2001 ANNUAL REPORT

MARYLAND

PREPAID COLLEGE TRUST

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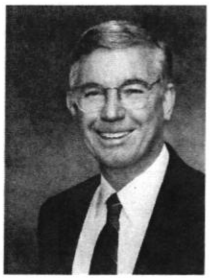
AKING COLLEGE AFFORDABLE FOR MARYLAND AND WASHINGTON D.C. FAMILIES



Parris N. Glendening
Governor

Kathleen Kennedy Townsend
Lt. Governor

Maryland Higher Education Investment Board

Edwin S. Crawford
Board Chair

Susan Buswell

Richard N. Dixon
State Treasurer

Nancy S. Grasmick, Ph.D.
Superintendent of Schools

Richard C. Hackney, Jr.

Karen Johnson
Secretary, Higher Education

Donald C. Linton, CPA/CFP

William Donald Schaefer
State Comptroller

Karl Spain

MARYLAND GUARANTEE LEGISLATIVE

MARYLAND
PREPAID COLLEGE TRUST

September 2001

Dear Maryland and District of Columbia families,

This past year has been another year of record breaking growth for the Maryland Prepaid College Trust. Holding its first enrollment period since Governor Parris N. Glendening and the Maryland General Assembly passed the Maryland legislative guarantee, the Trust again more than doubled in size. Families clearly responded favorably to the new legislative guarantee, with more than 5,500 new applications to the Trust during the past year. There are now more than 8,000 families contributing to more than 10,000 Trust accounts.

The Trust's assets grew substantially as well, from $35 million last year to nearly $70 million as of June 30th. We are very proud of the fact that families have now committed total savings of more than $200 million towards their children and grandchildren's future college education!

This year, we are pleased to announce that the Trust has begun to make tuition payments for its first class of nearly 60 students who are entering college this fall. As expected, these students have chosen to attend a wide variety of colleges - including public and private 2 and 4 year colleges and universities - both in Maryland and across the country.

Probably our most significant accomplishment is that the Trust remains both financially and actuarially sound! As all investors know, this has been a difficult year for the stock market. The Trust began the year with a strong surplus, which allowed the fund to absorb this year's investment loss and even allowed the Trust to retain an actuarial surplus at the end of the year. Families can continue to participate in the Trust with the assurance of sound fiscal management by our Board.

So, we believe you've made a "smart choice" to prepare for future college costs by participating in the Maryland Prepaid College Trust. In the coming year, we encourage you to consider another "smart choice" - the new Maryland College Investment Plan that will open later in 2001. With comparably attractive tax advantages and a variety of features and investment options, participation in both plans can offer an almost unbeatable combination of ways for families to save for all expected future college costs!

Sincerely,

Edwin S. Crawford

Edwin S. Crawford
Board Chair

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Maryland Prepaid College Trust Enrollment Doubles

Participation in the Maryland Prepaid College Trust has grown each enrollment period since our first offering in April of 1998. But never has the growth been as dramatic as it was during the October 2000 – February 2001 enrollment period.

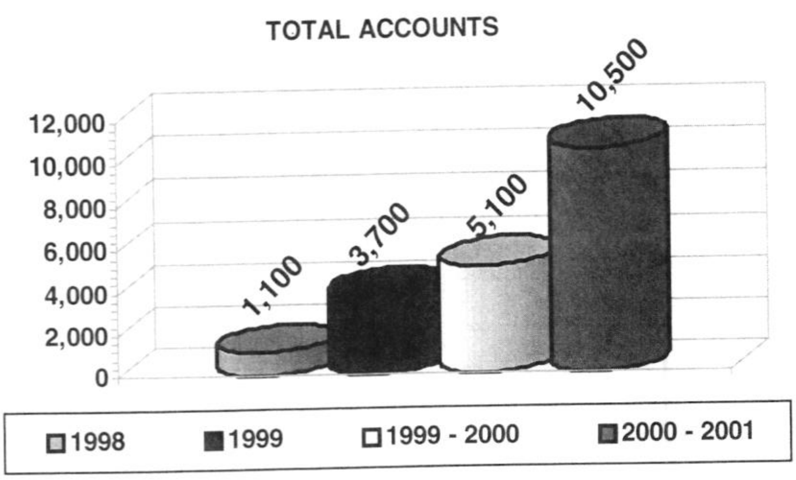
When the last application was delivered to the Trust's offices in early March, the total number of children enrolled had more than doubled, as had the number of families participating in the Trust! The main reason for the tremendous response was the addition of the new Legislative Guarantee, thanks to the Maryland General Assembly and Governor Parris N. Glendening during the 2000 Legislative Session.

