IAC/INTERACTIVECORP
Form 10-Q
November 10, 2008

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As filed with the Securities and Exchange Commission on November 10, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

ý **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Quarterly Period Ended September 30, 2008

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission File No. 0-20570

IAC/INTERACTIVECORP

(Exact name of registrant as specified in its charter)

Delaware	**59-2712887**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

555 West 18th Street, New York, New York 10011

(Address of Registrant's principal executive offices)

(212) 314-7300

(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ý	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting	Smaller reporting company o

company)

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No ý

As of October 31, 2008, the following shares of the Registrant's common stock were outstanding:

Common Stock	127,597,911
Class B Common Stock	12,799,999
Total outstanding Common Stock	140,397,910

The aggregate market value of the voting common stock held by non-affiliates of the Registrant as of October 31, 2008 was $1,574,345,100. For the purpose of the foregoing calculation only, all directors and executive officers of the Registrant are assumed to be affiliates of the Registrant.

PART I FINANCIAL STATEMENTS

Item 1. ***Consolidated Financial Statements***

IAC/INTERACTIVECORP AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET

	September 30, 2008	December 31, 2007
	(unaudited)	(audited)
	(In thousands, except share data)	
ASSETS		
Cash and cash equivalents	$ 1,342,112	$ 1,585,302
Marketable securities	121,515	326,788
Accounts receivable, net of allowance of $16,291 and $8,714, respectively	118,149	116,670
Prepaid expenses and other current assets	185,956	377,443
Current assets of discontinued operations		1,020,034
Total current assets	1,767,732	3,426,237
Property and equipment, net	335,537	334,341
Goodwill	1,910,918	1,823,779
Intangible assets, net	410,669	401,915
Long-term investments	256,839	301,023
Other non-current assets	401,445	201,764
Non-current assets of discontinued operations		6,101,743
TOTAL ASSETS	$ 5,083,140	$ 12,590,802
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES:		
Accounts payable, trade	$ 60,325	$ 41,957
Deferred revenue	50,474	48,110
Current maturities of long-term obligations		12,090
Accrued expenses and other current liabilities	293,916	366,769
Current liabilities of discontinued operations		1,265,307
Total current liabilities	404,715	1,734,233
Long-term obligations, net of current maturities	95,844	834,542
Income taxes payable	382,275	264,113
Other long-term liabilities	14,637	13,893
Non-current liabilities of discontinued operations		1,127,479
Minority interest	32,063	32,880
Commitments and contingencies		
SHAREHOLDERS' EQUITY:		
Preferred stock $.01 par value; authorized 100,000,000 shares; 0 shares and 758 shares issued and outstanding, respectively		
Common stock $.001 par value; authorized 1,600,000,000 shares; issued 209,996,655 and 208,538,800 shares, respectively, and outstanding 127,589,273 and 129,131,418 shares, respectively, including 0 shares and 100,000 shares, respectively, of restricted stock	210	209
Class B convertible common stock $.001 par value; authorized 400,000,000 shares; issued 16,157,499 shares and outstanding 12,799,999 shares	16	16
Additional paid-in capital	11,096,473	14,744,542
Retained earnings	28	567,820

Accumulated other comprehensive (loss) income	(28,792)	39,814
Treasury stock 82,407,382 and 79,407,382 shares, respectively	(6,914,329)	(6,768,739)
Total shareholders' equity	4,153,606	8,583,662
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 5,083,140	$ 12,590,802

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

IAC/INTERACTIVECORP AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF OPERATIONS

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	**2007**	**2008**	**2007**
	(In thousands, except per share data)			
Service revenue	$341,691	$312,962	$1,010,548	$890,379
Product sales	27,589	22,399	83,552	63,323
Net revenue	369,280	335,361	1,094,100	953,702
Cost of sales service revenue (exclusive of depreciation shown separately below)	115,142	125,265	341,545	344,647
Cost of sales product sales (exclusive of depreciation shown separately below)	19,068	15,379	56,627	44,404
Gross profit	235,070	194,717	695,928	564,651
Selling and marketing expense	102,620	81,639	327,758	283,029
General and administrative expense	110,997	64,910	278,340	189,442
Other operating expense	12,329	12,029	41,922	33,177
Amortization of non-cash marketing	6,138	9,072	12,005	33,080
Amortization of intangibles	8,287	10,267	24,028	26,304
Depreciation	17,337	15,107	52,055	43,954
Operating (loss) income	(22,638)	1,693	(40,180)	(44,335)
Other income (expense):				
Interest income	6,549	13,644	20,325	47,988
Interest expense	(5,002)	(14,919)	(30,866)	(44,676)
Equity in income of unconsolidated affiliates	3,146	3,885	15,373	16,543
Other (expense) income	(68,657)	10,295	(157,581)	19,174
Total other (expense) income, net	(63,964)	12,905	(152,749)	39,029
(Loss) earnings from continuing operations before income taxes and minority interest	(86,602)	14,598	(192,929)	(5,306)
Income tax benefit (provision)	85,335	(11,132)	103,573	(3,365)
Minority interest in losses of consolidated subsidiaries	381	1,452	1,195	1,490
(Loss) earnings from continuing operations	(886)	4,918	(88,161)	(7,181)
Gain (loss) on sale of discontinued operations, net of tax	767	(1,557)	23,314	33,524
(Loss) income from discontinued operations, net of tax	(14,718)	67,110	(318,771)	199,481
Net (loss) earnings available to common shareholders	$ (14,837)	$ 70,471	$ (383,618)	$225,824
(Loss) earnings per share from continuing operations:				
Basic (loss) earnings per share	$ (0.01)	$ 0.03	$ (0.63)	$ (0.05)
Diluted (loss) earnings per share	$ (0.01)	$ 0.03	$ (0.63)	$ (0.05)
Net (loss) earnings per share available to common shareholders:				
Basic (loss) earnings per share	$ (0.11)	$ 0.49	$ (2.75)	$ 1.58
Diluted (loss) earnings per share	$ (0.11)	$ 0.47	$ (2.75)	$ 1.58

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

IAC/INTERACTIVECORP AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

(Unaudited)

	Total	Preferred Stock $.01 Par Value $	Preferred Stock $.01 Par Value Shares	Common Stock $.001 Par Value $	Common Stock $.001 Par Value Shares	Class B Convertible Common Stock $.001 Par Value $	Class B Convertible Common Stock $.001 Par Value Shares	Additional Paid-in Capital	Retained Earnings	Accum. Other Comp. Income (Loss)	Treasury Stock
	(In thousands)										
Balance as of December 31, 2007	$ 8,583,662	$	1	$ 209	208,539	$ 16	16,157	$ 14,744,542	$ 567,820	$ 39,814	$ (6,768,739)
Comprehensive loss:											
Net loss for the nine months ended September 30, 2008	(383,618)								(383,618)		
Foreign currency translation	(29,377)									(29,377)	
Unrealized losses on available-for-sale securities	(47,820)									(47,820)	
Unrealized losses recognized into earnings in connection with the impairment of available-for-sale securities	46,058									46,058	
Comprehensive loss	(414,757)										
Non-cash compensation expense	123,813							123,813			
Issuance of common stock upon exercise of stock options and vesting of restricted stock units, net of withholding taxes	(23,183)			1	1,226			(23,184)			
Income tax benefit related to the exercise of stock options and vesting of restricted stock units	(9,883)							(9,883)			
Redemption of preferred shares	(21)		(1)					(21)			
Issuance of common stock upon conversion of convertible notes	10,849				232			10,849			
Purchase of treasury stock	(145,590)										(145,590)
Spin-off of HSNi, ILG, Ticketmaster and Tree.com to shareholders	(3,971,284)							(3,749,643)	(184,174)	(37,467)	
Balance as of September 30, 2008	$ 4,153,606	$		$ 210	209,997	$ 16	16,157	$ 11,096,473	$ 28	$ (28,792)	$ (6,914,329)

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

IAC/INTERACTIVECORP AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS

(Unaudited)

	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
	(In thousands)	
Cash flows from operating activities attributable to continuing operations:		
Net (loss) earnings available to common shareholders	$ (383,618)	$ 225,824
Less: loss (income) from discontinued operations, net of tax	295,457	(233,005)
Loss from continuing operations	(88,161)	(7,181)
Adjustments to reconcile loss from continuing operations to net cash provided by operating activities attributable to continuing operations:		
Depreciation and amortization of intangibles	76,083	70,258
Impairment of available-for-sale securities	132,587	
Non-cash compensation expense	76,174	52,360
Amortization of non-cash marketing	12,005	33,080
Deferred income taxes	(79,755)	(817)
Equity in income of unconsolidated affiliates	(15,373)	(16,543)
Loss on extinguishment of Senior Notes	63,218	
Gain on sale of long-term investment	(29,130)	
Increase in the fair value of the derivative asset created in the sale of HSE	(5,785)	(7,771)
Net increase in the fair value of the derivative assets and liabilities created in Expedia spin-off	(545)	(4,383)
Minority interest in losses of consolidated subsidiaries	(1,195)	(1,490)
Changes in current assets and liabilities:		
Accounts receivable	(6,517)	371
Prepaid expenses and other current assets	(6,167)	(9,769)
Accounts payable and other current liabilities	33,662	(13,480)
Income taxes payable	(23,355)	(109,655)
Deferred revenue	3,516	6,127
Other, net	6,099	9,025
Net cash provided by operating activities attributable to continuing operations	147,361	132
Cash flows from investing activities attributable to continuing operations:		
Acquisitions, net of cash acquired	(130,704)	(45,824)
Capital expenditures	(51,348)	(77,769)
Proceeds from sales and maturities of marketable securities	330,316	1,188,409
Purchases of marketable securities	(140,878)	(695,855)
Proceeds from sales of long-term investments	60,945	109,923
Increase in long-term investments	(59,700)	(229,455)
Proceeds from sale of discontinued operation	32,723	4,173
Net cash distribution from spun-off businesses	427,834	
Other, net	189	12,985
Net cash provided by investing activities attributable to continuing operations	469,377	266,587
Cash flows from financing activities attributable to continuing operations:		
Repurchase of Senior Notes	(514,943)	
Principal payments on long-term obligations	(8)	(7,577)
Purchase of treasury stock	(145,590)	(542,946)
Issuance of common stock, net of withholding taxes	(12,774)	21,944
Excess tax benefits from stock-based awards	726	5,813
Collection of note receivable from key executive for common stock issuance		4,998
Other, net	(1,438)	(1,108)
Net cash used in financing activities attributable to continuing operations	(674,027)	(518,876)
Total cash used in continuing operations	(57,289)	(252,157)

Net cash provided by operating activities attributable to discontinued operations	274,415	598,289
Net cash used in investing activities attributable to discontinued operations	(495,131)	(215,228)
Net cash provided by (used in) financing activities attributable to discontinued operations	50,484	(209,923)
Total cash (used in) provided by discontinued operations	(170,232)	173,138
Effect of exchange rate changes on cash and cash equivalents	(15,669)	29,472
Net decrease in cash and cash equivalents	(243,190)	(49,547)
Cash and cash equivalents at beginning of period	1,585,302	1,428,140
Cash and cash equivalents at end of period	$ 1,342,112	$ 1,378,593

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 ORGANIZATION

On August 20, 2008, IAC completed its previously announced plan to separate into five publicly traded companies:

- IAC, which includes:
  - the businesses comprising its Media & Advertising segment;
  - the Match and ServiceMagic segments;
  - the businesses comprising its Emerging Businesses segment, including Shoebuy and ReserveAmerica, which were formerly included in the Retailing and Ticketmaster segments, respectively; and
  - certain investments in unconsolidated affiliates.
- HSN, Inc. ("HSNi"), which includes HSN TV, *HSN.com*, and the Cornerstone Brands, Inc. portfolio of catalogs, websites and retail locations;
- Interval Leisure Group, Inc. ("ILG"), which includes the businesses that comprised the Interval segment;
- Ticketmaster, which includes its primary domestic and international operations as well as certain investments in unconsolidated affiliates; and
- Tree.com, Inc. ("Tree.com"), which includes the businesses that comprised the Lending and Real Estate segments.

We refer to this transaction as the "Spin-Off". Immediately subsequent to the Spin-Off, IAC effected a one-for-two reverse stock split. All share information, unless otherwise noted, reflects the impact of the reverse stock split and is not adjusted for the relative values of the spun-off businesses.

The results of operations of HSNi, ILG, Ticketmaster and Tree.com have been classified as discontinued operations for all periods presented.

All references to "IAC," the "Company," "we," "our" or "us" in this report are to IAC/InterActiveCorp.

During the first quarter of 2008, in contemplation of the Spin-Off, IAC reorganized its then existing Retailing, Ticketmaster and Emerging Businesses reporting segments. Shoebuy and ReserveAmerica, which were previously included in the Retailing and Ticketmaster reporting segments, respectively, are now included in the Emerging Businesses segment. Information for all prior periods has been reclassified to conform with the current year segment presentation.

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and notes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Interim results are not necessarily indicative of the results that may be expected for a full year. For further information, refer to the

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (Continued)

consolidated financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended December 31, 2007, as amended.

Accounting Estimates

Management of the Company is required to make certain estimates and assumptions during the preparation of the consolidated financial statements in accordance with U.S. generally accepted accounting principles. These estimates and assumptions impact the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as of the date of the consolidated financial statements. They also impact the reported amount of net earnings during any period. Actual results could differ from those estimates.

Significant estimates underlying the accompanying consolidated financial statements include: recovery of marketable securities; the allowance for doubtful accounts; recoverability of long-lived assets, including definite-lived intangible assets; recovery of goodwill and indefinite-lived intangible assets; recovery of derivative assets; income taxes payable and deferred income taxes, including related reserves and valuation allowances; sales return and other revenue allowances; various other allowances, reserves and accruals; and, assumptions related to the determination of stock based compensation.

Long-term Investments

On June 19, 2007, as part of the consideration for the sale of Home Shopping Europe GmbH & Co. KG, and its affiliated TV station HSE 24 ("HSE") to Arcandor AG ("ARO"), IAC received approximately 5.5 million shares of ARO stock (the "ARO Shares") valued at €141 million or $190.1 million plus additional consideration in the form of a contingent value right ("CVR"). The CVR has a value of up to €54 million within three years from the date of sale. The ultimate value of the CVR is dependent, in part, upon the average closing value of the ARO Shares for the 90 days preceding June 19, 2010 (the "Average Value"). To the extent that the Average Value is equal to or less than €141 million, IAC will receive a cash payment equal to €54 million. To the extent that the Average Value is equal to or greater than €195 million, IAC will receive no additional consideration. To the extent that the Average Value is between €141 million and €195 million, IAC will receive a pro rata portion of the €54 million. If the closing value of an ARO share equals or exceeds €35.68 per share for at least 30 consecutive trading days during the three year period from June 20, 2007 through June 19, 2010, the CVR expires without any payment being made. The CVR is accounted for as a derivative asset and maintained at fair value each reporting period with any changes in fair value recognized in current earnings as a component of other income (expense) in the consolidated statement of operations each period. During the three and nine months ended September 30, 2008, the change in the fair value of the CVR resulted in a loss of $5.1 million and a gain of $5.8 million, respectively. During the three and nine months ended September 30, 2007, the change in the fair value of the CVR resulted in gains of $5.9 million and $7.8 million, respectively. The loss of $5.1 million for the three months ended September 30, 2008 was due in part to an increase in the discount rate related to credit risk. The CVR was valued at $58.6 million at September 30, 2008 and $54.7 million at December 31, 2007. The ARO stock is an available-for-sale marketable equity security that is accounted for in accordance with Statement of Financial Accounting Standards ("SFAS") No. 115, "Accounting for Certain Investments in Debt and Equity Securities," and is included in "Long-term investments" in the accompanying consolidated balance sheet, with a carrying value of $18.4 million at September 30, 2008 and $130.8 million at December 31, 2007. During the second quarter of 2008, the

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (Continued)

Company concluded that the decline in price of the ARO Shares was other-than-temporary and thus recorded a $132.6 million impairment charge that is included in "Other (expense) income" for the nine months ended September 30, 2008 in the accompanying consolidated statement of operations. The loss was determined to be other-than-temporary due to (1) the significant, 72% decline in the ARO stock price from €25.90 at June 19, 2007 to €7.38 at June 30, 2008, and the duration of the decline in the ARO stock price and (2) the Company's assessment of the near-to-medium term prospects for a recovery to levels proximate to the initial carrying value of the ARO Shares. During the third quarter of 2008, the ARO stock price declined further from €7.38 at June 30, 2008 to €2.33 at September 30, 2008. The Company does not believe that this decline is other-than-temporary due to the duration of the stock price decline and the Company's assessment of the prospects for a recovery to a €7.38 price level during the Company's expected holding period. Accordingly, the €27.6 million or $40.4 million decline in the ARO stock price during the third quarter of 2008 has been recorded in "Accumulated other comprehensive income (loss)" in the accompanying consolidated statement of shareholders' equity.

Recent Accounting Pronouncements

In December 2007, the Financial Accounting Standards Board ("FASB") issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements an amendment of Accounting Research Bulletin No. 51" ("SFAS No. 160"). SFAS No. 160 establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income attributable to the parent and to the noncontrolling interest, changes in a parent's ownership interest and the valuation of retained noncontrolling equity investments when a subsidiary is deconsolidated. The Statement also establishes reporting requirements that provide sufficient disclosures that clearly identify and distinguish between the interests of the parent and the interests of the noncontrolling owners. SFAS No. 160 is effective for fiscal years beginning after December 15, 2008. SFAS No. 160 will be applied prospectively, except as it relates to disclosures, for which the effects will be applied retrospectively for all periods presented. Early adoption is not permitted. The Company is currently assessing the impact of SFAS No. 160 on its consolidated financial position, results of operations and cash flows.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), "Business Combinations" ("SFAS No. 141R"), which replaces FASB Statement No. 141. SFAS No. 141R establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any noncontrolling interest in the acquiree and the goodwill acquired. The Statement also establishes disclosure requirements that will enable users to evaluate the nature and financial effects of the business combination. SFAS No. 141R applies prospectively to business combinations in fiscal years beginning after December 15, 2008. Early adoption is not permitted. The Company is currently assessing the impact of the adoption of SFAS No. 141R on its consolidated financial position, results of operations and cash flows.

Reclassifications

The accompanying consolidated balance sheet at December 31, 2007 has been reclassified to present HSNi, ILG, Ticketmaster and Tree.com as discontinued operations. The consolidated statements of operations for the three and nine months ended September 30, 2007 and cash flows for the nine months ended September 30, 2007 have been reclassified to present HSNi, ILG, Ticketmaster,

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (Continued)

Tree.com and Entertainment Publications, Inc. ("EPI"), which previously comprised IAC's Entertainment segment, as discontinued operations.

In addition, certain other prior period amounts have been reclassified to conform with the current year presentation.

Other

Effective April 1, 2007, the Company began to capitalize and amortize the costs associated with certain arrangements that require it to pay a fee per access point delivered. These access points are generally in the form of downloadable search toolbars associated with the Company's Media & Advertising businesses. These fees are amortized over the estimated useful lives of the access points to the extent the Company can reasonably estimate a probable future economic benefit and the period over which such benefit will be realized (generally 18 months). Otherwise, the fees are charged to expense as incurred. For fees paid prior to April 1, 2007, such benefit or period could not be reasonably estimated and the fees were charged to expense as incurred. The effect of capitalizing and amortizing these costs was to reduce expense by $5.1 million and $12.8 million in the nine months ended September 30, 2008 and 2007, respectively.

NOTE 3 GOODWILL AND INTANGIBLE ASSETS

The balance of goodwill and intangible assets, net is as follows (in thousands):

	September 30, 2008	December 31, 2007
Goodwill	$ 1,910,918	$ 1,823,779
Intangible assets with indefinite lives	351,551	329,013
Intangible assets with definite lives, net	59,118	72,902
Total goodwill and intangible assets, net	$ 2,321,587	$ 2,225,694

Intangible assets with indefinite lives relate to trade names and trademarks acquired in various acquisitions. At September 30, 2008, intangible assets with definite lives relate to the following (in thousands):

	Cost	Accumulated Amortization	Net	Weighted Average Amortization Life (Years)
Technology	$113,856	$ (73,336)	$40,520	4.9
Customer lists	19,773	(19,587)	186	1.1
Supplier agreements	24,670	(9,523)	15,147	5.7
Distribution agreements	4,600	(3,682)	918	4.0
Other	22,188	(19,841)	2,347	2.9
Total	$185,087	$ (125,969)	$59,118	

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 3 GOODWILL AND INTANGIBLE ASSETS (Continued)

At December 31, 2007, intangible assets with definite lives relate to the following (in thousands):

	Cost	Accumulated Amortization	Net	Weighted Average Amortization Life (Years)
Technology	$113,915	$ (55,907)	$58,008	4.9
Customer lists	20,586	(19,768)	818	1.1
Supplier agreements	15,770	(7,060)	8,710	6.0
Distribution agreements	4,600	(2,819)	1,781	4.0
Other	20,471	(16,886)	3,585	2.9
Total	$175,342	$ (102,440)	$72,902	

Amortization of intangible assets with definite lives is computed on a straight-line basis and, based on December 31, 2007 balances, such amortization for the next five years and thereafter is estimated to be as follows (in thousands):

Years Ending December 31,	
2008	$30,421
2009	26,398
2010	13,449
2011	1,204
2012	1,167
2013 and thereafter	263
	$72,902

The following table presents the balance of goodwill by segment, including changes in the carrying amount of goodwill, for the nine months ended September 30, 2008 (in thousands):

	Balance as of January 1, 2008	Additions	(Deductions)	Foreign Exchange Translation	Balance as of September 30, 2008
Media & Advertising	$1,361,914	$ 88,698	$ (3,697)	$ (5)	$ 1,446,910
Match	233,397			(1,108)	232,289
ServiceMagic	99,641				99,641
Emerging Businesses	128,827	4,703	(414)	(1,038)	132,078
Total	$1,823,779	$ 93,401	$ (4,111)	$ (2,151)	$ 1,910,918

Additions principally relate to acquisitions. Deductions principally relate to the establishment of deferred tax assets related to acquired tax attributes and the income tax benefit realized pursuant to the exercise of stock options assumed in business acquisitions that were vested at the transaction date and are treated as a reduction in goodwill when the income tax deductions are realized.

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 4 PROPERTY AND EQUIPMENT

The balance of property and equipment, net is as follows (in thousands):

	September 30, 2008	December 31, 2007
Computer equipment and capitalized software	$ 234,256	$ 207,035
Buildings and leasehold improvements	230,994	206,340
Furniture and other equipment	44,301	43,731
Projects in progress	24,894	40,836
Land	5,117	5,117
	539,562	503,059
Less: accumulated depreciation and amortization	(204,025)	(168,718)
Total property and equipment, net	$ 335,537	$ 334,341

NOTE 5 SEGMENT INFORMATION

The overall concept that IAC employs in determining its operating segments is to present the financial information in a manner consistent with how the chief operating decision maker and executive management view the businesses, how the businesses are organized as to segment management, and the focus of the businesses with regards to the types of products or services offered or the target market. Entities included in discontinued operations, as described in Note 6, are excluded from the schedules below except for the schedule of assets, in which they are included in corporate and other. Operating segments are combined for reporting purposes if they have similar economic characteristics and meet the aggregation criteria of SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information."

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(In thousands)			
Revenue:				
Media & Advertising	$ 193,273	$ 189,824	$ 595,136	$ 531,901
Match	93,540	89,109	277,358	258,111
ServiceMagic	33,799	24,591	98,618	71,453
Emerging Businesses	49,644	36,319	141,945	99,341
Inter-segment elimination	(976)	(4,482)	(18,957)	(7,104)
Total	$ 369,280	$ 335,361	$ 1,094,100	$ 953,702

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 5 SEGMENT INFORMATION (Continued)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(In thousands)			
Operating (Loss) Income:				
Media & Advertising	$ 32,106	$ 15,675	$ 93,166	$ 15,484
Match	23,978	29,272	50,740	49,603
ServiceMagic	8,111	4,626	22,627	16,103
Emerging Businesses	(7,390)	(9,912)	(25,829)	(8,990)
Corporate	(79,443)	(37,968)	(180,884)	(116,535)
Total	$ (22,638)	$ 1,693	$ (40,180)	$ (44,335)

The Company's primary metric is Operating Income Before Amortization, which is defined as operating income excluding, if applicable: (1) non-cash compensation expense, (2) amortization of non-cash marketing, (3) amortization and impairment of intangibles, (4) goodwill impairment, (5) pro forma adjustments for significant acquisitions, and (6) one-time items. The Company believes this measure is useful to investors because it represents the consolidated operating results from IAC's segments, taking into account depreciation, which it believes is an ongoing cost of doing business, but excluding the effects of any other non-cash expenses. Operating Income Before Amortization has certain limitations in that it does not take into account the impact to IAC's statement of operations of certain expenses, including non-cash compensation, non-cash marketing, and acquisition related accounting. IAC endeavors to compensate for the limitations of the non-GAAP measure presented by providing the comparable GAAP measure with equal or greater prominence, financial statements prepared in accordance with generally accepted accounting principles, and descriptions of the reconciling items, including quantifying such items, to derive the non-GAAP measure.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(In thousands)			
Operating Income Before Amortization:				
Media & Advertising	$ 38,810	$ 27,898	$ 112,189	$ 56,835
Match	30,274	29,530	63,278	57,508
ServiceMagic	8,651	5,420	24,245	18,744
Emerging Businesses	(6,070)	(3,457)	(21,705)	35
Corporate	(41,201)	(21,724)	(105,980)	(65,713)
Total	$ 30,464	$ 37,667	$ 72,027	$ 67,409

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 5 SEGMENT INFORMATION (Continued)

The following tables reconcile Operating Income Before Amortization to operating (loss) income for the Company's reporting segments and to net (loss) earnings available to common shareholders in total (in thousands):

	For the Three Months Ended September 30, 2008				
	Operating Income Before Amortization	Non-Cash Compensation Expense(A)	Amortization of Non-Cash Marketing	Amortization of Intangibles	Operating Income (Loss)
Media & Advertising	$ 38,810	$	$	$ (6,704)	$ 32,106
Match	30,274		(6,138)	(158)	23,978
ServiceMagic	8,651	(155)		(385)	8,111
Emerging Businesses	(6,070)	(280)		(1,040)	(7,390)
Corporate	(41,201)	(38,242)			(79,443)
Total	$ 30,464	$ (38,677)	$ (6,138)	$ (8,287)	(22,638)
Other expense, net					(63,964)
Loss from continuing operations before income taxes and minority interest					(86,602)
Income tax benefit					85,335
Minority interest in losses of consolidated subsidiaries					381
Loss from continuing operations					(886)
Gain on sale of discontinued operations					767
Loss from discontinued operations, net of tax					(14,718)
Net loss available to common shareholders					$ (14,837)

(A) Non-cash compensation expense includes $3.0 million, $3.3 million, $32.3 million and $0.1 million which are included in cost of sales, selling and marketing expense, general and administrative expense and other operating expense, respectively, in the accompanying consolidated statement of operations.

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 5 SEGMENT INFORMATION (Continued)

	For the Three Months Ended September 30, 2007				
	Operating Income Before Amortization	Non-Cash Compensation Expense(B)	Amortization of Non-Cash Marketing	Amortization of Intangibles	Operating Income (Loss)
Media & Advertising	$ 27,898	$	$ (6,062)	$ (6,161)	$ 15,675
Match	29,530		(23)	(235)	29,272
ServiceMagic	5,420	(155)		(639)	4,626
Emerging Businesses	(3,457)	(236)	(2,987)	(3,232)	(9,912)
Corporate	(21,724)	(16,244)			(37,968)
Total	$ 37,667	$ (16,635)	$ (9,072)	$ (10,267)	1,693
Other income, net					12,905
Earnings from continuing operations before income taxes and minority interest					14,598
Income tax provision					(11,132)
Minority interest in losses of consolidated subsidiaries					1,452
Earnings from continuing operations					4,918
Loss on sale of discontinued operations					(1,557)
Income from discontinued operations, net of tax					67,110
Net earnings available to common shareholders					$ 70,471

(B) Non-cash compensation expense includes $1.3 million, $1.4 million and $13.9 million which are included in cost of sales, selling and marketing expense and general and administrative expense, respectively, in the accompanying consolidated statement of operations.

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 5 SEGMENT INFORMATION (Continued)

	For The Nine Months Ended September 30, 2008				
	Operating Income Before Amortization	Non-Cash Compensation Expense(C)	Amortization of Non-Cash Marketing	Amortization of Intangibles	Operating Income (Loss)
Media & Advertising	$ 112,189	$	$	$ (19,023)	$ 93,166
Match	63,278		(12,005)	(533)	50,740
ServiceMagic	24,245	(467)		(1,151)	22,627
Emerging Businesses	(21,705)	(803)		(3,321)	(25,829)
Corporate	(105,980)	(74,904)			(180,884)
Total	$ 72,027	$ (76,174)	$ (12,005)	$ (24,028)	(40,180)
Other expense, net					(152,749)
Loss from continuing operations before income taxes and minority interest					(192,929)
Income tax benefit					103,573
Minority interest in losses of consolidated subsidiaries					1,195
Loss from continuing operations					(88,161)
Gain on sale of discontinued operations					23,314
Loss from discontinued operations, net of tax					(318,771)
Net loss available to common shareholders					$ (383,618)

(C) Non-cash compensation expense includes $5.9 million, $6.5 million, $63.6 million and $0.2 million which are included in cost of sales, selling and marketing expense, general and administrative expense and other operating expense, respectively, in the accompanying consolidated statement of operations.

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 5 SEGMENT INFORMATION (Continued)

	For The Nine Months Ended September 30, 2007				
	Operating Income Before Amortization	Non-Cash Compensation Expense(D)	Amortization of Non-Cash Marketing	Amortization of Intangibles	Operating Income (Loss)
Media & Advertising	$ 56,835	$	$ (22,849)	$ (18,502)	$ 15,484
Match	57,508		(7,244)	(661)	49,603
ServiceMagic	18,744	(467)		(2,174)	16,103
Emerging Businesses	35	(1,071)	(2,987)	(4,967)	(8,990)
Corporate	(65,713)	(50,822)			(116,535)
Total	$ 67,409	$ (52,360)	$ (33,080)	$ (26,304)	(44,335)
Other income, net					39,029
Loss from continuing operations before income taxes and minority interest					(5,306)
Income tax provision					(3,365)
Minority interest in losses of consolidated subsidiaries					1,490
Loss from continuing operations					(7,181)
Gain on sale of discontinued operations					33,524
Income from discontinued operations, net of tax					199,481
Net earnings available to common shareholders					$ 225,824

(D) Non-cash compensation expense includes $4.0 million, $4.4 million, $43.8 million and $0.1 million which are included in cost of sales, selling and marketing expense, general and administrative expense and other operating expense, respectively, in the accompanying consolidated statement of operations.

The Company maintains operations in the United States, the United Kingdom and other international territories. Geographic information about the United States and international territories is presented below:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(In thousands)			
Revenue:				
United States	$298,331	$284,208	$ 880,443	$818,092
All other countries	70,949	51,153	213,657	135,610
Total	$369,280	$335,361	$1,094,100	$953,702

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 5 SEGMENT INFORMATION (Continued)

	September 30, 2008	December 31, 2007
	(In thousands)	
Assets:		
Media & Advertising	$ 2,083,480	$ 1,961,934
Match	319,990	333,407
ServiceMagic	124,798	125,216
Emerging Businesses	209,661	208,210
Corporate and other	2,345,211	9,962,035
Total	$ 5,083,140	$ 12,590,802

	September 30, 2008	December 31, 2007
	(In thousands)	
Long-lived assets (excluding goodwill and intangible assets):		
United States	$ 333,634	$ 332,311
All other countries	1,903	2,030
Total	$ 335,537	$ 334,341

NOTE 6 DISCONTINUED OPERATIONS

On August 20, 2008, IAC completed the Spin-Off. In addition, on May 30, 2008 IAC sold EPI for approximately $34.9 million, which resulted in a pre-tax loss of $37.4 million and an after-tax gain of $22.3 million.

On June 19, 2007, IAC sold HSE, previously reported in the International segment of IAC's former Retailing sector, for approximately $216.5 million, which resulted in a pre-tax gain of $52.0 million, and an after-tax gain of $35.1 million. The pre-tax gain and the after-tax gain on the sale of HSE were subsequently reduced to $45.7 million and $31.1 million, respectively, in the third quarter of 2007. The pre-tax gain included $22.8 million of foreign currency translation gains that were recognized into earnings at the time of the sale.

Accordingly, HSNi, ILG, Ticketmaster and Tree.com are presented as discontinued operations in the accompanying consolidated balance sheet and consolidated statements of operations and cash flows for all periods presented. EPI and HSE are presented as discontinued operations through May 30, 2008 and June 19, 2007, respectively.

