

**Alabama Prepaid Affordable College
Tuition Program**

Montgomery, Alabama

**Financial Statements
and Supplementary Information**

September 30, 2022

Alabama Prepaid Affordable College Tuition Program
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Independent Auditor's Report

The Board of Trustees
Alabama Prepaid Affordable College Tuition Program
Montgomery, Alabama

Opinion

We have audited the accompanying financial statements of the Alabama Prepaid Affordable College Tuition Program (the "PACT Program"), a program of the Wallace-Folsom Savings Investment Plan and a private-purpose trust fund of the State of Alabama, which are comprised of the statement of fiduciary net position and statement of changes in fiduciary net position as of and for the year ended September 30, 2022, and the related notes to the financial statements, which collectively comprise the PACT Program's basic financial statements as listed in the table of contents.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the PACT Program, as of September 30, 2022, and the changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the PACT Program, and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the Alabama Prepaid Affordable College Tuition Program, a private-purpose trust fund, and do not purport to, and do not present fairly the financial position of the State of Alabama as of September 30, 2022, the changes in its financial position, or where applicable, its cash flows, for the year ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Kassouf & Co., P.C.

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Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the PACT Program's ability to continue as a going concern for twelve months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with generally accepted auditing standards, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 PACT Program's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the PACT Program's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the schedule of funding progress be presented to supplement the basic financial statements. Such information is the responsibility of management and, 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.

Supplementary Information

Our audit was conducted for the purpose of forming opinion on the financial statements that collectively comprise the PACT Program's basic financial statements. The combining schedule of fiduciary net position and the combining schedule of changes in fiduciary net position are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such 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. The 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 schedule of fiduciary net position and the combining schedule of changes in fiduciary net position 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 February 8, 2023, on our consideration of the PACT Program's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is solely 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 effectiveness of internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Governmental Auditing Standards* in considering the PACT Program's internal control over financial reporting and compliance.

KASSOUF & CO., P.C.



Certified Public Accountants

February 8, 2023

**Alabama Prepaid Affordable College Tuition Program
Management's Discussion and Analysis
September 30, 2022**

The following discussion is designed to provide an understanding of various factors related to the Alabama Prepaid Affordable College Tuition Program's (the "PACT Program") operations and financial condition. This information should be read in conjunction with the financial statements and related notes. The purpose of this information is to focus on significant changes in the financial condition during the fiscal year ended September 30, 2022 and highlight events that occurred during the year.

The statement of fiduciary net position presents information on the PACT Program's cash and investments, accounts payable and accrued liabilities, and net position at the end of the fiscal year. Assets less liabilities result in the net position at the end of the fiscal year.

The statement of changes in fiduciary net position reports all additions and deductions of the PACT Program's recent fiscal year. Additions minus deductions provide the change in fiduciary net position for the fiscal year.

The notes to the financial statements include the program descriptions, a summary of significant accounting policies, credit risk disclosures for cash and investments, concentration of investments disclosures, and additional actuarial information relevant to the latest actuarial valuations.

The required supplementary information following the notes to the financial statements includes the schedule of funding progress, combining schedule of fiduciary net position, and the combining schedule of changes in fiduciary net position.

The PACT Program is classified as a fiduciary fund in the State of Alabama Annual Comprehensive Financial Report (ACFR).

Assets

The assets of the PACT Program include cash, receivables, investments, and other assets. Assets were \$254,191,365 and \$90,337,807 as of September 30, 2022 and 2021, respectively. The increase was primarily due to Education Trust Fund appropriation payments in the amount of \$209,555,200.

The composition of the PACT Program's investment securities portfolio reflects the Board's investment strategy to preserve capital by minimizing the probability of loss of principal over its investment horizon while maintaining an appropriate level of liquidity to meet tuition benefit obligations. The adopted asset allocation as of September 30, 2022 is 79% Short Duration Fixed and 21% cash and cash equivalents.

**Alabama Prepaid Affordable College Tuition Program
Management’s Discussion and Analysis – Continued
September 30, 2022**

The following table represents the PACT Program’s investment portfolio and asset allocation as of September 30, 2022. Positions in various equity accounts totaling less than 0.01% of total assets are comprised of values remaining after liquidation, many of which are liabilities contingent on corporate action, the value of which (if any) cannot be immediately realized.