Following the Trust's second enrollment period in 1999, a survey was conducted among 5,000 Marylanders who were interested in the Trust, but had not yet enrolled their children or grandchildren. They were asked what one change or improvement could be made that would get them to enroll. The top responses – in reverse order – were:

5. Expand enrollment age
4. Include room and board plans
3. Make the enrollment booklet easier to read
2. Allow the benefits to be used at private or out-of-state colleges…
1. The overwhelming response (by nearly 40 percent of those surveyed) was to add a State guarantee!

Since the survey was conducted, the Trust opened enrollment to 10th graders; allows benefits to be used for room, board, and other eligible college expenses when the child receives a scholarship, grant, or tuition remission; and has greatly improved the readability of the enrollment materials. The Trust has always been available for use at nearly any private or out-of-state college nationwide – and can even be used toward qualified colleges with overseas locations or study abroad programs.

More than 10,000 children can now look forward to attending college using the Trust and receiving either the full in-state tuition and mandatory fees at any Maryland Public College – or the weighted average tuition at nearly any private or out-of-state college nationwide. Their families now have the security of knowing that the Trust's Legislative Guarantee backs the investment. If for any reason, the Trust cannot meet its financial obligations in any academic year; the Governor is mandated to include the difference needed to cover the shortfall in the State's budget. As with all budget items, the General Assembly has final approval.



ONLINE ENROLLMENT PROVES POPULAR

During the October 2000 — February 2001 enrollment period, the Trust added a new feature to help make the application process easier for parents, grandparents and others interested in taking advantage of all the Trust has to offer — online enrollment. Very little was done to publicize this new service, other than the Trust issuing a press release once the system was ready.

It is easy to imagine our surprise when more than a third of the new applications we received for enrollment came in through our web site. And when you factor in another 10 to 15 percent of the enrollment forms we received were printed from the web site, and mailed in — you get an understanding of how important the Internet has quickly become, not only to the Trust, but also to our participants.

In the coming year, the Trust will expand the use of the web to include on-line account access for our participants.

PROFILE OF MARYLAND PREPAID COLLEGE TRUST PARTICIPANTS

Who is a typical Maryland Prepaid College Trust participant? And has the person who is taking advantage of the Trust's benefits changed since 1998?

You could easily say that the people who have opened Prepaid College Trust accounts for their children, grandchildren, nieces, or nephews, etc., share an understanding of the importance of a college education, and the value of locking in to the current cost of college as a hedge against tuition inflation. Those participants who are also Maryland taxpayers value the State tax benefits the Trust offers. The following charts provide a snapshot of who is taking advantage of the Trust and the benefits it offers:

COUNTY OF RESIDENCY – BY ENROLLMENT PERIOD

	00/01	99/00	99	98
◆ MONTGOMERY COUNTY	24%	26%	26%	32%
◆ BALTIMORE COUNTY	13%	12%	13%	12%
◆ HOWARD	11%	11%	10%	8%
◆ PRINCE GEORGE'S	11%	12%	12%	13%
◆ ANNE ARUNDEL	10%	10%	10%	13%
◆ SOUTHERN MD	5%	6%	6%	5%
◆ BALTIMORE CITY	5%	4%	5%	4%
◆ FREDERICK	5%	5%	4%	3%
◆ HARFORD	5%	4%	3%	3%
◆ EASTERN SHORE	4%	5%	6%	3%
◆ CARROLL	3%	2%	2%	2%
◆ WESTERN MD	2%	1%	2%	1%
◆ DISTRICT OF COLUMBIA*	1%	1%	N/A	N/A
◆ OUTSIDE MARYLAND	1%	1%	1%	1%