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

The net revenue and net earnings, net of the effect of any minority interest, for the aforementioned discontinued operations for the applicable periods were as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Net revenue	$658,720	$1,179,331	$3,144,662	$3,756,351
(Loss) earnings before income taxes and minority interest	$ (2,461)	$ 101,362	$ (312,968)	$ 300,489
Income tax provision	(12,920)	(35,706)	(7,914)	(102,664)
Minority interest in losses of consolidated subsidiaries	663	1,454	2,111	1,656
Net (loss) earnings	$ (14,718)	$ 67,110	$ (318,771)	$ 199,481

The assets and liabilities of EPI at December 31, 2007 have been classified in the accompanying consolidated balance sheet as "Assets held for sale" (which is included in "Prepaid expenses and other current assets") and "Liabilities held for sale" (which is included in "Accrued expenses and other current liabilities"). Such net assets held for sale consist of the following (in thousands):

	December 31, 2007
Current assets	$ 30,847
Goodwill	19,350
Intangible assets, net	41,660
Other non-current assets	35,139
Assets held for sale	126,996
Current liabilities	(56,928)
Other long-term liabilities	(2,761)
Liabilities held for sale	(59,689)
Net assets held for sale	$ 67,307

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

The assets and liabilities transferred to HSNi, ILG, Ticketmaster and Tree.com as of August 20, 2008 and reported as discontinued operations as of December 31, 2007 were as follows (in thousands):

	August 20, 2008	December 31, 2007
Current assets	$ 1,662,321	$ 1,020,034
Goodwill	4,559,660	4,629,885
Intangible assets, net	946,007	961,322
Other non-current assets	631,443	510,536
Non-current assets	6,137,110	6,101,743
Current liabilities	(1,265,478)	(1,265,307)
Deferred income taxes	(955,746)	(962,170)
Other long-term liabilities	(1,606,923)	(165,309)
Non-current liabilities	(2,562,669)	(1,127,479)
Net assets	$ 3,971,284	$ 4,728,991

NOTE 7 EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted (loss) earnings per share.

	Three Months Ended September 30,			
	2008		2007	
	Basic	Diluted	Basic	Diluted
	(In thousands, except per share data)			
Numerator:				
Net (loss) earnings from continuing operations(a)(b)	$ (886)	$ (886)	$ 4,918	$ 4,918
(Loss) income from discontinued operations, net of tax	(13,951)	(13,951)	65,553	65,553
Net (loss) earnings available to common shareholders	$ (14,837)	$ (14,837)	$ 70,471	$ 70,471
Denominator:				
Basic shares outstanding	140,054	140,054	142,481	142,481
Dilutive securities including stock options, warrants and restricted stock and share units				6,492
Denominator for earnings per share weighted average shares(c)(d)	140,054	140,054	142,481	148,973
(Loss) earnings per share:				
(Loss) earnings from continuing operations	$ (0.01)	$ (0.01)	$ 0.03	$ 0.03
Discontinued operations, net of tax	(0.10)	(0.10)	0.46	0.44
(Loss) earnings available to common shareholders	$ (0.11)	$ (0.11)	$ 0.49	$ 0.47

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 7 EARNINGS PER SHARE (Continued)

	Nine Months Ended September 30,			
	2008		2007	
	Basic	Diluted	Basic	Diluted
	(In thousands, except per share data)			
Numerator:				
Net loss from continuing operations(a)(b)	$ (88,161)	$ (88,161)	$ (7,181)	$ (7,181)
(Loss) income from discontinued operations, net of tax	(295,457)	(295,457)	233,005	233,005
Net (loss) earnings available to common shareholders	$ (383,618)	$ (383,618)	$ 225,824	$ 225,824
Denominator:				
Basic shares outstanding	139,625	139,625	143,253	143,253
Dilutive securities including stock options, warrants and restricted stock and share units				
Denominator for earnings per share weighted average shares(c)(d)	139,625	139,625	143,253	143,253
(Loss) earnings per share:				
Loss from continuing operations	$ (0.63)	$ (0.63)	$ (0.05)	$ (0.05)
Discontinued operations, net of tax	(2.12)	(2.12)	1.63	1.63
(Loss) earnings available to common shareholders	$ (2.75)	$ (2.75)	$ 1.58	$ 1.58

(a) During the second quarter of 2008 all outstanding Convertible Notes were fully converted.

(b) For the three and nine months ended September 30, 2007, approximately 0.2 million and 0.3 million weighted average common shares, respectively, related to the assumed conversion of the Company's Convertible Notes were excluded from the calculation of diluted earnings per share because the effect would be anti-dilutive.

(c) Weighted average common shares outstanding include the incremental shares that would be issued upon the assumed exercise of stock options and warrants and vesting of restricted stock units. For the three and nine months ended September 30, 2008, approximately 56.6 million that could potentially dilute basic earnings per share in the future were excluded from the calculation of diluted earnings per share because their inclusion would have been anti-dilutive.

(d) Weighted average common shares outstanding include the incremental shares that would be issued upon the assumed exercise of stock options and warrants, vesting of restricted stock units and conversion of the Company's Convertible Notes. For the three and nine months ended September 30, 2007, approximately 17.6 million and 10.1 million shares, respectively, that could potentially dilute basic earnings per share in the future were excluded from the calculation of diluted earnings per share because their inclusion would have been anti-dilutive.

NOTE 8 EQUITY INVESTMENTS IN UNCONSOLIDATED AFFILIATES

At September 30, 2008 and December 31, 2007, the Company's equity investments in unconsolidated affiliates totaled $187.5 million and $148.0 million, respectively, and are included in "Long-term investments" in the accompanying consolidated balance sheet. Pursuant to an agreement with Points International, Ltd. ("Points"), on June 11, 2008, IAC converted its preferred shares of

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 8 EQUITY INVESTMENTS IN UNCONSOLIDATED AFFILIATES (Continued)

Points into 29.4 million common shares of Points, sold 27.8 million of such common shares to a syndicate of underwriters for $42.4 million and surrendered the remaining 1.6 million common shares to Points for cancellation. In addition, IAC's nominees to the board of directors of Points stepped down. The transaction resulted in a pre-tax gain of $29.1 million, which is included in "Other (expense) income" in the accompanying consolidated statement of operations. As a result of this transaction, IAC no longer accounts for its remaining investment in Points using the equity method of accounting but rather accounts for such investment as available-for-sale marketable equity securities in accordance with SFAS No. 115.

Summarized financial information for the Company's equity investment in Jupiter Shop Channel is as follows (in thousands):

	Nine Months Ended September 30,	
	2008	**2007**
Net sales	$729,001	$619,118
Gross profit	293,745	240,060
Net income	70,985	61,840

Summarized aggregated financial information for the Company's remaining equity investments is as follows (in thousands):

	Nine Months Ended September 30,	
	2008	**2007**
Net sales	$ 7,161	$ 560
Gross profit	3,777	N/A
Net loss	(16,934)	(5,400)

NOTE 9 LONG-TERM OBLIGATIONS

	September 30, 2008	**December 31, 2007**
	(In thousands)	
7.00% Senior Notes due January 15, 2013 (the "Senior Notes"); interest payable each January 15 and July 15 which commenced July 15, 2003	$ 15,844	$ 750,000
5% New York City Industrial Development Agency Liberty Bonds due September 1, 2035; interest payable each March 1 and September 1 which commenced March 1, 2006	80,000	80,000
Ask Zero Coupon Convertible Subordinated Notes due June 1, 2008 (the "Convertible Notes")		12,349
Total gross obligations	95,844	842,349
Fair value basis adjustment attributable to hedged debt obligations		4,542
Unamortized discount		(259)
Total long-term obligations	95,844	846,632
Less current maturities of long-term obligations		(12,090)
Long-term obligations, net of current maturities	$ 95,844	$ 834,542

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 9 LONG-TERM OBLIGATIONS (Continued)

On August 20, 2008, the Company purchased for cash $456.7 million in principal amount of Senior Notes validly tendered pursuant to its amended tender offer to purchase the outstanding Senior Notes. Concurrent with the tender offer and in connection with the Spin-Off, the Company exchanged an additional $277.4 million in principal amount of Senior Notes for the debt of ILG. In connection with the tender offer and the exchange, the Company recorded a net loss of $63.2 million on the extinguishment of $734.2 million of the Senior Notes which is recorded in "Other (expense) income" in the accompanying consolidated statement of operations. The Company also unwound its remaining interest rate swap agreements for nominal gains.

During the second quarter of 2008, the Convertible Notes were fully converted.

Aggregate contractual maturities of long-term obligations are as follows (in thousands):

Years Ending September 30,	
2013	$15,844
2035	80,000
	$95,844

NOTE 10 FAIR VALUE MEASUREMENTS

Effective January 1, 2008, the Company adopted SFAS No. 157, "Fair Value Measurements" ("SFAS No. 157"). In accordance with SFAS No. 157, the Company categorizes its assets and liabilities measured at fair value into a fair value hierarchy that prioritizes the assumptions used in pricing the asset or liability into the following three levels:

Level 1: Observable inputs such as quoted prices for identical assets and liabilities in active markets obtained from independent sources.

Level 2: Other inputs that are observable directly or indirectly, such as quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active and inputs that are derived principally from or corroborated by observable market data.

Level 3: Unobservable inputs for which there is little or no market data and require the Company to develop its own assumptions, based on the best information available in the circumstances, about the assumptions market participants would use in pricing the asset or liability.

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 10 FAIR VALUE MEASUREMENTS (Continued)

The following table presents the Company's assets and liabilities that are measured at fair value on a recurring basis at September 30, 2008:

	Recurring Fair Value Measurements Using			
	Quoted Market Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value Measurements
	(In thousands)			
Marketable securities	$ 120,672	$ 843	$	$ 121,515
Long-term investments	33,932		13,250	47,182
Derivative assets created in the Expedia spin-off			5	5
Derivative liabilities created in the Expedia spin-off			(70)	(70)
Derivative asset created in the HSE sale			58,617	58,617
Total	$ 154,604	$ 843	$ 71,802	$ 227,249

The following tables present the changes in the Company's assets and liabilities that are measured at fair value on a recurring basis using significant unobservable inputs (Level 3):

	For the Three Months Ended September 30, 2008		
	Long-Term Investments	Net Derivatives Created in the Expedia Spin-Off	Derivative Asset Created in the HSE Sale
	(In thousands)		
Balance at July 1, 2008	$ 13,835	$ (100)	$ 69,730
Total net gains or losses (realized and unrealized):			
Included in earnings		35	(5,137)
Included in other comprehensive income	(585)		(5,976)
Balance at September 30, 2008	$ 13,250	$ (65)	$ 58,617

	For The Nine Months Ended September 30, 2008		
	Long-Term Investments	Net Derivatives Created in the Expedia Spin-Off	Derivative Asset Created in the HSE Sale
	(In thousands)		
Balance at January 1, 2008	$ 14,763	$ 890	$ 54,656
Total net gains or losses (realized and unrealized):			
Included in earnings		545	5,785
Included in other comprehensive income	(1,513)		(1,824)
Purchases, sales, issuances and settlements, net		(1,500)	

Balance at September 30, 2008	$ 13,250	$ (65)	$ 58,617

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 10 FAIR VALUE MEASUREMENTS (Continued)

The following tables present the gains and losses included in earnings for the three and nine months ended September 30, 2008 relating to the Company's assets and liabilities that are measured at fair value on a recurring basis using significant unobservable inputs (Level 3):

	For the Three Months Ended September 30, 2008	
	Net Derivatives Created in the Expedia Spin-Off	Derivative Asset Created in the HSE Sale
	(In thousands)	
Total gains (losses) included in earnings for the three months ended September 30, 2008:		
Other income (expense)	$ 35	$ (5,137)
Total	$ 35	$ (5,137)
Change in unrealized gains (losses) relating to assets and liabilities still held at September 30, 2008:		
Other income (expense)	$ 35	$ (5,137)
Total	$ 35	$ (5,137)

	For The Nine Months Ended September 30, 2008	
	Net Derivatives Created in the Expedia Spin-Off	Derivative Asset Created in the HSE Sale
	(In thousands)	
Total gains included in earnings for the nine months ended September 30, 2008:		
Other income	$ 545	$ 5,785
Total	$ 545	$ 5,785
Change in unrealized gains relating to assets and liabilities still held at September 30, 2008:		
Other income	$ 145	$ 5,785
Total	$ 145	$ 5,785

Long-term Investments

Long-term investments in the table above that are measured at fair value using significant unobservable inputs (Level 3) include available-for-sale auction rate securities accounted for in accordance with SFAS No. 115. In the third quarter of 2007, these auction rate securities had failed auctions due to sell orders exceeding buy orders. These auction rate securities are valued by discounting the future cash flow streams of the securities over the estimated period that the securities will be held. Credit spreads and other risk factors are also considered in establishing a fair value. At September 30, 2008, $13.3 million, which is net of an unrealized loss of $1.7 million, was associated with failed auctions and accordingly, was reclassified as long-term investments in the first quarter of 2008. These auction rate securities are rated either AA/A2 or AA/Aa3. Due to their high rating and the general quality of the investments underlying the portfolios, the unrealized loss related to these securities is not considered to be an other-than-temporary impairment.

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 10 FAIR VALUE MEASUREMENTS (Continued)

Derivative assets and liabilities created in the Expedia spin-off and sale of HSE

The derivative assets and derivative liabilities created in the Expedia spin-off and the derivative asset created in the sale of HSE are maintained at fair value. The derivative asset created in the sale of HSE is valued using Monte Carlo simulation relying on various observable and unobservable inputs including risk free interest rates, stock price volatility and credit risk.

NOTE 11 SUPPLEMENTAL CASH FLOW INFORMATION

Supplemental Disclosure of Non-Cash Transactions for the Nine Months ended September 30, 2008

During the nine months ended September 30, 2008, $12.3 million in aggregate principal amount of Convertible Notes was converted by the holders. Upon conversion, 0.2 million shares of IAC common stock and 0.2 million shares of Expedia common stock were issued to the holders.

After the close of trading on August 20, 2008, IAC completed the Spin-Off. The net assets comprising the spun-off businesses, net of cash of $728.0 million, amounted to $3.2 billion and is included in the accompanying consolidated statement of shareholders' equity as a reduction to additional paid-in capital and retained earnings.

Additionally, on August 20, 2008, the Company exchanged $277.4 million of the Senior Notes for the debt of ILG in connection with the Spin-Off.

Supplemental Disclosure of Non-Cash Transactions for the Nine Months ended September 30, 2007

On June 19, 2007, IAC completed the sale of HSE and received approximately 5.5 million shares of ARO stock and a derivative asset, valued at $190.1 million and $27.1 million, respectively.

During the nine months ended September 30, 2007, $7.7 million in aggregate principal amount of Convertible Notes was converted by the holders. Upon conversion, 0.1 million shares of IAC common stock and 0.1 million shares of Expedia common stock were issued to the holders.

NOTE 12 COMPREHENSIVE INCOME

Comprehensive (loss) income is comprised of (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	**2007**	**2008**	**2007**
Net (loss) earnings available to common shareholders	$ (14,837)	$ 70,471	$ (383,618)	$ 225,824
Foreign currency translation	(41,285)	25,872	(29,377)	18,906
Unrealized losses on available for sale securities	(47,015)	(2,303)	(47,820)	(7,112)
Unrealized losses recognized into earnings in connection with the impairment of available-for-sale securities			46,058	
Net losses on derivative contracts		(94)		(2,355)
Other comprehensive (loss) income	(88,300)	23,475	(31,139)	9,439
Comprehensive (loss) income	$ (103,137)	$ 93,946	$ (414,757)	$ 235,263

For the nine months ended September 30, 2008, foreign currency translation gains, net of tax, relating to the ARO Shares of $5.8 million were recognized into earnings in connection with the other-than-temporary impairment of these shares recorded in the second quarter of 2008. There was no other-than-temporary impairment of the ARO Shares recorded in the third quarter of 2008.

IAC/INTERACTIVECORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 12 COMPREHENSIVE INCOME (Continued)

Accumulated other comprehensive (loss) income, net of tax, is comprised of (in thousands):

	September 30, 2008	December 31, 2007
Foreign currency translation	$ 18,931	$ 85,775
Unrealized losses on available for sale securities	(47,723)	(45,961)
Accumulated other comprehensive (loss) income	$ (28,792)	$ 39,814

NOTE 13 INCOME TAXES

The Company calculates its interim income tax provision in accordance with Accounting Principles Board Opinion No. 28 and FASB Interpretation No. 18. At the end of each interim period, the Company makes its best estimate of the annual expected effective tax rate and applies that rate to its ordinary year-to-date earnings or loss. The income tax provision or benefit related to significant, unusual, or extraordinary items that will be separately reported or reported net of their related tax effect are individually computed and recognized in the interim period in which those items occur. In addition, the effect of changes in enacted tax laws or rates, tax status, or judgment on the realizability of a beginning-of-the-year deferred tax asset in future years is recognized in the interim period in which the change occurs.

The computation of the annual expected effective tax rate at each interim period requires certain estimates and assumptions including, but not limited to, the expected operating income for the year, projections of the proportion of income (or loss) earned and taxed in foreign jurisdictions, permanent and temporary differences, and the likelihood of recovering deferred tax assets generated in the current year. The accounting estimates used to compute the provision for income taxes may change as new events occur, more experience is acquired, additional information is obtained or our tax environment changes. To the extent that the estimated annual effective tax rate changes during a quarter, the effect of the change on prior quarters is included in tax expense for the current quarter. Included in the income tax provision for the three months ended September 30, 2008 is a provision of $0.7 million due to a change in the estimated annual effective tax rate from that used in the second quarter.

For the three and nine months ended September 30, 2008, the Company recorded income tax benefits for continuing operations of $85.3 million and $103.6 million, respectively, which represent effective tax rates of 99% and 54%, respectively. These tax rates are higher than the federal statutory rate of 35% due principally to benefits from a net reduction in deferred tax liabilities caused by the Spin-Off, foreign income taxed at lower rates and state income tax benefits, partially offset by an increase in the valuation allowance on deferred tax assets related to the ARO Shares, changes in tax reserves, and non-deductible costs related to the Spin-Off.

For the three months ended September 30, 2007, the Company recorded an income tax provision for continuing operations of $11.1 million which represents an effective tax rate of 76%. For the nine months ended September 30, 2007, the Company recorded an income tax provision for continuing operations of $3.4 million despite a loss from continuing operations of $5.3 million. These income tax provisions are principally due to an increase in tax reserves and related interest and net adjustments related to the reconciliation of tax returns to provision accruals, partially offset by a non-taxable gain on the fair value of derivatives that were created in connection with the sale of HSE and the Expedia spin-off, foreign tax credits and tax exempt income.

At September 30, 2008 and December 31, 2007, the Company had unrecognized tax benefits of approximately $357.5 million and $231.0 million, respectively. Unrecognized tax benefits for the nine

NOTE 13 INCOME TAXES (Continued)

months ended September 30, 2008 increased by $126.5 million due principally to an unrecognized current year capital loss on the Company's investment in Tree.com, partially offset by the effective settlement of prior year tax positions with the Internal Revenue Service principally relating to the reversal of deductible temporary differences. The Company recognizes interest and, if applicable, penalties related to unrecognized tax benefits in income tax provision. Included in the income tax provision for the three and nine months ended September 30, 2008 is $1.0 million and $6.3 million, net of related deferred taxes, for interest on unrecognized tax benefits. At September 30, 2008, the Company has accrued $45.8 million for the payment of interest. There are no material accruals for penalties.

The Company is routinely under audit by federal, state, local and foreign authorities in the area of income tax. These audits include questioning the timing and the amount of deductions and the allocation of income among various tax jurisdictions. Income tax provisions include amounts considered sufficient to pay assessments that may result from examination of prior year returns; however, the amount paid upon resolution of issues raised may differ from the amount provided. Differences between the reserves for tax contingencies and the amounts owed by the Company are recorded in the period they become known. If unrecognized tax benefits are subsequently recognized, approximately $49.8 million and $172.0 million, net of related deferred tax assets, would reduce income tax expense from continuing operations and discontinued operations, respectively.

The IRS is currently examining the Company's tax returns for the years ended December 31, 2001 through 2003. The statute of limitations for these years has been extended to December 31, 2009. Various state, local and foreign jurisdictions are currently under exam, the most significant of which are California, Florida, New York and New York City, for various tax years after December 31, 2001, and the examinations are expected to be completed in 2009. The Company believes that it is reasonably possible that its unrecognized tax benefits could decrease by approximately $17.5 million within twelve months of the current reporting date due to settlements and the reversal of deductible temporary differences which will result in a corresponding increase in net deferred tax liabilities. An estimate of other changes in unrecognized tax benefits, while potentially significant, cannot be made.

NOTE 14 CONTINGENCIES

In the ordinary course of business, the Company is a party to various lawsuits. The Company establishes reserves for specific legal matters when it determines that the likelihood of an unfavorable outcome is probable and the loss is reasonably estimable. Management has also identified certain other legal matters where we believe an unfavorable outcome is not probable and, therefore, no reserve is established. Although management currently believes that resolving claims against us, including claims where an unfavorable outcome is reasonably possible, will not have a material impact on the liquidity, results of operations, or financial condition of the Company, these matters are subject to inherent uncertainties and management's view of these matters may change in the future. It is possible that an unfavorable outcome of one or more of these lawsuits could have a material impact on the liquidity, results of operations, or financial condition of the Company. The Company also evaluates other contingent matters, including tax contingencies, to assess the probability and estimated extent of potential loss. See Note 13 for additional information related to income tax contingencies.

Item 2. ***Management's Discussion and Analysis of Financial Condition and Results of Operations***

GENERAL

Management Overview

On August 20, 2008, IAC completed its previously announced plan to separate into five publicly traded companies:

- IAC, which includes:
  - the businesses comprising its Media & Advertising segment;
  - the Match and ServiceMagic segments;
  - the businesses comprising its Emerging Businesses segment, including Shoebuy and ReserveAmerica, which were formerly included in the Retailing and Ticketmaster segments, respectively; and
  - certain investments in unconsolidated affiliates.
- HSN, Inc. ("HSNi"), which includes HSN TV, *HSN.com*, and the Cornerstone Brands, Inc. portfolio of catalogs, websites and retail locations;
- Interval Leisure Group, Inc. ("ILG"), which includes the businesses that comprised the Interval segment;
- Ticketmaster, which includes its primary domestic and international operations as well as certain investments in unconsolidated affiliates; and
- Tree.com, Inc. ("Tree.com"), which includes the businesses that comprised the Lending and Real Estate segments.

We refer to this transaction as the "Spin-Off". Immediately subsequent to the Spin-Off, IAC effected a one-for-two reverse stock split. All share information, unless otherwise noted, reflects the impact of the reverse stock split and is not adjusted for the relative values of the spun-off businesses.

The results of operations of HSNi, ILG, Ticketmaster and Tree.com have been classified as discontinued operations for all periods presented.

All references to "IAC," the "Company," "we," "our" or "us" in this report are to IAC/InterActiveCorp.

During the first quarter of 2008, in contemplation of the Spin-Off, IAC reorganized its then existing Retailing, Ticketmaster and Emerging Businesses reporting segments. Shoebuy and ReserveAmerica, which were previously included in the Retailing and Ticketmaster reporting segments, respectively, are now included in the Emerging Businesses segment. Information for all prior periods has been reclassified to conform with the current year segment presentation.

For a more detailed presentation of the Company's operating businesses, see the Company's annual report on Form 10-K for the year ended December 31, 2007, as amended.

Results of operations for the three and nine months ended September 30, 2008 compared to the three and nine months ended September 30, 2007:

Set forth below are the contributions made by our various segments and corporate expenses to consolidated revenue, operating (loss) income and Operating Income Before Amortization (as defined in IAC's Principles of Financial Reporting) for the three and nine months ended September 30, 2008 and 2007 (rounding differences may occur):

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2008	2007	Growth	2008	2007	Growth
	(Dollars in thousands)					
Revenue:						
Media & Advertising	$193,273	$189,824	2%	$ 595,136	$531,901	12%
Match	93,540	89,109	5%	277,358	258,111	7%
ServiceMagic	33,799	24,591	37%	98,618	71,453	38%
Emerging Businesses	49,644	36,319	37%	141,945	99,341	43%
Inter-segment elimination	(976)	(4,482)	78%	(18,957)	(7,104)	(167)%
Total	$369,280	$335,361	10%	$1,094,100	$953,702	15%

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2008	2007	Growth	2008	2007	Growth
	(Dollars in thousands)					
Operating (Loss) Income:						
Media & Advertising	$ 32,106	$ 15,675	105%	$ 93,166	$ 15,484	502%
Match	23,978	29,272	(18)%	50,740	49,603	2%
ServiceMagic	8,111	4,626	75%	22,627	16,103	41%
Emerging Businesses	(7,390)	(9,912)	25%	(25,829)	(8,990)	(187)%
Corporate	(79,443)	(37,968)	(109)%	(180,884)	(116,535)	(55)%
Total	$(22,638)	$ 1,693	NM	$ (40,180)	$ (44,335)	9%

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2008	2007	Growth	2008	2007	Growth
	(Dollars in thousands)					
Operating Income Before Amortization:						
Media & Advertising	$ 38,810	$ 27,898	39%	$ 112,189	$ 56,835	97%
Match	30,274	29,530	3%	63,278	57,508	10%
ServiceMagic	8,651	5,420	60%	24,245	18,744	29%
Emerging Businesses	(6,070)	(3,457)	(76)%	(21,705)	35	NM
Corporate	(41,201)	(21,724)	(90)%	(105,980)	(65,713)	(61)%
Total	$ 30,464	$ 37,667	(19)%	$ 72,027	$ 67,409	7%

Refer to Note 5 to the consolidated financial statements for reconciliations by segment of Operating Income Before Amortization to Operating (Loss) Income.

Consolidated Results

Revenue

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

Revenue in 2008 increased 10% or $33.9 million from 2007 primarily as a result of revenue increases of $13.3 million from Emerging Businesses, $9.2 million from ServiceMagic, $4.4 million from Match and $3.4 million from Media & Advertising. The contribution from Emerging Businesses was driven primarily by strong revenue growth at Pronto.com and Shoebuy. The increase at ServiceMagic reflected a more active service provider network and a 41% increase in service requests driven by increased marketing efforts. Also contributing to the increased revenue was a 3% increase in average revenue per subscriber, primarily in international markets, and a 3% increase in worldwide subscribers at Match. The increase at Media & Advertising was driven by strong growth from proprietary search properties. Revenue per query on proprietary web search properties grew primarily from improved economics associated with the renewed partnership with Google and, even excluding the renewed partnership, revenue per query grew. Entirely offsetting this increase in proprietary revenue is a sharp decline in network revenue, resulting from the planned discontinuation of relationships with certain partners that took place during 2008 in conjunction with the renewed partnership. Media & Advertising revenue was further impacted by the acquisition of Lexico, which includes Dictionary.com and Thesaurus.com, on July 3, 2008 which contributed $3.6 million to revenue in 2008.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

Revenue in 2008 increased 15% or $140.4 million from 2007 primarily as a result of revenue increases of $63.2 million from Media & Advertising, $42.6 million from Emerging Businesses, $27.2 million from ServiceMagic and $19.2 million from Match. The growth from Media & Advertising, Emerging Businesses, ServiceMagic and Match was primarily due to the factors described above in the three month discussion.

Cost of sales

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

	Three Months Ended September 30,		
	2008	**% Change**	**2007**
	(Dollars in thousands)		
Cost of sales	$134,210	(5)%	$140,644
As a percentage of total revenue	36%	(559) bp	42%
Gross margins	64%	559 bp	58%

bp = basis points

Cost of sales consists primarily of traffic acquisition costs, compensation and other employee-related costs (including stock-based compensation) for personnel engaged in data center functions, customer acquisition costs, the cost of products sold and shipping and handling costs. Traffic acquisition costs consist of revenue share payments to partners that have distributed toolbars and/or integrated sponsored listings into their websites and similar arrangements with third parties who direct traffic to our websites.

Cost of sales in 2008 decreased $6.4 million from 2007 primarily due to a decrease of $14.6 million from Media & Advertising, partially offset by increases of $4.7 million from ServiceMagic and $3.6 million from Emerging Businesses. The decrease in cost of sales from Media & Advertising was principally due to a decrease of $14.6 million in revenue share payments to third party traffic sources. Overall revenue share payments during the quarter decreased as a direct result of a decrease in network revenue, partially offset by growth in distribution revenue included as a component of proprietary revenue at IAC Search & Media. As a percentage of revenue, traffic acquisition costs associated with network revenue generated from integrated sponsored listings are lower than traffic acquisition costs associated with distribution revenue generated from partners who redirect traffic to the Ask.com landing page. The increase in cost of sales from ServiceMagic was primarily due to an increase in customer acquisition costs as it continued to focus its spend on driving higher margin home repair and improvement requests and increasing service requests during this weak macro environment. Cost of sales from Emerging Businesses increased primarily due to an increase of $2.4 million in cost of products sold and $0.9 million in shipping and handling costs at Shoebuy.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

	Nine Months Ended September 30,		
	2008	**% Change**	**2007**
	(Dollars in thousands)		
Cost of sales	$398,172	2%	$389,051
As a percentage of total revenue	36%	(440) bp	41%
Gross margins	64%	440 bp	59%

Cost of sales in 2008 increased $9.1 million from 2007 primarily due to increases of $17.4 million from Emerging Businesses and $13.9 million from ServiceMagic, partially offset by decreases of $17.2 million from Media & Advertising and $4.9 million from Match. The increase in cost of sales from Emerging Businesses was primarily due to an increase of $6.9 million in cost of products sold and $2.8 million in shipping and handling costs at Shoebuy. Cost of sales from Emerging Businesses was further impacted by increased costs associated with Gifts.com and various early stage businesses not in the year ago period. Also contributing to the increase in cost of sales were increased customer acquisition costs from ServiceMagic as described above in the three month discussion. Partially offsetting these increases in cost of sales was a decrease in revenue share payments to third party traffic sources from Media & Advertising and decreased domestic customer acquisition costs from Match. The decrease in domestic acquisition costs from Match was due primarily to improved economics with certain distribution partners.

Selling and marketing expense

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

	Three Months Ended September 30,		
	2008	**% Change**	**2007**
	(Dollars in thousands)		
Selling and marketing expense	$102,620	26%	$81,639
As a percentage of total revenue	28%	345 bp	24%

Selling and marketing expense consists primarily of advertising and promotional expenditures and compensation and other employee-related costs (including stock-based compensation) for personnel engaged in customer service and sales functions. Advertising and promotional expenditures include online marketing, including fees paid to search engines and distribution partners, and offline marketing, including television, print and radio advertising.

Selling and marketing expense in 2008 increased $21.0 million from 2007 primarily due to increases of $7.5 million from Emerging Businesses, $6.5 million from Match and $3.8 million from Media & Advertising. The increase in selling and marketing expense from Emerging Businesses resulted primarily from an increase of $5.6 million in online marketing from Pronto.com. Selling and marketing expense from Match increased primarily due to an increase of $4.4 million in advertising and promotional expenditures, including those associated with television advertising and online marketing related to various international marketing campaigns. Also contributing to the increase in selling and marketing expense is increased expense from Media & Advertising primarily due to an increase of $3.5 million in compensation and other employee-related costs, partially offset by reduced marketing expense. The increase in compensation and other employee-related costs is due in part to recent acquisitions not in the year ago period at IAC Search & Media and an 11% increase in average headcount at Citysearch.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

	Nine Months Ended September 30,		
	2008	% Change	2007
	(Dollars in thousands)		
Selling and marketing expense	$327,758	16%	$283,029
As a percentage of total revenue	30%	28 bp	30%

Selling and marketing expense in 2008 increased $44.7 million from 2007, primarily due to increases of $21.6 million from Emerging Businesses, $15.6 million from Match and $3.9 million from ServiceMagic. The increase in selling and marketing expense from Emerging Businesses is primarily due to an increase of $17.5 million in online marketing from Pronto.com. Selling and marketing expense from Match increased primarily due to an increase of $14.9 million in advertising and promotional expenditures, including marketing costs primarily related to Chemistry.com. Also contributing to the increase in selling and marketing expense is an increase of $3.8 million in compensation and other employee-related costs from ServiceMagic primarily related to the expansion of its sales force due in part to the opening of a new call center in Kansas City in the second quarter of 2007.

General and administrative expense

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

	Three Months Ended September 30,		
	2008	% Change	2007
	(Dollars in thousands)		
General and administrative expense	$110,997	71%	$64,910
As a percentage of total revenue	30%	1,070 bp	19%

General and administrative expense consists primarily of compensation and other employee-related costs (including stock-based compensation) for personnel engaged in finance, legal, tax, human resources and executive management functions, facilities costs and fees for professional services.

General and administrative expense in 2008 increased $46.1 million from 2007 primarily due to increases of $38.9 million from corporate and $3.8 million from Emerging Businesses. The increase from corporate is principally due to $20.8 million of expenses related to the Spin-Off and an increase of $18.3 million in non-cash compensation expense. The increase in non-cash compensation expense is primarily due to the acceleration and modification of certain equity awards associated with the Spin-Off. General and administrative expense from Emerging Businesses increased primarily due to increased operating expenses associated with various early stage businesses not in the year ago period as well as Connected Ventures.

As of September 30, 2008, there was approximately $135.1 million of unrecognized compensation cost, net of estimated forfeitures, related to all equity based awards, which is currently expected to be recognized over a weighted average period of approximately 2.7 years.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

	Nine Months Ended September 30,		
	2008	% Change	2007
	(Dollars in thousands)		
General and administrative expense	$278,340	47%	$189,442
As a percentage of total revenue	25%	558 bp	20%

General and administrative expense in 2008 increased $88.9 million from 2007 primarily due to increases of $61.2 million from corporate and $22.0 million from Emerging Businesses. The increase from corporate is principally due to $42.0 million of expenses related to the Spin-Off and an increase of $20.1 million in non-cash compensation expense. The increase in non-cash compensation expense is primarily due to the factors described above in the three month discussion. General and administrative expense from Emerging Businesses increased primarily due to the inclusion in the prior year of an $8.2 million reimbursement of previously expensed advances related to the restructuring of our interests in a business venture as well as increased operating expenses associated with InstantAction.com, Connected Ventures, RushmoreDrive.com and various early stage businesses not in the year ago period.