Asset Category	Market Value	Percent
Fixed Income	\$ 200,576,032	78.9%
Cash/Cash Equivalents	53,615,333	21.1%

Liabilities

Liabilities of the PACT Program consist of payables and accruals. Liabilities were \$7,587,457 and \$7,935,373 at September 30, 2022 and 2021, respectively. The decrease in liabilities was primarily due to the decrease of tuition benefits, timing of payments paid and invoicing at the end of the fiscal year.

Additions

Additions totaled \$208,206,926 and \$32,355,677 for fiscal years ended September 30, 2022 and 2021, respectively, representing a 543.49% increase. The increase primarily is due to the prepayment of monies from the Education Trust Fund of fiscal years 2023-2027 in the aggregate amount of \$177,373,600. No additional transfers from the Education Trust Fund are expected to be received over the remaining life of the PACT Program. Contract payments decreased by \$125,100 to \$209,679 from \$334,779 fiscal year over fiscal year due to the continued reduction of monthly payments received on contracts not paid in full. The reduction in net investment income of \$2,441,039 is a result of unrealized losses incurred in the current fiscal year due to rising interest rate environment compared to an unrealized loss of \$127,759 for the prior fiscal year.

Deductions

Deductions totaled \$44,005,451 and \$43,423,555 for fiscal years ending September 30, 2022 and 2021, respectively. Deductions include salaries, professional services, contract cancellation refunds, and benefits paid to colleges and universities. The largest deduction from the PACT Program is the amount of monies paid to the colleges and universities for tuition and qualified fees.

For fiscal year ending 2022, the PACT Program paid \$40.7 million to 358 colleges and universities across the nation for 4,574 beneficiaries, as compared to \$40.8 million paid in the fiscal year ending 2021 for approximately 5,389 beneficiaries.

**Alabama Prepaid Affordable College Tuition Program
Management's Discussion and Analysis – Continued
September 30, 2022**

Summary

According to the actuarial report for fiscal year ending 2022, the PACT Program had assets of \$238.6 million. Dividing the assets of \$238.6 million by the actuarial present value of future tuition benefit payments and administrative costs of \$129.8 million, results in an actuarial funded status of 179.8%. This is an increase from the 2021 actuarial funded status of 119.4% due primarily to the prepayment of all remaining future Education Trust Fund appropriations.

Actuarial assumptions are reviewed and approved by the Board annually to reflect expected results believed to be realistic based on terms of the settlement, historical information, economic data, and expert guidance. The 2022 Actuarial Report is available at www.treasury.alabama.gov. The report should be read in its entirety in conjunction with the financial statements so that projections can be properly interpreted.

During 2014, the PACT Program established a reserve for administrative costs within the PACT trust fund. Approximately \$12.9 million was allocated for the purpose of paying future administrative cost of the PACT Program effective October 2014. Any unexpended funds allocated for administrative expenses will remain available for payment of future PACT Program benefits. During fiscal year 2022, \$415,000 was transferred from the Trust Fund to cover administrative costs. The cumulative total of transfers from the Trust Fund to cover administrative costs is approximately \$3.1 million as of September 30, 2022.

During 2022, the PACT Program Board of Directors approved a 24% increase to the current rate paid by the PACT Program for benefit payments. This increase was effective fall semester 2022. Under the 2011 Class action Settlement Agreement, PACT is required to pay tuition and qualified fees at the fall 2010 rates as certified by each respective Alabama public eligible educational institution. The agreement was negotiated to allow for an increase in benefit payments if the actuarial condition of the PACT Program improves. The first increase of 3% was made in 2015 followed by a 6% increase in 2016, 8% increase in 2017, 7% increase in 2018, 7% increase in 2019, 7% increase in 2020, 10% increase in 2021, and a 24% increase in 2022, compounded.

**Alabama Prepaid Affordable College Tuition Program
Management’s Discussion and Analysis – Continued
September 30, 2022**

Economic Factors and Fiscal Year 2023 Budget

Economic conditions for the PACT Program remain stable in the current environment.

- The PACT Program relies on the State of Alabama appropriation to fund its activities. The primary source of funding is the transfer from the Education Trust Fund, which comprised 99% of additions in the fiscal year 2022. During 2022, the State of Alabama prefunded the remaining Education Trust Fund appropriations of \$177,373,600. There are no additional projected transfers from the Education Trust Fund.
- The 2023 actuarial projected payment for tuition and qualified fees to colleges and universities from the PACT Program is projected to be \$38,900,000.
- Administrative costs are funded from the reserve established in 2014.

