Treasurer's Short-Term Investment Fund, which totaled \$6,391,586 and \$7,947,798 as of June 30, 2006 and 2005, respectively.

The State Treasurer's Short-Term Investment Fund is an investment pool managed by the State Treasurer's Office. The fair value of the Authority's position in the pool is the same as the value of the pool shares.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investments – In accordance with Governmental Accounting Standards Board Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools,* the Authority presents all investments at fair value, except for non-participating interest earning investment contracts, which are carried at amortized cost.

The Authority maintains guaranteed investment contracts with AIG Matched Funding Corporation, MBIA, Inc., FGIC Capital Market Services, IXIS Funding (formerly known as CDC Funding Corporation), Society Generale, Berkshire Hathaway, Inc., Westdeutsche Landesbank, and Rabobank International. Under these agreements, all investment transactions must be authorized investments, defined by the bond resolutions as including primarily securities issued or guaranteed by the United States Government, corporate debt obligations having a bond rating of "A" or higher, mortgage participation certificates issued by the Federal Home Loan Mortgage Corporation and mortgage pass-through certificates issued by the Federal National Mortgage Association.

There were no significant investment losses for the years ended June 30, 2006 and 2005.

Loans Receivable and Allowance for Loan Losses – Interest on loans receivable is accrued and credited to operations based upon the principal amount outstanding. Loans are placed on non-accrual status when management believes principal or interest on such loans may not be collected in the normal course of business. The allowance for loan losses has been provided through charges against operations based on management's evaluation of the loan portfolio and maintained at a level believed adequate to absorb potential losses in the loan portfolio. Loans are typically written off against the allowance for loan losses (net of loan recoveries) in the period in which the loans become non-performing and no payments have been made for 12 consecutive months. However, a loan may be written off at any time management believes the repayment of such loan is doubtful. Collection of loans previously written-off are pursued until management believes that further recoveries are doubtful.

Restricted Assets – Under provisions of the bond resolutions, certain assets are restricted for the repayment of bond principal and interest, for the issuance of student loans, and anticipated operating costs.

Bond Issuance Costs – Bond issuance costs are amortized over the term of the related bonds.

Arbitrage Rebates – Under the Internal Revenue Code of 1986 (the Code), the Authority is required to rebate to the federal government certain excess earnings on investments from funds obtained with its tax-exempt bonds, as defined by the Code. The Authority is also presently required to reduce the yield on loans made with the proceeds of certain of its tax-exempt bonds. The Authority accrues or adjusts for this liability as incurred.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Deferred Revenue – The Authority charges a 3 percent reserve fee on loans governed by the 2003 Master Revenue Bond Resolution and a 2 percent reserve fee on loans governed by the 1990 Revenue Bond Resolution. The fee, net of origination costs, is deferred and recognized over the life of the loan.

Income Taxes – The Authority is exempt from state and federal income taxes.

NOTE 2 – CASH DEPOSITS AND INVESTMENTS

Cash Deposits – Governmental Accounting Standards Board Statement No. 3, *Deposits with Financial Institutions, Investments, and Repurchase Agreements,* requires governmental organizations to categorize their cash deposits into three levels of risk. Category 1 includes amounts, which are insured or collateralized with securities held by the Authority or by its agent in the Authority's name. Category 2 includes amounts, which are collateralized with securities held by the pledging financial institution's trust department or agent in the name of the Authority. Category 3 includes amounts, which are uninsured and uncollateralized, including any bank balance that is collateralized with securities held by the pledging financial institutions, or by its trust department or agent, but not in the name of the Authority.

For purposes of this disclosure, cash deposits include bank deposits and exclude cash equivalents (see Note 1). As of June 30, 2006 and 2005, the carrying amount of the Authority's unrestricted and restricted cash deposits totaled $642,831 and $457,969, respectively. As of June 30, 2006, the bank balance totaled $59,076, which was insured by the Federal Deposit Insurance Corporation (Category 1).