Other operating expense

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

	Three Months Ended September 30,		
	2008	**% Change**	**2007**
	(Dollars in thousands)		
Other operating expense	$12,329	2%	$12,029
As a percentage of total revenue	3%	(25) bp	4%

Other operating expense consists primarily of compensation and other employee-related costs (including stock-based compensation) for personnel engaged in product development at IAC Search & Media and various emerging businesses. Other operating expense includes costs related to the design, development, testing and enhancement of technology that are not capitalized.

Other operating expense in 2008 increased $0.3 million from 2007, primarily due to an increase in compensation and other employee-related costs from Emerging Businesses.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

	Nine Months Ended September 30,		
	2008	**% Change**	**2007**
	(Dollars in thousands)		
Other operating expense	$41,922	26%	$33,177
As a percentage of total revenue	4%	35 bp	3%

Other operating expense in 2008 increased $8.7 million from 2007, primarily due to an increase of $6.8 million in compensation and other employee-related costs from Media & Advertising. The increase from Media & Advertising is due in part to a 9% increase in average headcount, as it continues to upgrade and enhance its search technology and products.

Depreciation

For the three and nine months ended September 30, 2008 compared to the three and nine months ended September 30, 2007

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2008	**% Change**	**2007**	**2008**	**% Change**	**2007**
	(Dollars in thousands)					
Depreciation	$17,337	15%	$15,107	$52,055	18%	$43,954
As a percentage of total revenue	5%	19 bp	5%	5%	15 bp	5%

Depreciation for the three and nine months ended September 30, 2008 increased $2.2 million and $8.1 million, respectively, primarily due to the incremental depreciation associated with capital expenditures made during 2007 and 2008, partially offset by certain fixed assets becoming fully depreciated during the period.

Operating Income Before Amortization

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

	Three Months Ended September 30,		
	2008	% Change	2007
	(Dollars in thousands)		
Operating Income Before Amortization	$30,464	(19)%	$37,667
As a percentage of total revenue	8%	(298) bp	11%

Operating Income Before Amortization in 2008 decreased $7.2 million from 2007 primarily due to an increase in corporate expenses of $19.5 million, partially offset by growth of $10.9 million from Media & Advertising. The decrease in Operating Income Before Amortization from corporate is principally due to $20.8 million of expenses related to the Spin-Off. This increase in corporate expenses was partially offset by lower traffic acquisition costs and higher revenue from Media & Advertising.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

	Nine Months Ended September 30,		
	2008	% Change	2007
	(Dollars in thousands)		
Operating Income Before Amortization	$72,027	7%	$67,409
As a percentage of total revenue	7%	(49) bp	7%

Operating Income Before Amortization in 2008 increased $4.6 million from 2007 primarily due to growth of $55.4 million, $5.8 million and $5.5 million from Media & Advertising, Match and ServiceMagic, respectively. These increases in Operating Income Before Amortization were partially offset by decreases of $40.3 million from corporate and $21.7 million from Emerging Businesses. Contributing favorably to Operating Income Before Amortization is the impact of higher revenue and lower traffic acquisition costs from Media & Advertising. Partially offsetting the increases in Operating Income Before Amortization at certain segments are $42.0 million of expenses from corporate related to the Spin-Off and the favorable impact in the prior year of an $8.2 million reimbursement of previously expensed advances related to the restructuring of our interests in a business venture within Emerging Businesses, as well as increased operating expenses associated with RushmoreDrive.com, various early stage businesses not in the year ago period, InstantAction.com and Connected Ventures.

Operating (loss) income

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

	Three Months Ended September 30,		
	2008	% Change	2007
	(Dollars in thousands)		
Operating (loss) income	$(22,638)	NM	$1,693
As a percentage of total revenue	(6)%	NM	1%

The operating loss in 2008 of $22.6 million versus operating income in 2007 of $1.7 million was primarily due to the decrease of $7.2 million in Operating Income Before Amortization described above and an increase of $22.0 million in non-cash compensation expense, partially offset by a decrease of $2.9 million in amortization of non-cash marketing and a decrease of $2.0 million in amortization of intangibles. The increase in non-cash compensation expense is primarily due to the acceleration and modification of certain equity awards associated with the Spin-Off. The amortization of non-cash marketing referred to in this report consists of non-cash advertising secured from Universal Television as part of the transaction pursuant to which Vivendi Universal Entertainment, LLLP ("VUE") was created, and the subsequent transaction by which IAC sold its partnership interests in VUE.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

	Nine Months Ended September 30,		
	2008	% Change	2007
	(Dollars in thousands)		
Operating loss	$(40,180)	9%	$(44,335)
As a percentage of total revenue	(4)%	(98) bp	(5)%

Operating loss in 2008 decreased $4.2 million from 2007 primarily due to the increase of $4.6 million in Operating Income Before Amortization described above, a decrease of $21.1 million in amortization of non-cash marketing, primarily from Media & Advertising, and a decrease of $2.3 million in amortization of intangibles, partially offset by an increase of $23.8 million in non-cash compensation expense. The increase in non-cash compensation expense is primarily due to the factors described above in the three month discussion.

Other income (expense)

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

	Three Months Ended September 30,		
	2008	% Change	2007
	(Dollars in thousands)		
Other income (expense):			
Interest income	$ 6,549	(52)%	$ 13,644
Interest expense	(5,002)	(66)%	(14,919)
Equity in income of unconsolidated affiliates	3,146	(19)%	3,885
Other (expense) income	(68,657)	NM	10,295

Interest income in 2008 decreased $7.1 million from 2007 primarily due to lower cash and marketable securities balances in 2008, as well as lower average interest rates. Interest expense in 2008 decreased $9.9 million from 2007 as average interest rates decreased and the amount of outstanding debt decreased year over year due to the extinguishment of $734.2 million of the Company's 7% Senior Notes due 2013 (the "Senior Notes") as described below. The remaining outstanding principal of the Senior Notes at September 30, 2008 is $15.8 million.

Equity in income of unconsolidated affiliates in 2008 decreased $0.7 million from 2007 primarily due to losses from various Company investments, including those not in the year ago period, partially offset by higher earnings from its investment in Jupiter Shop Channel, a shopping channel in Japan.

Other expense in 2008 of $68.7 million is primarily due to a loss of $63.2 million on the extinguishment of the Senior Notes. On August 20, 2008, IAC purchased for cash all validly tendered Senior Notes pursuant to its amended tender offer to purchase the outstanding Senior Notes. Concurrent with the tender offer and in connection with the Spin-Off, the Company exchanged a portion of the Senior Notes for the debt of ILG.

Other expense in 2008 also includes a loss of $5.1 million related to the derivative asset received by the Company in connection with the sale of its German TV and internet retailer, Home Shopping Europe GmbH & Co. KG, and its affiliated TV station HSE24 ("HSE"). This loss was due in part to an increase in the discount rate related to credit risk. Other income in 2007 of $10.3 million was primarily due to gains of $5.8 million and $2.7 million associated with the derivative asset received by the Company in connection with the sale of HSE and the derivatives created in the Expedia spin-off, respectively.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

	Nine Months Ended September 30,		
	2008	% Change	2007
	(Dollars in thousands)		
Other income (expense):			
Interest income	$ 20,325	(58)%	$ 47,988
Interest expense	(30,866)	(31)%	(44,676)
Equity in income of unconsolidated affiliates	15,373	(7)%	16,543
Other (expense) income	(157,581)	NM	19,174

Interest income, interest expense and equity in income of unconsolidated affiliates in 2008 decreased $27.7 million, $13.8 million and $1.2 million, respectively, from 2007 primarily due to the factors described above in the three month discussion.

Other expense in 2008 of $157.6 million is primarily due to the write-down of $132.6 million on the Company's investment in Arcandor AG ("ARO") and the $63.2 million loss on the extinguishment of $734.2 million of the Senior Notes, described above in the three month discussion, partially offset by a gain of $29.1 million associated with the sale of the Company's preferred investment in Points International, Ltd ("Points"). As part of the consideration for the sale of HSE in June 2007, the Company received approximately 5.5 million shares of ARO stock ("ARO Shares"). During the second quarter of 2008, the Company considered the value of the ARO Shares to be other-than-temporarily impaired and wrote the value of the investment down to €7.38 per share, the stock's closing price on June 30, 2008.

Other income in 2007 of $19.2 million was primarily due to gains of $7.8 million and $4.4 million associated with the derivative asset received by the Company in connection with the sale of HSE and the derivatives created in the Expedia spin-off, respectively. Other income also included a gain of $3.1 million on the sale of fixed assets in 2007.

Income tax provision

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

In 2008 the Company recorded an income tax benefit for continuing operations of $85.3 million which represents an effective tax rate of 99%. The 2008 tax rate is higher than the federal statutory rate of 35% due principally to benefits from a net reduction in deferred tax liabilities caused by the Spin-Off, foreign income taxed at lower rates and state income tax benefits, partially offset by an increase in the valuation allowance on deferred tax assets related to the ARO Shares, changes in tax reserves, and non-deductible costs related to the Spin-Off. In 2007 the Company recorded an income tax provision for continuing operations of $11.1 million which represents an effective tax rate of 76%. The 2007 tax rate is higher than the federal statutory rate of 35% due principally to an increase in tax reserves and related interest and net adjustments related to the reconciliation of tax returns to provision accruals, partially offset by a non-taxable gain on the fair value of derivatives that were created in connection with the sale of HSE and the Expedia spin-off, foreign tax credits and tax exempt income.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

In 2008 the Company recorded an income tax benefit for continuing operations of $103.6 million which represents an effective tax rate of 54%. The 2008 tax rate is higher than the federal statutory rate of 35% due principally to benefits from a net reduction in deferred tax liabilities caused by the Spin-Off, foreign income taxed at lower rates and state income tax benefits, partially offset by an increase in the valuation allowance on deferred tax assets related to the ARO Shares, changes in tax reserves, and non-deductible costs related to the Spin-Off. In 2007 the Company recorded an income tax provision for continuing operations of $3.4 million despite a loss from continuing operations of $5.3 million. This income tax provision was principally due to an increase in tax reserves and related interest and net adjustments related to the reconciliation of tax returns to provision accruals, partially offset by a non-taxable gain on the fair value of derivatives that were created in connection with the sale of HSE and the Expedia spin-off, foreign tax credits and tax exempt income.

At September 30, 2008 and December 31, 2007, the Company had unrecognized tax benefits of approximately $357.5 million and $231.0 million, respectively. Unrecognized tax benefits for the nine months ended September 30, 2008 increased by $126.5 million due principally to an unrecognized current year capital loss on the Company's investment in Tree.com, partially offset by the effective settlement of prior year tax positions with the Internal Revenue Service principally relating to the reversal of deductible temporary differences. The Company recognizes interest and, if applicable, penalties related to unrecognized tax benefits in income tax provision. Included in the income tax provision for the three and nine months ended September 30, 2008 is $1.0 million and $6.3 million, net of related deferred taxes, for interest on unrecognized tax benefits. At September 30, 2008 the Company has accrued $45.8 million for the payment of interest. There are no material accruals for penalties.

The Company is routinely under audit by federal, state, local and foreign authorities in the area of income tax. These audits include questioning the timing and the amount of deductions and the allocation of income among various tax jurisdictions. Annual tax provisions include amounts considered sufficient to pay assessments that may result from examination of prior year returns; however, the amount paid upon resolution of issues raised may differ from the amount provided. Differences between the reserves for tax contingencies and the amounts owed by the Company are recorded in the period they become known. The Company believes that it is reasonably possible that its unrecognized tax benefits could decrease by approximately $17.5 million within twelve months of the current reporting date due to settlements and the reversal of deductible temporary differences which will result in a corresponding increase in net deferred tax liabilities. An estimate of other changes in unrecognized tax benefits, while potentially significant, cannot be made.

Discontinued operations

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

Discontinued operations in the accompanying consolidated statement of operations include HSNi, ILG, Ticketmaster and Tree.com through August 20, 2008, EPI through May 30, 2008 and HSE through June 19, 2007. Results from these discontinued operations, net of tax, in the third quarter of 2008 and 2007 were losses of $14.7 million and income of $67.1 million, respectively. The 2008 amount is principally due to losses of Tree.com, HSNi and Ticketmaster, partially offset by income of ILG. The 2007 amount is principally due to the income of Ticketmaster, HSNi and ILG, partially offset by losses of Tree.com.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

Results from discontinued operations, net of tax, in 2008 and 2007 were losses of $318.8 million and income of $199.5 million, respectively. The 2008 amount is principally due to the losses of HSNi, Tree.com and EPI, which include impairment charges related to goodwill and indefinite-lived intangible assets of $221.5 million and $78.5 million for HSNi, respectively, and $132.5 million and $33.4 million, respectively, for Tree.com. The losses from HSNi, Tree.com and EPI were partially offset by income of Ticketmaster and ILG. The 2007 amount is principally due to the income of Ticketmaster, HSNi and ILG, partially offset by losses of Tree.com and EPI.

Additionally, the Company recognized after-tax gains in 2008 and 2007 of $22.3 million and $31.1 million on the sales of EPI in the second quarter of 2008 and HSE in the second quarter of 2007, respectively.

Segment Results

In addition to the discussion of the consolidated results above, the following is a discussion of the results of each segment.

Media & Advertising

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

Media & Advertising consists of proprietary search properties such as Ask.com, Fun Web Products, Dictionary.com and Iwon, and our proprietary local site Citysearch, and network properties which include distributed search, sponsored listings and toolbars.

Revenue grew 2% to $193.3 million, primarily driven by strong growth from proprietary search properties. The growth in queries at Ask.com internationally and Fun Web Products was partially offset by declines in queries at Ask.com in the U.S. due to significantly lower marketing spend in the period. Ask.com's core user base, where frequency and monetization are the highest, grew queries strongly. Revenue per query on proprietary web search properties grew primarily from improved economics associated with the renewed partnership with Google and, even excluding the renewed partnership, revenue per query grew due to continued optimization of how and when we display sponsored listings. Proprietary revenue represented 71.5% of total Media & Advertising revenue during the quarter. Offsetting these increases in revenue was a sharp decline in network revenue, resulting from the planned discontinuation of relationships with certain partners that took place during 2008 in conjunction with the renewed partnership. The acquisition of Lexico, which includes Dictionary.com and Thesaurus.com, on July 3, 2008 contributed $3.6 million to revenue in 2008. Citysearch continued to grow users and revenue during the quarter.

Operating Income Before Amortization increased 39% to $38.8 million, primarily due to the reduction in the current year of $14.6 million in revenue share payments to third party traffic sources, partially offset by an increase of $3.8 million in selling and marketing expense. Overall revenue share payments during the quarter decreased as a direct result of a decrease in network revenue, partially offset by growth in distribution revenue included as a component of proprietary revenue at IAC Search & Media. As a percentage of revenue, traffic acquisition costs associated with network revenue generated from integrated sponsored listings are lower than traffic acquisition costs associated with distribution revenue generated from partners who redirect traffic to the Ask.com landing page. The increase in selling and marketing expense is primarily due to an increase of $3.5 million in compensation and other employee-related costs, due in part to recent acquisitions not in the year ago period at IAC Search & Media and an 11% increase in average headcount at Citysearch. This increase in selling and marketing expense is partially offset by a decrease of $1.6 million in advertising and promotional expenditures due largely to reduced marketing spend.

Operating income increased 105% to $32.1 million, primarily due to the increase in Operating Income Before Amortization described above and the inclusion in the prior year period of $6.1 million in amortization of non-cash marketing.

As discussed, the Company renewed its paid listings agreement with Google effective January 1, 2008. The new contract limits our ability to distribute sponsored listings to certain network partners. This has led to a greater percentage of revenues for our Media & Advertising segment in 2008 coming from the higher-margin proprietary side of the business, and a lesser percentage from the lower-margin network business. The trend will continue for the rest of the year.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

Revenue grew 12% to $595.1 million, primarily due to improved economics associated with the renewed partnership with Google, which resulted in an increase in revenue per query across most proprietary search sites. Revenue also benefited from an increase in both queries and revenue per query at Fun Web Products and from distributed search. Revenue and revenue per query at Ask.com grew, even excluding the benefits of the renewed partnership. Queries declined overall due largely to significantly reduced marketing which more than offset growth in the core user base which searches most frequently. Network revenue declined as expected due to the planned discontinuation of relationships with certain partners that took place during 2008, as described above in the three month discussion.

Operating Income Before Amortization increased 97% to $112.2 million, primarily due to a decrease of $10.2 million in advertising and promotional expenditures at IAC Search & Media, increased revenue growth noted above and a decrease of $6.3 million in revenue share payments to third party traffic sources. Partially offsetting these factors was an increase of $7.0 million in other operating expense. The decrease in revenue share payments is primarily due to the factors described above in the three month discussion. The increase in other operating expense was primarily due to an increase of $6.8 million in compensation and other employee-related costs due in part to a 9% increase in average headcount, as our Media & Advertising businesses continued to upgrade and enhance their search technology and products.

Operating income increased 502% to $93.2 million, primarily due to the increase in Operating Income Before Amortization described above and the inclusion in the prior year period of $22.8 million in amortization of non-cash marketing.

Match

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

Revenue grew 5% to $93.5 million, reflecting a 6% increase in both international subscribers and revenue per subscriber, and a 1% and 2% growth in North America subscribers and revenue per subscriber, respectively. The growth in international subscribers was driven by expansion in several markets, most notably Latin America, United Kingdom, Scandinavia and Australia. Domestically, Chemistry.com continued to grow subscribers during the third quarter of 2008.

Operating Income Before Amortization increased 3% to $30.3 million, primarily reflecting lower customer acquisition costs as a percentage of revenue due to more favorable economic terms associated with certain distribution partners, partially offset by increased marketing spend and compensation and other employee-related costs related to product investments. In 2008, Match experienced increases in advertising associated with television advertising and online marketing related to various international marketing campaigns.

Operating income decreased 18% to $24.0 million despite the increase in Operating Income Before Amortization discussed above primarily due to the current year inclusion of $6.1 million in amortization of non-cash marketing.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

Revenue grew 7% to $277.4 million, reflecting a 6% and 11% increase in international subscribers and revenue per subscriber, respectively, and a 1% and 4% growth in North America subscriber and revenue per subscriber, respectively. The growth in international subscribers was driven by factors described above in the three month discussion.

Operating Income Before Amortization increased 10% to $63.3 million, growing at a faster rate than revenue primarily due to lower international customer acquisition costs as a percentage of revenue and a decrease in domestic customer acquisition costs. The decrease in domestic customer acquisition costs reflects improved economics with certain distribution partners as noted above in the three month discussion, partially offset by an increase in spending related to Chemistry.com, which continues to grow subscribers.

Operating income increased 2% to $50.7 million primarily due to the increase in Operating Income Before Amortization discussed above, partially offset by an increase of $4.8 million in amortization of non-cash marketing.

ServiceMagic

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

Revenue grew 37% to $33.8 million, benefiting from a more active service provider network and a 41% increase in service requests driven by increased marketing efforts. During 2008, ServiceMagic experienced a 34% increase in the number of times service requests are accepted by a service professional.

Operating Income Before Amortization increased 60% to $8.7 million, primarily due to the increase in revenue noted above, partially offset by increases of $4.7 million in cost of sales and $1.0 million in general and administrative expense. The increase in costs of sales is primarily driven by increased customer acquisition costs as ServiceMagic continued to focus its spend on driving higher margin home repair and improvement requests and increasing service requests during this weak macro environment. Contributing to the increase in general and administrative expense are increases of $0.3 million and $0.2 million in bad debt expense and compensation and other employee-related costs, respectively.

Operating income increased 75% to $8.1 million, primarily due to the increase in Operating Income Before Amortization discussed above and a decrease of $0.3 million in amortization of intangibles.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

Revenue grew 38% to $98.6 million, driven primarily by the factors described above in the three month discussion.

Operating Income Before Amortization increased 29% to $24.2 million, primarily due to the increase in revenue noted above, partially offset by increases of $13.9 million in cost of sales, $3.9 million in selling and marketing expense and $3.3 million in general and administrative expense. The increase in costs of sales is primarily driven by increased customer acquisition costs as described above in the three month discussion. Selling and marketing expense reflects increased compensation and other employee-related costs associated with the expansion of the sales force due in part to the opening of a new customer call center in Kansas City in the second quarter of 2007. Contributing to the increase in general and administrative expense are increases of $1.1 million, $0.8 million and $0.7 million in compensation and other employee-related costs, bad debt expense and facilities costs, respectively.

Operating income increased 41% to $22.6 million, primarily due to the increase in Operating Income Before Amortization discussed above and a decrease of $1.0 million in amortization of intangibles.

Emerging Businesses

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

Emerging Businesses include Shoebuy, ReserveAmerica, Pronto.com, Gifts.com, InstantAction.com, Connected Ventures, 23/6, VeryShortList.com, RushmoreDrive.com, Life123.com and The Daily Beast, as well as other early stage businesses.

Revenue grew 37% to $49.6 million reflecting strong growth at Pronto.com and Shoebuy.

Operating Income Before Amortization decreased $2.6 million to a loss of $6.1 million. Losses increased due primarily to increased operating expenses associated with early stage businesses not in the year ago period, as well as InstantAction.com and RushmoreDrive.com. Partially offsetting the decrease in Operating Income Before Amortization is the first full quarter of profitability at Pronto.com.

Operating loss decreased 25% to $7.4 million despite the increased Operating Income Before Amortization loss discussed above primarily due to the inclusion in the prior year period of $3.0 million in amortization of non-cash marketing related to Shoebuy and a $2.2 million decrease in amortization of intangibles. The decrease in amortization of intangibles resulted from certain intangibles at Connected Ventures being fully amortized in 2007.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

Revenue grew 43% to $141.9 million reflecting strong growth at Pronto.com and Shoebuy.

Operating Income Before Amortization and operating income decreased $21.7 million and $16.8 million, respectively, to losses of $21.7 million and $25.8 million, respectively, due to the inclusion in the prior year's results of an $8.2 million reimbursement of previously expensed advances related to the restructuring of our interests in a business venture, as well as increased operating expenses associated with RushmoreDrive.com, various early stage businesses not in the year ago period, InstantAction.com and Connected Ventures. Operating loss was favorably impacted by the inclusion in the prior year period of $3.0 million in amortization of non-cash marketing and a $1.6 million decrease in amortization of intangibles.

Corporate

For the three months ended September 30, 2008 compared to the three months ended September 30, 2007

Operating Income Before Amortization loss increased by $19.5 million to a loss of $41.2 million reflecting the incurrence of $20.8 million in expenses related to the Spin-Off.

Operating loss increased 109% to $79.4 million, primarily due to the increase in Operating Income Before Amortization loss discussed above and an increase of $22.0 million in non-cash compensation expense. The increase in non-cash compensation expense is primarily due to the acceleration and modification of certain equity awards associated with the Spin-Off. To a lesser degree, non-cash compensation expense increased due to expense related to equity grants issued subsequent to the third quarter of 2007, partially offset by a decrease in expense associated with unvested stock options assumed in the IAC Search & Media acquisition as these awards vest, as well as the impact of expense relating to equity modifications recorded in the prior year.

For the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007

Operating Income Before Amortization loss increased by $40.3 million to a loss of $106.0 million, primarily due to the incurrence of $42.0 million in expenses related to the Spin-Off.

Operating loss increased 55% to $180.9 million, primarily due to the increase in Operating Income Before Amortization loss discussed above and an increase of $24.1 million in non-cash compensation expense. The increase in non-cash compensation expense is primarily due to the factors described above in the three month discussion.

FINANCIAL POSITION, LIQUIDITY AND CAPITAL RESOURCES

All IAC common stock share information has been adjusted to reflect IAC's one-for-two reverse stock split in August 2008.

As of September 30, 2008, the Company had $1.3 billion of cash and cash equivalents, $121.5 million of marketable securities and $95.8 million in long-term debt. Long-term debt consists of $80.0 million in Liberty Bonds due September 1, 2035 and $15.8 million in Senior Notes.

During the nine months ended September 30, 2008 and 2007, IAC purchased 3.0 million and 7.8 million shares of IAC common stock for aggregate consideration, on a trade date basis, of $145.6 million and $508.6 million, respectively. In 2006, the Company announced that its Board of Directors authorized the repurchase of up to 30 million shares of IAC common stock of which 22.4 million shares remain at October 31, 2008. IAC may purchase shares over an indefinite period of time, depending on those factors IAC management deems relevant at any particular time, including, without limitation, market conditions, share price and future outlook.

Net cash provided by operating activities attributable to continuing operations was $147.4 million and $0.1 million in 2008 and 2007, respectively. The increase of $147.2 million in net cash provided by operating activities reflects lower cash taxes paid of $114.3 million and an increase in accounts payable.

Net cash provided by investing activities attributable to continuing operations in 2008 of $469.4 million includes the net cash distribution from the spun-off businesses of $427.8 million, the net proceeds of $189.4 million related to the sales, maturities and purchases of marketable securities, the proceeds of $60.9 million from the sale of long-term investments and the proceeds of $32.7 million from the sale of discontinued operations, partially offset by acquisitions, net of cash acquired, of $130.7 million, an increase in long-term investments of $59.7 million and capital expenditures of $51.3 million. The increase in long-term investments is primarily due to the Company's equity investment in The HealthCentral Network. The proceeds from the sale of long-term investments and discontinued operations relate primarily to the sale of Points and EPI, respectively. Net cash provided by investing activities attributable to continuing operations in 2007 of $266.6 million includes the net proceeds of $492.6 million related to the sales, maturities and purchases of marketable securities, partially offset by an net increase in long-term investments of $119.5 million, capital expenditures of $77.8 million and acquisitions, net of cash acquired, of $45.8 million.

Net cash used in financing activities attributable to continuing operations in 2008 of $674.0 million was primarily due to $514.9 million relating to the repurchase of Senior Notes and the purchase of treasury stock of $145.6 million. Net cash used in financing activities attributable to continuing operations in 2007 of $518.9 million was primarily due to the purchase of treasury stock of $542.9 million and principal payments on long-term obligations of $7.6 million, partially offset by the proceeds from the issuance of common stock, net of withholding taxes, of $21.9 million and the excess tax benefits from stock-based awards of $5.8 million.

Net cash used in discontinued operations in 2008 of $170.2 million and net cash provided by discontinued operations in 2007 of $173.1 million relate primarily to the operations of Ticketmaster, HSNi, ILG and Tree.com. The Company does not expect future cash flows associated with existing discontinued operations to be material.

IAC anticipates that it will need to make capital and other expenditures in connection with the development and expansion of its overall operations. The Company may make a number of acquisitions which could result in the reduction of its cash balance or the incurrence of debt. IAC expects that 2008 capital expenditures will be lower than 2007.

IAC believes that its cash on hand along with its anticipated operating cash flows in 2008 and its access to capital markets are sufficient to fund its operating needs, capital, investing and other commitments and contingencies for the foreseeable future.

CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

	Payments Due by Period				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
			(In thousands)		
Contractual Obligations(a)					
Long-term obligations(b)	$204,752	$ 5,099	$10,183	$ 25,470	$ 164,000
Purchase obligations(c)	5,874	4,379	&nbiscussed further below, management measures the profitability of the Company s operating segments based on Core Earnings net income. Accordingly, information regarding the Company s reportable segments is provided based on a Core Earnings basis. The Company s Core Earnings performance measures are not defined terms within GAAP and may not be comparable to similarly titled measures reported by other companies. Core Earnings net income reflects only current period adjustments to GAAP net income as described below. Unlike financial accounting, there is no comprehensive, authoritative guidance for management reporting. The management		

reporting process measures the performance of the operating segments based on the management structure of the Company and is not necessarily comparable with similar information for any other financial institution. The Company s operating segments are defined by the products and services they offer or the types of customers they serve, and they reflect the manner in which financial information is currently evaluated by management. Intersegment revenues and expenses are netted within the appropriate financial statement line items consistent with the income statement presentation provided to management. Changes in management structure or allocation methodologies and procedures may result in changes in reported segment financial information.

The Company s principal operations are located in the United States, and its results of operations and long-lived assets in geographic regions outside of the United States are not significant. In the Lending segment, no individual customer accounted for more than 10 percent of its total revenue during the six months ended June 30, 2006 and 2005. United Student Aid Funds, Inc. (USA Funds) is the Company s largest customer in both the DMO and Corporate and Other segments. During the six months ending June 30, 2006 and 2005, it accounted for 38 percent and 42 percent, respectively, of the aggregate revenues generated by the Company s DMO and Corporate and Other segments. No other customers accounted for more than 10 percent of total revenues in those segments for the years mentioned.

Lending

In the Company s Lending business segment, the Company originates and acquires both federally guaranteed student loans, which are administered by the U.S. Department of Education (ED), and Private Education Loans, which are not federally guaranteed. Private Education Loans are primarily used by borrowers to supplement FFELP loans to meet the rising cost of education. The Company manages student loans for approximately 10 million customers; its Managed student loan portfolio totaled $130.1 billion at June 30, 2006, of which $111.1 billion or 85 percent are federally insured. In addition to education lending, the Company also originates mortgage and consumer loans with the intent of selling the majority of such loans. During the six months ended June 30, 2006, the Company originated $905 million in mortgage and consumer loans of which $718 million pertained to mortgages in the held for sale portfolio. The Company s mortgage and consumer loan portfolio totaled $670 million at June 30, 2006.

In addition to its federally insured FFELP products, the Company originates and acquires Private Education Loans which consist of two general types: (1) those that are designed to bridge the gap between the cost of higher education and the amount financed through either capped federally insured loans or the borrowers resources, and (2) those that are used to meet the needs of students in alternative learning programs such as career training, distance learning and lifelong learning programs. Most higher education Private Education Loans are made in conjunction with a FFELP Stafford loan and as such are marketed through the same channel as FFELP loans by the same sales force. Unlike FFELP loans, Private Education Loans are subject to the full credit risk of the borrower. The Company manages this additional

SLM CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Information at June 30, 2006 and for the three and six months ended
June 30, 2006 and 2005 is unaudited)
(Dollars in thousands, except per share amounts, unless otherwise noted)

11. Segment Reporting (Continued)

risk through industry-tested loan underwriting standards and a combination of higher interest rates and loan origination fees that compensate the Company for the higher risk.

DMO

The Company provides a wide range of accounts receivable and collections services through six operating units that comprise its DMO operating segment. These services include defaulted student loan portfolio management services, contingency collections services for student loans and other asset classes, student loan default aversion services, and accounts receivable management and collection for purchased portfolios of receivables that have been charged off by their original creditors, as well as sub-performing and nonperforming mortgage loans. The Company s DMO operating segment primarily serves the student loan marketplace through a broad array of default management services on a contingency fee or other pay-for-performance basis to 12 FFELP guarantors and for campus-based programs.

In addition to collecting on its own purchased receivables and mortgage loans, the DMO operating segment provides receivable management and collection services for large federal agencies, credit card clients and other holders of consumer debt.

Corporate and Other

The Company s Corporate and Other business segment includes the aggregate activity of its smaller operating segments, including its Guarantor Servicing and Loan Servicing business segments, other products and services as well as corporate overhead.

In the Guarantor Servicing operating segment, the Company provides a full complement of administrative services to FFELP guarantors including guarantee issuance, account maintenance, and guarantee fulfillment. In the Loan Servicing operating segment, the Company provides a full complement of activities required to service student loans on behalf of lenders who are unrelated to the Company. Such servicing activities generally commence once a loan has been fully disbursed and include sending out payment coupons to borrowers, processing borrower payments, originating and disbursing Consolidation Loans on behalf of the lender, and other administrative activities required by ED. The Company s other products and services include comprehensive financing and loan delivery solutions that it provides to college financial aid offices and students to streamline the financial aid process. Corporate overhead includes all of the typical headquarter functions such as executive management, accounting and finance, human resources and marketing.

Measure of Profitability

The tables below include the condensed operating results for each of the Company s reportable segments. Management, including the chief operating decision maker, evaluates the Company on certain performance measures that the Company refers to as Core Earnings performance measures for each operating segment. While Core Earnings results are not a substitute for reported results under GAAP, the Company relies on Core Earnings performance measures to manage each operating segment because it believes these measures provide additional information regarding the operational and performance indicators that are most closely assessed by management.

Core Earnings performance measures are the primary financial performance measures used by management to develop the Company s financial plans, track results, and establish corporate performance targets and incentive compensation. Management believes this information provides additional insight into

SLM CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Information at June 30, 2006 and for the three and six months ended June 30, 2006 and 2005 is unaudited)
(Dollars in thousands, except per share amounts, unless otherwise noted)

11. Segment Reporting (Continued)

the financial performance of the core business activities of its operating segments. Accordingly, the tables presented below reflect Core Earnings operating measures reviewed and utilized by management to manage the business. Reconciliations of the Core Earnings segment totals to the Company s consolidated operating results in accordance with GAAP are also included in the tables below.