* *The Trust was not open to DC residents until the 99—00 enrollment period*

Household Income

	00/01	99/00	99	98
◆ $150,000 plus	15%	13%	12%	N/A
◆ $100,000 - 150,000	30%	26%	23%	27%
◆ $ 80,000 - 100,000	21%	20%	19%	24%
◆ $ 60,000 - 80,000	16%	18%	20%	20%
◆ $ 40,000 - 60,000	12%	13%	16%	18%
◆ $ 20,000 - 40,000	5%	9%	9%	10%
◆ $ 0 - 20,000	1%	1%	1%	1%

Participants by Race vs. US Census/Maryland

Race	00/01	99/00	99	98	State
◆ White	72%	68%	73%	69%	64%
◆ African American	17%	19%	18%	20%	28%
◆ Asian	5%	7%	5%	6%	4%
◆ Hispanic	2%	2%	1%	2%	4%
◆ Multi-Cultural	2%	3%	1%	1%	N/A
◆ Native American	0.1%	0%	0%	0%	0.3%
◆ Other / No Response	1.9%	1%	2%	2%	0.1%

Grade or Age of Beneficiary

While the percentage of children enrolled at infant and pre-school age is rising, most children are enrolled while in the 4th – 7th grades

	00/01	99/00	99	98
◆ Infant - 4 years old	24%	21%	21%	19%
◆ Kindergarten - 3rd Grade	27%	27%	24%	25%
◆ 4th Grade - 7th Grade	33%	35%	33%	33%
◆ 8th Grade - 10th Grade	16%	17%	22%	23%

The Maryland Prepaid College Trust Class of 2001

The Trust is pleased to announce that it is now paying benefits for its first class of college bound students, the 59 students in the Class of 2001. As of September 1, 2001, 81 percent (48) have informed us that they will be attending college this fall. Seventy-five percent of those attending college plan to attend one of Maryland's public colleges, 21 percent will attend private colleges, and 4 percent are going to out-of-state public colleges. Approximately 10 percent of the Class of 2001 is opting to delay the use of their benefits until a future year. These students have ten years – or until 2011 – to start using their benefits.

The number one Maryland public college selected is the University of Maryland College Park, followed by Towson University, Frostburg State University, and Anne Arundel Community College. Morgan State University, Howard Community College, and Prince George's Community College will have two Trust students each matriculating this fall; while Frederick Community College, Montgomery College, and Salisbury State University will each have one Trust student. These students will have their full in-state tuition and mandatory fees paid by the Trust — or — payments made towards their room & board, books, or other eligible college expenses if they receive scholarships, grants, or tuition remission.

The out-of-state public colleges include the University of Virginia and George Mason University. The private colleges selected include one in Maryland, with the rest in Pennsylvania, Virginia, North Carolina, New York, New Jersey, Massachusetts, Tennessee, and Texas. These students will receive this year's weighted average tuition of Maryland's public colleges - $4,954 - towards their college tuition.

New Federal Tax Benefits

The Maryland Prepaid College Trust and its participants received some extremely welcomed news in May, when President George W. Bush signed the Economic Growth and Tax Reconciliation Act of 2001 into law. Effective on January 1, 2002, earnings from the Trust will be tax-free at the federal level when used for eligible college expenses. Currently, there is a federal tax imposed on the earnings distributed, but at the child's tax rate. The Trust already provides Maryland taxpayers with tax-free earnings at the State level when used for college, as well as a State income deduction for Trust payments.

This is tremendous news for parents, grandparents, and everyone who wants to save for a future college education. When you team Maryland's existing tax incentives with the new federal incentives and add in the State Legislative Guarantee, the Maryland Prepaid College Trust is an excellent choice to save for a child's future college education.

The good news contained in the new legislation also includes several other significant enhancements:

- Providing for a rollover to the same beneficiary once every 12 months between Section 529 plans — qualified state tuition plans. Previously, all rollovers had to include a change of beneficiary,
- Adding first cousins to the list of family members for account transfers, and
- Removing the penalty for investing in both an Education IRA and a qualified state tuition plan in the same year for the same child.

The new tax bill, unfortunately, also included a sunset provision on the federal tax-free treatment of earnings. Unless Congress takes further action, the tax-free clause for earnings on qualified college savings plans will expire on December 31, 2010.