Investments – In accordance with the provisions of Statement No. 3 of the Governmental Accounting Standards Board, the Authority's investments, including cash equivalents, must be categorized to give an indication of the level of risk assumed at year-end. Category 1 includes investments that are insured or registered in the Authority's name or are held by the Authority or its agent in the Authority's name. Category 2 includes uninsured and unregistered investments, which are held by a counter party's trust department or by its agent in the Authority's name. Category 3 includes uninsured or unregistered securities, which are held by a counter party, its trust department or by its agent, but not held in the Authority's name.

NOTE 2 – CASH DEPOSITS AND INVESTMENTS (Continued)

The Authority's investments consist of guaranteed investment contracts, which are not required to be classified under GASB Statement No. 3 because they are direct contractual investments, and are not securities. The State of Connecticut Short-Term Investments Funds, which are presented as cash equivalents, are pooled investments and are not required to be classified under GASB Statement No. 3.

NOTE 3 – LOANS RECEIVABLE

Under the Bond Fund Program, the Authority makes loans to individuals from the proceeds of bonds issued by the Authority. Loans receivable by outstanding bond series as of June 30, 2006 are as follows:

Bond Series	Number	Balance	Interest Rate (%)
1996A	1,216	6,741,294	8.10
1998A&B	1,042	7,436,964	7.50
1999A	593	5,361,734	7.50
1999B	260	1,862,321	7.50
2000A	894	8,416,620	7.25
2000B	346	2,926,848	7.25
2001A*	1,409	14,752,388	6.7 & 9.7
2003A	1,137	14,117,715	4.99
2003B**	1,072	7,910,154	4.99 & 9.2
2005 A&B***	2,289	16,399,033	5.5, 8.25,& 8.4
	10,258	85,925,071	
Add: Non-performing loans		1,545,783	
Less: Allowance for loan losses		(2,070,000)	
		$ 85,400,854	

* Includes loans issued under the 1990 Series A bonds which were refunded by the 2001 Series A bonds.

** Includes loans issued under the 1991 Series A bonds which were refunded by the 2003 Series B bonds.

*** Includes loans issued under the 1993 and 1994 Series A bonds which were refunded by the 2005 Series B bonds.

Outstanding loans receivable bear interest at rates ranging from 4.99% to 9.7%.

NOTE 3 – LOANS RECEIVABLE (Continued)

The Authority currently defines non-performing loans as those on which the borrower has defaulted and not made payments for the most recent three months. As of June 30, 2006 and 2005, non-performing loans totaled $1,545,784 and $1,793,301, respectively, for which interest income of approximately $111,286 and $134,200 respectively, was not accrued.

The Authority has a policy to write-off uncollectible loans against the allowance for loan losses when certain criteria are met (see Note 1). In connection with this policy, the Authority wrote-off loans receivable of $486,412 and $285,392 for the years ended June 30, 2006 and 2005, respectively, which had been previously provided for through the allowance for loan losses. The Authority recovered $296,324 and $392,583 in fiscal 2006 and 2005, respectively, in loans receivable and other credits written-off in previous years.

NOTE 4 – BONDS PAYABLE

The following is a summary of changes in bonds payable for the years ended June 30, 2006 and 2005.

	Balance at June 30, 2004	Increases	Decreased	Balance at June 30, 2005
Bonds payable - principal	$ 115,220,613	$ 36,784,228	$ 21,786,032	$ 130,218,809

	Balance at June 30, 2005	Increases	Decreased	Balance at June 30, 2006	Amount Due Within One Year
Bonds payable - principal	$ 130,645,000	$ -	$ 14,830,001	$ 115,814,999	$ 5,865,044
Discount	(597,628)	-	(19,870)	(577,758)	(19,870)
Premium	591,760	-	38,170	553,590	38,170
Deferred amount on refunding	(420,323)	-	(88,020)	(332,303)	(88,020)
	$ 130,218,809	$ -	$ 14,760,281	$ 115,458,528	$ 5,795,324

The bonds of the Authority bear interest at rates, varying between 1.7% and 6%. Future amounts needed to pay principal and interest on bonds outstanding at June 30, 2006 is as follows:

NOTE 4 – BONDS PAYABLE (Continued)

Year Ending June 30,	Principal	Interest
2007	$ 6,670,000	$ 5,078,804
2008	7,570,000	4,835,928
2009	5,950,000	4,528,208
2010	7,170,000	4,252,939
2011	9,585,000	3,881,896
2012-2016	49,195,000	12,802,016
2017-2021	26,775,000	3,306,960
2022-2026	2,900,000	65,188
	$ 115,815,000	$ 38,751,939

Outstanding principal of each bond issue at June 30, 2006 and 2005 is as follows:

	Original Amount	Outstanding June 30, 2006	Outstanding June 30, 2005
1996 Series A, 4.75%-5.875%, due serially from November 15, 2001 to November 15, 2017	25,000,000	7,355,000	9,820,000
1998 Series A, 4.10%-5.15%, due serially from November 15, 2002 to November 15, 2016	15,000,000	3,765,000	5,615,000
1998 Series B, 4%-4.875%, due serially from November 15, 2001 to November 15, 2010	3,560,000	2,935,000	2,935,000
1999 Series A, 4.7%-6%, due serially from November 15, 2002 to November 15, 2017	12,500,000	3,850,000	5,440,000
1999 Series B, 4.5%-6%, due serially from November 15, 2002 to November 15, 2012	4,390,000	3,995,000	3,995,000
2000 Series A, 4.625%-5.5%, due serially from November 15, 2008 to November 15, 2020	16,410,000	7,915,000	10,000,000
2000 Series B, 4.75%-5.2%, due serially from November 15, 2001 to November 15, 2012	5,975,000	3,035,000	3,845,000
2001 Series A, 4.25%-5.25%, due serially from November 15, 2010 to November 15, 2021	25,000,000	19,740,000	22,575,000

NOTE 4 – BONDS PAYABLE (Continued)

	Original Amount	Outstanding June 30, 2006	Outstanding June 30, 2005
2003 Series A, 1.7%-4.5%, due serially from November 15, 2004 to November 15, 2020	18,000,000	16,300,000	17,000,000
2003 Series B, 2%-5%, due serially from November 15, 2004 to November 15, 2017	12,915,000	10,570,000	12,065,000
2005 Series A, 2.5%-4.375% due serially from November 15, 2005 to November 15, 2021	31,455,000	30,455,000	31,455,000
2005 Series B, 4% due serially from November 15, 2008 to 2010	5,900,000	5,900,000	5,900,000
	$ 176,105,000	$ 115,815,000	$ 130,645,000

Each Series A bond is subject to a special mandatory redemption in whole or in part from excess loan payments. During the year ended June 30, 2006 and 2005, the Authority redeemed bonds in the following amounts:

	2006	2005
1993 Series A	$ -	$ 235,000
1994 Series A	-	765,000
1996 Series A	1,755,000	1,555,000
1998 Series A	1,565,000	1,990,000
1999 Series A	1,295,000	1,670,000
2000 Series A	2,085,000	2,095,000
2001 Series A	2,835,000	-
	$ 9,535,000	$ 8,310,000

Debt Refunding – During the year ended June 30, 2005, the Authority issued $5,900,000 of 2005 Series B bonds with an average interest rate of approximately 4% and utilized $2,670,000 of proceeds from previous bond offerings to refund $2,020,000 of 1993 Series A bonds and $6,650,000 of 1994 Series A bonds with an average interest rate of approximately 6.06%. The primary purpose of the refunding was to refinance current obligations of the Authority on a long-term basis. The refunding decreased the Authority's total debt service payments over the next 10 years by approximately $2,770,000 and resulted in an economic gain (difference between the present values of the debt service payments of the old and new bonds) of approximately $2,424,010. The reacquisition price exceeded the carrying amount of the old bonds by $338,978. This amount is being netted against the new bonds and amortized over the life of the 2005 Series B bonds, which is shorter than the remaining life of the refunded bonds.