Segment Results and Reconciliations to GAAP

	Three Months Ended June 30, 2006					
(Dollars in millions)	**Lending**	**DMO**	**Corporate and Other**	**Total Core Earnings**	**Adjustments[3]**	**Total GAAP**
Interest income:						
FFELP Stafford and Other Student Loans	$ 719	$	$	$ 719	$ (382)	$ 337
Consolidation Loans	1,114			1,114	(273)	841
Private Education Loans	485			485	(251)	234
Other loans	24			24		24
Cash and investments	170		1	171	(46)	125
Total interest income	2,512		1	2,513	(952)	1,561
Total interest expense	1,904	5	1	1,910	(706)	1,204
Net interest income	608	(5)		603	(246)	357
Less: provisions for losses	60			60	8	68
Net interest income after provisions for losses	548	(5)		543	(254)	289
Fee income		90	33	123		123
Collections revenue		67		67		67
Other income	51		24	75	869	944
Operating expenses[1]	163	85	50	298	18	316
Income before income taxes and minority interest in net earnings of subsidiaries	436	67	7	510	597	1,107
Income tax expense[2]	161	26	2	189	193	382
Minority interest in net earnings of subsidiaries		1		1		1
Net income	$ 275	$ 40	$ 5	$ 320	$ 404	$ 724

(1) Operating expenses for the Lending, DMO, and Corporate and Other Business segments include $8 million, $2 million, and $4 million, respectively, of stock-based compensation expense due to the implementation of SFAS No. 123(R) in the first quarter of 2006.

(2) Income taxes are based on a percentage of net income (loss) before tax for the individual reportable segment.

(3) Core Earnings adjustments to GAAP:

	Three Months Ended June 30, 2006				
	Net Impact of Securitization Accounting	**Net Impact of Derivative Accounting**	**Net Impact of Floor Income**	**Amortization of Acquired Intangibles**	**Total**
(Dollars in millions)					
Net interest income	$ (236)	$ 42	$ (52)	$	$ (246)
Less: provisions for losses	8				8
Net interest income after provisions for losses	(244)	42	(52)		(254)
Fee income					
Collections revenue					
Other income	746	123			869
Operating expenses				18	18
Total pre-tax Core Earnings adjustments to GAAP	$ 502	$ 165	$ (52)	$ (18)	597
Income tax expense					193
Minority interest in net earnings of subsidiaries					
Total Core Earnings adjustments to GAAP					$ 404

SLM CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Information at June 30, 2006 and for the three and six months ended June 30, 2006 and 2005 is unaudited)
(Dollars in thousands, except per share amounts, unless otherwise noted)

11. Segment Reporting (Continued)

	Three Months Ended June 30, 2005					
(Dollars in millions)	Lending	DMO	Corporate and Other	Total Core Earnings	Adjustments[3]	Total GAAP
Interest income:						
FFELP Stafford and Other Student Loans	$ 582	$	$	$ 582	$ (343)	$ 239
Consolidation Loans	667			667	(113)	554
Private Education Loans	247			247	(120)	127
Other loans	20			20		20
Cash and investments	77		1	78	(24)	54
Total interest income	1,593		1	1,594	(600)	994
Total interest expense	1,073	4	1	1,078	(414)	664
Net interest income	520	(4)		516	(186)	330
Less: provisions for losses	14			14	65	79
Net interest income after provisions for losses	506	(4)		502	(251)	251
Fee income		82	26	108		108
Collections revenue		42		42		42
Other income	36		29	65	297	362
Operating expenses[1]	141	67	63	271	17	288
Income (loss) before income taxes and minority interest in net earnings of subsidiaries	401	53	(8)	446	29	475
Income tax expense (benefit)[2]	148	20	(3)	165	11	176
Minority interest in net earnings of subsidiaries	1	1		2		2
Net income (loss)	$ 252	$ 32	$ (5)	$ 279	$ 18	$ 297

[1] Income taxes are based on a percentage of net income (loss) before tax for the individual reportable segment.

(2) In the first quarter of 2006, the Company changed its method for allocating certain overhead and other expenses between its business segments. Balances for the three months ending June 30, 2005 have been updated to reflect the new allocation methodology.

(3) Core Earnings adjustments to GAAP:

	Three Months Ended June 30, 2005				
(Dollars in millions)	Net impact of Securitization Accounting	Net Impact of Derivative Accounting	Net Impact of Floor Income	Amortization of Acquired Intangibles	Total
Net interest income	$ (230)	$ 95	$ (51)	$	$ (186)
Less: provisions for losses	65				65
Net interest income after provisions for losses	(295)	95	(51)		(251)
Fee income					
Collections revenue					
Other income	403	(106)			297
Operating expenses	1			16	17
Total pre-tax Core Earnings adjustments to GAAP	$ 107	$ (11)	$ (51)	$ (16)	29
Income tax expense					11
Minority interest in net earnings of subsidiaries					
Total Core Earnings adjustments to GAAP					$ 18

SLM CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Information at June 30, 2006 and for the three and six months ended June 30, 2006 and 2005 is unaudited)
(Dollars in thousands, except per share amounts, unless otherwise noted)

11. Segment Reporting (Continued)

	Six Months Ended June 30, 2006					
(Dollars in millions)	**Lending**	**DMO**	**Corporate and Other**	**Total Core Earnings**	**Adjustments[3]**	**Total GAAP**
Interest income:						
FFELP Stafford and Other Student Loans	$ 1,369	$	$	$ 1,369	$ (734)	$ 635
Consolidation Loans	2,142			2,142	(479)	1,663
Private Education Loans	914			914	(439)	475
Other loans	47			47		47
Cash and investments	300		2	302	(81)	221
Total interest income	4,772		2	4,774	(1,733)	3,041
Total interest expense	3,562	11	3	3,576	(1,280)	2,296
Net interest income	1,210	(11)	(1)	1,198	(453)	745
Less: provisions for losses	135			135	(7)	128
Net interest income after provisions for losses	1,075	(11)	(1)	1,063	(446)	617
Fee income		182	60	242		242
Collections revenue		124		124		124
Other income	92		55	147	907	1,054
Operating expenses[1]	324	175	109	608	32	640
Income before income taxes and minority interest in net earnings of subsidiaries	843	120	5	968	429	1,397
Income tax expense[2]	312	44	2	358	161	519
Minority interest in net earnings of subsidiaries		3		3		3
Net income	$ 531	$ 73	$ 3	$ 607	$ 268	$ 875

(1) Operating expenses for the Lending, DMO, and Corporate and Other Business segments include $18 million, $5 million, and $9 million, respectively, of stock-based compensation expense due to the implementation of

SFAS No. 123(R) in the first quarter of 2006.

(2) Income taxes are based on a percentage of net income (loss) before tax for the individual reportable segment.

(3) Core Earnings adjustments to GAAP:

	Six Months Ended June 30, 2006				
(Dollars in millions)	**Net Impact of Securitization Accounting**	**Net Impact of Derivative Accounting**	**Net Impact of Floor Income**	**Amortization of Acquired Intangibles**	**Total**
Net interest income	$ (438)	$ 90	$ (105)	$	$ (453)
Less: provisions for losses	(7)				(7)
Net interest income after provisions for losses	(431)	90	(105)		(446)
Fee income					
Collections revenue					
Other income	871	36			907
Operating expenses				32	32
Total pre-tax Core Earnings adjustments to GAAP	$ 440	$ 126	$ (105)	$ (32)	429
Income tax expense					161
Minority interest in net earnings of subsidiaries					
Total Core Earnings adjustments to GAAP					$ 268

SLM CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Information at June 30, 2006 and for the three and six months ended June 30, 2006 and 2005 is unaudited)
(Dollars in thousands, except per share amounts, unless otherwise noted)

11. Segment Reporting (Continued)

	Six Months Ended June 30, 2005					
(Dollars in millions)	**Lending**	**DMO**	**Corporate and Other**	**Total Core Earnings**	**Adjustments[3]**	**Total GAAP**
Interest income:						
FFELP Stafford and Other Student Loans	$ 1,092	$	$	$ 1,092	$ (663)	$ 429
Consolidation Loans	1,248			1,248	(185)	1,063
Private Education Loans	474			474	(217)	257
Other loans	40			40		40
Cash and investments	156		2	158	(42)	116
Total interest income	3,010		2	3,012	(1,107)	1,905
Total interest expense	1,991	8	3	2,002	(774)	1,228
Net interest income	1,019	(8)	(1)	1,010	(333)	677
Less: provisions for losses	69			69	57	126
Net interest income after provisions for losses	950	(8)	(1)	941	(390)	551
Fee income		168	58	226		226
Collections revenue		77		77		77
Other income	72		61	133	450	583
Operating expenses[1]	275	132	114	521	29	550
Income before income taxes and minority interest in net earnings of subsidiaries	747	105	4	856	31	887
Income tax expense[2]	277	39	1	317	46	363
Minority interest in net earnings of subsidiaries	2	2		4		4
Net income	$ 468	$ 64	$ 3	$ 535	$ (15)	$ 520

[1] Income taxes are based on a percentage of net income (loss) before tax for the individual reportable segment.

(2) In the first quarter of 2006, the Company changed its method for allocating certain overhead and other expenses between its business segments. Balances for the six months ending June 30, 2005 have been updated to reflect the new allocation methodology.

(3) Core Earnings adjustments to GAAP:

	Six Months Ended June 30, 2005				
(Dollars in millions)	**Net Impact of Securitization Accounting**	**Net Impact of Derivative Accounting**	**Net Impact of Floor Income**	**Amortization of Acquired Intangibles**	**Total**
Net interest income	$ (458)	$ 219	$ (94)	$	$ (333)
Less: provisions for losses	57				57
Net interest income after provisions for losses	(515)	219	(94)		(390)
Fee income					
Collections revenue					
Other income	590	(140)			450
Operating expenses				29	29
Total pre-tax Core Earnings adjustments to GAAP	$ 75	$ 79	$ (94)	$ (29)	31
Income tax expense					46
Minority interest in net earnings of subsidiaries					
Total Core Earnings adjustments to GAAP					$ (15)

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SLM CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Information at June 30, 2006 and for the three and six months ended June 30, 2006 and 2005 is unaudited)
(Dollars in thousands, except per share amounts, unless otherwise noted)

11. Segment Reporting (Continued)

Summary of Core Earnings Adjustments to GAAP

The adjustments required to reconcile from the Company s Core Earnings results to its GAAP results of operations relate to differing treatments for securitization transactions, derivatives, Floor Income related to the Company s student loans, and certain other items that management does not consider in evaluating the Company s operating results. The following table reflects aggregate adjustments associated with these areas for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in millions)	**2006**	**2005**	**2006**	**2005**
Core Earnings adjustments to GAAP:				
Net impact of securitization accounting(1)	$ 502	$ 107	$ 440	$ 75
Net impact of derivative accounting(2)	165	(11)	126	79
Net impact of Floor Income(3)	(52)	(51)	(105)	(94)
Amortization of acquired intangibles(4)	(18)	(16)	(32)	(29)
Net tax effect(5)	(193)	(11)	(161)	(46)
Total Core Earnings adjustments to GAAP	$ 404	$ 18	$ 268	$ (15)

(1) **Securitization:** Under GAAP, certain securitization transactions in the Company s Lending operating segment are accounted for as sales of assets. Under the Company s Core Earnings presentation for the Lending operating segment, the Company presents all securitization transactions on a Core Earnings basis as long-term non-recourse financings. The upfront gains on sale from securitization transactions as well as ongoing servicing and securitization revenue presented in accordance with GAAP are excluded from Core Earnings net income and replaced by the interest income, provisions for loan losses, and interest expense as they are earned or incurred on the securitization loans. The Company also excludes transactions with its off-balance sheet trusts from Core Earnings net income as they are considered intercompany transactions on a Core Earnings basis.

(2) **Derivative accounting:** Core Earnings net income excludes periodic unrealized gains and losses arising primarily in the Company s Lending operating segment, and to a lesser degree in the Company s Corporate and Other reportable segment, that are caused primarily by the one-sided mark-to-market derivative valuations prescribed by SFAS No. 133 on derivatives that do not qualify for hedge treatment under GAAP. Under the Company s Core Earnings presentation, the Company recognizes the economic effect of these hedges, which generally results in any cash paid or received being recognized ratably as an expense or revenue over the hedged item s life. Core Earnings net income also excludes the gain or loss on equity forward contracts that under SFAS No. 133, are required to be accounted for as derivatives and are marked-to-market through GAAP net income.

(3)

Floor Income: The timing and amount (if any) of Floor Income earned in the Company s Lending operating segment is uncertain and in excess of expected spreads. Therefore, the Company excludes such income from Core Earnings net income when it is not economically hedged. The Company employs derivatives, primarily Floor Income Contracts and futures, to economically hedge Floor Income. As discussed above in Derivative Accounting, these derivatives do not qualify as effective accounting hedges and therefore, under GAAP, are marked-to-market through the gains (losses) on derivative and hedging activities, net line on the income statement with no offsetting gain or loss recorded for the economically hedged items. For Core Earnings net income, the Company reverses the fair value adjustments on the Floor Income Contracts and futures economically hedging Floor Income and includes the amortization of net premiums received (net of Eurodollar futures contracts realized gains or losses) in income.

(4) **Other items:** The Company excludes goodwill impairment and amortization of acquired intangibles.

(5) Such tax effect is based upon the Company s Core Earnings effective tax rate for the year. The net tax effect results primarily from the exclusion of the permanent income tax impact of the equity forward contracts.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
Three and six months ended June 30, 2006 and 2005
(Dollars in millions, except per share amounts, unless otherwise noted)

FORWARD-LOOKING AND CAUTIONARY STATEMENTS

This quarterly report contains forward-looking statements and information that are based on management s current expectations as of the date of this document. When used in this report, the words anticipate, believe, estimate, intend and expect and similar expressions are intended to identify forward-looking statements. These forward-looking statements are subject to risks, uncertainties, assumptions and other factors that may cause the actual results to be materially different from those reflected in such forward-looking statements. These factors include, among others, changes in the terms of student loans and the educational credit marketplace arising from the implementation of applicable laws and regulations and from changes in these laws and regulations, which may reduce the volume, average term and yields on student loans under the Federal Family Education Loan Program (FFELP) or result in loans being originated or refinanced under non-FFELP programs or may affect the terms upon which banks and others agree to sell FFELP loans to SLM Corporation, more commonly known as Sallie Mae, and its subsidiaries (collectively, the Company). In addition, a larger than expected increase in third party consolidations of our FFELP loans could materially adversely affect our results of operations. The Company could also be affected by changes in the demand for educational financing or in financing preferences of lenders, educational institutions, students and their families; incorrect estimates or assumptions by management in connection with the preparation of our consolidated financial statements; changes in the composition of our Managed FFELP and Private Education Loan portfolios; a significant decrease in our common stock price, which may result in counterparties terminating equity forward positions with us, which, in turn, could have a materially dilutive effect on our common stock; changes in the general interest rate environment and in the securitization markets for education loans, which may increase the costs or limit the availability of financings necessary to initiate, purchase or carry education loans; losses from loan defaults; changes in prepayment rates and credit spreads; and changes in the demand for debt management services and new laws or changes in existing laws that govern debt management services.

OVERVIEW

We are the largest source of funding, delivery and servicing support for education loans in the United States. Our primary business is to originate, acquire and hold both federally guaranteed student loans and Private Education Loans, which are not federally guaranteed. The primary source of our earnings is from net interest income earned on those student loans as well as gains on the sales of such loans in securitization transactions. We also earn fees for pre-default and post-default receivables management services on student loans, such that we are engaged in every phase of the student loan life cycle from originating and servicing student loans to default prevention and ultimately the collection on defaulted student loans. In addition, we provide a wide range of other financial services, processing capabilities and information technology to meet the needs of educational institutions, lenders, students and their families, and guarantee agencies. SLM Corporation, more commonly known as Sallie Mae, is a holding company that operates through a number of subsidiaries and references in this report to the Company refer to SLM Corporation and its subsidiaries.

We have used both internal growth and strategic acquisitions to attain our leadership position in the education finance marketplace. Our sales force, which delivers our products on campuses across the country, is the largest in the student loan industry. The core of our marketing strategy is to promote our on-campus brands, which generate student loan originations through our Preferred Channel. Loans generated through our Preferred Channel are more profitable than loans acquired through other acquisition channels because we own them earlier in the student loan s life and generally incur lower costs to acquire such loans. We have built brand leadership among the Sallie Mae name, the brands of our subsidiaries and those of our lender partners. These sales and marketing efforts are supported by the largest and most diversified servicing capabilities in the industry, providing an unmatched array of servicing capability to financial aid offices.

In recent years we have diversified our business through the acquisition of several companies that provide default management and loan collections services, all of which are combined in our Debt Management Operations (DMO) business segment. Our capabilities now include a full range of accounts receivable management services to a number of different industries. The DMO business segment has been expanding rapidly such that revenue grew 25 percent in the six months ended June 30, 2006, compared to the same period in 2005, and we now employ approximately 4,000 people in this segment.

We manage our business through two primary operating segments: the Lending operating segment and the DMO operating segment. Accordingly, the results of operations of the Company s Lending and DMO segments are presented separately below under BUSINESS SEGMENTS. These operating segments are considered reportable segments under the Financial Accounting Standards Board s (FASB) Statement of Financial Accounting Standards (SFAS) No. 131, Disclosures about Segments of an Enterprise and Related Information, based on quantitative thresholds applied to the Company s financial statements.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

A discussion of the Company s critical accounting policies, which include premiums, discounts and Borrower Benefits, securitization accounting and Retained Interests, provisions for loan losses, derivative accounting and the effects of Consolidation Loan activity on estimates, can be found in the Company s Annual Report on Form 10-K for the year ended December 31, 2005. There have been no material changes to these policies during the second quarter of 2006.

SELECTED FINANCIAL DATA

Condensed Statements of Income

	Three Months Ended June 30,		Increase (Decrease)		Six Months Ended June 30,		Increase (Decrease)	
	2006	**2005**	**$**	**%**	**2006**	**2005**	**$**	**%**
Net interest income	$ 357	$ 330	$ 27	8%	$ 745	$ 677	$ 68	10%
Less: provisions for losses	68	79	(11)	(14)	128	126	2	2
Net interest income after provisions for losses	289	251	38	15	617	551	66	12
Gains on student loan securitizations	671	262	409	156	701	312	389	125
Servicing and securitization revenue	83	150	(67)	(45)	182	293	(111)	(38)
Gains (losses) on derivative and hedging activities, net	123	(106)	229	216	36	(140)	176	126
Guarantor servicing fees	33	26	7	27	60	58	2	3
Debt management fees	90	82	8	10	182	168	14	8
Collections revenue	67	42	25	60	124	77	47	61
Other income	67	56	11	20	135	118	17	14
Operating expenses	316	288	28	10	640	550	90	16
Income taxes	382	176	206	117	519	363	156	43
Minority interest in net earnings of subsidiaries	1	2	(1)	(50)	3	4	(1)	(25)
Net income	724	297	427	144	875	520	355	68
Preferred stock dividends	9	4	5	125	17	7	10	143
Net income attributable to common stock	$ 715	$ 293	$ 422	144%	$ 858	$ 513	$ 345	67%
Basic earnings per common share	$ 1.74	$ .70	$ 1.04	149%	$ 2.08	$ 1.22	$ .86	70%
Diluted earnings per common share	$ 1.52	$ .66	$ .86	130%	$ 1.96	$ 1.15	$ .81	70%
Dividends per common share	$ .25	$ .22	$ .03	14%	$ .47	$ .41	$ .06	15%

Condensed Balance Sheets

	June 30, 2006	December 31, 2005	Increase (Decrease) $	Increase (Decrease) %
Assets				
FFELP Stafford and Other Student Loans, net	$ 21,391	$ 19,988	$ 1,403	7%
Consolidation Loans, net	54,055	54,859	(804)	(1)
Private Education Loans, net	6,833	7,757	(924)	(12)
Other loans, net	1,051	1,138	(87)	(8)
Cash and investments	6,204	4,868	1,336	27
Restricted cash and investments	3,489	3,300	189	6
Retained Interest in off-balance sheet securitized loans	3,152	2,406	746	31
Goodwill and acquired intangible assets, net	1,081	1,105	(24)	(2)
Other assets	4,651	3,918	733	19
Total assets	$ 101,907	$ 99,339	$ 2,568	3%
Liabilities and Stockholders Equity				
Short-term borrowings	$ 3,801	$ 3,810	$ (9)	%
Long-term borrowings	90,507	88,119	2,388	3
Other liabilities	3,230	3,609	(379)	(11)
Total liabilities	97,538	95,538	2,000	2
Minority interest in subsidiaries	9	9		
Stockholders equity before treasury stock	5,238	4,364	874	20
Common stock held in treasury at cost	878	572	306	53
Total stockholders equity	4,360	3,792	568	15
Total liabilities and stockholders equity	$ 101,907	$ 99,339	$ 2,568	3%

RESULTS OF OPERATIONS

CONSOLIDATED EARNINGS SUMMARY

Three Months Ended June 30, 2006 Compared to Three Months Ended June 30, 2005

For the three months ended June 30, 2006, net income of $724 million ($1.52 diluted earnings per share) was a 144 percent increase from net income of $297 million for the three months ended June 30, 2005. Second quarter 2006 pre-tax income of $1.1 billion was a 133 percent increase from $475 million earned in the second quarter of 2005. The larger percentage increase in year-over-year, after-tax net income versus pre-tax net income is driven by the permanent impact of excluding non-taxable gains and losses on equity forward contracts in the Company s stock from taxable income. This resulted in a decrease of the effective tax rate from 37 percent in the second quarter of 2005 to 35 percent in the second quarter of 2006. Under SFAS No. 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity, we are required to mark the equity forward contracts to market each quarter and recognize the change in their value in income. Conversely, these unrealized gains and losses are not recognized on a tax basis. In the second quarter of 2006, the unrealized gains on our outstanding equity forward contracts were $39 million versus unrealized gains of $10 million in the second quarter of 2005, both of which were caused by an increase in the Company s stock price over each period.

There were several factors that contributed to the increase in the pre-tax results of the second quarter of 2006 versus the year-ago quarter, the two largest of which were a $229 million increase in the net gain on derivative and hedging activities, and an increase in securitization gains of $409 million. The increase in net gains and losses on derivative and hedging activities primarily relates to an unrealized gain for the second quarter of 2006 versus an unrealized loss in the year-ago quarter on Floor Income Contracts. The unrealized gain in the second quarter of 2006 was due to rising forward interest rates. In the year-ago quarter, forward interest rates fell resulting in an unrealized loss. Securitization gains in the second quarter of 2006 of $671 million were largely driven by the two Private Education Loan securitizations totaling $4.0 billion of student loans. In the second quarter of 2005, there was only one Private Education Loan securitization totaling $1.5 billion of student loans.

We incurred impairment losses in the second quarter of 2006 to our Retained Interests in securitizations of $91 million versus $15 million in the year-ago quarter. The 2006 losses were primarily the result of the combined high level of Consolidation Loan activity and the impairment of Embedded Floor Income as a result of higher interest rates. The increase in year-over-year impairment losses was the major driver of the $67 million decrease in servicing and securitization revenue.

Net interest income increased by $27 million or 8 percent year-over-year due to the 18 percent increase in average interest earning assets, offset by a 15 basis point decrease in the net interest margin. The year-over-year decrease in the net interest margin is due to the build-up in funding in anticipation of record Consolidation Loan activity as borrowers locked in lower rates before the interest rate reset on FFELP Stafford Loans. The net interest margin was also negatively impacted by a 4 basis point decrease in the on-balance sheet student loan spread, which was primarily due to lower Floor Income.

In the second quarter of 2006, fee and other income and collections revenue totaled $257 million, an increase of 25 percent over the year-ago quarter. This increase was primarily driven by the $25 million or 60 percent increase in collections revenue.

Our Managed student loan portfolio grew by $13.6 billion, from $116.5 billion at June 30, 2005 to $130.1 billion at June 30, 2006. This growth was fueled by the acquisition of $7.9 billion of student loans, including $1.7 billion in Private Education Loans, in the quarter ended June 30, 2006, versus $7.8 billion acquired in the year-ago quarter, of which $1.3 billion were Private Education Loans. In the quarter ended June 30, 2006, we originated $3.2 billion of student loans through our Preferred Channel, an increase of 14 percent over the $2.8 billion originated in the year-ago quarter.

Six Months Ended June 30, 2006 Compared to Six Months Ended June 30, 2005

For the six months ended June 30, 2006, our net income increased by 68 percent to $875 million ($1.96 diluted earnings per share) from net income of $520 million ($1.15 diluted earnings per share) in 2005. Pre-tax income for the six months ended June 30, 2006 increased by 57 percent to $1.4 billion versus $887 million in the first six months of 2005. The larger percentage increase in year-over-year net income versus pre-tax income is primarily due to the decrease in the effective tax rate from 41 percent in the six months ended June 30, 2005 to 37 percent in the six months ended June 30, 2006, caused by the decrease in unrealized losses on equity forward contracts as described above. In the six months ended June 30, 2006, we recognized unrealized losses on our outstanding equity forward contracts of $83 million versus unrealized losses of $98 million in the first six months of 2005.

The increase in pre-tax income is primarily due to a $389 million increase in securitization gains in the six months ended June 30, 2006. The securitization gains in the first half of 2006 were primarily driven by the two second quarter Private Education Loan securitizations referenced above. In the year-ago period, there was only one Private Education Loan securitization that had a pre-tax gain of $231 million or 15 percent of the amount securitized.

The year-over-year results were negatively impacted by impairments of our Retained Interests in securitizations of $143 million in the first half of 2006 versus $24 million in the first half of 2005. These impairments were the primary reason for the $111 million year-over-year decrease in servicing and securitization revenue.

The $176 million increase in the gain on derivative and hedging activities primarily relates to unrealized and realized gains and losses on derivatives that do not receive hedge accounting treatment. For the six months ended June 30, 2006, realized losses decreased by $127 million versus the first six months of 2005. The majority of these losses related to net settlements on Floor Income Contracts, which were offset by Floor Income earned on student loans. Unrealized derivative gains are primarily due to the effect of higher forward interest rates on the liability for outstanding Floor Income Contracts. Forward interest rates increased during the first half of both 2006 and 2005; however, during the first half of 2006, the increase in forward interest rates was greater, resulting in greater unrealized gains for the first half of 2006. These gains were partially offset by unrealized losses on basis swaps economically hedging our inflation-indexed debt.

Our Managed student loan portfolio grew by $13.6 billion, from $116.5 billion at June 30, 2005 to $130.1 billion at June 30, 2006. This growth was fueled by the acquisition of $16.5 billion of student loans, including $3.6 billion in Private Education Loans, in the six months ended June 30, 2006, a 7 percent increase over the $15.3 billion acquired in the year-ago period, of which $2.6 billion were Private Education Loans. In the six months ended June 30, 2006, we originated $10.8 billion of student loans through our Preferred Channel, an increase of 13 percent over the $9.5 billion originated in the year-ago period.

NET INTEREST INCOME

Net interest income, including interest income and interest expense, is derived primarily from our portfolio of student loans that remain on-balance sheet and to a lesser extent from other loans, cash and investments. The Taxable Equivalent Net Interest Income analysis below is designed to facilitate a comparison of non-taxable asset yields to taxable yields on a similar basis. Additional information regarding the return on our student loan portfolio is set forth under Student Loan Spread *Student Loan Spread Analysis On-Balance Sheet.* Information regarding the provisions for losses is included in Note 3 to the consolidated financial statements, Allowance for Student Loan Losses.

Taxable Equivalent Net Interest Income

The amounts in the following table are adjusted for the impact of certain tax-exempt and tax-advantaged investments based on the marginal federal corporate tax rate of 35 percent.

	Three Months Ended June 30, 2006		**Increase (Decrease)**		**Six Months Ended June 30,**		**Increase (Decrease)**	
	2006	**2005**	**$**	**%**	**2006**	**2005**	**$**	**%**
Interest income:								
Student loans	$ 1,412	$ 920	$ 492	53%	$ 2,773	$ 1,749	$ 1,024	59%
Other loans	24	20	4	20	47	40	7	18
Cash and investments	125	54	71	131	221	116	105	91
Taxable equivalent adjustment	1	1			1	2	(1)	(50)
Total taxable equivalent interest income	1,562	995	567	57	3,042	1,907	1,135	60
Interest expense	1,204	664	540	81	2,296	1,228	1,068	87
Taxable equivalent net interest income	$ 358	$ 331	$ 27	8%	$ 746	$ 679	$ 67	10%

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Average Balance Sheets

The following table reflects the rates earned on interest earning assets and paid on interest bearing liabilities for the three and six months ended June 30, 2006 and 2005. This table reflects the net interest margin for the entire Company on a consolidated basis.

	Three Months Ended June 30,			
	2006		2005	
	Balance	Rate	Balance	Rate
Average Assets				
FFELP Stafford and Other Student Loans	$ 20,562	6.58%	$ 20,673	4.63%
Consolidation Loans	52,201	6.47	43,531	5.11
Private Education Loans	7,961	11.77	6,376	7.98
Other loans	1,090	8.72	1,051	7.83
Cash and investments	8,867	5.67	5,206	4.24
Total interest earning assets	90,681	6.91%	76,837	5.20%
Non-interest earning assets	8,648		6,627	
Total assets	$ 99,329		$ 83,464	
Average Liabilities and Stockholders Equity				
Short-term borrowings	$ 4,393	5.07%	$ 5,308	3.63%
Long-term borrowings	87,364	5.27	71,673	3.45
Total interest bearing liabilities	91,757	5.26%	76,981	3.46%
Non-interest bearing liabilities	3,501		3,309	
Stockholders equity	4,071		3,174	
Total liabilities and stockholders equity	$ 99,329		$ 83,464	
Net interest margin		1.58%		1.73%

	Six Months Ended June 30,			
	2006		2005	
	Balance	Rate	Balance	Rate
Average Assets				
FFELP Stafford and Other Student Loans	$ 20,045	6.39%	$ 19,604	4.42%
Consolidation Loans	53,251	6.30	43,204	4.96
Private Education Loans	8,485	11.29	6,321	8.18

Other loans	1,131	8.42	1,074	7.74
Cash and investments	7,959	5.61	6,473	3.65
Total interest earning assets	90,871	6.75%	76,676	5.02%
Non-interest earning assets	8,307		6,507	
Total assets	$ 99,178		$ 83,183	
Average Liabilities and Stockholders Equity				
Short-term borrowings	$ 4,284	4.93%	$ 4,388	3.59%
Long-term borrowings	87,346	5.06	72,461	3.20
Total interest bearing liabilities	91,630	5.05%	76,849	3.22%
Non-interest bearing liabilities	3,600		3,267	
Stockholders equity	3,948		3,067	
Total liabilities and stockholders equity	$ 99,178		$ 83,183	
Net interest margin		1.65%		1.78%

Rate/ Volume Analysis

The following rate/volume analysis illustrates the relative contribution of changes in interest rates and asset volumes.

	Taxable Equivalent Increase (Decrease)	Increase (Decrease) Attributable to Change in Rate	Increase (Decrease) Attributable to Change in Volume
Three months ended June 30, 2006 vs. three months ended June 30, 2005			
Taxable equivalent interest income	$ 567	$ 386	$ 181
Interest expense	540	413	127
Taxable equivalent net interest income	$ 27	$ (27)	$ 54

	Taxable Equivalent Increase (Decrease)	Increase (Decrease) Attributable to Change in Rate	Increase (Decrease) Attributable to Change in Volume
Six months ended June 30, 2006 vs. six months ended June 30, 2005			
Taxable equivalent interest income	$ 1,135	$ 761	$ 374
Interest expense	1,068	834	234
Taxable equivalent net interest income	$ 67	$ (73)	$ 140

The decrease in the net interest margin for both the three and six months ended June 30, 2006 versus the year-ago periods is primarily due to fluctuations in the student loan spread as discussed under Student Loan Spread *Student Loan Spread Analysis On-Balance Sheet*, and to the build-up of funding in anticipation of record Consolidation Loan activity as at the end of the second quarter, borrowers locked in lower interest rates before the July 1 reset on FFELP Stafford loans.

Student Loans

For both federally insured and Private Education Loans, we account for premiums paid, discounts received and certain origination costs incurred on the origination and acquisition of student loans in accordance with SFAS No. 91, Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases. The unamortized portion of the premiums and discounts is included in the carrying value of the student loan on the consolidated balance sheet. We recognize income on our student loan portfolio based on the expected yield of the student loan after giving effect to the amortization of purchase premiums and the accretion of student loan discounts, as well as interest rate reductions and rebates expected to be earned through Borrower Benefits programs. Discounts on Private Education Loans are deferred and accreted to income over the lives of the student loans. In the table below, this accretion of discounts is netted with the amortization of the premiums.

Student Loan Spread

An important performance measure closely monitored by management is the student loan spread. The student loan spread is the difference between the income earned on the student loan assets and the interest paid on the debt funding those assets. A number of factors can affect the overall student loan spread such as:

- the mix of student loans in the portfolio, with Consolidation Loans having the lowest spread and Private Education Loans having the highest spread;

the premiums paid, borrower fees charged and capitalized costs incurred to acquire student loans which impact the spread through subsequent amortization;

the type and level of Borrower Benefits programs for which the student loans are eligible;

the level of Floor Income and, when considering the Core Earnings basis student loan spread, the amount of Floor Income-eligible loans that have been hedged through Floor Income Contracts; and

funding and hedging costs.

The student loan spread is highly susceptible to liquidity, funding and interest rate risk. These risks are discussed separately in our 2005 Annual Report on Form 10-K at LIQUIDITY AND CAPITAL RESOURCES and in the RISK FACTORS discussion.