Requests for Information

This financial report is designed to provide a general overview of the PACT Program’s finances for all those with an interest in the PACT Program’s activities and finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Office of State Treasurer at the Alabama State Capital, 600 Dexter Avenue, Room S-106, Montgomery, Alabama 36104.

Alabama Prepaid Affordable College Tuition Program
Statement of Fiduciary Net Position
September 30, 2022

Assets

Cash and cash equivalents	\$ 53,615,333
Investments	200,576,032
Total Assets	<u>254,191,365</u>

Liabilities

Accounts payable	7,504,979
Accrued liabilities	82,478
Total Liabilities	<u>7,587,457</u>

Net Position

Held in trust for tuition payments and other purposes	<u><u>\$ 246,603,908</u></u>
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See accompanying notes.

Alabama Prepaid Affordable College Tuition Program
Statement of Changes in Fiduciary Net Position
For the Year Ended September 30, 2022

Additions	
Contract income	\$ 209,679
Investment Earnings	
Interest and dividend income	773,300
Loss on investments	(2,441,039)
Net investment loss	<u>(1,667,739)</u>
Other income	109,786
Transfers from other funds	209,555,200
Total Additions	<u>208,206,926</u>
Deductions	
Tuition benefits	40,705,895
Salaries and other administrative expenses	449,883
Professional services	120,313
Cancellation refunds	2,729,360
Total Deductions	<u>44,005,451</u>
Changes in Net Position	164,201,475
Net Position at Beginning of Year	82,402,433
Net Position at End of Year	<u>\$ 246,603,908</u>

See accompanying notes.

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements
September 30, 2022

Note 1. Summary of Significant Accounting Policies

Description of Entity

The Alabama Prepaid Affordable College Tuition Program (the PACT Program) is a part of the Wallace-Folsom Savings Investment Plan. The PACT Program includes the PACT Trust Fund and the PACT Administrative Fund. These financial statements do not include any other programs of the Wallace-Folsom Savings Investment Plan.

The PACT Program operates under the provisions of the Code of Alabama 1975, Section 16-33C-1 through 9, as amended. The PACT Program is administratively located within the Alabama State Treasurer's office. The PACT Program's property, income, and operations have been statutorily exempted from all taxation by the State and its political subdivisions. The PACT Program Disclosure Statement provides that neither the contract purchaser nor beneficiary has any recourse against the Treasurer, the Board, the PACT Program, any other state or federal government agency, or the State of Alabama in connection with any obligations arising out of the PACT contracts.

The PACT Program is governed by a 15 member Board of Trustees consisting of the Director of Finance of the State of Alabama; the Treasurer of the State of Alabama; the Executive Director of the Alabama Commission on Higher Education, or designee; the Chancellor of the Alabama Community College System, or designee; the President of the Alabama Association of Independent Colleges or Universities, or designee; the President of the Council of College and University Presidents, or designee; the Chief Executive Officer of the RSA, or designee; two persons appointed by the Governor; two persons appointed by the Speaker of the House of Representatives; one member of the House appointed by the Speaker; one person appointed by the Lieutenant Governor; one member of the Senate appointed by the Lieutenant Governor; and one person appointed by the Senate President Pro Tempore.

The PACT Program was initially established to provide a mechanism whereby four years of undergraduate tuition and mandatory fees could be paid in advance. The PACT Program entered into contracts with contract purchasers which provided that, in return for a specified actuarially determined payment, the PACT Program would provide the contract beneficiary's undergraduate tuition (up to 128 or 135 semester hours) and mandatory fees (up to eight semesters) at any Alabama public university or community college. For beneficiaries that choose to attend private or out-of-state institutions, the PACT Program would provide tuition payments at the current weighted average cost of tuition at Alabama public four-year institutions. The purchase price of the contract was based on several factors, including tuition costs, the beneficiary's age and grade in school, anticipated investment earnings, and anticipated tuition rate increases. Enrollment in the PACT Program is closed permanently to new participants and no new applications will be accepted.