NOTE 5 – STATE OF CONNECTICUT DEPOSIT REQUIREMENT

Deficiencies, if any, in the Debt Service Reserve Fund balances within the Bond Funds will be funded from the amount on deposit in the applicable Special Capital Reserve Fund. Both the Debt Service Reserve Fund and the Special Capital Reserve Fund are components of restricted investments. In accordance with the Act, the State must deposit with the Trustee monies necessary to restore the Special Capital Reserve Fund requirement (i.e., an amount equal to the maximum amount of principal and interest becoming due by reason of maturity in any one succeeding calendar year or some lesser amount specified by the Authority in its resolution authorizing the issuance of any such bonds.) As of June 30, 2006 and 2005, the State has not made nor was it required to make any such deposit.

NOTE 6 – RELATED PARTY TRANSACTIONS

The Authority shares rental space, office supplies, office equipment and utilities with and shares the services of the Vice President of the Connecticut Conference of Independent Colleges (CCIC). Currently, the executive director of CHESLA serves as Vice President of CCIC. Fees charged to the Authority by CCIC for providing administrative services were $102,000 for each of the years ended June 30, 2006 and 2005. In addition, the Authority reimbursed CCIC directly for actual general and administrative expenses incurred.

NOTE 7 – EMPLOYEE BENEFIT PLANS

The Authority has a Simplified Employee Pension Plan (the Plan). Under the provisions of the Plan, the Authority will make annual contributions directly to the individual retirement accounts (IRA) of all eligible employees, equal to eight percent of the employee's salary. Employees have the right to withdraw amounts from the IRA in accordance with the terms and conditions of the IRA. In 2006 and 2005, the Authority made contributions of $8,624 and $8,231, respectively, to the Plan.

NOTE 8 – DESIGNATED NET ASSETS

The Board of Directors has designated $1,000,000 of its unrestricted net assets to be used to maintain future operations required to monitor the loan portfolio should the Authority cease to issue new loans.

NOTE 9 – RISK MANAGEMENT

The Authority is exposed to various risks of loss related to torts, theft of, damage to, or destruction of assets, errors or omissions, injuries to employees, or acts of God. The Authority purchases commercial insurance to mitigate loss from these risks. Neither the Authority nor its insurers have settled any claims that have exceeded insurance coverage in the last three years. There was no reduction in insurance coverage from that of the prior year.

NOTE 10 - SUBSEQUENT EVENT

In August 2006, the Authority closed the 2006 Series A bond deal. The 2006 Series A bonds are subject to the 2003 Master Revenue Bond Resolution. The 2006 Series A bonds raised proceeds of $32,769,999, a portion of which will be used to refund the 1996 Series A bonds.

INDEPENDENT AUDITORS' REPORT ON SUPPLEMENTARY INFORMATION

To the Board of Directors of the
CONNECTICUT HIGHER EDUCATION SUPPLEMENTAL LOAN AUTHORITY
West Hartford, Connecticut

Our report on our audits of the basic financial statements of Connecticut Higher Education Supplemental Loan Authority for the years ended June 30, 2006 and 2005 appears on page 1. These audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information contained on pages 25 to 27 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements, and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Rocky Hill, Connecticut
September 9, 2006

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*

To the Board of Directors of the
CONNECTICUT HIGHER EDUCATION
SUPPLEMENTAL LOAN AUTHORITY
West Hartford, Connecticut

We have audited the accompanying basic financial statements of the Connecticut Higher Education Supplemental Loan Authority ("Authority"), a component unit of the State of Connecticut, as of and for the years ended June 30, 2006 and 2005, and have issued our report thereon dated September 9, 2006. We conducted our audits 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.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audits, we considered the Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the basic financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the Authority's basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of basic financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audits, 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*.

This report is intended solely for the information and use of the board of directors and management of the Authority and the State of Connecticut Office of the Comptroller and is not intended to be and should not be used by anyone other than these specified parties.