Student Loan Spread Analysis On-Balance Sheet

The following table analyzes the reported earnings from student loans on-balance sheet. For an analysis of our student loan spread for the entire portfolio of Managed student loans on a similar basis to the on-balance sheet analysis, see LENDING BUSINESS SEGMENT Student Loan Spread Analysis Core Earnings Basis.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
On-Balance Sheet				
Student loan yield, before Floor Income	7.92%	5.79%	7.71%	5.68%
Gross Floor Income	.04	.32	.05	.36
Consolidation Loan Rebate Fees	(.67)	(.63)	(.67)	(.65)
Borrower Benefits	(.11)	(.11)	(.11)	(.14)
Premium and discount amortization	(.16)	(.15)	(.14)	(.15)
Student loan net yield	7.02	5.22	6.84	5.10
Student loan cost of funds	(5.27)	(3.43)	(5.05)	(3.19)
Student loan spread	1.75%	1.79%	1.79%	1.91%
Average Balances				
On-balance sheet student loans	$ 80,724	$ 70,580	$ 81,781	$ 69,129

Discussion of Student Loan Spread Effects of Floor Income and Derivative Accounting

One of the primary drivers of fluctuations in our on-balance sheet student loan spread is the level of gross Floor Income (Floor Income earned before payments on Floor Income Contracts) earned in the period. For the three months ended June 30, 2006 and 2005, we earned gross Floor Income of $8 million (4 basis points) and $56 million (32 basis points), respectively. The reduction in gross Floor Income is primarily due to the increase in short-term interest rates. We believe that we have economically hedged practically all of the Floor Income through the sale of Floor Income Contracts, under which we receive an upfront fee and agree to pay the counterparty the Floor Income earned on a notional amount of student loans. These contracts do not qualify for hedge accounting treatment and as a result the payments on the Floor Income Contracts are included on the income statement with gains (losses) on derivative and hedging activities, net rather than in student loan interest income. Payments on Floor Income Contracts associated with on-balance sheet student loans for the three months ended June 30, 2006 and 2005 totaled $8 million (4 basis points) and $52 million (30 basis points), respectively.

In addition to Floor Income Contracts, we also extensively use basis swaps to manage our basis risk associated with interest rate sensitive assets and liabilities. These swaps generally do not qualify as accounting hedges and are likewise required to be accounted for in the gains (losses) on derivative and hedging activities, net line on the income statement. As a result, they are not considered in the calculation of the cost of funds in the above table.

Discussion of Student Loan Spread Effects of Significant Events in the Quarters Presented

The second quarter 2006 spread includes $10 million or 5 basis points of income associated with non-recurring SAP that we accrued on PLUS loans as a result of program changes required by the Higher Education Reconciliation Act of 2005 (Reconciliation Legislation).

In the second quarters of 2006 and 2005, the increase in premium amortization is largely due to the write-off of unamortized premiums on loans consolidated with third parties. In addition, in the second quarter of 2006, we increased the Constant Prepayment Rate (CPR) for our FFELP Stafford loan portfolio in response to the increased rate of loan prepayments occurring through consolidation.

In the second quarter of 2005, we revised our estimates regarding the qualification for Borrower Benefits which resulted in a reduction of the liability for Borrower Benefits of $7 million or 4 basis points. In addition, in the second quarter of 2005, we reduced student loan interest income by $14 million or 9 basis points to reflect a revision of our estimates pertaining to our non-accrual policy for interest income.

In both the second quarters of 2006 and 2005, there was an increase in Consolidation Loan activity as FFELP Stafford borrowers locked in lower interest rates by consolidating their loans prior to the July 1 interest rate reset for FFELP Stafford loans. In addition, reconsolidation of Consolidation Loans through the Direct Loan Program continued in the second quarter of 2006 from the backlog of processing applications after the March 31, 2006 prohibition (see LENDING BUSINESS SEGMENT Student Loan Activity for further discussion). This increase in Consolidation Loan activity resulted in an increase in student loan premium write-offs for both FFELP Stafford and Consolidation Loans consolidated with third parties. Loans lost through consolidation benefit the student loan spread to a lesser extent through the write-off of the Borrower Benefits liability associated with these loans. Furthermore, in both the second quarters of 2006 and 2005, we accrued a net write-off to our Borrower Benefits liability for loans whose consolidation applications had been received but not yet processed by June 30th, resulting in a further reduction to Borrower Benefits expense.

Discussion of Student Loan Spread Other Quarter-over-Quarter Fluctuations

When compared to the prior year, the 2006 student loan spread benefited from the 25 percent increase in the average balance of Private Education Loans, which now constitutes 10 percent of the total average balance of on-balance sheet student loans versus 9 percent in the prior year. Also, the portfolio of on-balance sheet Private Education Loans in the second quarter of 2006 had higher average spreads than the on-balance sheet Private Education Loans in the second quarter of 2005.

Floor Income

For on-balance sheet student loans, gross Floor Income is included in student loan income whereas payments on Floor Income Contracts are included in the gains (losses) on derivative and hedging activities, net line in other income. The following table summarizes the components of Floor Income from on-balance sheet student loans, net of payments under Floor Income Contracts, for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended					
	June 30, 2006			June 30, 2005		
	Fixed Borrower Rate	Variable Borrower Rate	Total	Fixed Borrower Rate	Variable Borrower Rate	Total
Floor Income:						
Gross Floor Income	$ 8	$	$ 8	$ 56	$	$ 56
Payments on Floor Income Contracts	(8)		(8)	(52)		(52)
Net Floor Income	$	$	$	$ 4	$	$ 4
Net Floor Income in basis points				2		2

	Six Months Ended					
	June 30, 2006			June 30, 2005		
	Fixed Borrower Rate	Variable Borrower Rate	Total	Fixed Borrower Rate	Variable Borrower Rate	Total
Floor Income:						
Gross Floor Income	$ 22	$	$ 22	$ 122	$	$ 122
Payments on Floor Income Contracts	(22)		(22)	(112)		(112)
Net Floor Income	$	$	$	$ 10	$	$ 10
Net Floor Income in basis points				3		3

The decrease in Floor Income for the three months ended June 30, 2006 versus the same period in 2005 is due to an increase in short-term interest rates.

As discussed in more detail under LIQUIDITY AND CAPITAL RESOURCES Securitization Activities, when we securitize a portfolio of student loans, we estimate the future Fixed Rate Embedded Floor Income earned on off-balance sheet student loans using a discounted cash flow option pricing model and recognize the fair value of such cash flows in the initial gain on sale and subsequent valuations of the Residual Interest. Variable Rate Embedded Floor Income is recognized as earned in servicing and securitization revenue.

FEDERAL AND STATE TAXES

The Company is subject to federal and state income taxes. Our effective tax rate for the three months ended June 30, 2006 was 35 percent versus 37 percent for the three months ended June 30, 2005 and for the six months ended June 30, 2006 was 37 percent versus 41 percent for the six months ended June 30, 2005. The effective tax rate reflects the permanent impact of the exclusion of the gains or losses on equity forward contracts recognized under SFAS No. 150.

BUSINESS SEGMENTS

The results of operations of the Company s Lending and Debt Management Operations (DMO) operating segments are presented below. These defined business segments operate in distinct business environments and are considered reportable segments under SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, based on quantitative thresholds applied to the Company s financial statements. In addition, we provide other complementary products and services, including guarantor and student loan servicing, through smaller operating segments that do not meet such thresholds and are aggregated in the Corporate and Other reportable segment for financial reporting purposes.

The management reporting process measures the performance of the Company s operating segments based on the management structure of the Company as well as the methodology used by management to evaluate performance and allocate resources. In accordance with the Rules and Regulations of the Securities and Exchange Commission (SEC), we prepare financial statements in accordance with GAAP. In addition to evaluating the Company s GAAP-based financial information, management, including the Company s chief operation decision maker, evaluates the performance of the Company s operating segments based on their profitability on a basis that, as allowed under SFAS No. 131, differs from GAAP. We refer to management s basis of evaluating our segment results as Core Earnings presentations for each business segment and we refer to these performance measures in our presentations with credit rating agencies and lenders. Accordingly, information regarding the Company s reportable segments is provided herein based on Core Earnings, which are discussed in detail below.

Our Core Earnings are not defined terms within GAAP and may not be comparable to similarly titled measures reported by other companies. Core Earnings net income reflects only current period adjustments to GAAP net income as described below. Unlike financial accounting, there is no comprehensive, authoritative guidance for management reporting and as a result, our management reporting is not necessarily comparable with similar information for any other financial institution. The Company s operating segments are defined by the products and services they offer or the types of customers they serve, and they reflect the manner in which financial information is currently evaluated by management. Intersegment revenues and expenses are netted within the appropriate financial statement line items consistent with the income statement presentation provided to management. Changes in management structure or allocation methodologies and procedures may result in changes in reported segment financial information.

Core Earnings are the primary financial performance measures used by management to develop the Company s financial plans, track results, and establish corporate performance targets and incentive compensation. While Core Earnings are not a substitute for reported results under GAAP, the Company relies on Core Earnings in operating its business because Core Earnings permit management to make meaningful period-to-period comparisons of the operational and performance indicators that are most closely assessed by management. Management believes this information provides additional insight into the financial performance of the core business activities of our operating segments. Accordingly, the tables presented below reflect Core Earnings which is reviewed and utilized by management to manage the business for each of the Company s reportable segments. A further discussion regarding Core Earnings is included under Limitations of Core Earnings and *Pre-tax Differences between Core Earnings ar GAAP by Business Segment.*

The Lending operating segment includes all discussion of income and related expenses associated with the net interest margin, the student loan spread and its components, the provisions for loan losses, and other fees earned on our Managed portfolio of student loans. The DMO operating segment reflects the fees earned and expenses incurred in providing accounts receivable management and collection services. Our Corporate and Other reportable segment includes our remaining fee businesses and other corporate expenses that do not pertain directly to the primary segments identified above.

	Three Months Ended June 30, 2006		
	Lending	DMO	Corporate and Other
Interest income:			
FFELP Stafford and Other Student Loans	$ 719	$	$
Consolidation Loans	1,114		
Private Education Loans	485		
Other loans	24		
Cash and investments	170		1
Total interest income	2,512		1
Total interest expense	1,904	5	1
Net interest income	608	(5)	
Less: provisions for losses	60		
Net interest income after provisions for losses	548	(5)	
Fee income		90	33
Collections revenue		67	
Other income	51		24
Operating expenses[1]	163	85	50
Income before income taxes and minority interest in net earnings of subsidiaries	436	67	7
Income tax expense[2]	161	26	2
Minority interest in net earnings of subsidiaries		1	
Core Earnings net income	$ 275	$ 40	$ 5

(1) Operating expenses for the Lending, DMO, and Corporate and Other business segments include $8 million, $2 million, and $4 million, respectively, of stock-based compensation expense due to the implementation of SFAS No. 123(R) in the first quarter of 2006.

(2) Income taxes are based on a percentage of net income before tax for the individual reportable segment.

	Three Months Ended June 30, 2005		
	Lending	DMO	Corporate and Other
Interest income:			
FFELP Stafford and Other Student Loans	$ 582	$	$
Consolidation Loans	667		
Private Education Loans	247		
Other loans	20		
Cash and investments	77		1
Total interest income	1,593		1
Total interest expense	1,073	4	1
Net interest income	520	(4)	
Less: provisions for losses	14		
Net interest income after provisions for losses	506	(4)	
Fee income		82	26
Collections revenue		42	
Other income	36		29
Operating expenses[(1)]	141	67	63
Income (loss) before income taxes and minority interest in net earnings of subsidiaries	401	53	(8)
Income tax expense (benefit)[(2)]	148	20	(3)
Minority interest in net earnings of subsidiaries	1	1	
Core Earnings net income (loss)	$ 252	$ 32	$ (5)

(1) In the first quarter of 2006, the Company changed its method for allocating certain overhead and other expenses between our business segments. Balances for the three months ending June 30, 2005 have been updated to reflect the new allocation methodology.

(2) Income taxes are based on a percentage of net income before tax for the individual reportable segment.

	Six Months Ended June 30, 2006		
	Lending	DMO	Corporate and Other
Interest income:			
FFELP Stafford and Other Student Loans	$ 1,369	$	$
Consolidation Loans	2,142		
Private Education Loans	914		
Other loans	47		
Cash and investments	300		2
Total interest income	4,772		2
Total interest expense	3,562	11	3
Net interest income	1,210	(11)	(1)
Less: provisions for losses	135		
Net interest income after provisions for losses	1,075	(11)	(1)
Fee income		182	60
Collections revenue		124	
Other income	92		55
Operating expenses(1)	324	175	109
Income before income taxes and minority interest in net earnings of subsidiaries	843	120	5
Income tax expense(2)	312	44	2
Minority interest in net earnings of subsidiaries		3	
Core Earnings net income	$ 531	$ 73	$ 3

(1) Operating expenses for the Lending, DMO, and Corporate and Other business segments include $18 million, $5 million, and $9 million, respectively, of stock-based compensation expense due to the implementation of SFAS No. 123(R) in the first quarter of 2006.

(2) Income taxes are based on a percentage of net income before tax for the individual reportable segment.

	Six Months Ended June 30, 2005		
	Lending	DMO	Corporate and Other
Interest income:			
FFELP Stafford and Other Student Loans	$ 1,092	$	$
Consolidation Loans	1,248		
Private Education Loans	474		
Other loans	40		
Cash and investments	156		2
Total interest income	3,010		2
Total interest expense	1,991	8	3
Net interest income	1,019	(8)	(1)
Less: provisions for losses	69		
Net interest income after provisions for losses	950	(8)	(1)
Fee income		168	58
Collections revenue		77	
Other income	72		61
Operating expenses[(1)]	275	132	114
Income before income taxes and minority interest in net earnings of subsidiaries	747	105	4
Income tax expense[(2)]	277	39	1
Minority interest in net earnings of subsidiaries	2	2	
Core Earnings net income	$ 468	$ 64	$ 3

(1) In the first quarter of 2006, the Company changed its method for allocating certain overhead and other expenses between our business segments. Balances for the six months ending June 30, 2005 have been updated to reflect the new allocation methodology.

(2) Income taxes are based on a percentage of net income before tax for the individual reportable segment.

Limitations of Core Earnings

While GAAP provides a uniform, comprehensive basis of accounting, for the reasons described above, management believes that Core Earnings are an important additional tool for providing a more complete understanding of the Company s results of operations. Nevertheless, Core Earnings are subject to certain general and specific limitations that investors should carefully consider. For example, as stated above, unlike financial accounting, there is no comprehensive, authoritative guidance for management reporting. Our Core Earnings are not defined terms within GAAP and may not be comparable to similarly titled measures reported by other companies. Unlike GAAP, Core Earnings reflect only current period adjustments to GAAP. Accordingly, the Company s Core Earnings presentation does not represent a comprehensive basis of accounting. Investors, therefore, may not compare our

Company s performance with that of other financial services companies based upon Core Earnings. Core Earnings results are only meant to supplement GAAP results by providing additional information regarding the operational and performance indicators that are most closely used by management, the Company s board of directors, rating agencies and lenders to assess performance.

Other limitations arise from the specific adjustments that management makes to GAAP results to derive Core Earnings results. For example, in reversing the unrealized gains and losses that result from SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, on derivatives that do not qualify for hedge treatment, as well as on derivatives that do qualify but are in part ineffective because they are not perfect hedges, we focus on the long-term economic effectiveness of those instruments relative to the underlying hedged item and isolate the effects of interest rate volatility, changing credit spreads and changes in our stock price on the fair value of such instruments during the period. Under GAAP, the effects of these factors on the fair value of the derivative instruments (but not on the underlying hedged item) tend to show more volatility in the short term. While our presentation of our results on a Core Earnings basis provides important information regarding the performance of our Managed portfolio, a limitation of this presentation is that we are presenting the ongoing spread income on loans that have been sold to a trust managed by us. While we believe that our Core Earnings presentation presents the economic substance of our Managed loan portfolio, it understates earnings volatility from securitization gains. Our Core Earnings results exclude certain Floor Income, which is real cash income, from our reported results and therefore may understate earnings in certain periods. Management s financial planning and valuation of operating results, however, does not take into account Floor Income because of its inherent uncertainty, except when it is economically hedged through Floor Income Contracts.

Pre-tax differences between Core Earnings and GAAP by Business Segment

Our Core Earnings are the primary financial performance measures used by management to evaluate performance and to allocate resources. Accordingly, financial information is reported to management on a Core Earnings basis by reportable segment, as these are the measures used regularly by our chief operating decision maker. Our Core Earnings are used in developing our financial plans and tracking results, and also in establishing corporate performance targets and determining incentive compensation. Management believes this information provides additional insight into the financial performance of the Company s core business activities. Core Earnings net income reflects only current period adjustments to GAAP net income, as described in the more detailed discussion of the differences between Core Earnings and GAAP that follows, which includes further detail on each specific adjustment required to reconcile our Core Earnings segment presentation to our GAAP earnings.

	Three Months Ended June 30,					
	2006			**2005**		
	Lending	**DMO**	**Corporate and Other**	**Lending**	**DMO**	**Corporate and Other**
Core Earnings adjustments to GAAP:						
Net impact of securitization accounting	$ 502	$	$	$ 107	$	$
Net impact of derivative accounting	126		39	(21)		10
Net impact of Floor Income	(52)			(51)		
Amortization of acquired intangibles	(13)	(4)	(1)	(12)	(3)	(1)
Total Core Earnings adjustments to GAAP	$ 563	$ (4)	$ 38	$ 23	$ (3)	$ 9

	Six Months Ended June 30,					
	2006			**2005**		
	Lending	**DMO**	**Corporate and Other**	**Lending**	**DMO**	**Corporate and Other**

Core Earnings adjustments to GAAP:						
Net impact of securitization accounting	$ 440	$	$	$ 75	$	$
Net impact of derivative accounting	209		(83)	177		(98)
Net impact of Floor Income	(105)			(94)		
Amortization of acquired intangibles	(22)	(8)	(2)	(21)	(5)	(3)
Total Core Earnings adjustments to GAAP	$ 522	$ (8)	$ (85)	$ 137	$ (5)	$ (101)

1) **Securitization:** Under GAAP, certain securitization transactions in our Lending operating segment are accounted for as sales of assets. Under the Company s Core Earnings presentation for the Lending operating segment, we present all securitization transactions on a Core Earnings basis as long-term non-recourse financings. The upfront gains on sale from securitization transactions as well as ongoing servicing and securitization revenue presented in accordance with GAAP are excluded from Core Earnings net income and replaced by the interest income, provisions for loan losses, and interest expense as they are earned or incurred on the securitization loans. We also exclude transactions with our off-balance sheet trusts from Core Earnings net income as they are considered intercompany transactions on a Core Earnings basis.

The following table summarizes the securitization adjustments in our Lending operating segment for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2006	**2005**	**2006**	**2005**
Core Earnings securitization adjustments:				
Net interest income on securitized loans, after provisions for losses	$ (242)	$ (295)	$ (430)	$ (515)
Gains on student loan securitizations	671	262	701	312
Servicing and securitization revenue	83	150	182	293
Intercompany transactions with off-balance sheet trusts	(10)	(10)	(13)	(15)
Total Core Earnings securitization adjustments	$ 502	$ 107	$ 440	$ 75

2) **Derivative Accounting:** Core Earnings net income excludes periodic unrealized gains and losses arising primarily in our Lending operating segment, and to a lesser degree in our Corporate and Other reportable segment, that are caused primarily by the one-sided mark-to-market derivative valuations prescribed by SFAS No. 133 on derivatives that do not qualify for hedge treatment under GAAP. Under the Company s Core Earnings presentation, we recognize the economic effect of these hedges, which generally results in any cash paid or received being recognized ratably as an expense or revenue over the hedged item s life. Core Earnings also excludes the gain or loss on equity forward contracts that under SFAS No. 133, are required to be accounted for as derivatives and are marked-to-market through earnings.

SFAS No. 133 requires that changes in the fair value of derivative instruments be recognized currently in earnings unless specific hedge accounting criteria, as specified by SFAS No. 133, are met. We believe that our derivatives are effective economic hedges, and as such, are a critical element of our interest rate risk management strategy. However, some of our derivatives, primarily Floor Income Contracts, certain Eurodollar futures contracts and certain basis swaps and equity forward contracts (discussed in detail below), do not qualify for hedge treatment as defined by SFAS No. 133, and the stand-alone derivative must be marked-to-market in the income statement with no consideration for the corresponding change in fair value of the hedged item. The gains and losses described in gains (losses) on derivative and hedging activities, net are primarily caused by interest rate volatility, changing credit spreads and changes in our stock price during the period as well as the volume and term of derivatives not receiving hedge treatment.

Our Floor Income Contracts are written options that must meet more stringent requirements than other hedging relationships to achieve hedge effectiveness under SFAS No. 133. Specifically, our Floor Income Contracts do not qualify for hedge accounting treatment because the paydown of principal of the student loans with the embedded Floor Income does not exactly match the change in the notional amount of our written Floor Income Contracts. Under SFAS No. 133, the upfront payment is deemed a liability and changes in fair value are recorded through income throughout the life of the contract. The change in the value of Floor Income Contracts is primarily caused by changing interest rates that cause the amount of Floor Income earned on the underlying student loans and paid to the counterparties to vary. This is economically offset by the change in value of the student loan portfolio, including our Retained Interests, earning Floor Income but that offsetting change in value is not recognized under SFAS No. 133. We believe the Floor Income Contracts are economic hedges because they effectively fix the amount of Floor Income earned over the contract period, thus eliminating the timing and uncertainty that changes in interest rates can have on Floor Income for that period. Prior to SFAS No. 133, we accounted for Floor Income Contracts as hedges and amortized the upfront cash compensation ratably over the lives of the contracts.

Basis swaps are used to convert floating rate debt from one interest rate index to another to better match the interest rate characteristics of the assets financed by that debt. We primarily use basis swaps to change the index of our floating rate debt to better match the cash flows of our student loan assets that are primarily indexed to a commercial paper, Prime or Treasury bill index. SFAS No. 133 requires that when using basis swaps, the change in the cash flows of the hedge effectively offset both the change in the cash flows of the asset and the change in the cash flows of the liability. Our basis swaps hedge variable interest rate risk, however they do not meet this effectiveness test because our FFELP student loans can earn at either a variable or a fixed interest rate depending on market interest rates. We also have basis swaps that do not meet the SFAS No. 133 effectiveness test that economically hedge off-balance sheet instruments. As a result, under GAAP these swaps are recorded at fair value with changes in fair value reflected in the income statement.

Generally, a decrease in current interest rates and the respective forward interest rate curves results in an unrealized loss related to our written Floor Income Contracts which is offset by an increase in the value of the economically hedged student loans. This increase is not recognized in income. We will experience unrealized gains/losses related to our basis swaps if the two underlying indices (and related forward curve) do not move in parallel.

Under SFAS No. 150, equity forward contracts that allow a net settlement option either in cash or the Company s stock are required to be accounted for as derivatives in accordance with SFAS No. 133. As a result, we account for our equity forward contracts as derivatives in accordance with SFAS No. 133 and mark them to market through earnings. They do not qualify as effective SFAS No. 133 hedges, as a requirement to achieve hedge accounting is the hedged item must impact net income and the settlement of these contracts through the purchase of our own stock does not impact net income.

The table below quantifies the adjustments for derivative accounting under SFAS No. 133 on our net income for the three and six months ended June 30, 2006 and 2005 when compared with the accounting principles employed in all years prior to the SFAS No. 133 implementation.

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2006	**2005**	**2006**	**2005**
Core Earnings derivative adjustments:				
Gains (losses) on derivative and hedging activities, net included in other income[(1)]	$ 123	$ (106)	$ 36	$ (140)
Less: Realized losses on derivative and hedging activities, net[(1)]	41	94	89	216
Unrealized gains (losses) on derivative and hedging activities, net[(1)]	164	(12)	125	76
Other pre-SFAS No. 133 accounting adjustments	1	1	1	3
Total net impact of SFAS No. 133 derivative accounting	$ 165	$ (11)	$ 126	$ 79

(1)

See *Reclassification of Realized Gains (Losses) on Derivative and Hedging Activities* below for a detailed breakdown of the components of both the realized and unrealized losses on derivative and hedging activities.

Reclassification of Realized Gains (Losses) on Derivative and Hedging Activities

SFAS No. 133 requires net settlement income/expense on derivatives and realized gains/losses related to derivative dispositions (collectively referred to as realized gains (losses) on derivative and hedging activities) that do not qualify as hedges under SFAS No. 133 to be recorded in a separate income statement line item below net interest income. The table below summarizes the realized losses on derivative and hedging activities, and where they are reclassified to on a Core Earnings basis for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
Reclassification of realized losses on derivative and hedging activities:				
Net settlement expense on Floor Income Contracts reclassified to net interest income	$ (12)	$ (77)	$ (33)	$ (165)
Net settlement expense on interest rate swaps reclassified to net interest income	(29)	(17)	(56)	(46)
Net realized losses on closed Eurodollar futures contracts and terminated derivative contracts reclassified to other income				(5)
Total reclassifications of realized losses on derivative and hedging activities	(41)	(94)	(89)	(216)
Add: Unrealized gains (losses) on derivative and hedging activities, net[1]	164	(12)	125	76
Gains (losses) on derivative and hedging activities, net	$ 123	$ (106)	$ 36	$ (140)

(1) Unrealized gains (losses) on derivative and hedging activities, net is comprised of the following unrealized mark-to-market gains (losses):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
Floor Income Contracts	$ 88	$ (146)	$ 232	$ 122
Equity forward contracts	39	10	(83)	(98)
Basis swaps	14	127	(68)	67
Other	23	(3)	44	(15)
Total unrealized gains (losses) on derivative and hedging activities, net	$ 164	$ (12)	$ 125	$ 76

3) **Floor Income:** The timing and amount (if any) of Floor Income earned in our Lending operating segment is uncertain and in excess of expected spreads. Therefore, we exclude such income from Core Earnings net income when it is not economically hedged. We employ derivatives, primarily Floor Income Contracts and futures, to economically hedge Floor Income. As discussed above in Derivative Accounting, these derivatives do not qualify as effective accounting hedges and therefore, under GAAP, they are marked-to-market through the gains (losses) on derivative and hedging activities, net line on the income statement with no offsetting gain or loss recorded for the economically hedged items. For Core Earnings net income, we reverse the fair value adjustments on the Floor Income Contracts and futures economically hedging Floor Income and include the amortization of net premiums received (net of Eurodollar futures contracts realized gains or losses) in income.

The following table summarizes the Floor Income adjustments in our Lending operating segment for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
Core Earnings Floor Income adjustments:				
Floor Income earned on Managed loans, net of payments on Floor Income Contracts	$	$ 6	$	$ 17
Amortization of net premiums on Floor Income Contracts and futures in net interest income	(52)	(57)	(105)	(111)
Total Core Earnings Floor Income adjustments	$ (52)	$ (51)	$ (105)	$ (94)

4) **Other Items:** We exclude goodwill impairment and amortization of acquired intangibles. These amounts totaled $18 million and $16 million, respectively, for the three months ended June 30, 2006 and 2005, and $32 million and $29 million, respectively, for the six months ended June 30, 2006 and 2005.

LENDING BUSINESS SEGMENT

In our Lending business segment, we originate and acquire federally guaranteed student loans, which are administered by the U.S. Department of Education (ED), and Private Education Loans, which are not federally guaranteed. The majority of our Private Education Loans is made in conjunction with a FFELP Stafford loan and as a result is marketed through the same marketing channels as FFELP Stafford Loans. While FFELP student loans and Private Education Loans have different overall risk profiles due to the federal guarantee of the FFELP student loans, they share many of the same characteristics such as similar repayment terms, the same marketing channel and sales force, and are originated and serviced on the same servicing platform. Finally, where possible, the borrower receives a single bill for both the federally guaranteed and privately underwritten loans.

The following table summarizes the Core Earnings results of operations for our Lending business segment.

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	% Increase (Decrease) 2006 vs. 2005	Six Months Ended June 30, 2006	Six Months Ended June 30, 2005	% Increase (Decrease) 2006 vs. 2005
Core Earnings interest income:						
FFELP and Other Student Loans	$ 719	$ 582	24%	$ 1,369	$ 1,092	25%
Consolidation loans	1,114	667	67	2,142	1,248	72
Private Education Loans	485	247	96	914	474	93
Other loans	24	20	20	47	40	18
Cash and investments	170	77	121	300	156	92
Total Core Earnings interest income	2,512	1,593	58	4,772	3,010	59
Total Core Earnings interest expense	1,904	1,073	77	3,562	1,991	79
Net Core Earnings interest income	608	520	17	1,210	1,019	19
Less: provisions for losses	60	14	329	135	69	96
Net Core Earnings interest income after provisions for losses	548	506	8	1,075	950	13
Other income	51	36	42	92	72	28
Operating expenses(1)(2)	163	141	16	324	275	18
Income before income taxes and minority interest in net earnings of subsidiaries	436	401	9	843	747	13
Income taxes	161	148	9	312	277	13
Income before minority interest in net earnings of subsidiaries	275	253	9	531	470	13
Minority interest in net earnings of subsidiaries		1	(100)		2	(100)
Core Earnings net income	$ 275	$ 252	9%	$ 531	$ 468	13%

(1) The three and six months ended June 30, 2006 operating expenses for the Lending segment include $8 million and $18 million, respectively, of stock-based compensation expense due to the implementation of SFAS No. 123(R) in the first quarter of 2006.

(2) In the first quarter of 2006, the Company changed its method for allocating certain overhead and other expenses between our business segments. Balances for the three and six months ending June 30, 2005 have been updated to reflect the new allocation methodology.

Summary of our Managed Student Loan Portfolio

The following tables summarize the components of our Managed student loan portfolio and show the changing composition of our portfolio.

Ending Balances (net of allowance for loan losses):

	June 30, 2006				
	FFELP Stafford and Other[1]	Consolidation Loans	Total FFELP	Private Education Loans	Total
On-balance sheet:					
In-school	$ 7,469	$	$ 7,469	$ 2,487	$ 9,956
Grace and repayment	13,512	53,264	66,776	4,894	71,670
Total on-balance sheet, gross	20,981	53,264	74,245	7,381	81,626
On-balance sheet unamortized premium/(discount)	417	801	1,218	(296)	922
On-balance sheet allowance for losses	(7)	(10)	(17)	(252)	(269)
Total on-balance sheet, net	21,391	54,055	75,446	6,833	82,279
Off-balance sheet:					
In-school	2,812		2,812	3,954	6,766
Grace and repayment	17,412	14,746	32,158	8,602	40,760
Total off-balance sheet, gross	20,224	14,746	34,970	12,556	47,526
Off-balance sheet unamortized premium/(discount)	323	397	720	(274)	446
Off-balance sheet allowance for losses	(12)	(3)	(15)	(92)	(107)
Total off-balance sheet, net	20,535	15,140	35,675	12,190	47,865
Total Managed	$ 41,926	$ 69,195	$ 111,121	$ 19,023	$ 130,144
% of on-balance sheet FFELP	28%	72%	100%		
% of Managed FFELP	38%	62%	100%		
% of total	32%	53%	85%	15%	100%

	December 31, 2005				
	FFELP Stafford and Other[1]	Consolidation Loans	Total FFELP	Private Education Loans	Total

On-balance sheet:					
In-school	$ 6,910	$	$ 6,910	$ 3,432	$ 10,342
Grace and repayment	12,705	54,033	66,738	4,834	71,572
Total on-balance sheet, gross	19,615	54,033	73,648	8,266	81,914
On-balance sheet unamortized premium/(discount)	379	835	1,214	(305)	909
On-balance sheet allowance for losses	(6)	(9)	(15)	(204)	(219)
Total on-balance sheet, net	19,988	54,859	74,847	7,757	82,604
Off-balance sheet:					
In-school	2,962		2,962	2,540	5,502
Grace and repayment	17,410	10,272	27,682	6,406	34,088
Total off-balance sheet, gross	20,372	10,272	30,644	8,946	39,590
Off-balance sheet unamortized premium/(discount)	306	305	611	(188)	423
Off-balance sheet allowance for losses	(8)	(2)	(10)	(78)	(88)
Total off-balance sheet, net	20,670	10,575	31,245	8,680	39,925
Total Managed	$ 40,658	$ 65,434	$ 106,092	$ 16,437	$ 122,529
% of on-balance sheet FFELP	27%	73%	100%		
% of Managed FFELP	38%	62%	100%		
% of total	33%	54%	87%	13%	100%

(1) FFELP category is primarily Stafford loans, but also includes federally insured PLUS and HEAL loans.