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 1. Summary of Significant Accounting Policies – Continued

Description of Entity – Continued

Following court-ordered mediation in April 2011, the PACT Program participants and the PACT Board reached a settlement to modify the terms of the PACT Program contracts. In July 2011, the proposed class action settlement was approved. Under the settlement, finite tuition and fee payments would be established as a baseline for all future payments by the PACT Program, and the PACT Program beneficiaries would be responsible for paying any tuition and fees in excess of the baseline rate. Two appeals were subsequently filed with the Alabama Supreme Court to challenge the settlement. During 2013, the Alabama Supreme Court upheld the settlement, and tuition and fee payments are being made in the specified baseline amounts. The settlement also allowed for future increases to the baseline tuition rate based upon actuarial projections resulting in a surplus in the fund.

During 2014, the PACT Program established a reserve for administrative costs within the PACT Trust Fund and approximately \$12.9 million will be allocated for the purpose of paying future administrative costs of the PACT Program effective October 2014. Any unexpended funds allocated for administrative expenses will remain available for payment of PACT benefits. The cumulative total of transfers from the PACT Trust Fund to cover administrative costs is \$3.1 million as of September 30, 2022.

During 2022, the PACT Program Board of Directors approved a 24% increase to the current rate paid by the PACT Program for benefit payments. This increase was effective for the fall semester of 2022. Under the 2011 class action settlement agreement, the PACT Program is required to pay tuition and qualified fees at the fall 2010 rates as certified by each respective Alabama public eligible educational institution. The agreement was negotiated to allow for an increase in benefit payments if the actuarial condition of the PACT Program improves. The first increase of 3% was made in 2015 followed by a 6% increase in 2016, 8% increase in 2017, 7% increase in 2018, 7% increase in 2019, 7% increase in 2020, 10% increase in 2021, and a 24% increase in 2022, compounded.

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 1. Summary of Significant Accounting Policies – Continued

Reporting Entity

The PACT Program is a part of the State of Alabama's reporting entity and is reported as a private-purpose trust fund in the State of Alabama Annual Comprehensive Financial Report (ACFR). The notes accompanying these financial statements relate directly to the PACT Program. The PACT Program issues separate financial statements.

The PACT Program is comprised of the following funds:

- Trust Fund (Fund 471) includes contract benefit payments, interest earnings from investments, and disbursements to universities and colleges for tuition.
- Administrative Fund (Fund 470) operates the administrative functions of the PACT Program.

Measurement Focus and Basis of Accounting

The financial statements contained in this report have been prepared in conformity with accounting principles generally accepted (GAAP) in the United States of America as prescribed by the Government Accounting Standards Board (GASB). These financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recognized and recorded when earned and expenses are recorded when a liability is incurred.

Cash and Cash Equivalents

The PACT Program considers all highly liquid investments with a maturity of 12 months or less at the time of issuance to be cash equivalents. Cash and cash equivalents may consist of bank deposits, amounts invested in repurchase agreements, money market mutual funds and commercial paper.

Contract Income

Contract income represents the payments received from contract holders.

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 1. Summary of Significant Accounting Policies – Continued

Fair Value Measurements

Fair value generally represents the price that would be received at the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. GAAP establishes a fair value hierarchy that prioritizes inputs used to measure fair value into three levels:

Level 1 - Unadjusted quoted prices in active markets for identical assets or liabilities that are available at the measurement date.

Level 2 - Prices that are based on other than exchange-quoted prices in active markets, which are observable for the asset or liability, either directly or indirectly; and the fair value is determined through the use of models or other valuation methodologies. A significant adjustment to a Level 2 input could result in the Level 2 measurement becoming a Level 3 measurement.

Level 3 - Pricing inputs are unobservable for the asset or liability and include situations where there is little, if any, market activity for the asset or liability. The inputs into the determination of fair value are based upon the best information available and may require significant management judgement or estimation.

Investment Valuation

The PACT Program follows GASB Statement No. 31, *Accounting and Reporting for Certain Investments and for External Investment Pools*, which requires that investments in equity securities with readily determinable fair values, all investments in debt securities and open-end mutual funds to be reported at fair value with gains and losses included as a component of revenues and expenses. All plan investments are managed by a third-party money manager and are reported at fair value in the statement of fiduciary net position, with all investment income, including changes in fair value, reported as additions (reductions) in the statement of changes in fiduciary net position. Fair values for investment securities are based on quoted market prices, where available. Otherwise, fair values are based on quoted market prices of comparable instruments. Purchases and sales of securities are recorded by the PACT Program custodian on the trade date. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date.

The PACT Program's investments are exposed to various risks, such as interest rate, credit, and overall market volatility risks. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in risks in the near term would affect the amounts reported in the accompanying statement of fiduciary net position.