Rocky Hill, Connecticut
September 9, 2006

CONNECTICUT HIGHER EDUCATION SUPPLEMENTAL LOAN AUTHORITY
COMBINING BALANCE SHEETS
JUNE 30, 2006 AND 2005
(See Independent Auditors' Report on Supplementary Information)

	June 30, 2006				June 30, 2005			
	AUTHORITY OPERATING	BOND FUNDS			AUTHORITY OPERATING	BOND FUNDS		
ASSETS	FUND	PRE 2003	2003	TOTAL	FUND	PRE 2003	2003	TOTAL
CURRENT ASSETS								
Unrestricted assets:								
Cash and cash equivalents	1,880,511	$ -	$ -	$ 1,880,511	$ 1,545,601	$ -	$ -	$ 1,545,601
Current portion of loans receivable, net of allowances for loan losses of $2,070,000 in 2006 and $2,300,000 in 2005	-	7,392,367	5,968,084	13,360,451	-	11,138,227	5,819,412	16,957,639
Interest receivable on investments	7,470	69,918	148,724	226,112	3,859	62,606	368,745	435,210
Interest receivable on loans receivable	-	199,264	122,144	321,408	-	260,800	110,018	370,818
Total Unrestricted Assets	1,887,981	7,661,549	6,238,952	15,788,482	1,549,460	11,461,633	6,298,175	19,309,268
Restricted assets:								
Cash and cash equivalents	-	1,176,194	3,977,712	5,153,906	-	3,115,382	3,762,624	6,878,006
Investments	-	7,639,672	19,305,956	26,945,628	-	7,851,535	30,761,558	38,613,093
Connecticut Higher Education Trust	2,154	-	-	2,154	2,085	-	-	2,085
Total Restricted Assets	2,154	8,815,866	23,283,668	32,101,688	2,085	10,966,917	34,524,182	45,493,184
Total Current Assets	1,890,135	16,477,415	29,522,620	47,890,170	1,551,545	22,428,550	40,822,357	64,802,452
NON-CURRENT ASSETS								
Restricted investments	-	1,800,000	5,200,000	7,000,000	-	1,800,000	5,200,000	7,000,000
Loans receivable, net of current portion	-	40,218,003	31,822,400	72,040,403	-	45,141,342	23,657,639	68,798,981
Bond issuance costs, net of accumulated amortization of $3,140,823 in 2006 and $2,786,922 in 2005	1,109,009	309,433	672,241	2,090,683	1,269,905	367,669	807,010	2,444,584
Total Non-Current assets	1,109,009	42,327,436	37,694,641	81,131,086	1,269,905	47,309,011	29,664,649	78,243,565
Total Assets	$ 2,999,144	$ 58,804,851	$ 67,217,261	$ 129,021,256	$ 2,821,450	$ 69,737,561	$ 70,487,006	$ 143,046,017

CONNECTICUT HIGHER EDUCATION SUPPLEMENTAL LOAN AUTHORITY
COMBINING BALANCE SHEETS (CONTINUED)
JUNE 30, 2006 AND 2005
(See Independent Auditors' Report on Supplementary Information)