Average Balances:

	Quarter Ended June 30, 2006				
	FFELP Stafford and Other[(1)]	**Consolidation Loans**	**Total FFELP**	**Private Education Loans**	**Total**
On-balance sheet	$ 20,562	$ 52,201	$ 72,763	$ 7,961	$ 80,724
Off-balance sheet	22,065	14,881	36,946	10,770	47,716
Total Managed	$ 42,627	$ 67,082	$ 109,709	$ 18,731	$ 128,440
% of on-balance sheet FFELP	28%	72%	100%		
% of Managed FFELP	39%	61%	100%		
% of Total	33%	52%	85%	15%	100%

	Quarter Ended June 30, 2005				
	FFELP Stafford and Other[(1)]	**Consolidation Loans**	**Total FFELP**	**Private Education Loans**	**Total**
On-balance sheet	$ 20,673	$ 43,531	$ 64,204	$ 6,376	$ 70,580
Off-balance sheet	26,912	9,819	36,731	7,060	43,791
Total Managed	$ 47,585	$ 53,350	$ 100,935	$ 13,436	$ 114,371
% of on-balance sheet FFELP	32%	68%	100%		
% of Managed FFELP	47%	53%	100%		
% of Total	41%	47%	88%	12%	100%

	Six Months Ended June 30, 2006				
	FFELP Stafford and Other[(1)]	**Consolidation Loans**	**Total FFELP**	**Private Education Loans**	**Total**
On-balance sheet	$ 20,045	$ 53,251	$ 73,296	$ 8,485	$ 81,781
Off-balance sheet	21,926	13,267	35,193	9,716	44,909
Total Managed	$ 41,971	$ 66,518	$ 108,489	$ 18,201	$ 126,690
% of on-balance sheet FFELP	27%	73%	100%		

% of Managed FFELP	39%	61%	100%		
% of Total	33%	53%	86%	14%	100%

Six Months Ended June 30, 2005

	FFELP Stafford and Other[1]	Consolidation Loans	Total FFELP	Private Education Loans	Total
On-balance sheet	$ 19,603	$ 43,205	$ 62,808	$ 6,321	$ 69,129
Off-balance sheet	27,578	8,661	36,239	6,607	42,846
Total Managed	$ 47,181	$ 51,866	$ 99,047	$ 12,928	$ 111,975
% of on-balance sheet FFELP	31%	69%	100%		
% of Managed FFELP	48%	52%	100%		
% of Total	42%	46%	88%	12%	100%

[1] FFELP category is primarily Stafford loans, but also includes federally insured PLUS and HEAL loans.

Student Loan Spread Analysis   Core Earnings   Basis

The following table analyzes the earnings from our portfolio of Managed student loans on a   Core Earnings   basis (see   BUSINESS SEGMENTS   *Pre-tax differences between   Core Earnings   and GAAP by Business Segment*). The   Core Earnings   Basis Student Loan Spread Analysis presentation and certain components used in the calculation differ from the On-Balance Sheet Student Loan Spread Analysis presentation. The   Core Earnings   basis presentation, when compared to our on-balance sheet presentation, is different in that it:

includes the net interest margin related to our off-balance sheet student loan securitization trusts. This includes any related fees or costs such as the Consolidation Loan Rebate Fees, premium/discount amortization and Borrower Benefits yield adjustments;

includes the reclassification of certain derivative net settlement amounts. The net settlements on certain derivatives that do not qualify as SFAS No. 133 hedges and are recorded as part of the unrealized gain on derivative and hedging activities for GAAP purposes are reclassified to the line item on the income statement that such derivative is economically hedging for the   Core Earnings   basis presentation. For our   Core Earnings   basis student loan spread, this would primarily include: (a) reclassifying the net settlement amounts related to our written Floor Income Contracts to student loan interest income and (b) reclassifying the net settlement amounts related to certain of our basis swaps to debt interest expense;

excludes unhedged Floor Income earned on the Managed student loan portfolio; and

includes the amortization of upfront payments on Floor Income Contracts in student loan income that we believe are economically hedging the Floor Income.

As discussed above, these differences result in the   Core Earnings   basis student loan spread not being a GAAP-basis presentation. Management relies on this measure to manage our Lending business segment. Specifically, management uses the   Core Earnings   basis student loan spread to evaluate the overall economic effect that certain factors have on all student loans either on- or off-balance sheet. These factors include the overall mix of student loans in our portfolio, acquisition costs, Borrower Benefits program costs, Floor Income and funding and hedging costs. Management believes that it is important to evaluate all of these factors on a   Core Earnings   basis to gain additional information about the economic effect of these factors on all student loans under management. Management believes that this additional information assists us in making strategic decisions about the Company s business model for the Lending business segment, including among other factors, how we acquire or originate student loans, how we fund acquisitions and originations, what Borrower Benefits we offer and what type of loans we purchase or originate. While management believes that the   Core Earnings   basis student loan spread is an important tool for evaluating the Company s performance for the reasons described above, it is subject to certain general and specific limitations that investors should carefully consider. See   BUSINESS SEGMENTS

Limitations of Core Earnings. One specific limitation is that the Core Earnings basis student loan spread includes the spread on loans that we have sold to securitization trusts.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Core earnings basis student loan yield	8.04%	5.92%	7.82%	5.79%
Consolidation Loan Rebate Fees	(.54)	(.48)	(.54)	(.48)
Borrower Benefits	(.07)	(.04)	(.07)	(.07)
Premium and discount amortization	(.19)	(.16)	(.17)	(.17)
Core earnings basis student loan net yield	7.24	5.24	7.04	5.07
Core earnings basis student loan cost of funds	(5.38)	(3.50)	(5.18)	(3.30)
Core earnings basis student loan spread	1.86%	1.74%	1.86%	1.77%
Average Balances				
On-balance sheet student loans	$ 80,724	$ 70,580	$ 81,781	$ 69,129
Off-balance sheet student loans	47,716	43,791	44,909	42,846
Managed student loans	$ 128,440	$ 114,371	$ 126,690	$ 111,975

Discussion of Core Earnings Basis Student Loan Spread Effects of Significant Events in the Quarters Presented

The second quarter 2006 spread includes $18 million or 6 basis points of income associated with non-recurring SAP that we accrued on PLUS loans in connection with the Higher Education Reconciliation Act of 2005.

In the second quarters of 2006 and 2005, the increase in premium amortization is largely due to the write-off of unamortized premiums on loans consolidated with third parties. In addition, in the second quarter of 2006, we increased the CPR for our FFELP Stafford loan portfolio in response to the increased rate of loan prepayments occurring through consolidation. In the second quarter of 2005, we revised our estimates regarding the qualification for Borrower Benefits which resulted in a reduction of the liability for Borrower Benefits of $13 million or 5 basis points.

In the second quarter of 2005, we reduced student loan interest income by $16 million or 6 basis points to reflect a revision of our estimates pertaining to our non-accrual policy for interest income.

In both the second quarters of 2006 and 2005, there was an increase in Consolidation Loan activity as FFELP Stafford borrowers locked in lower interest rates by consolidating their loans prior to the July 1 interest rate reset for FFELP Stafford loans. In addition, reconsolidation of Consolidation Loans through the Direct Loan Program continued in the second quarter of 2006 from the backlog of processing applications after the March 31, 2006 prohibition (see LENDING BUSINESS SEGMENT Student Loan Activity for further discussion). The increase in consolidations resulted in an increase in student loan premium write-offs for both FFELP Stafford and Consolidation Loans consolidated with third parties in the second quarter. Loans lost through consolidation benefit the student loan spread to a lesser extent through the write-off of the Borrower Benefits liability associated with these loans. Furthermore, in both the second quarters of 2006 and 2005, we accrued a net write-off to our Borrower Benefits liability for loans whose consolidation applications had been received but not yet processed by June 30th, resulting in reductions to Borrower Benefits expense.

Discussion of Core Earnings Basis Student Loan Spread Other Quarter-over Quarter Fluctuations

The average balance of Managed Private Education Loans now represents 15 percent of the average Managed student loan portfolio, up from 12 percent in the second quarter of 2005. Private Education Loans are subject to credit risk and therefore earn higher Core Earnings basis student loan spreads, which averaged 5.07 percent and 4.57 percent for the three months ended June 30, 2006 and 2005, respectively, for the Managed Private Education Loan portfolio, excluding the effect of non-recurring items. The Core Earnings basis student loan spread for the Managed guaranteed student loan portfolio was 1.24 percent and 1.38 percent for the three months ended June 30, 2006 and 2005, respectively, excluding the effect of non-recurring items.

Floor Income Managed Basis

The following table analyzes the ability of the FFELP student loans in our Managed student loan portfolio to earn Floor Income after June 30, 2006 and 2005.

	June 30, 2006			**June 30, 2005**		
(Dollars in billions)	**Fixed Borrower Rate**	**Variable Borrower Rate**	**Total**	**Fixed Borrower Rate**	**Variable Borrower Rate**	**Total**
Student loans eligible to earn Floor Income:						
On-balance sheet student loans	$ 52.5	$ 19.7	$ 72.2	$ 43.3	$ 16.8	$ 60.1
Off-balance sheet student loans	14.7	19.8	34.5	10.9	22.5	33.4
Managed student loans eligible to earn Floor Income	67.2	39.5	106.7	54.2	39.3	93.5
Less: notional amount of Floor Income Contracts	(24.5)		(24.5)	(26.2)		(26.2)
Net Managed student loans eligible to earn Floor Income	$ 42.7	$ 39.5	$ 82.2	$ 28.0	$ 39.3	$ 67.3
Net Managed student loans earning Floor Income	$	$	$	$ 1.8	$	$ 1.8

The reconsolidation of Consolidation Loans has had an unanticipated impact on Consolidation Loans underlying Floor Income Contracts. The Floor Income Contracts are economically hedging the fixed borrower interest rate earned on Consolidation Loans. Generally, Consolidation Loans are eligible to earn Floor Income, and over time we have sold Floor Income Contracts to hedge the potential Floor Income from specifically identified pools of Consolidation Loans. The balance of the Floor Income Contracts did not anticipate the reconsolidation of Consolidation Loans and as a consequence, higher rate Consolidation Loans that underlie certain contracts have been reconsolidated. As a result, as of June 30, 2006, the notional amount of Floor Income Contracts roughly equals the outstanding balance of the Consolidation Loans that the Floor Income Contracts were hedging. Recently passed legislation discontinues reconsolidation June 30, 2006, and, on March 17, 2006, ED issued a Dear Colleague letter that prohibits the reconsolidation of Consolidation Loans through the Direct Lending program unless the borrower applied for a Direct Loan consolidation by March 31, 2006. Since we were close to parity between the floor eligible loans and Floor Income Contracts at March 31, 2006, the processing of the backlog of reconsolidation applications in the second quarter has resulted in the balance of Floor Income Contracts for certain strikes exceeding the balance of the loans for those strikes on an immaterial notional value of those contracts, leaving us in a slightly oversold position. As of June 30, 2006, we have substantially processed the backlog of reconsolidation applications so we do not anticipate a material increase in our oversold position going forward.

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The following table presents a projection of the average Managed balance of Consolidation Loans whose Fixed Rate Floor Income has already been economically hedged through Floor Income Contracts for the period July 1, 2006 to June 30, 2010. These loans are both on- and off-balance sheet and the related hedges do not qualify under SFAS No. 133 accounting as effective hedges.

(Dollars in billions)	July 1, 2006 to December 31, 2006	2007	2008	2009	2010
Average balance of Consolidation Loans whose Floor Income is economically hedged (Managed Basis)	$ 25	$ 16	$ 15	$ 10	$ 2

Private Education Loans

All Private Education Loans are initially acquired on-balance sheet. When we securitize Private Education Loans, we no longer own the loans and they are accounted for off-balance sheet. For our Managed presentation in the table below, we reduce the on-balance sheet allowance for amounts previously provided and then provide for these loans in the off-balance sheet section with the total of both on and off-balance sheet residing in the Managed presentation.

When Private Education Loans in the majority of our securitized trusts become 180 days delinquent, we typically exercise our contingent call option to repurchase these loans at par value out of the trust and record a loss for the difference in the par value paid and the fair market value of the loan at the time of purchase. If these loans reach the 212-day delinquency, a charge-off for the remaining balance of the loan is triggered. On a Managed Basis, the losses recorded under GAAP for loans repurchased at day 180 are reversed and the full amount is charged off at day 212.

The off-balance sheet allowance is increasing as more loans are securitized but is lower than the on-balance sheet percentage when measured as a percentage of ending loans in repayment because of the different mix of loans on-balance sheet and off-balance sheet, as described above. Additionally, a larger percentage of the off-balance sheet loan borrowers are still in-school status and not required to make payments on their loans. Once repayment begins, the allowance requirements increase to reflect the increased risk of loss as loans enter repayment.

Activity in the Allowance for Private Education Loan Losses

The provision for student loan losses represents the periodic expense of maintaining an allowance sufficient to absorb losses, net of recoveries, inherent in the portfolio of Private Education Loans.

The following table summarizes changes in the allowance for Private Education Loan losses for the three and six months ended June 30, 2006 and 2005.

Activity in Allowance for Private Education Loan Losses

	On-Balance Sheet		Off-Balance Sheet		Managed Basis	
	Three Months Ended		Three Months Ended		Three Months Ended	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
Allowance at beginning of period	$ 232	$ 191	$ 91	$ 150	$ 323	$ 341
Provision for Private Education Loan losses	62	36	(7)	(4)	55	32
Change in estimate		40		(60)		(20)
Total provision	62	76	(7)	(64)	55	12
Charge-offs	(36)	(38)	(4)	(1)	(40)	(39)
Recoveries	6	5			6	5
Net charge-offs	(30)	(33)	(4)	(1)	(34)	(34)
Balance before securitization of Private Education Loans	264	234	80	85	344	319
Reduction for securitization of Private Education Loans	(12)	(6)	12	6		
Allowance at end of period	$ 252	$ 228	$ 92	$ 91	$ 344	$ 319
Net charge-offs as a percentage of average loans in repayment (annualized)	3.13%	4.33%	.32%	.13%	1.52%	2.04%
Allowance as a percentage of the ending total loan balance	3.55%	3.61%	.75%	1.21%	1.78%	2.31%
Allowance as a percentage of ending loans in repayment	6.66%	7.41%	1.61%	2.32%	3.62%	4.56%
Average coverage of net charge-offs (annualized)	2.09	1.73	5.63	19.64	2.52	2.34
Average total loans	$ 7,961	$ 6,376	$ 10,770	$ 7,060	$ 18,731	$ 13,436
Ending total loans	$ 7,085	$ 6,325	$ 12,282	$ 7,493	$ 19,367	$ 13,818
Average loans in repayment	$ 3,838	$ 3,042	$ 5,163	$ 3,655	$ 9,001	$ 6,697
Ending loans in repayment	$ 3,777	$ 3,078	$ 5,731	$ 3,926	$ 9,508	$ 7,004

In general the provision for loans can fluctuate quarter to quarter due to the seasonality of loans entering repayment. The majority of loans typically enter repayment in the second and fourth quarters. This increase in loans entering repayment often leads to a near-term increase in early-stage delinquencies, or forbearance usage in the first and third quarters with some residual effect in the fourth quarter for the affected borrowers. This in turn, leads to higher provisions for those quarters. Therefore, all other factors being equal, the provision for loan losses in the second quarter will be lower.

In the second quarter of 2005, we enhanced our allowance methodology whereby we now use a status based reserving methodology and provide for losses inherent in the portfolio over a shorter period of time. The change in estimate adjustment in 2005 reflects the cumulative effect of that change.

Activity in Allowance for Private Education Loan Losses

	On-Balance Sheet		Off-Balance Sheet		Managed Basis	
	Six Months Ended		Six Months Ended		Six Months Ended	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
Allowance at beginning of period	$ 204	$ 172	$ 78	$ 143	$ 282	$ 315
Provision for Private Education Loan losses	116	79	6	4	122	83
Change in estimate		40		(60)		(20)
Total provision	116	119	6	(56)	122	63
Charge-offs	(69)	(66)	(4)	(2)	(73)	(68)
Recoveries	13	9			13	9
Net charge-offs	(56)	(57)	(4)	(2)	(60)	(59)
Balance before securitization of Private Education Loans	264	234	80	85	344	319
Reduction for securitization of Private Education Loans	(12)	(6)	12	6		
Allowance at end of period	$ 252	$ 228	$ 92	$ 91	$ 344	$ 319
Net charge-offs as a percentage of average loans in repayment (annualized)	3.05%	3.86%	.16%	.14%	1.37%	1.81%
Allowance as a percentage of the ending total loan balance	3.55%	3.61%	.75%	1.21%	1.78%	2.31%
Allowance as a percentage of ending loans in repayment	6.66%	7.41%	1.61%	2.32%	3.62%	4.56%
Average coverage of net charge-offs (annualized)	2.22	2.00	11.01	18.32	2.82	2.68
Average total loans	$ 8,485	$ 6,321	$ 9,716	$ 6,607	$ 18,201	$ 12,928
Ending total loans	$ 7,085	$ 6,325	$ 12,282	$ 7,493	$ 19,367	$ 13,818
Average loans in repayment	$ 3,720	$ 2,960	$ 5,191	$ 3,639	$ 8,911	$ 6,599
Ending loans in repayment	$ 3,777	$ 3,078	$ 5,731	$ 3,926	$ 9,508	$ 7,004

Delinquencies

The table below presents our Private Education Loan delinquency trends as of June 30, 2006 and 2005. Delinquencies have the potential to adversely impact earnings through increased servicing and collection costs in the event the delinquent accounts charge off.

	On-Balance Sheet Private Education Loan Delinquencies			
	June 30, 2006		June 30, 2005	
	Balance	%	Balance	%
Loans in-school/grace/deferment[1]	$ 3,305		$ 3,307	
Loans in forbearance[2]	299		190	
Loans in repayment and percentage of each status:				
Loans current	3,353	88.8%	2,756	89.5%
Loans delinquent 31-60 days[3]	176	4.7	133	4.4
Loans delinquent 61-90 days[3]	100	2.6	69	2.2
Loans delinquent greater than 90 days[3]	148	3.9	120	3.9
Total Private Education Loans in repayment	3,777	100%	3,078	100%
Total Private Education Loans, gross	7,381		6,575	
Private Education Loan unamortized discount	(296)		(250)	
Total Private Education Loans	7,085		6,325	
Private Education Loan allowance for losses	(252)		(228)	
Private Education Loans, net	$ 6,833		$ 6,097	
Percentage of Private Education Loans in repayment	51.2%		46.8%	
Delinquencies as a percentage of Private Education Loans in repayment	11.2%		10.5%	

(1) Loans for borrowers who still may be attending school or engaging in other permitted educational activities and are not yet required to make payments on the loans, e.g., residency periods for medical students or a grace period for bar exam preparation.

(2) Loans for borrowers who have requested extension of grace period or who have temporarily ceased making full payments due to hardship or other factors, consistent with the established loan program servicing policies and procedures.

(3) The period of delinquency is based on the number of days scheduled payments are contractually past due.

	Off-Balance Sheet Private Education Loan Delinquencies			
	June 30, 2006		June 30, 2005	
	Balance	%	Balance	%
Loans in-school/grace/deferment[1]	$ 6,074		$ 3,308	
Loans in forbearance[2]	751		400	
Loans in repayment and percentage of each status:				
Loans current	5,483	95.7%	3,749	95.5%
Loans delinquent 31-60 days[3]	151	2.6	96	2.4
Loans delinquent 61-90 days[3]	50	.9	35	1.0
Loans delinquent greater than 90 days[3]	47	.8	46	1.1
Total Private Education Loans in repayment	5,731	100%	3,926	100%
Total Private Education Loans, gross	12,556		7,634	
Private Education Loan unamortized discount	(274)		(141)	
Total Private Education Loans	12,282		7,493	
Private Education Loan allowance for losses	(92)		(91)	
Private Education Loans, net	$ 12,190		$ 7,402	
Percentage of Private Education Loans in repayment	45.6%		51.4%	
Delinquencies as a percentage of Private Education Loans in repayment	4.3%		4.5%	

(1) Loans for borrowers who still may be attending school or engaging in other permitted educational activities and are not yet required to make payments on the loans, e.g., residency periods for medical students or a grace period for bar exam preparation.

(2) Loans for borrowers who have requested extension of grace period or who have temporarily ceased making full payments due to hardship or other factors, consistent with the established loan program servicing policies and procedures.

(3) The period of delinquency is based on the number of days scheduled payments are contractually past due.

	Managed Private Education Loan Delinquencies			
	June 30, 2006		June 30, 2005	
	Balance	%	Balance	%
Loans in-school/grace/deferment[1]	$ 9,379		$ 6,615	
Loans in forbearance[2]	1,050		590	
Loans in repayment and percentage of each status:				
Loans current	8,836	92.9%	6,505	92.9%
Loans delinquent 31-60 days[3]	327	3.4	229	3.2
Loans delinquent 61-90 days[3]	150	1.6	104	1.5
Loans delinquent greater than 90 days[3]	195	2.1	166	2.4
Total Private Education Loans in repayment	9,508	100%	7,004	100%
Total Private Education Loans, gross	19,937		14,209	
Private Education Loan unamortized discount	(570)		(391)	
Total Private Education Loans	19,367		13,818	
Private Education Loan allowance for losses	(344)		(319)	
Private Education Loans, net	$ 19,023		$ 13,499	
Percentage of Private Education Loans in repayment	47.7%		49.3%	
Delinquencies as a percentage of Private Education Loans in repayment	7.1%		7.1%	

(1) Loans for borrowers who still may be attending school or engaging in other permitted educational activities and are not yet required to make payments on the loans, e.g., residency periods for medical students or a grace period for bar exam preparation.

(2) Loans for borrowers who have requested extension of grace period or who have temporarily ceased making full payments due to hardship or other factors, consistent with the established loan program servicing policies and procedures.

(3) The period of delinquency is based on the number of days scheduled payments are contractually past due.

Forbearance Managed Basis Private Education Loans

Private Education Loans are made to parent and student borrowers by our lender partners in accordance with our underwriting policies. These loans generally supplement federally guaranteed student loans, which are subject to federal lending caps. Private Education Loans are not guaranteed or insured against any loss of principal or interest. Traditional student borrowers use the proceeds of these loans to obtain higher education, which increases the likelihood of obtaining employment at higher income levels than would be available without the additional education. As a result, the borrowers repayment capability improves between the time the loan is made and the time they enter the post-education work force. We generally allow the loan repayment period on traditional Private Education Loans, except those generated by our SLM Financial subsidiary, to begin six to nine months after the student leaves school. This provides the borrower time to obtain a job to service his or her debt. For borrowers that need more time or experience other hardships, we permit additional delays in payment or partial payments (both referred to as forbearances) when we believe additional time will improve the borrower s ability to repay the loan. Forbearance is also granted to borrowers who may experience temporary hardship after entering repayment, when we believe that it will increase the likelihood of ultimate collection of the loan. Such forbearance is only granted within established guidelines and is closely monitored for compliance. Our policy does not grant any reduction in the repayment obligation (principal or interest) but does allow the borrower to stop or reduce monthly payments for an agreed period of time. When a loan that was delinquent prior to receiving forbearance ends forbearance and re-enters repayment, that loan is returned to current status.

Forbearance is used most heavily immediately after the loan enters repayment. As indicated in the tables below showing the composition and status of the Managed Private Education Loan portfolio by number of months aged from the first date of repayment, the percentage of loans in forbearance decreases the longer the loans have been in repayment. At June 30, 2006, loans in forbearance as a percentage of loans in repayment and forbearance was 12.3 percent for loans that have been in repayment one to twenty-four months. The percentage declined to 4.4 percent for loans that have been in repayment more than 48 months. Approximately 74 percent of our Managed Private Education Loans in forbearance have been in repayment less than 24 months. These borrowers are essentially extending their grace period as they transition to the workforce. Forbearance continues to be a positive collection tool for the Private Education Loans as we believe it can provide the borrower with sufficient time to obtain employment and income to support his or her obligation. We consider the potential impact of forbearance in the determination of the loan loss reserves.

The tables below show the composition and status of the Managed Private Education Loan portfolio by number of months aged from the first date of repayment.

	Months Since Entering Repayment				
	1 to 24 Months	**25 to 48 Months**	**More than 48 Months**	**After June 30, 2006[(1)]**	**Total**
June 30, 2006					
Loans in-school/grace/deferment	$	$	$	$ 9,379	$ 9,379
Loans in forbearance	776	194	80		1,050
Loans in repayment current	5,184	2,024	1,628		8,836
Loans in repayment delinquent 31-60 days	180	87	60		327
Loans in repayment delinquent 61-90 days	90	37	23		150
Loans in repayment delinquent greater than 90 days	101	60	34		195
Total	$ 6,331	$ 2,402	$ 1,825	$ 9,379	19,937
Unamortized discount					(570)
Allowance for loan losses					(344)
Total Managed Private Education Loans, net					$ 19,023
Loans in forbearance as a percentage of loans in repayment and forbearance	12.3%	8.1%	4.4%	%	9.9%

(1) Includes all loans in-school/grace/deferment.

	Months Since Entering Repayment				
	1 to 24 Months	25 to 48 Months	More than 48 Months	After June 30, 2005[1]	Total
June 30, 2005					
Loans in-school/grace/deferment	$	$	$	$ 6,615	$ 6,615
Loans in forbearance	437	106	47		590
Loans in repayment current	3,728	1,515	1,262		6,505
Loans in repayment delinquent 31-60 days	120	65	44		229
Loans in repayment delinquent 61-90 days	57	30	17		104
Loans in repayment delinquent greater than 90 days	80	55	31		166
Total	$ 4,422	$ 1,771	$ 1,401	$ 6,615	14,209
Unamortized discount					(391)
Allowance for loan losses					(319)
Total Managed Private Education Loans, net					$ 13,499
Loans in forbearance as a percentage of loans in repayment and forbearance	9.9%	6.0%	3.4%	%	7.8%

(1) Includes all loans in-school/grace/deferment.

The table below stratifies the portfolio of Managed Private Education Loans in forbearance by the cumulative number of months the borrower has used forbearance as of the dates indicated. As detailed in the table below, 8 percent of loans currently in forbearance have deferred their loan repayment more than 24 months, which is 2 percent lower than the year-ago period.

	June 30, 2006		June 30, 2005	
	Forbearance Balance	% of Total	Forbearance Balance	% of Total
Cumulative number of months borrower has used forbearance				
Up to 12 months	$ 753	72%	$ 426	72%
13 to 24 months	214	20	117	20
25 to 36 months	57	5	32	5
More than 36 months	26	3	15	3
Total	$ 1,050	100%	$ 590	100%

Total Loan Net Charge-offs

The following tables summarize the net charge-offs for all loan types on both an on-balance sheet basis and a Managed Basis for the three and six months ended June 30, 2006 and 2005. Almost all Private Education Loan charge-offs occur on-balance sheet due to the contingent call feature in a majority of the off-balance sheet securitization trusts, which is discussed in more detail at LENDING BUSINESS SEGMENT Private Education Loans.

Total on-balance sheet loan net charge-offs

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Private Education Loans	$ 30	$ 33	$ 56	$ 57
FFELP Stafford and Other Student Loans	1	1	2	2
Mortgage and consumer loans	1	1	2	2
Total on-balance sheet loan net charge-offs	$ 32	$ 35	$ 60	$ 61

Total Managed loan net charge-offs

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Private Education Loans	$ 34	$ 34	$ 60	$ 59
FFELP Stafford and Other Student Loans	1	1	2	2
Mortgage and consumer loans	1	1	2	2
Total Managed loan net charge-offs	$ 36	$ 36	$ 64	$ 63

Student Loan Premiums as a Percentage of Principal

The following table presents student loan premiums paid as a percentage of the principal balance of student loans acquired for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended				Six Months Ended			
	June 30, 2006		June 30, 2005		June 30, 2006		June 30, 2005	
	Volume	Rate	Volume	Rate	Volume	Rate	Volume	Rate
Student loan premiums paid:								
Sallie Mae brands	$ 1,671	.77%	$ 991	.26%	$ 4,975	.59%	$ 3,294	.28%

Lender partners	4,225	1.64	4,701	1.61	7,817	1.80	8,043	1.70
Total Preferred Channel	5,896	1.39	5,692	1.38	12,792	1.33	11,337	1.29
Other purchases[1]	493	4.23	641	3.66	668	3.64	1,146	3.47
Subtotal base purchases	6,389	1.61	6,333	1.61	13,460	1.45	12,483	1.49
Consolidations	853	3.37	926	2.79	1,750	2.66	1,839	2.38
Total	$ 7,242	1.82%	$ 7,259	1.76%	$ 15,210	1.58%	$ 14,322	1.60%

(1) Primarily includes spot purchases, other commitment clients, and subsidiary acquisitions.

The increase in premiums paid as a percentage of principal balance for Sallie Mae brands is primarily due to the increase in loans where we pay the origination fee on behalf of borrowers, a practice we call zero-fee lending. The borrower origination fee will be gradually phased out by the Reconciliation Legislation from 2007 to 2010. We include in Consolidation Loan premiums the 50 basis point

Consolidation Loan fee paid on loans that we consolidate, including loans that are already in our portfolio. The Consolidation Loan premium paid percentage is calculated on only consolidation volume that is incremental to our portfolio. Our premiums paid percentage will increase in periods when there is a higher percentage of our own FFELP Stafford loans that consolidated versus incremental volume.

Student Loan Acquisitions

In the six months ended June 30, 2006, 84 percent of our Managed student loan acquisitions were originated through our Preferred Channel. The following tables summarize the components of our student loan acquisition activity for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended June 30, 2006		
	FFELP	**Private**	**Total**
Preferred Channel	$ 4,380	$ 1,516	$ 5,896
Other commitment clients	88	1	89
Spot purchases	404		404
Consolidations from third parties	845	8	853
Acquisitions from off-balance sheet securitized trusts, primarily consolidations	2,107	16	2,123
Capitalized interest, premiums and discounts	376	29	405
Total on-balance sheet student loan acquisitions	8,200	1,570	9,770
Consolidations to SLM Corporation from off-balance sheet securitized trusts	(2,107)	(16)	(2,123)
Capitalized interest, premiums and discounts off-balance sheet securitized trusts	179	108	287
Total Managed student loan acquisitions	$ 6,272	$ 1,662	$ 7,934

	Three Months Ended June 30, 2005		
	FFELP	**Private**	**Total**
Preferred Channel	$ 4,463	$ 1,229	$ 5,692
Other commitment clients	161		161
Spot purchases	480		480
Consolidations from third parties	926		926
Acquisitions from off-balance sheet securitized trusts, primarily consolidations	2,421		2,421
Capitalized interest, premiums and discounts	331	(10)	321
Total on-balance sheet student loan acquisitions	8,782	1,219	10,001
Consolidations to SLM Corporation from off-balance sheet securitized trusts	(2,421)		(2,421)
Capitalized interest, premiums and discounts off-balance sheet securitized trusts	146	60	206

Total Managed student loan acquisitions	$ 6,507	$ 1,279	$ 7,786

	Six Months Ended June 30, 2006		
	FFELP	Private	Total
Preferred Channel	$ 9,411	$ 3,381	$ 12,792
Other commitment clients	202	3	205
Spot purchases	463		463
Consolidations from third parties	1,741	9	1,750
Acquisitions from off-balance sheet securitized trusts, primarily consolidations	3,436	16	3,452
Capitalized interest, premiums and discounts	722	52	774
Total on-balance sheet student loan acquisitions	15,975	3,461	19,436
Consolidations to SLM Corporation from off-balance sheet securitized trusts	(3,436)	(16)	(3,452)
Capitalized interest, premiums and discounts off-balance sheet securitized trusts	324	177	501
Total Managed student loan acquisitions	$ 12,863	$ 3,622	$ 16,485

	Six Months Ended June 30, 2005		
	FFELP	Private	Total
Preferred Channel	$ 8,774	$ 2,563	$ 11,337
Other commitment clients	247		247
Spot purchases	899		899
Consolidations from third parties	1,839		1,839
Acquisitions from off-balance sheet securitized trusts, primarily consolidations	4,248		4,248
Capitalized interest, premiums and discounts	671	(16)	655
Total on-balance sheet student loan acquisitions	16,678	2,547	19,225
Consolidations to SLM Corporation from off-balance sheet securitized trusts	(4,248)		(4,248)
Capitalized interest, premiums and discounts off-balance sheet securitized trusts	255	103	358
Total Managed student loan acquisitions	$ 12,685	$ 2,650	$ 15,335

As shown on the above table, off-balance sheet FFELP Stafford loans that consolidate with us become an on-balance sheet interest earning asset. This activity results in impairments of our Retained Interests in securitizations, but this is offset by an increase in on-balance sheet interest earning assets, for which we do not record an offsetting gain.

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The following table includes on-balance sheet asset information for our Lending business segment.

	June 30, 2006	December 31, 2005
FFELP Stafford and Other Student Loans, net	$ 21,391	$ 19,988
Consolidation Loans, net	54,055	54,859
Private Education Loans, net	6,833	7,757
Other loans, net	1,051	1,138
Investments(1)	9,540	7,748
Retained Interest in off-balance sheet securitized loans	3,152	2,406
Other(2)	4,188	3,576
Total assets	$ 100,210	$ 97,472

(1) Investments include cash and cash equivalents, investments, restricted cash and investments, leveraged leases, and municipal bonds.

(2) Other assets include accrued interest receivable, goodwill and acquired intangible assets and other non-interest earning assets.

Preferred Channel Originations

We originated $3.2 billion in student loan volume through our Preferred Channel in the three months ended June 30, 2006, respectively, versus $2.8 billion in the three months ended June 30, 2005, respectively.