WHAT'S AHEAD
MARYLAND COLLEGE INVESTMENT PLAN TO BE MANAGED BY T. ROWE PRICE

You may recall that during the 2000 legislative session, the Maryland General Assembly and Governor Glendening provided the Board with the framework to begin building the new Maryland College Investment Plan. In July 2001, the Maryland Board of Public Works approved a contract between the Maryland Higher Education Investment Board and T. Rowe Price Associates, Inc., paving the way to launch the new plan.

Starting later this year, under the umbrella of the College Savings Plans of Maryland, the State will offer two Section 529 plans: the Maryland Prepaid College Trust and the new Maryland College Investment Plan.

"We are excited about working with T. Rowe Price to develop our new Maryland College Investment Plan," said Edwin S. Crawford, Chairman of the Maryland Higher Education Investment Board, which oversees both plans. "The Board is very pleased to be working with a Maryland based investment management firm to manage Maryland's new Investment Plan."

"T. Rowe Price has a long-standing commitment to the economic future of Maryland and its citizens," said T. Rowe Price Vice Chairman James Riepe. "We appreciate the tremendous responsibility to manage these assets prudently and are pleased to be able to assist people in making one of the most important investments they can — in their children's higher education."

Thomas Rowe Price, Jr, founded the Baltimore-based asset management firm in 1937. Today, it is one of the nation's leading providers of no-load mutual funds for individual investors and corporate retirement programs.

By combining both plans under the umbrella of the College Savings Plans of Maryland, families saving for college will have the ability to choose the savings strategy that best fits their savings goals. Some parents and grandparents will choose to save using the Prepaid College Trust, because they are locking in payments based on the current cost of Maryland's public colleges. Others might be interested in being able to save at their own pace for all qualified college expenses, as will be offered by the new College Investment Plan. But with the College Savings Plans of Maryland, you will have a third choice as well. A smart choice might very well be to use both plans to save for college — the Prepaid College Trust for tuition and mandatory fees and the College Investment Plan for the other costs, such as additional tuition costs at a private or out-of-state colleges, room and board, books, etc. And by choosing both, if you are a Maryland State taxpayer, you could increase the amount of your State income deduction.

Not All 529 Plans Created Equal – Only Maryland Plans Provide Maryland Tax Benefits!

The College Savings Plans of Maryland cautions Maryland residents who have invested, or are considering investing in a college savings plan offered by a state other than Maryland or a plan offered by a broker or dealer representing a financial management firm "selling" college savings plans to be sure the investment is what you think it is!

Over the past 12 months, the college savings plan landscape has become very crowded. Today it is possible to have representatives trying to sell you one of more than a dozen different Section 529 plans, or your insurance agent selling universal life insurance policies designed to help pay for college. There are Uniform Gifts to Minors Act, Uniform Transfers to Minors Act, and even Education IRAs. Many claim to offer the best investment opportunities. Some even offer significant tax benefits. It is no wonder that the Trust receives daily telephone calls from parents and grandparents who are completely confused as to what they should do about saving for college. And this may be just the tip of the iceberg! Soon each state and the District of Columbia will be offering some form of Section 529-college savings plan.

Both the Maryland Prepaid College Trust and the new Maryland College Investment Plan, the two plans offered under the College Savings Plans of Maryland, are Section 529 plans. 529 plans are named after the section of the Internal Revenue Code that allows states to setup and manage tax deferred college savings plans. All 529 plans, whether a prepaid plan or a savings plan, offer the same federal tax benefits. However, only the two 529 plans offered under the College Savings Plans of Maryland umbrella provide Maryland State tax benefits for Maryland taxpayers!

Maryland residents are eligible to receive up to a $2,500 deduction each year from their State income for each contract they purchase in the Maryland Prepaid College Trust. In time, by carrying any balance forward, they are able to deduct the amount equal to their total payments from their Maryland State income. The Maryland College Investment Plan also provides a deduction from Maryland State income of up to $2,500 annually for each account opened in the Investment Plan. Account contributions above $2,500 may be carried forward and deducted for up to 10 years after the contribution is made. Also for Maryland residents, the earnings from either plan are tax-exempt when used to pay for eligible college expenses.

Remember that only investors in the Maryland Prepaid College Trust and Maryland College Investment Plan receive Maryland State Tax Benefits. If as a Maryland taxpayer you invest in a Section 529 plan offered by any other state or investment company on behalf of another state – not only do you not receive the Maryland income deduction, but you will be subject to full taxation by the State of Maryland on the earnings when these funds are used to pay for college, or are withdrawn for any other reason.