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 1. Summary of Significant Accounting Policies – Continued

Income Taxes

The Internal Revenue Code provides that state tuition plans that meet certain requirements are exempt from income taxation. The PACT Program's rules and regulations meet those requirements. Accordingly, no provision for income taxes has been made in these financial statements for accrual of income taxes for the year ended September 30, 2022, or for prior years.

Management 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 additions and deductions during each period. Actual results could differ from those estimates.

Recent Accounting Pronouncements

In June 2017, GASB issued Statement No. 87, *Leases* (GASB 87). The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows or resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundation principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities. The requirements of this Statement are effective for reporting periods beginning after December 15, 2021, with earlier application encouraged. The PACT Program has not completed the process of evaluating the impact of GASB 87 on its financial statements.

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 2. Cash and Cash Equivalents

The PACT Program maintains cash in a bank deposit account, an investment account and with the Alabama State Treasury Pool, which at times may exceed federally insured limits with the bank deposit accounts. The PACT Program has not experienced any losses in such accounts. Bank deposits in amounts above the federally insured limits are fully collateralized through the Security for Alabama Funds Enhancement (SAFE) Act. Under the SAFE Act, financial institutions holding public deposits in excess of the amounts insured by the FDIC must pledge collateral to a collateral pool in the name of the State Treasurer. The State Treasurer is responsible for monitoring compliance with the collateralization and reporting requirements of the SAFE Act.

Cash and cash equivalents at September 30, 2022 consist of the following:

Account Type	Fair Value
Cash – investment account	\$ 31,335,852
Cash – Alabama State Treasury Pool	22,131,645
Cash – interest earning accounts	144,640
Cash – encumbrances	3,196
Total	\$ 53,615,333

Note 3. Deposits and Investments

Investment securities at September 30, 2022 consisted of the following:

	Fair Value
U.S. treasuries	\$ 197,587,910
Mortgage and other asset-backed securities	2,106,077
U.S. agency securities	882,045
Total	\$ 200,576,032

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 3. Deposits and Investments – Continued

As of September 30, 2022, the PACT Program had one external money manager to invest plan assets. The PACT Program’s investments are presented in the statement of fiduciary net position in the aggregate at fair value and include the following at September 30, 2022:

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Fixed Maturity				
U.S. treasuries	\$ 197,587,910	\$ -	\$ 197,587,910	\$ -
Mortgage and other asset-backed securities	2,106,077	-	2,106,077	-
U.S. agency securities	882,045	-	882,045	-
Total	<u>\$ 200,576,032</u>	<u>\$ -</u>	<u>\$ 200,576,032</u>	<u>\$ -</u>

Deposits and investments are subject to certain types of risk including interest rate risk, custodial credit risk, and credit risk. The following describes those risks:

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The fair value of fixed maturity investments fluctuates in response to changes in market interest rates. Increases in prevailing interest rates generally translate into decreases in fair value of those instruments. The fair value of interest sensitive instruments may also be affected by the creditworthiness of the issuer, prepayment options, relative values of alternative investments, and other general market conditions. Certain fixed maturity investments have call provisions that could result in shorter maturity periods.

Custodial Credit Risk

For an investment, custodial credit risk is the risk that an entity will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party if the counterparty fails. The PACT Program’s custodian holds all investments of the PACT Program in the PACT Program’s name, with the exception of repurchase agreements. The securities underlying repurchase agreements are held in trust for the PACT Program in the name of the custodian, not in the name of the PACT Program.

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 3. Deposits and Investments – Continued

Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. Nationally recognized statistical rating organizations provide ratings of debt securities' quality based on a variety of factors, such as the financial condition of the issuers, which provide investors with some idea of the issuer's ability to meet its obligations.

Concentration of Credit Risk

The investment policy limits the aggregate amount that can be invested in each class of investments and provides further limitations on investments by the money manager. The policy limits are as follows:

- General fixed income and cash:
 - No more than 5% of the total market value of the portfolio can be invested in the debt obligation of any one issuer (does not apply to United States Government and Agency securities).
 - Holdings of any individual issue must be 5% or less of the outstanding value of the total issue.
 - The average duration of the portfolio must be maintained within a range of +/- 20% of the benchmark index duration.
 - Turnover of securities should not exceed 200% in any rolling 12-month period. Fixed income managers shall be excluded from this restriction for the first six months of their retention.
 - The benchmark for the portfolio is the Bloomberg Barclay's 1-3 Year Government Index once fully transitioned.