In the second quarter of 2006, we grew our Preferred Channel Originations by 14 percent versus the year-ago quarter. For the three months ended June 30, 2006, our internally marketed brands constituted 55 percent of our Preferred Channel Originations, up from 39 percent in the year-ago period. The pipeline of loans that we currently service and are committed to purchase was $4.4 billion and $5.0 billion at June 30, 2006 and 2005, respectively. The following tables further break down our Preferred Channel Originations by type of loan and source.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Preferred Channel Originations Type of Loan				
Stafford	$ 1,877	$ 1,739	$ 6,303	$ 5,912
PLUS	229	223	1,231	1,184
Total FFELP	2,106	1,962	7,534	7,096
Private Education Loans	1,070	812	3,255	2,440
Total	$ 3,176	$ 2,774	$ 10,789	$ 9,536
Preferred Channel Originations Source				
Internally marketed brands	$ 1,757	$ 1,083	$ 5,312	$ 3,439
Lender partners	1,419	1,691	5,477	6,097

Total	$ 3,176	$ 2,774	$ 10,789	$ 9,536

Student Loan Activity

The following tables summarize the activity in our on-balance sheet, off-balance sheet and Managed portfolios of FFELP student loans and Private Education Loans and highlight the effects of Consolidation Loan activity on our FFELP portfolios.

On-Balance Sheet
Three Months Ended June 30, 2006

	FFELP Stafford and Other(1)	Consolidation Loans	Total FFELP	Total Private Education Loans	Total On-Balance Sheet Portfolio
Beginning balance	$ 18,883	$ 53,451	$ 72,334	$ 9,311	$ 81,645
Acquisitions	4,821	426	5,247	1,547	6,794
Incremental consolidations from third parties		845	845	8	853
Consolidations to third parties	(386)	(835)	(1,221)	(4)	(1,225)
Net acquisitions	4,435	436	4,871	1,551	6,422
Internal consolidations	(1,588)	3,474	1,886	20	1,906
New securitizations		(2,532)	(2,532)	(3,729)	(6,261)
Repayments/claims/resales/other	(339)	(774)	(1,113)	(320)	(1,433)
Ending balance	$ 21,391	$ 54,055	$ 75,446	$ 6,833	$ 82,279

Off-Balance Sheet
Three Months Ended June 30, 2006

	FFELP Stafford and Other(1)	Consolidation Loans	Total FFELP	Total Private Education Loans	Total Off-Balance Sheet Portfolio
Beginning balance	$ 23,457	$ 13,211	$ 36,668	$ 8,557	$ 45,225
Acquisitions	120	60	180	107	287
Incremental consolidations from third parties					
Consolidations to third parties	(436)	(278)	(714)	(5)	(719)
Net acquisitions	(316)	(218)	(534)	102	(432)
Internal consolidations	(1,711)	(175)	(1,886)	(20)	(1,906)
New securitizations		2,532	2,532	3,729	6,261
Repayments/claims/resales/other	(895)	(210)	(1,105)	(178)	(1,283)

Ending balance	$ 20,535	$ 15,140	$ 35,675	$ 12,190	$ 47,865

Managed Portfolio
Three Months Ended June 30, 2006

	FFELP Stafford and Other[1]	Consolidation Loans	Total FFELP	Total Private Education Loans	Total Managed Basis Portfolio
Beginning balance	$ 42,340	$ 66,662	$ 109,002	$ 17,868	$ 126,870
Acquisitions	4,941	486	5,427	1,654	7,081
Incremental consolidations from third parties		845	845	8	853
Consolidations to third parties	(822)	(1,113)	(1,935)	(9)	(1,944)
Net acquisitions	4,119	218	4,337	1,653	5,990
Internal consolidations	(3,299)	3,299			
New securitizations					
Repayments/claims/resales/other	(1,234)	(984)	(2,218)	(498)	(2,716)
Ending balance	$ 41,926	$ 69,195	$ 111,121	$ 19,023	$ 130,144

[1] FFELP category is primarily Stafford loans and also includes PLUS and HEAL loans.

On-Balance Sheet
Three Months Ended June 30, 2005

	FFELP Stafford and Other(1)	Consolidation Loans	Total FFELP	Total Private Education Loans	Total On-Balance Sheet Portfolio
Beginning balance	$ 18,933	$ 44,446	$ 63,379	$ 6,527	$ 69,906
Acquisitions	5,188	251	5,439	1,215	6,654
Incremental consolidations from third parties		926	926		926
Consolidations to third parties	(182)	(165)	(347)	(2)	(349)
Net acquisitions	5,006	1,012	6,018	1,213	7,231
Internal consolidations	(1,335)	3,653	2,318		2,318
New securitizations		(4,045)	(4,045)	(1,407)	(5,452)
Repayments/claims/resales/other	(511)	(425)	(936)	(236)	(1,172)
Ending balance	$ 22,093	$ 44,641	$ 66,734	$ 6,097	$ 72,831

Off-Balance Sheet
Three Months Ended June 30, 2005

	FFELP Stafford and Other(1)	Consolidation Loans	Total FFELP	Total Private Education Loans	Total Off-Balance Sheet Portfolio
Beginning balance	$ 28,392	$ 7,410	$ 35,802	$ 5,991	$ 41,793
Acquisitions	97	49	146	60	206
Incremental consolidations from third parties					
Consolidations to third parties	(326)	(64)	(390)	(4)	(394)
Net acquisitions	(229)	(15)	(244)	56	(188)
Internal consolidations	(2,318)		(2,318)		(2,318)
New securitizations		4,045	4,045	1,407	5,452
Repayments/claims/resales/other	(812)	(206)	(1,018)	(52)	(1,070)
Ending balance	$ 25,033	$ 11,234	$ 36,267	$ 7,402	$ 43,669

Managed Portfolio
Three Months Ended June 30, 2005

	FFELP Stafford and Other[1]	Consolidation Loans	Total FFELP	Total Private Education Loans	Total Managed Basis Portfolio
Beginning balance	$ 47,325	$ 51,856	$ 99,181	$ 12,518	$ 111,699
Acquisitions	5,285	300	5,585	1,275	6,860
Incremental consolidations from third parties		926	926		926
Consolidations to third parties	(508)	(229)	(737)	(6)	(743)
Net acquisitions	4,777	997	5,774	1,269	7,043
Internal consolidations	(3,653)	3,653			
New securitizations					
Repayments/claims/resales/other	(1,323)	(631)	(1,954)	(288)	(2,242)
Ending balance	$ 47,126	$ 55,875	$ 103,001	$ 13,499	$ 116,500

[1] FFELP category is primarily Stafford loans and also includes PLUS and HEAL loans.

	On-Balance Sheet Six Months Ended June 30, 2006				
	FFELP Stafford and Other[(1)]	Consolidation Loans	Total FFELP	Total Private Education Loans	Total On-Balance Sheet Portfolio
Beginning balance	$ 19,988	$ 54,859	$ 74,847	$ 7,757	$ 82,604
Acquisitions	10,095	701	10,796	3,439	14,235
Incremental consolidations from third parties		1,741	1,741	9	1,750
Consolidations to third parties	(693)	(1,407)	(2,100)	(8)	(2,108)
Net acquisitions	9,402	1,035	10,437	3,440	13,877
Internal consolidations	(2,372)	5,097	2,725	20	2,745
New securitizations	(5,034)	(5,571)	(10,605)	(3,729)	(14,334)
Repayments/claims/resales/other	(593)	(1,365)	(1,958)	(655)	(2,613)
Ending balance	$ 21,391	$ 54,055	$ 75,446	$ 6,833	$ 82,279

	Off-Balance Sheet Six Months Ended June 30, 2006				
	FFELP Stafford and Other[(1)]	Consolidation Loans	Total FFELP	Total Private Education Loans	Total Off-Balance Sheet Portfolio
Beginning balance	$ 20,670	$ 10,575	$ 31,245	$ 8,680	$ 39,925
Acquisitions	208	118	326	174	500
Incremental consolidations from third parties					
Consolidations to third parties	(864)	(456)	(1,320)	(10)	(1,330)
Net acquisitions	(656)	(338)	(994)	164	(830)
Internal consolidations	(2,452)	(273)	(2,725)	(20)	(2,745)
New securitizations	5,034	5,571	10,605	3,729	14,334
Repayments/claims/resales/other	(2,061)	(395)	(2,456)	(363)	(2,819)
Ending balance	$ 20,535	$ 15,140	$ 35,675	$ 12,190	$ 47,865

	Managed Portfolio Six Months Ended June 30, 2006				
	FFELP Stafford and Other[1]	Consolidation Loans	Total FFELP	Total Private Education Loans	Total Managed Basis Portfolio
Beginning balance	$ 40,658	$ 65,434	$ 106,092	$ 16,437	$ 122,529
Acquisitions	10,303	819	11,122	3,613	14,735
Incremental consolidations from third parties		1,741	1,741	9	1,750
Consolidations to third parties	(1,557)	(1,863)	(3,420)	(18)	(3,438)
Net acquisitions	8,746	697	9,443	3,604	13,047
Internal consolidations	(4,824)	4,824			
New securitizations					
Repayments/claims/resales/other	(2,654)	(1,760)	(4,414)	(1,018)	(5,432)
Ending balance	$ 41,926	$ 69,195	$ 111,121	$ 19,023	$ 130,144

(1) FFELP category is primarily Stafford loans and also includes PLUS and HEAL loans.

	On-Balance Sheet Six Months Ended June 30, 2005				
	FFELP Stafford and Other[(1)]	Consolidation Loans	Total FFELP	Total Private Education Loans	Total On-Balance Sheet Portfolio
Beginning balance	$ 18,965	$ 41,596	$ 60,561	$ 5,420	$ 65,981
Acquisitions	10,027	567	10,594	2,544	13,138
Incremental consolidations from third parties		1,839	1,839		1,839
Consolidations to third parties	(332)	(249)	(581)	(4)	(585)
Net acquisitions	9,695	2,157	11,852	2,540	14,392
Internal consolidations	(2,052)	5,849	3,797	(1)	3,796
New securitizations	(3,542)	(4,044)	(7,586)	(1,407)	(8,993)
Repayments/claims/resales/other	(973)	(917)	(1,890)	(455)	(2,345)
Ending balance	$ 22,093	$ 44,641	$ 66,734	$ 6,097	$ 72,831

	Off-Balance Sheet Six Months Ended June 30, 2005				
	FFELP Stafford and Other[(1)]	Consolidation Loans	Total FFELP	Total Private Education Loans	Total Off-Balance Sheet Portfolio
Beginning balance	$ 27,825	$ 7,570	$ 35,395	$ 6,062	$ 41,457
Acquisitions	162	90	252	106	358
Incremental consolidations from third parties					
Consolidations to third parties	(642)	(91)	(733)	(8)	(741)
Net acquisitions	(480)	(1)	(481)	98	(383)
Internal consolidations	(3,789)	(8)	(3,797)		(3,797)
New securitizations	3,542	4,044	7,586	1,407	8,993
Repayments/claims/resales/other	(2,065)	(371)	(2,436)	(165)	(2,601)
Ending balance	$ 25,033	$ 11,234	$ 36,267	$ 7,402	$ 43,669

	Managed Portfolio Six Months Ended June 30, 2005				
	FFELP Stafford and Other[1]	Consolidation Loans	Total FFELP	Total Private Education Loans	Total Managed Basis Portfolio
Beginning balance	$ 46,790	$ 49,166	$ 95,956	$ 11,482	$ 107,438
Acquisitions	10,189	657	10,846	2,650	13,496
Incremental consolidations from third parties		1,839	1,839		1,839
Consolidations to third parties	(974)	(340)	(1,314)	(12)	(1,326)
Net acquisitions	9,215	2,156	11,371	2,638	14,009
Internal consolidations	(5,841)	5,841		(1)	(1)
New securitizations					
Repayments/claims/resales/other	(3,038)	(1,288)	(4,326)	(620)	(4,946)
Ending balance	$ 47,126	$ 55,875	$ 103,001	$ 13,499	$ 116,500

(1) FFELP category is primarily Stafford loans and also includes PLUS and HEAL loans.

The increase in consolidations to third parties from 2005 to 2006 is primarily due to some FFELP lenders reconsolidating Consolidation Loans using the Direct Lending program as a pass-through entity to circumvent the statutory prohibition on the reconsolidation of Consolidation Loans. On March 17, 2006, ED issued a Dear Colleague letter that prohibited this two-step process unless the FFELP consolidation borrower applied for a Direct Loan consolidation by March 31, 2006. Accordingly, in the second quarter of 2006, there was a temporary increase in the reconsolidation of Consolidation Loans to process the back log of FDLP applications. By the end of the quarter, consolidation activity had returned to recent historical levels. The Higher Education Reconciliation Act of 2005 restricted further reconsolidation; as of July 1, 2006, borrowers with a FFELP Consolidation Loan may only reconsolidate with the FDLP if they are delinquent, referred to the guaranty agency for default aversion activity, and enter into the income contingent repayment program (ICR) in the FDLP.

Other Income Lending Business Segment

The following table summarizes the components of other income, net, for our Lending business segment for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
Late fees	$ 26	$ 24	$ 51	$ 44
Gains on sales of mortgages and other loan fees	4	4	7	8
Other	21	8	34	20
Total other income, net	$ 51	$ 36	$ 92	$ 72

The increase in other income is primarily due to settlements received on the final dispositions of leveraged leases that we had previously fully reserved.

Operating Expense Lending Business Segment

The following table summarizes the components of operating expenses for our Lending business segment for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
Sales and originations	$ 79	$ 77	$ 163	$ 144
Servicing and information technology	52	47	102	96
Corporate overhead	32	17	59	35
Total operating expenses	$ 163	$ 141	$ 324	$ 275

Operating expenses for our Lending business segment include costs incurred to service our Managed student loan portfolio and acquire student loans, as well as other general and administrative expenses. The increase in second quarter operating expenses is primarily due to the increase in sales expenses in connection with the shift of more volume to our internal brands. For the three and six months ended June 30, 2006, operating expenses for the Lending business segment also include $10 million and $18 million, respectively, of stock-based compensation expense, due to the implementation of SFAS No. 123(R) (see Note 1, Significant Accounting Policies Accounting for Stock-Based Compensation, and Note 8, Stock-Based Compensation Plans to the consolidated financial statements).

DEBT MANAGEMENT OPERATIONS (DMO) BUSINESS SEGMENT

The following table includes the Core Earnings results of operations for our DMO business segment.

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	% Increase (Decrease) 2006 vs. 2005	Six Months Ended June 30, 2006	Six Months Ended June 30, 2005	% Increase (Decrease) 2006 vs. 2005
Total interest income	$	$	%	$	$	%
Total interest expense	5	4	25	11	8	38
Net interest income	(5)	(4)	(25)	(11)	(8)	(38)
Less provisions for losses						
Net interest income after provisions for losses	(5)	(4)	(25)	(11)	(8)	(38)
Fee income	90	82	10	182	168	8
Collections revenue	67	42	60	124	77	61
Total other income	157	124	27	306	245	25
Operating expenses[(1)(2)]	85	67	27	175	132	33
Income before income taxes and minority interest in net earnings of subsidiaries	67	53	26	120	105	14
Income taxes	26	20	30	44	39	13
Income before minority interest in net earnings of subsidiaries	41	33	24	76	66	15
Minority interest in net earnings of subsidiaries	1	1		3	2	50
Core Earnings net income	$ 40	$ 32	25%	$ 73	$ 64	14%

(1) The three and six months ended June 30, 2006 operating expenses for the DMO segment include $2 million and $5 million, respectively, of stock-based compensation expense due to the implementation of SFAS No. 123(R) in the first quarter of 2006.

(2) In the first quarter of 2006, the Company changed its method for allocating certain overhead and other expenses between our business segments. Balances for the three and six months ending June 30, 2005 have been updated to reflect the new allocation methodology.

DMO Revenue by Product

	Three Months Ended June 30,	Six Months Ended June 30,

	2006	2005	2006	2005
Purchased paper collections revenue	$ 67	$ 42	$ 124	$ 78
Contingency:				
Student loans	69	63	139	129
Other	9	9	19	18
Total contingency	78	72	158	147
Other	12	10	24	20
Total	$ 157	$ 124	$ 306	$ 245
USA Funds[1]	$ 46	$ 43	$ 92	$ 89
% of total DMO revenue	29%	35%	30%	36%

(1) United Student Aid Funds, Inc. (USA Funds)

The $33 million, or 27 percent, increase in DMO revenue for the second quarter of 2006 compared to the second quarter of 2005 can be attributed to the year-over-year growth in the purchased paper business of Arrow Financial Services (AFS) and to revenue generated by GRP Financial Services (GRP) (acquired in August 2005). The year-over-year growth in contingency fee revenue was primarily driven by the growth in guaranty agency collections.

Purchased Paper Non-Mortgage

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Face value of purchases	$ 461	$ 444	$ 992	$ 1,416
Purchase price	41	41	75	65
% of face value purchased	8.9%	9.2%	7.6%	4.6%
Gross Cash Collections (GCC)	$ 93	$ 61	$ 182	$ 118
Collections revenue	54	42	103	77
% of GCC	58%	69%	56%	66%
Carrying value of purchases	$ 152	$ 79	$ 152	$ 79

The amount of face value of purchases in any quarter is a function of a combination of factors including the amount of receivables available for purchase in the marketplace, average age of each portfolio, the asset class of the receivables, and competition in the marketplace. As a result, the percentage of face value purchased will vary from quarter to quarter. The decrease in collections revenue as a percentage of GCC versus the prior year can primarily be attributed to the increase in new portfolio purchases in the second half of 2005. Typically, revenue recognition based on a portfolio s effective interest rate is a lower percentage of cash collections in the early stages of servicing a portfolio.

Purchased Paper Mortgage/ Properties

	Three Months Ended June 30, 2006	Six Months Ended June 30, 2006
Face value of purchases	$ 191	$ 323
Collections revenue	13	21
Collateral value of purchases	212	362
Purchase price	160	273
% of collateral value	76%	76%
Carrying value of purchases	$ 453	$ 453

GRP was purchased in August 2005. Prior to this acquisition, the Company was not in the mortgage purchased paper business. The purchase price for sub-performing and non-performing mortgage loans is generally determined as a percentage of the underlying collateral. Fluctuations in the purchase price as a percentage of collateral value can be caused by a number of factors including the percentage of second mortgages in the portfolio and the level of private mortgage insurance associated with particular assets.

Contingency Inventory

The following table presents the outstanding inventory of receivables that are currently being serviced through our DMO business.

	June 30,	December 31,

		2006	2005
Contingency:			
Contingency	Student loans	$ 7,174	$ 7,205
Contingency	Other	2,594	2,178
Total		$ 9,768	$ 9,383

Operating Expenses DMO Business Segment

For the three months ended June 30, 2006 and 2005, operating expenses for our DMO business segment totaled $85 million and $67 million, respectively. The increase in operating expenses of $18 million or 27 percent versus the year-ago quarter was primarily due to increased expenses for outsourced collections and recovery costs associated with large 2005 fourth quarter portfolio purchases. The increases in DMO contingency fee expenses are consistent with the growth in revenue and accounts serviced, as a high percentage of DMO expenses are variable.

For the three and six months ended June 30, 2006, operating expenses for the DMO business segment also include $3 million and $5 million, respectively, of stock-based compensation expense, due to the implementation of SFAS No. 123(R) (see Note 1, Significant Accounting Policies Accounting for Stock-Based Compensation, and Note 8, Stock-Based Compensation Plans to the consolidated financial statements).

At June 30, 2006 and December 31, 2005, the DMO business segment had total assets of $1.3 billion and $1.1 billion, respectively.

CORPORATE AND OTHER BUSINESS SEGMENT

The following table includes Core Earnings results of operations for our Corporate and Other business segment.

	Three Months Ended June 30,		% Increase (Decrease)	Six Months Ended June 30,		% Increase (Decrease)
	2006	2005	2006 vs. 2005	2006	2005	2006 vs. 2005
Total interest income	$ 1	$ 1	%	$ 2	$ 2	%
Total interest expense	1	1		3	3	
Net interest income				(1)	(1)	
Less provisions for losses						
Net interest income after provisions for losses				(1)	(1)	
Fee income	33	26	27	60	58	3
Other income	24	29	(17)	55	61	(10)
Total revenue	57	55	4	115	119	(3)
Operating expenses(1)(2)	50	63	(21)	109	114	(4)
Income (loss) before income taxes	7	(8)	188	5	4	25
Income tax expense (benefit)	2	(3)	167	2	1	100
Core Earnings net income (loss)	$ 5	$ (5)	200%	$ 3	$ 3	%

(1) For the three and six months ended June 30, 2006, operating expenses for the Corporate and Other Business segment include $4 million and $9 million, respectively, of stock-based compensation expense due to the implementation of SFAS No. 123(R) in the first quarter of 2006.

(2) In the first quarter of 2006, the Company changed its method for allocating certain overhead and other expenses between our business segments. Balances for the three and six months ending June 30, 2005 have been updated to reflect the new allocation methodology.

Fee and Other Income   Corporate and Other Business Segment

The following table summarizes the components of fee and other income for our Corporate and Other business segment for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
Guarantor servicing fees	$ 33	$ 26	$ 60	$ 58
Loan servicing fees	7	12	15	25
Other income	17	17	40	36
Total fee and other income	$ 57	$ 55	$ 115	$ 119

The increase in guarantor servicing fees versus the year-ago quarter is due to a $10 million increase in account maintenance fees caused by a negotiated agreement with USA Funds such that USA Funds was able to cover the previous shortfall caused by the cap on payments from ED to guarantors in fiscal year 2006. This cap is removed by legislation reauthorizing the student loan programs of the Higher Education Act that will not go into effect before October 1, 2006.

USA Funds, the nation s largest guarantee agency, accounted for 85 percent and 86 percent, respectively, of guarantor servicing fees and 37 percent and 33 percent, respectively, of revenues associated with other products and services for the three months ended June 30, 2006 and 2005.

Operating Expenses   Corporate and Other Business Segment

The following table summarizes the components of operating expenses for our Corporate and Other Business segment for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
Operating expenses	$ 30	$ 37	$ 68	$ 71
Corporate overhead	20	26	41	43
Total operating expenses	$ 50	$ 63	$ 109	$ 114

Operating expenses for our Corporate and Other business segment include direct costs incurred to service loans for unrelated third parties and to perform guarantor servicing on behalf of guarantor agencies, as well as information technology expenses related to these functions. For the three and six months ended June 30, 2006, operating expenses for our Corporate and Other business segment also include $4 million and $9 million, respectively, of stock-based compensation expense, due to the implementation of SFAS No. 123(R) (see Note 1,   Significant Accounting Policies Accounting for Stock-Based Compensation,   and Note 8,   Stock-Based Compensation Plans   to the consolidated financial statements).

At June 30, 2006 and December 31, 2005, the Corporate and Other business segment had total assets of $408 million and $719 million, respectively.

LIQUIDITY AND CAPITAL RESOURCES

Except in the case of acquisitions, which are discussed separately, our DMO and Corporate and Other business segments are not capital intensive businesses and as such a minimal amount of debt and equity capital is allocated to these segments. Therefore, the following Liquidity and Capital Resources discussion relates primarily to our Lending business segment.

We depend on the debt capital markets to support our business plan. To meet business plan objectives, we must maintain cost effective liquidity to fund the growth in our Managed portfolio of student loans as well as to refinance previously securitized loans when borrowers choose to refinance their loans through a Consolidation Loan with the Company. At the same time, we must continue to control interest rate risk. Our main source of funding is student loan securitization. We securitized $17.5 billion in student loans in seven transactions in the six months ended June 30, 2006, versus $11.3 billion securitized in six transactions in the year-ago period. FFELP securitizations are unique securities in the asset-backed market in that they are collateralized by student loans with an explicit federal guarantee on 100 percent of principal and interest upon default. This guarantee is subject to service compliance and the Company retaining its EP designation. The amount of the guarantee will be reduced to 99 percent after July 1, 2006 through legislation (see RECENT DEVELOPMENTS Reauthorization). Securitizations comprised 69 percent of our financing at June 30, 2006 versus 68 percent at June 30, 2005 related to our Managed portfolio.

In addition to securitizations, we also fund our operations by accessing the corporate debt markets on a regular basis. In the six months ended June 30, 2006, we issued $4.7 billion in SLM Corporation term, unsecured debt. At June 30, 2006, on-balance sheet debt, exclusive of on-balance sheet securitizations and secured indentured trusts, totaled $42.9 billion versus $36.5 billion at June 30, 2005.

Liquidity is important to the Company in that it enables us to effectively fund our student loan acquisitions, meet maturing debt obligations, and fund operations. The following table details our sources of liquidity and the available capacity at June 30, 2006.

	June 30, 2006	**December 31, 2005**
	Available Capacity	**Available Capacity**
Sources of primary liquidity:		
Unrestricted cash and liquid investments	$ 5,376	$ 3,928
Commercial paper and bank lines of credit	5,500	5,500
ABCP borrowing capacity	23	41
Total sources of primary liquidity	10,899	9,469
Sources of stand-by liquidity:		
Unencumbered FFELP student loans	24,741	24,530
Total sources of primary and stand-by liquidity	$ 35,640	$ 33,999

We believe our unencumbered FFELP student loan portfolio provides an additional source of potential or stand-by liquidity because the maturation of the government guaranteed student loan securitization marketplace has created a wide and deep marketplace for such transactions. The whole loan sale market for FFELP student loans provides an additional potential source of stand-by liquidity. At June 30, 2006, we had $686 million of investments on our balance sheet that were not included in the above table as these investments were pledged as collateral related to certain derivative positions.

In addition to liquidity, a major objective when financing our business is to minimize interest rate risk by matching the interest rate and reset characteristics of our Managed assets and liabilities, generally on a pooled basis, to the extent practicable. In this process we use derivative financial instruments extensively to reduce our interest rate and foreign currency exposure. This interest rate risk management helps us to stabilize our student loan spread in various and changing interest rate environments. (See also Interest Rate Risk Management below.)

Managed Borrowings

The following tables present the ending balances of our Managed borrowings at June 30, 2006 and 2005 and average balances and average interest rates of our Managed borrowings for the three and six months ended June 30, 2006 and 2005. The average interest rates include derivatives that are economically hedging the underlying debt, but do not qualify for hedge accounting treatment under SFAS No. 133. (See BUSINESS SEGMENTS *Pre-tax differences Between Core Earnings and GAAP by Business Segment Reclassification of Realized Gains (Losses) on Derivative and Hedging Activities.*)

Ending Balances

	As of June 30,					
	2006			2005		
	Ending Balance			Ending Balance		
	Short Term	Long Term	Total Managed Basis	Short Term	Long Term	Total Managed Basis
Unsecured borrowings	$ 3,739	$ 39,170	$ 42,909	$ 4,262	$ 32,234	$ 36,496
Indentured trusts (on-balance sheet)	62	3,201	3,263	418	3,991	4,409
Securitizations (on-balance sheet)		48,212	48,212		38,076	38,076
Securitizations (off-balance sheet)		52,357	52,357		47,524	47,524
Total	$ 3,801	$ 142,940	$ 146,741	$ 4,680	$ 121,825	$ 126,505

Average Balances

	Three Months Ended June 30,				Six Months Ended June 30,			
	2006		2005		2006		2005	
	Average Balance	Average Rate	Average Balance	Average Rate	Average Balance	Average Rate	Average Balance	Average Rate
Unsecured borrowings	$ 42,520	5.42%	$ 36,422	3.67%	$ 42,048	5.24%	$ 35,447	3.49%
Indentured trusts (on-balance sheet)	3,325	4.52	4,450	3.43	3,352	4.36	5,662	3.06
Securitizations (on-balance sheet)	45,912	5.33	36,108	3.38	46,229	5.10	35,740	3.16
Securitizations (off-balance sheet)	51,143	5.39	46,600	3.46	48,033	5.21	45,420	3.30
Total	$ 142,900	5.36%	$ 123,580	3.50%	$ 139,662	5.16%	$ 122,269	3.30%

Unsecured On-Balance Sheet Financing Activities

The following table presents the senior unsecured credit ratings on our debt from major rating agencies.

	S&P	Moody s	Fitch
Short-term unsecured debt	A-1	P-1	F1+
Long-term unsecured debt	A	A2	A+

The table below presents our unsecured on-balance sheet term funding by funding source for the three and six months ended June 30, 2006 and 2005.

	Debt Issued for the Three Months Ended June 30,		Debt Issued for the Six Months Ended June 30,		Outstanding at June 30,	
	2006	2005	2006	2005	2006	2005
Convertible debentures	$	$	$	$	$ 1,995	$ 1,990
Retail notes	110	246	267	579	3,869	3,409
Foreign currency denominated notes[1]	1,052	857	1,475	1,000	10,261	5,782
Extendible notes	999	500	999	500	5,246	4,747
Global notes (Institutional)	871		1,945	1,184	19,737	17,906
Medium-term notes (Institutional)					1,800	2,630
Total	$ 3,032	$ 1,603	$ 4,686	$ 3,263	$ 42,908	$ 36,464

[1] All foreign currency denominated notes are swapped back to U.S. dollars.

In addition to the term issuances reflected in the table above, we also use our commercial paper program for short-term liquidity purposes. The average balance of commercial paper outstanding during the three months ended June 30, 2006 and 2005 was $0 and $690 million, respectively, and during the six months ended June 30, 2006 and 2005 was $165 million and $408 million, respectively. The maximum daily amount outstanding for the three months ended June 30, 2006 and 2005 was $0 and $1.9 billion, respectively, and for the six months ended June 30, 2006 and 2005 was $2.2 billion and $1.9 billion, respectively.

Contingently Convertible Debentures

At June 30, 2006, we have approximately $2 billion Contingently Convertible Debentures (Co-Cos) outstanding. The Co-Cos are eligible to be called at par on or after July 25, 2007, under certain circumstances. The following table provides the historical effect of our Co-Cos on our common stock equivalents (CSEs) and after-tax interest expense.

(In thousands)	Three Months Ended June 30, 2006	Six Months Ended June 30, 2006	Year Ended December 31, 2005	Three Months Ended December 31, 2005	Three Months Ended September 30, 2005	Three Months Ended June 30, 2005	Three Months Ended March 31, 2005
CSE impact of Co-Cos (shares)	30,312	30,312	30,312	30,312	30,312	30,312	30,312
Co-Cos after-tax interest expense	$ 16,460	$ 31,277	$ 44,572	$ 13,685	$ 11,971	$ 10,297	$ 8,619

The table below outlines the effect of the Co-Cos on the numerators and denominators for the diluted EPS calculations for the three and six months ended June 30, 2006 and 2005. The net effect of the Co-Cos on diluted EPS will vary with the period to period changes in net income of the Company.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
Numerator:				
Net income attributable to common stock	$ 714,991	$ 292,607	$ 858,291	$ 513,116
Adjusted for debt expense of Co-Cos, net of taxes	16,460	10,297	31,277	18,916
Adjusted for non-taxable unrealized gains on equity forwards[1]	(39,717)			
Net income attributable to common stock, adjusted	$ 691,734	$ 302,904	$ 889,568	$ 532,032
Denominator: ***(shares in thousands)***				
Weighted average shares used to compute basic EPS	410,957	419,497	411,811	420,206
Effect of dilutive securities:				
Dilutive effect of stock options, nonvested deferred compensation, nonvested restricted stock, restricted stock units, ESPP, and equity forwards	13,045	12,091	11,680	11,936
Dilutive effect of Co-Cos	30,312	30,312	30,312	30,312
Dilutive potential common shares[2]	43,357	42,403	41,992	42,248
Weighted average shares used to compute diluted EPS	454,314	461,900	453,803	462,454
Net earnings per share:				
Basic EPS	$ 1.74	$ .70	$ 2.08	$ 1.22
Dilutive effect of stock options, nonvested deferred compensation, nonvested restricted stock, restricted stock units, ESPP, and equity forwards	(.05)	(.02)	(.05)	(.03)
Dilutive effect of Co-Cos	(.08)	(.02)	(.07)	(.04)
Dilutive effect of non-taxable unrealized gains on equity forwards[1]	(.09)			
Diluted EPS	$ 1.52	$ .66	$ 1.96	$ 1.15

(1) SFAS No. 128, Earnings per Share, and the additional guidance provided by EITF Topic No. D-72, Effect of Contracts That May Be Settled in Stock or Cash on the Computation of Diluted Earnings per Share, require both the denominator and the numerator to be adjusted in calculating the potential impact of the Company s equity forward contracts on diluted EPS. Under this guidance, when certain conditions are satisfied, the impact of the equity forwards is dilutive. Specifically, the impact is dilutive when: (1) the average share price is lower than the respective strike prices on our equity forward contracts, and (2) we recognized a gain on derivative and hedging activities related to our equity forward contracts. These

conditions occurred during the three months ended June 30, 2006. At the time of our second quarter 2006 press release (the Press Release) filed on Form 8-K on July 20, 2006, we adjusted only the denominator in calculating the effects of our equity forward contracts. The diluted EPS of $1.52 in the table above reflects the effects of adjusting both the numerator and denominator and corrects the information previously reported in our Press Release. This guidance does not affect our net income for the quarter and does not require us to adjust our diluted EPS for the six months ended June 30, 2006 or any prior period.

(2) For the three months ended June 30, 2006 and 2005, stock options and equity forwards of approximately 8 million shares and 14 million shares, respectively, and for the six months ended June 30, 2006 and 2005, stock options and equity forwards of approximately 12 million shares and 19 million shares, respectively, were outstanding but not included in the computation of diluted earnings per share because they were antidilutive.

Securitization Activities

Securitization Program

The following table summarizes our securitization activity for the three and six months ended June 30, 2006 and 2005. Those securitizations listed as sales are off-balance sheet transactions and those listed as financings remain on-balance sheet.