Executive Summary

Adequacy of Trust

The Trust is actuarially sound; this means the expected value of the assets exceeds the expected value of liabilities. The assumptions used to project the actuarial status of the Trust are those set by the Board. The significant results are shown below:

Present value of June 30, 2001 **(Thousands)**

Assets		
	Investments	$68,511
	Future Contract Payments	87,520
	Other	515
Total Assets		$156,546
Liabilities and Actuarial Reserves		
	Future Contract Benefits and other expenses	$155,308
	Other Liabilities	1,185
	Actuarial Reserve	53
Total Liabilities and Reserves		$156,546

Assumptions

- Yield on Investments – 7.65%
- The Trust is exempt from federal taxes.
- Future Tuition Increases – 5.0% per annum
- Future Mandatory Fee Increases – 10.0% per annum

Expected Cash Flows

Cash flows to the Trust are expected to be positive through fiscal year 2008 and negative from 2009 until 2023 and positive from then until liabilities are satisfied. A positive cash flow occurs when contract payments and investment income exceed tuition and mandatory fee payments. When negative cash flows occur, asset sales will provide the necessary cash.

Investment Strategy

The investment policy of the Trust is designed to enable the Board to meet the actuarially determined Program liabilities. The purpose of the Board's Comprehensive Investment Plan is to meet the projected future liabilities.

The Board has selected the Vanguard Groups Institutional Fund to invest the equity portion of the Trust's assets. The fixed income portion of the Trust's assets is invested in the Summit Limited Term Bond Fund at T. Rowe Price.

PRICEWATERHOUSECOOPERS

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gust 24, 2001

. Edwin S. Crawford, Chairman
ıryland Prepaid College Trust
7 East Redwood Street
ite 2050
ltimore, Maryland 21202

ar Mr. Crawford:

:hard M. Kaye & Associates in conjunction with PricewaterhouseCoopers LLP (PwC) has formed an actuarial valuation of the Maryland Prepaid College Trust as of the June 30, 2001 . e valuation compares the value of the assets of the program to the value of expected future ion payments to beneficiaries. The following pages summarize the actuarial valuation of the st fund as of June 30, 2001.

omparison of the assets and liabilities of the trust fund shows that as of June 30, 2001 there is ırplus of $52,576.

e actuarial valuation was performed based upon generally accepted actuarial principles, and s were performed as considered necessary to ensure the accuracy of the results. We certify t the amounts presented in the following pages have been appropriately determined according he actuarial assumptions stated herein.

spectfully submitted,

cewaterhouseCoopers LLP

:hard M. Kaye

hard M. Kaye
hard M. Kaye & Associates
nsultant to PricewaterhouseCoopers LLP

T. Devereux, FCAS, MAAA
ipal Consultant, PricewaterhouseCoopers LLP

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Report of Independent Auditors

To the Maryland Higher Education
Investment Board

We have audited the accompanying balance sheet of the Maryland Prepaid College Trust (the Trust), as of June 30, 2001, and the related statements of revenues, expenses and changes in retained earnings and cash flows for the year then ended. These financial statements are the responsibility of the Trust's management. 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Maryland Prepaid College Trust, as of June 30, 2001, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States.

We have not audited the other data included in this Annual Report and, accordingly, we express no opinion thereon.

Ernst & Young LLP

August 10, 2001

MARYLAND PREPAID COLLEGE TRUST

Balance Sheet
As of June 30, 2001

ASSETS	
Cash and cash equivalents	$28,881,862
Investments, at fair value	39,629,233
Tuition contracts receivable	87,520,125
Fixed assets, net	514,615
TOTAL ASSETS	$156,545,835
LIABILITIES AND RETAINED EARNINGS	
Accounts payable and accrued expenses	$101,808
Due to Primary Government	85,936
Current portion of:	
Software license fee payable	165,060
Loans payable to Maryland Higher Education Commission	130,000
Long Term portion of:	
Software license fee payable	165,060
Loans payable to Maryland Higher Education Commission	490,000
Accrued tuition benefits payable	155,308,004
Other liabilities	47,391
TOTAL LIABILITIES	156,493,259
Retained earnings	52,576
TOTAL LIABILITIES AND RETAINED EARNINGS	$156,545,835