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 3. Deposits and Investments – Continued

- Short duration fixed income:
 - At the time of purchase, all securities purchased must be classified as investment grade by two of the three major rating services. For this purpose, the rating must be at least Baa3 by Moody's, BBB- by Standard & Poor's, and BBB- by Fitch. If only one rating exists, this one rating will determine investment grade status.
 - Securities downgraded below investment grade after purchase should be sold within six months of the downgrade.
 - The weighted average credit quality of the portfolio shall not fall below A or equivalent.
 - Agency residential and commercial mortgage-backed securities, non-agency commercial mortgage-backed securities, and agency collateralized mortgage obligations cannot comprise more than 50% of the portfolio combined.
 - Asset-backed securities are limited to 10% of the portfolio.
 - Commercial mortgage-backed securities are limited to 10% of the portfolio.
 - Rule 144A securities are limited to 10% of the portfolio.
 - Investments in collateralized bond obligations (CBOs) or similar pools of commercial loans are prohibited.
 - Investments in Interest-Only (IO) and Principal-Only (PO) collateralized mortgage obligations are not allowed.
 - Investments in non-United States Dollar denomination securities are not permitted.
 - The maximum allowable maturity of any bullet security is 63 months. However, for securities with puts, sinking funds, or regular amortization/paydowns, the weighted average life will be used, and restricted to three years.

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 3. Deposits and Investments – Continued

The overall portfolio design and asset allocation have been structured to provide the most appropriate structure and asset allocation from a risk and return perspective to meet the objectives of the PACT Board. The investment portfolio shall be diversified both by asset class and within asset classes, by economic sector and industry. The purpose of diversification is to reduce specific risk associated with any single security or class of securities. Asset allocation will be reviewed annually. The Board has established an asset allocation of 100% short duration fixed income for the life of the portfolio.

On September 30, 2022, the PACT Program did not have investments in any one organization which represents greater than 5% of plan net assets other than Federal Home Loan Mortgage and United States Treasury Notes. The 5% policy limit is not applicable to U.S. Government and Agency securities.

The following table provides information as of September 30, 2022, concerning the fair value of investments and interest rate risk:

Type of Investment	Investment Maturities at Fair Value (In Years)				Total Fair Value
	Less Than 1	1-5	6-10	More Than 10	
Fixed Maturity					
U.S. treasury	\$ 107,831,990	\$ 89,755,920	\$ -	\$ -	\$ 197,587,910
Mortgage and other asset-backed securities	7,927	1,420,287	664,425	13,438	2,106,077
U.S. agency securities	882,045	-	-	-	882,045
Total Investments	\$ <u>108,721,962</u>	\$ <u>91,176,207</u>	\$ <u>664,425</u>	\$ <u>13,438</u>	\$ <u>200,576,032</u>

The following table provides information as of September 30, 2022, concerning credit risk:

Moody's Ratings	Fair Value	Fair Value as a Percent of Total Fixed Maturity Fair Value
Aaa	\$200,576,032	100%

* Moody's ratings are used when available. Standard & Poor's rating is used when it is available and a Moody's rating is not.

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 3. Deposits and Investments – Continued

Mortgage-backed Securities

As of September 30, 2022, the PACT Program had investments in mortgage-backed securities. Embedded prepayment options cause these investments to be highly sensitive to changes in interest rates. Prepayments by the obligees of the underlying assets reduce the total interest payments to be received. Generally, when interest rates fall, obligees tend to prepay the mortgages thus eliminating the stream of interest payments that would have been received under the original amortization schedule. The resulting reduction in cash flow diminishes the fair value of mortgage-backed securities. Maturities may differ from contractual maturities (as shown in the table of investments) in mortgage-backed securities due to prepayment characteristics of these securities. Average life is an acceptable expected maturity. As of September 30, 2022, there were no investments held in forward settling TBA mortgage-backed securities.

Note 4. Interfund Transfers

The PACT Program received funds transferred out of the State of Alabama Education Trust Fund in the amount of \$209,555,200 in compliance with legislative appropriation acts. The interfund transfers included a prepayment of fiscal years 2023-2027 appropriation in the aggregate amount of \$177,373,600. There are no additional projected transfers from the Education Trust Fund.