	June 30, 2006				June 30, 2005			
	AUTHORITY OPERATING	BOND FUNDS			AUTHORITY OPERATING	BOND FUNDS		
LIABILITIES AND NET ASSETS	FUND	PRE 2003	2003	TOTAL	FUND	PRE 2003	2003	TOTAL
CURRENT LIABILITIES								
Current portion of bonds payable	$ -	2,445,000	3,350,324	$ 5,795,324	-	2,100,000	3,125,280	5,225,280
Accounts payable and accrued liabilities	51,885	17,517	20,233	89,635	52,004	18,871	19,645	90,520
Current portion of arbitrage rebate payable	-	117,345	-	117,345	-	154,183	-	154,183
Accrued interest payable	-	334,205	315,740	649,945	-	429,784	593,403	1,023,187
Due to/(from) other funds	(254,383)	(3,905,115)	4,159,498	-	(254,485)	(3,822,984)	4,077,469	-
Current portion of deferred revenue	-	302,205	82,641	384,846	-	352,837	52,547	405,384
Total Current Liabilities	(202,498)	(688,843)	7,928,436	7,037,095	(202,481)	(767,309)	7,868,344	6,898,554
LONG-TERM LIABILITIES								
Bonds payable, net of current portion	-	50,145,000	59,518,204	109,663,204	-	62,125,000	62,868,529	124,993,529
Arbitrage rebate payable, net of current portion	-	47,493	-	47,493	-	130,736	-	130,736
Deferred revenue, net of current portion	-	1,459,666	741,000	2,200,666	-	1,779,426	492,608	2,272,034
Total Long-Term Liabilities	-	51,652,159	60,259,204	111,911,363	-	64,035,162	63,361,137	127,396,299
Total Liabilities	(202,498)	50,963,316	68,187,640	118,948,458	(202,481)	63,267,853	71,229,481	134,294,853
UNRESTRICTED NET ASSETS	3,201,642	7,841,535	(970,379)	10,072,798	3,023,931	6,469,708	(742,475)	8,751,164
TOTAL LIABILITIES AND NET ASSETS	$ 2,999,144	$ 58,804,851	$ 67,217,261	$ 129,021,256	2,821,450	69,737,561	70,487,006	143,046,017

CONNECTICUT HIGHER EDUCATION SUPPLEMENTAL LOAN AUTHORITY
COMBINING STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
JUNE 30, 2006 AND 2005
(See Independent Auditors' Report on Supplementary Information)

	June 30, 2006				June 30, 2005			
	AUTHORITY OPERATING FUND	BOND FUNDS			AUTHORITY OPERATING FUND	BOND FUNDS		
		PRE 2003	2003	TOTAL		PRE 2003	2003	TOTAL
OPERATING REVENUES								
Interest income on investments	$ 111,949	$ 643,418	$ 1,195,316	$ 1,950,683	$ 38,505	$ 772,059	$ 644,816	$ 1,455,380
Interest income on loans receivable	-	4,411,575	1,994,558	6,406,133	-	6,468,163	1,517,814	7,985,977
Administrative fees	740,623	-	-	740,623	697,588	-	-	697,588
Other operating income	-	-	15,822	15,822	-	-	-	-
Total Operating Revenues	852,572	5,054,993	3,205,696	9,113,261	736,093.00	7,240,222	2,162,630	10,138,945
OPERATING EXPENSES								
Interest expense	-	3,029,670	2,618,574	5,648,244	-	3,989,528	1,603,406	5,592,934
Administrative fees	-	351,828	388,795	740,623	-	483,306	214,282	697,588
Loan collection fees	-	378,142	214,498	592,640	-	591,883	164,082	755,965
General and administrative expenses	251,726	7,891	8,963	268,580	256,970	67,968	2,186	327,124
Amortization of bond issuance costs	160,895	58,236	134,770	353,901	221,739	56,495	62,423	340,657
Professional fees	154,470	-	-	154,470	204,088	-	-	204,088
Arbitrage rebate expense	-	117,345	-	117,345	-	154,183	-	154,183
Salaries	107,770	-	-	107,770	98,615	-	-	98,615
Trustee fees	-	30,054	8,000	38,054	-	36,092	8,000	44,092
Provision for loan losses	-	(290,000)	60,000	(230,000)	-	(700,000)	400,000	(300,000)
Total Operating Expenses	674,861	3,683,166	3,433,600	7,791,627	781,412	4,679,455	2,454,379	7,915,246
CHANGE IN NET ASSETS	177,711	1,371,827	(227,904)	1,321,634	(45,319)	2,560,767	(291,749)	2,223,699
NET ASSETS, beginning	3,023,931	6,469,708	(742,475)	8,751,164	3,069,250	3,908,941	(450,726)	6,527,465
NET ASSETS, ending	$ 3,201,642	$ 7,841,535	$ (970,379)	$ 10,072,798	$ 3,023,931	$ 6,469,708	$ (742,475)	$ 8,751,164