See accompanying notes to financial statements

Statement of Revenues, Expenses and Changes in Retained Earnings
For the Fiscal Year Ended June 30, 2001

Revenues:	
Tuition contracts	$80,406,18
Application and other fees	498,91
Total Revenues	80,905,10
Operating Expenses:	
Salaries, wages and benefits	435,41
Technical and special fees	95,04
Communication	101,12
Travel	11,12
Marketing	545,94
Contractual Services	224,90
Supplies	15,34
Equipment	55,69
Fixed Charges	47,87
Depreciation	112,78
Other Expenses	445,48
Tuition benefits	79,130,67
Total Operating Expenses	81,221,42
Operating Loss	(316,32
Non-operating income:	
Grant from Maryland Higher Education Commission	370,00
Unrealized net loss on investments	(4,767,85
Investment income	1,014,72
Total non-operating income (loss)	(3,383,13
Net Loss	(3,699,45
Retained Earnings, Beginning of Year	3,752,03
Retained Earnings, End of Year	$52,57

See accompanying notes to financial statements

Statement of Cash Flows
For the Fiscal Year Ended June 30, 2001

Operating loss	($316,320)
Adjustments to reconcile operating loss to Net Cash Provided by Operating Activities:	
Depreciation	112,782
Changes in assets and liabilities:	
Increase in accounts payable	22,493
Increase in software license fee payable	330,120
Increase in due to primary government	85,936
Increase in other liabilities	20,726
Increase in tuition contracts receivable	(41,732,179)
Increase in accrued tuition benefits payable	78,670,361
Net cash provided by operating activities	37,193,919
Cash Flows from Investing Activities:	
Investment income	1,014,721
Purchase of fixed assets	(621,151)
Purchase of investments	(10,212,000)
Net cash used by investing activities	(9,818,430)
Cash Flows from Non-capital Financing Activities:	
Proceeds from Grant from Maryland Higher Education Commission	370,000
Net cash provided by non-capital financing activities	370,000
Net Increase in cash and cash equivalents	27,429,168
Cash and cash equivalents, Beginning of Year	1,452,694
Cash and cash equivalents, End of Year	$28,881,862
Non-cash Transactions:	
Unrealized loss on investments	($4,767,855)

See accompanying notes to financial statements

1. ORGANIZATION AND PURPOSE

The purpose of the Maryland Prepaid College Trust (the Trust) is to provide a simple and convenient way for Maryland families to save in advance for a college education. It provides for the payment of tuition and mandatory fees based in part on these costs at Maryland public colleges and universities. A purchaser enters into a contract for the future payment of tuition and fees for a designated beneficiary. When the beneficiary enrolls in college, the Trust will pay the contract benefits. Following graduation from high school, the beneficiary has ten years plus the number of years purchased to use the contract benefits. This time period may be extended by any time served in active military duty. The contract benefits are based on resident rates for Maryland public colleges and universities, but can be used towards these costs at any accredited, non-profit, degree granting, private or out-of-state college or university.

The Maryland General Assembly created the Trust during the 1997 legislative session. The program is an independent agency of the State of Maryland, authorized by the Maryland Code Annotated Education Article, Section 18, Subtitle 19. The Maryland Higher Education Investment Board (the Board) directs the Trust. The Board consists of nine members; four of which are ex-officio members. The ex-officio members are the Comptroller, the Treasurer, the Secretary of the Maryland Higher Education Commission, and the State Superintendent of Schools. The five remaining members are public members appointed by the Governor.

The Trust is an independent state agency, but, by law, its funds are not considered moneys of the State and may not be deposited into the Treasury. Funds remaining in the Program at the end of any fiscal year remain in the Trust rather than reverting to the State General Fund.

Legislation passed in 2000 established an additional financial guarantee that requires the Governor to include in his budget, the amount of any shortfall of Trust's assets to pay current contract liabilities. Legislation passed in 1998 and 1999 established tax incentives for Maryland residents participating in the Trust. All contributions to the Trust can be deducted from Maryland State income at a rate of up to $2,500 for each contract annually. Earnings on those payments are exempt from Maryland taxes when used for qualified expenses of college. Contributions grow on a tax-deferred basis at the federal level while in the Trust.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The activities operated by the Trust are accounted for in an enterprise fund. Such funds focus on the flow of economic resources, which, together with the maintenance of equity, is an important financial indicator. Therefore, the accompanying financial statements have been prepared on the accrual basis of accounting whereby revenues are recorded when earned and expenses are recorded when incurred.