Note 5. Future Tuition Benefit Payments and Future Contract Payments

An actuary determines future tuition benefit payments and future contract payments. The standardized measurement is the actuarial present value of such payments. This valuation method reflects the present value of estimated tuition benefits that will be paid in future years, the present value of estimated contract payments that will be received from installment contract purchasers in future years, and the present value of future payments from the State of Alabama. The net assets available for benefits exclude tuition paid after September 30, 2022.

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 5. Future Tuition Benefit Payments and Future Contract Payments – Continued

The funded status of the PACT Trust Fund as of the latest actuarial valuation is as follows:

Actuarial Valuation Date: September 30, 2022

Net Assets Available for Benefits	Actuarial Value of Future Contract Payments	Actuarial Value of Future State Payments	Total Assets	Actuarial Present Value of Future Tuition Benefit Payments and Expenses	Assets in Excess of Tuition Benefit Payments and Expenses	Assets as a Percentage of Tuition Benefit Payments and Expenses
\$238,576,509	\$767,057	\$ -	\$239,343,566	\$133,086,585	\$106,256,981	179.8%

The schedules of funding progress, presented as required supplementary information (RSI) following the notes to financial statements, present multi-year trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the actuarial accrued liability.

The significant actuarial assumptions from the most recent valuation as of September 30, 2022, are as follows:

Assumptions:

Investment Return Rate

Fiscal Year Ending	Expected Rates of Return
2023	2.90%
2024	3.10%
2025	2.85%
2026	2.30%
2027	1.80%
2028	1.75%

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 5. Future Tuition Benefit Payments and Future Contract Payments – Continued

Matriculation Schedule

College Type	Percent Enrolled
Private/Out-of-state	17.00%
Community College	15.00%
University of Alabama and Auburn University	53.00%
Other Alabama Universities	15.00%
Total	100.00%

Additional Assumption: Beneficiaries who enroll in a community college will transfer to a four-year university after two years.

The expected tuition and qualified fees to be paid were based on the average of the Fall 2022 tuition and qualified fees at each of the four-year universities, weighted by PACT enrollment and semester hours paid to each university, college and technical school.

Contract Cancellations: The actuarial valuation recognizes cancellations in accordance with the following schedule:

Age 0 through 9th grade	0% per year
10th grade	1%
11th grade	1%
12th grade	1%

Additionally, actuarial assumptions assume that beneficiaries who matriculate will utilize 128 hours out of the maximum of either 128 or 135 hours of contract benefits. It is assumed that each beneficiary will use 12 hours of contract benefit per semester for the first ten semesters and 8 hours of contract benefits in the eleventh semester starting after the completion of the 12th grade.

Payment of tuition and qualified fees is assumed to occur three times annually: 45% on November 15th, 45% on March 15th, and 10% on August 15th.

For the 2022 actuarial valuation, a load of \$525,000 was included for administrative fees for future fiscal years through 2027. From 2028 to 2031, it is lowered \$100,000 per year.

Alabama Prepaid Affordable College Tuition Program
Notes to Financial Statements – Continued
September 30, 2022

Note 5. Future Tuition Benefit Payments and Future Contract Payments – Continued

The trust funded ratio increased from 119.4% in 2021 to 179.8% in 2022. The increase in the trust funded ratio was primarily due to a change in the method of determining the future valuation of tuition and fee payments and the prepayment of future Education Trust Fund transfers received in May. It also includes a significant change in the expected value of payments to schools.

Note 6. Subsequent Events

The PACT Program has evaluated subsequent events through February 8, 2023, which is the date these financial statements were available to be issued. All subsequent events requiring recognition as of September 30, 2022, have been incorporated into these financial statements.

Required Supplemental Information

**Alabama Prepaid Affordable College Tuition Program
Required Supplementary Information
Schedule of Funding Progress
September 30, 2022**

Schedule of Funding Progress for the PACT Program through September 30, 2022 is as follows:

Actuarial Valuation Date	Net Assets Available for Benefits	Actuarial Value of Future Contract Payments	Actuarial Value of Future State Payments	Total Assets	Actuarial Present Value of Future Tuition Benefit Payments and Expenses	Assets in Excess of Tuition Benefit Payments and Expenses	Assets as a Percentage of Tuition Benefit Payments and Expenses
September 30, 2013	233,795,658	15,643,284	485,606,200	735,045,142	668,569,296	66,475,846	109.9%
September 30, 2014	175,783,822	11,965,193	488,464,061	676,213,076	597,610,944	78,602,132	113.1%
September 30, 2015	121,034,200	9,258,001	475,753,759	606,045,960	523,195,414	82,850,546	115.8%
September 30, 2016	89,577,934	7,000,914	450,917,767	547,496,615	479,334,255	68,162,360	114.2%
September 30, 2017	90,881,156	5,081,634	373,712,526	469,675,316	406,753,048	62,922,268	115.5%
September 30, 2018	99,190,043	5,991,869	322,237,628	427,419,540	355,574,464	71,845,076	120.2%
September 30, 2019	97,564,083	4,011,668	269,644,592	371,220,343	318,261,976	52,958,367	116.6%
September 30, 2020	99,965,199	2,467,299	217,416,567	319,849,065	268,016,301	51,832,764	119.3%
September 30, 2021	90,303,872	1,425,038	192,055,093	283,784,003	237,630,828	46,153,175	119.4%
September 30, 2022	238,576,509	767,057	-	239,343,566	133,086,585	106,256,981	179.8%

See accompanying notes.

Supplemental Information

Alabama Prepaid Affordable College Tuition Program
Combining Schedule of Fiduciary Net Position
September 30, 2022

	<u>Trust Fund</u>	<u>Administrative Fund</u>	<u>Total</u>
Assets			
Cash and cash equivalents	\$ 52,766,208	\$ 849,125	\$ 53,615,333
Investments	200,576,032	-	200,576,032
Total Assets	<u>253,342,240</u>	<u>849,125</u>	<u>254,191,365</u>
Liabilities			
Accounts payable	7,504,979	-	7,504,979
Accrued liabilities	-	82,478	82,478
Total Liabilities	<u>7,504,979</u>	<u>82,478</u>	<u>7,587,457</u>
Net Position			
Held in trust for tuition payments and other purposes	<u>\$ 245,837,261</u>	<u>\$ 766,647</u>	<u>\$ 246,603,908</u>

See accompanying notes.

Alabama Prepaid Affordable College Tuition Program
Combining Schedule of Changes in Fiduciary Net Position
For the Year Ended September 30, 2022

	<u>Trust Fund</u>	<u>Administrative Fund</u>	<u>Combining Entry</u>	<u>Total</u>
Additions				
Contract income	\$ 209,679	\$ -	\$ -	\$ 209,679
Investment Earnings				
Interest and dividend income	773,300	-	-	773,300
Loss on investments	(2,441,039)	-	-	(2,441,039)
Net investment loss	(1,667,739)	-	-	(1,667,739)
Other income	-	109,786	-	109,786
Transfers from other funds	209,555,200	414,280	(414,280)	209,555,200
Total Additions	<u>208,097,140</u>	<u>524,066</u>	<u>(414,280)</u>	<u>208,206,926</u>
Deductions				
Tuition benefits	40,705,895	-	-	40,705,895
Salaries and other administrative expenses	-	449,883	-	449,883
Professional services	59,598	60,715	-	120,313
Cancellation refunds	2,729,360	-	-	2,729,360
Transfers to other funds	414,280	-	(414,280)	-
Total Deductions	<u>43,909,133</u>	<u>510,598</u>	<u>(414,280)</u>	<u>44,005,451</u>
Change in Net Position	164,188,007	13,468	-	164,201,475
Net Position at Beginning of Year	81,649,254	753,179	-	82,402,433
Net Position at End of Year	<u>\$ 245,837,261</u>	<u>\$ 766,647</u>	<u>\$ -</u>	<u>\$ 246,603,908</u>

See accompanying notes.



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 Trustees
Alabama Prepaid Affordable College Tuition Program
Montgomery, Alabama

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 the Alabama Prepaid Affordable College Tuition Program (the PACT Program), a program of the Wallace-Folsom College Savings Investment Plan and a private-purpose trust fund of the State of Alabama, as of and for the year ended September 30, 2022, and the related notes to financial statements, which comprise the basic financial statements, and have issued our report thereon dated February 8, 2023.

Report on Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the PACT Program's internal control over financial reporting (internal control) as a basis for designing 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 PACT Program's internal control. Accordingly, we do not express an opinion on the effectiveness of the PACT Program's internal control.

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

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

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the PACT Program'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 financial statements. 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 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 PACT Program'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 PACT Program's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

KASSOUF & CO., P.C.

A handwritten signature in black ink that reads "Kassouf & Co." in a cursive script.

Certified Public Accountants

February 8, 2023