As permitted by Governmental Accounting Standards Board (GASB) Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting, the Trust has elected not to adopt Financial Accounting Standards Board (FASB) statements and interpretations issued after November 30, 1989, unless GASB specifically adopts such FASB statements or interpretations.

Investments

Investments are stated at fair value as provided in GASB Statement No. 31. Unrealized appreciation on investments due to changes in fair value is recognized in the Trust's operations each year.

Fixed Assets

Fixed assets are stated at cost less accumulated depreciation. Fixed assets are depreciated on a straight-line basis over the following useful lives:

Computers	3 years
Furniture	10 years
Equipment	5 years
Software	3 years
Perpetual Software License	7 years

Compensated Absences

The Trust accrues for obligations that may arise in connection with compensated absences for annual leave and eligible sick leave at the current rate of employee pay. Employees fully vested in all earned but unused annual leave, up to maximum of 400 hours, are eligible to receive compensation, at the current rate of employee pay, on termination of State employment. In accordance with state personnel policies, eligible employees may participate in the Sick Leave Incentive Program. This Program permits payments for up to 56 hours of unused sick leave, per calendar year, for employees who used no more than 24 hours of sick leave during that calendar year and have a sick leave balance of at least 240 hours on December 31 of that year. The Trust also permits payments for up to 40 hours of unused sick leave, per calendar year, for employees who used no more that 40 hours of sick leave during the calendar year and have a sick leave balance of at least 240 hours on December 31 of that calendar year.

Risk Management

The Trust is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to and illness of employees; and natural disasters. The Trust participates in the State's various self-insurance programs. The State is self-insured for general liability, property and casualty, workers compensation, environmental and anti-trust liabilities and certain employee health benefits.

The State allocates the cost of providing claims servicing and claims payment by charging a premium to the Trust based on a percentage of the Trust's estimated current-year payroll or based on the average loss experienced by the Trust. This charge considers recent trends in actual claims experience of the State as a whole and makes provisions for catastrophic losses.

3. DEPOSITS AND INVESTMENTS

Cash and cash equivalents consist of amounts maintained in a bank account controlled by the Trust, pooled cash maintained by the State Treasurer and overnight investments with original maturities of 90 days or less. Cash deposits of the Trust are made in accordance with the Annotated Code of Maryland, which requires depositories to give security in the form of collateral as provided in the Code, for the safekeeping, when required, of these deposits.

As of June 30, 2001, the carrying amount of the Trust's cash and cash equivalents was $28,881,862 and the bank balance totaled $28,980,749. Of the bank balances $81,100 represents deposits covered by federal depository insurance and $28,899,649 represents repurchase agreements categorized as uninsured and unregistered, (with securities held by the pledging financial institution's agent but not in the Trust's name).

The Trust's comprehensive investment plan (the Plan), authorized by the Annotated Code of Maryland, allows the Trust to purchase investments including domestic equities, intermediate term investment grade bonds, and other governmental agency instruments, as well as money market deposits based on the Plan's specified portfolio allocation.

The investment plan adopted by the Board specifies the portfolio allocation, which considers the investment safety and liquidity to characteristics while aiming for the specified yield targets of the Trust.

The Trust's investments, excluding repurchase agreements treated as cash equivalents, as of June 30, 2001 are not subject to classification by credit risk because the Trust owns units rather than specific securities, which by their nature are not subject to risk categorization. All such investments are in mutual fund shares stated at fair value based upon quoted market prices.

At year-end, the Trust's investment balances in mutual funds were as follows:

	Cost	Fair Value	Unrealized Gain (Loss)
Common Stock Funds	$ 33,931,952	$ 31,114,901	$(2,817,051)
Bond Funds	8,381,439	8,514,332	132,893
	$ 42,313,391	$ 39,629,233	$ (2,684,158)

4. FIXED ASSETS

As of June 30, 2001, fixed assets consist of the following:

Computers	$ 81,149
Furniture	9,540
Equipment	10,076
Software	52,621
Perpetual Software License	495,180
Total	648,566
Less: Accumulated depreciation	133,951
Fixed assets, net of accumulated deprecation	$ 514,615

5. LOANS PAYABLE

In fiscal year 2000, the Trust was granted a loan of $250,000 from the Maryland Higher Education Commission (MHEC). Additionally in fiscal year 1999, the Trust was granted and received loans totaling $400,000, of which $30,000 has been repaid. The loans are non-interest bearing. During the 2000 legislative session, the General Assembly included a provision in the annual budget bill, which permits the Trust to delay its outstanding loan repayments until the Trust is financially self-sufficient.

6. LICENSE FEE PAYABLE

In fiscal year 2001, the Trust entered into an agreement to fund the perpetual software license fee purchased from SCT Software Resource and Management Corporation. This agreement requires payments in the amount of $165,060 to be made July 1st of each of the next two fiscal years.

7. PENSION AND POSTRETIREMENT BENEFITS

Eligible employees of the Trust, as employees of the State, are covered under the retirement plans of the State Retirement and Pension System of Maryland (the System) and are also entitled to certain healthcare benefits upon retirement. This system is a cost sharing multiple-employer defined benefit pension plan administered by the System Board of Trustees in accordance with Article 73 B of the Annotated Code of Maryland. Eligible employees are required to contribute to the System a fixed percentage of their regular salaries and wages, which exceed the Social Security wage base, and the Trust is required to make contributions to the System based on actuarial valuations. The contribution requirements of eligible employees and the Trust are established and may be amended by the System Board of Trustees. The Trust's only liability for retirement and post employment benefits is its required annual contribution, which it has fully funded during the years ended June 30, 2001, 2000, 1999 and 1998. These contributions amounted to $20,068, $23,691, $19,534 and $6,118 for the years ended June 30, 2001, 2000, 1999 and 1998, respectively. The System prepares a separate audited Comprehensive Annual Financial Report, which can be obtained from the State Retirement and Pension System of Maryland, 120 East Baltimore Street, Baltimore, Maryland 21202.

8. TAX EXEMPT STATUS

The Trust is exempt from federal taxation in accordance with Section 529 if the Internal Revenue Code. Additionally, the Trust is exempt from state and Local taxation in accordance with Senate Bill 232, which established the Trust.

9. ACCRUED TUITION BENEFITS

The Trust's consulting actuary independently determines the Program's actuarial present value of future contract tuition benefits payments. The actuarial calculation is based on the present value of estimated tuition benefit payments made from the Trust, which includes assumptions for future tuition and mandatory fee increases and contract terminations that are determined by the Board and its actuaries.

The significant assumptions used for this calculation are discussed below:

Tuition and Mandatory Fee Increases The Weighted Average Tuition (WAT) for universities and community colleges is projected to increase 5% and 10% per annum for tuition and mandatory fees respectively, based on historical data.

Investment Return The actuarial valuation of the Trust Fund was determined using an assumed 7.65% rate of return on investments. It is further assumed that the Trust fund is exempt from federal income tax.

Enrollment of Beneficiaries It is assumed that beneficiaries will attend college full-time commencing with their expected matriculation date. Contract beneficiaries are assumed to attend the various colleges and universities in the same proportion as the headcount information that was used to determine the 1999-2000 WAT with a 6% bias load added.

Bias Load The assumed bias load is 6% and is based on a credibility weighted average of the mix of current enrollment statistics and a disproportionate number of beneficiaries attending more expensive schools. The credibility factor is based on the number of contracts sold and the sales figures needed for full credibility.

Death and Disabilities Mortality rates for beneficiaries are assumed to follow the 1990 U.S. Life Tables.

10. SUBSEQUENT EVENTS

On July 11, 2001, the Maryland Higher Education Investment Board entered into an agreement with T. Rowe Price to provide a complementary savings product to individuals seeking to save for the future cost of higher education. This product will be designed to comply with Section 529 of the Internal Revenue Code. Individuals will be permitted to contribute up to $175,000 for the benefit of a single beneficiary. The following investment options will be offered as part of this new product: age-based portfolios, a balanced portfolio, a 100% equity portfolio and a 100% fixed income portfolio. Individuals will be permitted to open multiple accounts for a single beneficiary.

MARYLAND GUARANTEE LEGISLATIVE
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