	Three Months Ended June 30,											
	2006						2005					
	No. of Transactions		Loan Amount Securitized		Pre-Tax Gain	Gain %	No. of Transactions		Loan Amount Securitized		Pre-Tax Gain	Gain %
FFELP Stafford/ PLUS loans		$		$		%		$		$		%
Consolidation Loans	1		2,500		23	.9	2		4,011		31	.8
Private Education Loans	2		4,000		648	16.2	1		1,505		231	15.3
Total securitizations sales	3		6,500	$	671	10.3%	3		5,516	$	262	4.7%
Consolidation Loans[1]	1		3,001				1		2,226			
Total securitizations financings	1		3,001				1		2,226			
Total securitizations	4	$	9,501				4	$	7,742			

	Six Months Ended June 30,							
	2006				2005			
	No. of Transactions	Loan Amount Securitized	Pre-Tax Gain	Gain %	No. of Transactions	Loan Amount Securitized	Pre-Tax Gain	Gain %

FFELP Stafford/ PLUS loans	2	$	5,004	$	17	.3%	2	$	3,530	$	50	1.4%
Consolidation Loans	2		5,502		36	.7	2		4,011		31	.8
Private Education Loans	2		4,000		648	16.2	1		1,505		231	15.3
Total securitizations sales	6		14,506	$	701	4.8%	5		9,046	$	312	3.4%
Consolidation Loans[1]	1		3,001				1		2,226			
Total securitizations financings	1		3,001				1		2,226			
Total securitizations	7	$	17,507				6	$	11,272			

(1) In certain Consolidation Loan securitization structures, the Company holds certain rights that can affect the remarketing of certain bonds such that these securitizations did not qualify as qualifying special purpose entities (QSPEs). Accordingly, they are accounted for on-balance sheet as variable interest entities (VIEs).

The decrease in the FFELP Stafford/ PLUS gain as a percentage of loans securitized from 1.4 percent for the six months ended June 30, 2005 to 0.3 percent for the six months ended June 30, 2006 is primarily due to: 1) an increase in the CPR assumption to account for continued high levels of Consolidation Loan activity; 2) an increase in the discount rate to reflect higher long-term interest rates; 3) the re-introduction of Risk Sharing with the Reconciliation Legislation reauthorizing the student loan programs of the Higher Education Act; and 4) an increase in the amount of student loan premiums included in the carrying value of the loans sold. The higher premiums on these loans were primarily due to the allocation of the purchase price to student loan portfolios acquired through the acquisitions of several companies in the student loan industry. Higher premiums were also due to loans acquired through zero-fee lending and the school-as-lender channel.

Liquidity Risk and Funding Long-Term

With the dissolution of the GSE, our long-term funding, credit spread and liquidity exposure to the corporate and asset-backed capital markets has increased significantly. A major disruption in the fixed income capital markets that limits our ability to raise funds or significantly increases the cost of those funds could have a material impact on our ability to acquire student loans, or on our results of operations. Going forward, securitizations will continue to be the primary source of long-term financing and liquidity. Our securitizations are structured such that we are not obligated to provide any material level of financial, credit or liquidity support to any of the trusts, thus limiting our exposure to the recovery of the Retained Interest asset on the balance sheet for off-balance sheet securitizations to the loss of the earnings spread for loans securitized on-balance sheet. While all of our Retained Interests are subject to some prepayment risk, Retained Interests from our FFELP Stafford securitizations have significant prepayment risk primarily arising from borrowers opting to consolidate their Stafford/ PLUS loans. When consolidation activity is higher than projected, the increase in prepayment could materially impair the value of our Retained Interest. However, this negative effect on our Retained Interest is somewhat offset by the loans that consolidate back on our balance sheet, which we view as trading one interest bearing asset for another, whereas loans that consolidate with third parties represent a complete economic loss to the Company. We discuss our short-term liquidity risk, including a table of our sources of liquidity at the beginning of this LIQUIDITY AND CAPITAL RESOURCES section.

Retained Interest in Securitized Receivables

The following tables summarize the fair value of the Company s Residual Interests, included in the Company s Retained Interest (and the assumptions used to value such Residual Interests), along with the underlying off-balance sheet student loans that relate to those securitizations in transactions that were treated as sales as of June 30, 2006 and December 31, 2005.

	As of June 30, 2006			
	FFELP Stafford and PLUS	**Consolidation Loan Trusts[1]**	**Private Education Loan Trusts**	**Total**
Fair value of Residual Interests[2]	$ 773	$ 524	$ 1,855	$ 3,152
Underlying securitized loan balance[3]	20,224	14,746	12,556	47,526
Weighted average life	2.5 yrs.	8.1 yrs.	8.4 yrs.	
Prepayment speed (annual rate)[4]	10%-40% [5]	6%	4%	
Expected credit losses (% of student loan principal)	.07%	.07%	4.73%	
Residual cash flows discount rate	13.0%	11.1%	13.1%	

	As of December 31, 2005			
	FFELP Stafford and PLUS	**Consolidation Loan Trusts[1]**	**Private Education Loan Trusts**	**Total**
Fair value of Residual Interests[2]	$ 773	$ 483	$ 1,150	$ 2,406
Underlying securitized loan balance [3]	20,372	10,272	8,946	39,590
Weighted average life	2.7 yrs.	8.0 yrs.	7.8 yrs.	
Prepayment speed (annual rate)[4]	10%-20% [5]	6%	4%	
Expected credit losses (% of student loan principal)	.14%	.23%	4.74%	
Residual cash flows discount rate	12.3%	10.3%	12.4%	

(1) Includes $115 million and $235 million related to the fair value of the Embedded Floor Income as of June 30, 2006 and December 31, 2005, respectively. The decrease in the fair value of the Embedded Floor Income is primarily due to rising interest rates during the period.

(2) At June 30, 2006 and December 31, 2005, the Company had unrealized gains (pre-tax) in accumulated other comprehensive income of $401 million and $370 million, respectively, that related to the Retained Interests.

(3) In addition to student loans in off-balance sheet trusts, the Company had $41.3 billion and $40.9 billion of securitized student loans outstanding (face amount) as of June 30, 2006 and December 31, 2005, respectively, in

on-balance sheet securitization trusts.

(4) The prepayment speed assumptions include the impact of projected defaults. Previous disclosures for Private Education Loans excluded projected default assumptions.

(5) 40% for the third quarter of 2006, 30% for the fourth quarter of 2006, 15% for 2007 and 10% thereafter for June 30, 2006 valuations and 20% for 2006, 15% for 2007 and 10% thereafter for December 31, 2005 valuations.

Servicing and Securitization Revenue

Servicing and securitization revenue, the ongoing revenue from securitized loan pools accounted for off-balance sheet as QSPEs, includes the interest earned on the Residual Interest asset and the revenue we receive for servicing the loans in the securitization trusts. Interest income recognized on the Residual Interest is based on our anticipated yield determined by estimating future cash flows each quarter.

The following table summarizes the components of servicing and securitization revenue for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
Servicing revenue	$ 88	$ 86	$ 168	$ 171
Securitization revenue, before Embedded Floor Income and impairment	84	72	153	135
Servicing and securitization revenue, before Embedded Floor Income and impairment	172	158	321	306
Embedded Floor Income	4	24	10	50
Less: Floor Income previously recognized in gain calculation	(2)	(17)	(6)	(39)
Net Embedded Floor Income	2	7	4	11
Servicing and securitization revenue, before impairment	174	165	325	317
Retained Interest impairment	(91)	(15)	(143)	(24)
Total servicing and securitization revenue	$ 83	$ 150	$ 182	$ 293
Average off-balance sheet student loans	$ 47,716	$ 43,791	$ 44,909	$ 42,846
Average balance of Retained Interest	$ 3,004	$ 2,576	$ 2,754	$ 2,448
Servicing and securitization revenue as a percentage of the average balance of off-balance sheet student loans (annualized)	.70%	1.37%	.82%	1.38%

Servicing and securitization revenue is primarily driven by the average balance of off-balance sheet student loans and the amount of and the difference in the timing of Embedded Floor Income recognition on off-balance sheet student loans.

Servicing and securitization revenue can be negatively impacted by impairments of the value of our Retained Interest, caused primarily by the effect of higher than expected Consolidation Loan activity on FFELP Stafford/ PLUS student loan securitizations and the effect of market interest rates on the Embedded Floor Income included in the Retained Interest. The majority of the consolidations bring the loans back on-balance sheet so for those loans we retain the value of the asset on-balance sheet versus in the trust. For the three months ended June 30, 2006 and 2005, we recorded impairments to the Retained Interests of $91 million and $15 million, respectively, and for the six months ended June 30, 2006 and 2005, we recorded impairments of $143 million and $24, respectively. These impairment charges were primarily the result of FFELP Stafford loans prepaying faster than projected through loan consolidation

($92 million and $20 million for the six months ended June 30, 2006 and 2005, respectively), and the effect of market interest rates on the Embedded Floor Income which is part of the Retained Interest ($51 million and $4 million for the six months ended June 30, 2006 and 2005, respectively). The impairment for the six months ended June 30, 2006 also reflects the increase in our CPR assumption for the remainder of 2006 from 20 percent to 40 percent for the third quarter and 30 percent for the fourth quarter, to account for the surge in Consolidation Loan applications received in the second quarter that will be processed in the third and fourth quarters of 2006. The level and timing of Consolidation Loan activity is highly volatile, and in response we continue to revise our estimates of the effects of Consolidation Loan activity on our Retained Interests and it may result in additional impairment recorded in future periods if Consolidation Loan activity remains higher than projected.

Interest Rate Risk Management

Asset and Liability Funding Gap

The tables below present our assets and liabilities (funding) arranged by underlying indices as of June 30, 2006. In the following GAAP presentation, the funding gap only includes derivatives that qualify as effective SFAS No. 133 hedges (those derivatives which are reflected in net interest margin, as opposed to in the derivative market value adjustment). The difference between the asset and the funding is the funding gap for the specified index. This represents our exposure to interest rate risk in the form of basis risk and repricing risk, which is the risk that the different indices may reset at different frequencies or may not move in the same direction or at the same magnitude.

Management analyzes interest rate risk on a Managed basis, which consists of both on-balance sheet and off-balance sheet assets and liabilities and includes all derivatives that are economically hedging our debt whether they qualify as effective hedges under SFAS No. 133 or not. Accordingly, we are also presenting the asset and liability funding gap on a Managed basis in the table that follows the GAAP presentation.

GAAP Basis

Index	Frequency of Variable Resets	Assets	Funding[1]	Funding Gap
(Dollars in billions)				
3 month Commercial paper	daily	$ 63.4	$	$ 63.4
3 month Treasury bill	weekly	7.9	.3	7.6
Prime	annual	.6		.6
Prime	quarterly	1.2		1.2
Prime	monthly	5.1		5.1
PLUS Index	annual	2.6		2.6
3-month LIBOR	daily			
3-month LIBOR	quarterly	1.6	78.1	(76.5)
1-month LIBOR	monthly	.1	2.5	(2.4)
CMT/ CPI index	monthly/quarterly		3.5	(3.5)
Non discreet reset[2]	monthly		7.8	(7.8)
Non discreet reset[3]	daily/weekly	7.8		7.8
Fixed Rate[4]		11.6	9.7	1.9
Total		$ 101.9	$ 101.9	$

(1) Includes all derivatives that qualify as hedges under SFAS No. 133.

(2) Consists of asset-backed commercial paper and auction rate securities, which are discount note type instruments that generally roll over monthly.

(3) Includes restricted and non-restricted cash equivalents and other overnight type instruments.

(4) Includes receivables/payables, other assets (including Retained Interest), other liabilities and stockholders equity (excluding Series B Preferred Stock).

The funding gaps in the above table are primarily interest rate mismatches in short-term indices between our assets and liabilities. We address this issue primarily through the use of basis swaps that primarily convert quarterly 3-month LIBOR to other indices that are more correlated to our asset indices.

These basis swaps do not qualify as effective hedges under SFAS No. 133 and as a result the effect on the funding index is not included in our interest margin and is therefore excluded from the GAAP presentation.

Managed Basis

Index	**Frequency of Variable Resets**	**Assets**	**Funding[1]**	**Funding Gap**
(Dollars in billions)				
3 month Commercial paper	daily	$ 89.4	$ 16.2	$ 73.2
3 month Treasury bill	weekly	15.8	17.2	(1.4)
Prime	annual	1.0		1.0
Prime	quarterly	7.4	5.5	1.9
Prime	monthly	10.3	9.7	.6
PLUS Index	annual	4.6	5.8	(1.2)
3-month LIBOR	daily		72.3	(72.3)
3-month LIBOR	quarterly	1.5	8.2	(6.7)
1-month LIBOR	monthly	.1	1.5	(1.4)
Non discreet reset[2]	monthly		8.2	(8.2)
Non discreet reset[3]	daily/weekly	12.8		12.8
Fixed Rate[4]		9.8	8.1	1.7
Total		$ 152.7	$ 152.7	$

(1) Includes all derivatives that management considers economic hedges of interest rate risk and reflects how we internally manage our interest rate exposure.

(2) Consists of asset-backed commercial paper and auction rate securities, which are discount note type instruments that generally roll over monthly.

(3) Includes restricted and non-restricted cash equivalents and other overnight type instruments.

(4) Includes receivables/payables, other assets, other liabilities and stockholders equity (excluding Series B Preferred Stock).

To the extent possible, we generally fund our assets with debt (in combination with derivatives) that has the same underlying index (index type and index reset frequency). When it is more economical, we also fund our assets with debt that has a different index and/or reset frequency than the asset, but only in instances where we believe there is a high degree of correlation between the interest rate movement of the two indices. For example, we use daily reset 3-month LIBOR to fund a large portion of our daily reset 3-month commercial paper indexed assets. In addition, we use quarterly reset 3-month LIBOR to fund a portion of our quarterly reset Prime rate indexed Private Education Loans. We also use our monthly Non Discreet reset funding (asset-backed commercial paper program and auction rate securities) to fund various asset types. In using different index types and different index reset frequencies to fund our assets, we are exposed to interest rate risk in the form of basis risk and repricing risk, which is the risk that the different indices that may reset at different frequencies will not move in the same direction or at the same magnitude.

We believe that this risk is low as all of these indices are short-term with rate movements that are highly correlated over a long period of time. We use interest rate swaps and other derivatives to achieve our risk management objectives.

When compared with the GAAP presentation, the Managed basis presentation includes all of our off-balance sheet assets and funding, and also includes basis swaps that primarily convert quarterly 3-month LIBOR to other indices that are more correlated to our asset indices. Our basis swaps do not qualify for GAAP hedge accounting treatment and are therefore not considered in the GAAP Asset and Liability Funding GAP table.

Interest Rate Gap Analysis

In the table below, the Company s variable rate assets and liabilities are categorized by reset date of the underlying index. Fixed rate assets and liabilities are categorized based on their maturity dates. An interest rate gap is the difference between volumes of assets and volumes of liabilities maturing or repricing during specific future time intervals. The following gap analysis reflects rate-sensitive positions at June 30, 2006 and is not necessarily reflective of positions that existed throughout the period.

	Interest Rate Sensitivity Period					
	3 Months or Less	**3 Months to 6 Months**	**6 Months to 1 Year**	**1 to 2 Years**	**2 to 5 Years**	**Over 5 Years**
Assets						
Student loans	$ 81,373	$ 626	$ 213	$ 6	$ 58	$ 3
Other loans	140	51	101	10	3	746
Cash and investments, including restricted	8,041	70	62	586	682	253
Other assets	2,567	90	180	395	647	5,004
Total assets	92,121	837	556	997	1,390	6,006
Liabilities and Stockholders Equity						
Short-term borrowings	2,072	516	1,213			
Long-term borrowings	65,125	268		1,384	11,426	12,304
Other liabilities	1,711					1,519
Minority interest in subsidiaries						9
Stockholders equity						4,360
Total liabilities and stockholders equity	68,908	784	1,213	1,384	11,426	18,192
Period gap before adjustments	23,213	53	(657)	(387)	(10,036)	(12,186)
Adjustments for Derivatives and Other Financial Instruments						
Interest rate swaps	(23,075)	83	(59)	477	10,390	12,184
Total derivatives and other financial instruments	(23,075)	83	(59)	477	10,390	12,184
Period gap	$ 138	$ 136	$ (716)	$ 90	$ 354	$ (2)
Cumulative gap	$ 138	$ 274	$ (442)	$ (352)	$ 2	$
Ratio of cumulative gap to total assets	.1%	.3%	(.4)%	(.3)%	%	%

Weighted Average Life

The following table reflects the weighted average life for our Managed earning assets and liabilities at June 30, 2006.

(Averages in Years)	On-Balance Sheet	Off-Balance Sheet	Managed
Earning assets			
Student loans	9.7	5.5	9.5
Other loans	7.7		7.7
Cash and investments	.7	.1	.5
Total earning assets	8.8	5.0	8.6
Borrowings			
Short-term borrowings	.5		.5
Long-term borrowings	6.9	5.5	6.4
Total borrowings	6.7	5.5	6.3

In the above table, Treasury receipts, although generally liquid assets, extend the weighted average remaining term to maturity of cash and investments to .5 years. Long-term debt issuances likely to be called by us or putable by the investor have been categorized according to their call or put dates rather than their maturity dates. In recent years the shift in the composition of our FFELP student loan portfolio from Stafford loans to Consolidation Loans has lengthened the Managed weighted average life of the student loan portfolio from 8.2 years at December 31, 2004, to 9.5 years at June 30, 2006.

COMMON STOCK

The following table summarizes our common share repurchases, issuances and equity forward activity for the three and six months ended June 30, 2006 and 2005.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
(Shares in millions)				
Common shares repurchased:				
Equity forwards	2.1	3.3	4.5	6.4
Benefit plans[(1)]	.4	.3	1.3	.6
Total shares repurchased	2.5	3.6	5.8	7.0
Average purchase price per share	$ 53.93	$ 48.55	$ 54.62	$ 49.46
Common shares issued	1.4	1.8	4.3	3.5
Equity forward contracts:				

Outstanding at beginning of period	42.7	46.6	42.7	42.8
New contracts	5.3	8.4	7.7	15.3
Exercises	(2.1)	(3.3)	(4.5)	(6.4)
Outstanding at end of period	45.9	51.7	45.9	51.7
Authority remaining at end of period to repurchase or enter into equity forwards	10.9	20.5	10.9	20.5

(1) Includes shares withheld from stock option exercises and vesting of performance stock to satisfy minimum statutory tax withholding obligations and shares tendered by employees to satisfy option exercise costs.

As of June 30, 2006, the expiration dates and purchase prices for outstanding equity forward contracts were as follows:

Year of Maturity (Contracts in millions of shares)	Outstanding Contracts	Range of Purchase Prices	Average Purchase Price
2007	.8	$54.74	$ 54.74
2008	7.3	54.74	54.74
2009	14.7	54.74	54.74
2010	15.0	54.74	54.74
2011	8.1	$51.86-$53.76	53.02
	45.9		$ 54.44

The closing price of the Company s common stock on June 30, 2006 was $52.92.

RECENT DEVELOPMENTS

Upromise, Inc. Acquisition

On June 1, 2006, the Company announced that it had signed a purchase agreement to acquire Upromise, Inc. (Upromise) pending regulatory approvals. Upromise s popular rewards service one of the largest rewards marketing coalitions in the U.S. has more than seven million members who have joined Upromise to save for college when they and their families buy gas or groceries, dine out, or purchase other goods and services from more than 450 participating companies. Upromise is also the largest administrator of direct-to-consumer 529 college savings plans, administering nearly one million college savings accounts and over $10 billion in assets with tax-advantaged 529 investment options through partnerships with seven states. Upromise offers its rewards service members the opportunity to link their Upromise account to a participating 529 plan so that their savings can be transferred automatically into their plan on a periodic basis. Under the terms of the transaction, Upromise will become a wholly owned subsidiary of SLM Corporation. Upromise, which employs approximately 250 individuals, will retain its separate brand identity, management team and operations in Needham, MA. The Company expects to close the acquisition in the third quarter of 2006.

Reauthorization

On February 8, 2006, the President signed the Higher Education Reconciliation Act of 2005 (Reconciliation Legislation). The Reconciliation Legislation was included as Title VIII of the Deficit Reduction Act of 2005 (S. 1932), an omnibus budget bill that cut nearly $40 billion in spending over five years, with $12 billion coming from federal student loan programs. The vast majority of the savings are generated by requiring lenders to rebate Floor Income under the new loans issued after April 1, 2006. The major new student loan provisions include the following, with effective dates generally July 1, 2006 unless otherwise indicated:

Lenders rebate Floor Income on new loans after April 1, 2006.

Borrower origination fees are gradually reduced to zero in FFELP by 2010, and to one percent in Direct Loan program by 2010.

Collection of one percent FFELP guaranty fee is mandated for all guarantors, including those with voluntary flexible agreements, but can be paid on behalf of the borrower by lenders or guarantors.

Lender reinsurance is reduced to 99 percent with Exceptional Performer designation for claims filed after July 1, 2006, and 97 percent without designation on loans disbursed after July 1, 2006.

Super 2-Step and in-school consolidation loopholes will be closed as of July 1, 2006.

Recycling of 9.5 percent loans is prohibited for loan holders with more than $100 million in 9.5 percent loans, as of date of enactment, and other 9.5 percent reforms enacted in 2004 are made permanent.

The limitation on SAP for PLUS loans made after January 1, 2000 is repealed, effective April 1, 2006.

Certain loan limits are increased effective July 1, 2007. For undergraduate students, loan limits are raised for first-year students, from $2,625 to $3,500, and for second-year students, from $3,500 to $4,500. These increases allow students to borrow more over the first four years (from $17,125 to $19,000); the cumulative graduate limit was left unchanged at $23,000. Annual loan limits for unsubsidized Stafford loans are increased from $10,000 to $12,000 for graduate students and from $5,000 to $7,000 for graduate students getting a State teaching certificate or credential and professional coursework (see also APPENDIX A, FEDERAL FAMILY EDUCATION LOANS PROGRAM Stafford Loan Program *Loan Limits* included in the Company s Annual Report on Form 10-K for the year ended December 31, 2005).

A moratorium on new schools-as-lender is created after April 1, 2006, and additional requirements are created for schools continuing to participate in this program.

Graduate students become eligible to take out PLUS loans.

Compensation for guarantor collections via loan consolidation is reduced from a maximum of 18.5 percent to 10 percent, along with a cap on the proportion of collection via consolidations. Requirements for collections via loan rehabilitations are made somewhat easier.

New grant programs are available for Pell-eligible students.

The Reconciliation Legislation does not change the interest rates on Stafford loans which, under legislation enacted in 2002, are scheduled to become fixed 6.8 percent for all loans disbursed after July 1, 2006. Under the previous legislation, the PLUS rate was scheduled to become fixed at 7.9 percent after July 1, 2006. The Reconciliation Legislation raises this rate to 8.5 percent for FFELP PLUS loans. Due to a drafting error in the bill, the PLUS rate for the FDLP was not changed and remains at 7.9 percent in the statute. The rates for Consolidation Loans are unchanged by the Reconciliation Legislation; the formula remains the weighted average of the rates on the underling loans, rounded up to the nearest eighth. The Reconciliation Legislation reauthorizes the student loan programs through 2012.

The Emergency Supplemental Appropriations Act for Defense, the Global War on Terror and Hurricane Recovery, 2006 (the Appropriations Act), signed by the President on June 15, 2006, made two changes to the Higher Education Act affecting loan consolidation in the FFELP and FDLP. Of significance, effective for applications received on or after June 15, 2006, the Appropriations Act repealed the single holder rule which required a borrower whose loans were held by a single lender to obtain, in most cases, a Consolidation Loan from that lender. As a result, a borrower with Stafford or PLUS loans may choose their consolidation lender.

Congress has yet to complete action on the rest of the Higher Education Act reauthorization. On June 30, 2006, the President signed into law P.L. 109-238, another three month extension of the Higher Education Act. Although the House passed its version of the reauthorization, the College Access and Opportunity Act of 2005, on March 30, 2006, the Senate has not yet taken action. It is not clear whether there will enough time in September for the Senate to take up its version of the Higher Education Act reauthorization, S. 1614, but the Company expects that it is unlikely that there will be a completed conference report before another extension will be required at the end of September.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Sensitivity Analysis

The effect of short-term movements in interest rates on our results of operations and financial position has been limited through our interest rate risk management. The following tables summarize the effect on earnings for the three and six months ended June 30, 2006 and 2005 and the effect on fair values at June 30, 2006 and December 31, 2005, based upon a sensitivity analysis performed by management assuming a hypothetical increase in market interest rates of 100 basis points and 300 basis points while funding spreads remain constant.

	Three Months Ended June 30,							
	2006				2005			
	Interest Rates:				Interest Rates:			
	Change from Increase of 100 Basis Points		Change from Increase of 300 Basis Points		Change from Increase of 100 Basis Points		Change from Increase of 300 Basis Points	
	$	%	$	%	$	%	$	%
(Dollars in millions, except per share amounts)								
Effect on Earnings								
Increase/(decrease) in pre-tax net income before unrealized gains (losses) on derivative and hedging activities	$ (2)	%	$ (9)	(1)%	$ 6	1%	$ 10	2%
Unrealized gains (losses) on derivative and hedging activities	101	61	157	96	348	2,973	669	5,712
Increase in net income before taxes	$ 99	9%	$ 148	13%	$ 354	74%	$ 679	143%
Increase in diluted earnings per common share	$ .15	9%	$ .23	14%	$ .50	75%	$ .96	145%

	Six Months Ended June 30,			
	2006		2005	
	Interest Rates:		Interest Rates:	
	Change from Increase of 100 Basis	Change from Increase of 300 Basis	Change from Increase of 100 Basis	Change from Increase of 300 Basis

	Points		Points		Points		Points	
	$	**%**	**$**	**%**	**$**	**%**	**$**	**%**
(Dollars in millions, except per share amounts)								
Effect on Earnings								
Increase/(decrease) in pre-tax net income before unrealized gains (losses) on derivative and hedging activities	$ (7)	(1)%	$ (27)	(2)%	$ 13	2%	$ 29	4%
Unrealized gains (losses) on derivative and hedging activities	101	80	157	126	348	455	669	874
Increase in net income before taxes	$ 94	7%	$ 130	9%	$ 361	41%	$ 698	79%
Increase in diluted earnings per common share	$ .145	7%	$ .221	11%	$ .51	45%	$ 1.01	87%

	At June 30, 2006				
		Interest Rates:			
		Change from Increase of 100 Basis Points		Change from Increase of 300 Basis Points	
	Fair Value	$	%	$	%
(Dollars in millions)					
Effect on Fair Values					
Assets					
Total FFELP student loans	$ 77,363	$ (118)	%	$ (203)	%
Private Education Loans	8,335				
Other earning assets	10,769	(46)		(132)	(1)
Other assets	8,883	(300)	(3)	(410)	(5)
Total assets	$ 105,350	$ (464)	%	$ (745)	(1)%
Liabilities					
Interest bearing liabilities	$ 94,467	$ (1,432)	(2)%	$ (3,580)	(4)%
Other liabilities	3,229	1,007	31	2,876	89
Total liabilities	$ 97,696	$ (425)	%	$ (704)	(1)%

	At December 31, 2005				
		Interest Rates:			
		Change from Increase of 100 Basis Points		Change from Increase of 300 Basis Points	
	Fair Value	$	%	$	%
(Dollars in millions)					
Effect on Fair Values					
Assets					
Total FFELP student loans	$ 76,492	$ (215)	%	$ (385)	(1)%
Private Education Loans	9,189				

Other earning assets	9,344	(57)	(1)	(164)	(2)
Other assets	7,429	(292)	(4)	(377)	(5)
Total assets	$ 102,454	$ (564)	(1)%	$ (926)	(1)%
Liabilities					
Interest bearing liabilities	$ 92,026	$ (1,437)	(2)%	$ (3,612)	(4)%
Other liabilities	3,609	975	27	2,863	79
Total liabilities	$ 95,635	$ (462)	%	$ (749)	(1)%

A primary objective in our funding is to minimize our sensitivity to changing interest rates by generally funding our floating rate student loan portfolio with floating rate debt. However, as discussed under LENDING BUSINESS SEGMENT Summary of our Managed Student Loan Portfolio *Floor Income Managed Basis,* we can have a fixed versus floating mismatch in funding if the student loan earns at the fixed borrower rate and the funding remains floating, which results in us earning Floor Income.

During the three and six months ended June 30, 2006 and 2005, certain FFELP student loans were earning Floor Income and we locked in a portion of that Floor Income through the use of futures and Floor Income Contracts that converted a portion of the fixed rate nature of student loans to variable rate.

These hedging transactions also fixed the relative spread between the student loan asset rate and the variable rate liability.

In the above table, under the scenario where interest rates increase 100 and 300 basis points, the changes in pre-tax net income before the unrealized gains (losses) on derivative and hedging activities is primarily due to the impact of (i) our off-balance sheet hedged Consolidation Loan securitizations and the related Embedded Floor Income recognized as part of the gain on sale, which results in a decrease in payments on the written Floor contracts that more than offset impairment losses on the Embedded Floor Income in the Residual Interest; (ii) our unhedged on-balance sheet loans not currently having significant Floor Income due to the recent increase in interest rates, which results in these loans being more variable rate; and (iii) a portion of our fixed rate assets being funded with variable debt. The first item will generally cause income to increase when interest rates increase from a low interest rate environment, whereas, the second and third items will generally offset this increase. In the 100 and 300 basis point scenario for the three and six months ended June 30, 2006, the first two items had little impact allowing the third item to cause a net decrease in income. In the three and six months ended June 30, 2005, the first item had a greater impact than the last item.

In addition to interest rate risk addressed in the preceding tables, the Company is also exposed to risks related to foreign currency exchange rates and the equity price of its own stock. Foreign currency exchange risk is the result of foreign denominated debt issued by the Company. The Company s policy is to use cross currency interest rate swaps to swap all foreign denominated debt payments (fixed and floating) to U.S. dollar LIBOR using a fixed exchange rate. In the tables above, there would be an immaterial impact on earnings if exchange rates were to decrease or increase, due to the terms of the hedging instrument and hedged items matching. The balance sheet interest bearing liabilities would be affected by a change in exchange rates, however, the change would be materially offset by the cross currency interest rate swaps in other assets or other liabilities. Equity price risk of the Company s own stock is due to equity forward contracts used in the Company s share repurchase program. A hypothetical decrease in the Company s stock price per share of $5.00 and $10.00 would decrease unrealized gains (losses) on derivative and hedging activities by $230 million and $459 million, respectively. In addition to the net income impact, other assets would decrease by the aforementioned amounts. Stock price decreases can also result in the counterparty exercising its right to demand early settlement on a portion of or the total contract depending on trigger prices set in each contract. With the $5.00 and $10.00 decrease in unit stock price above, none of these triggers would be met and no counterparty would have the right to early settlement.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of June 30, 2006. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer, concluded that, as of June 30, 2006, our disclosure controls and procedures were effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is (a) recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms and (b) accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended) occurred during the fiscal quarter ended June 30, 2006 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The Company was named as a defendant in a putative class action lawsuit brought by three Wisconsin residents on December 20, 2001 in the Superior Court for the District of Columbia. The lawsuit sought to bring a nationwide class action on behalf of all borrowers who allegedly paid undisclosed improper and excessive late fees over the past three years. The plaintiffs sought damages of $1,500 per violation plus punitive damages and claimed that the class consisted of two million borrowers. In addition, the plaintiffs alleged that the Company charged excessive interest by capitalizing interest quarterly in violation of the promissory note. On February 27, 2003, the Superior Court granted the Company s motion to dismiss the complaint in its entirety. On March 4, 2004, the District of Columbia Court of Appeals affirmed the Superior Court s decision granting the Company s motion to dismiss the complaint, but granted plaintiffs leave to re-plead the first count, which alleged violations of the D.C. Consumer Protection Procedures Act. On September 15, 2004, the plaintiffs filed an amended class action complaint. On October 15, 2004, the Company filed a motion to dismiss the amended complaint with the Superior Court for failure to state a claim and non-compliance with the Court of Appeals ruling. On December 27, 2004, the Superior Court granted the Company s motion to dismiss the plaintiffs amended complaint. Plaintiffs appealed the Superior Court s dismissal order to the Court of Appeals. On June 8, 2006, the Court of Appeals issued an opinion reversing the order of the trial court dismissing the amended complaint. The Court of Appeals did not address the merits of the complaint but concluded that the trial court improperly relied upon facts extrinsic to the complaint. The Company does not believe that it is reasonably likely that a nationwide class will be certified. The Court of Appeals noted in its decision that the plaintiffs failed to file a motion for class certification within the time required by the District of Columbia rules.

The Company is also subject to various claims, lawsuits and other actions that arise in the normal course of business. Most of these matters are claims by borrowers disputing the manner in which their loans have been processed or the accuracy of the Company s reports to credit bureaus. In addition, the collections subsidiaries in the Company s debt management operation group are occasionally named in individual plaintiff or class action lawsuits in which the plaintiffs allege that the Company has violated a federal or state law in the process of collecting their account. Management believes that these claims, lawsuits and other actions will not have a material adverse effect on its business, financial condition or results of operations.

Item 1A. Risk Factors

There have been no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2005.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table summarizes the Company s common share repurchases during the second quarter of 2006 pursuant to the stock repurchase program (see Note 6, Stockholders Equity, to the consolidated financial statements) first authorized in September 1997 by the Board of Directors. Since the inception of the program, which has no expiration date, the Board of Directors has authorized the purchase of up to 308 million shares as of June 30, 2006.

(Common shares in millions)	Total Number of Shares Purchased[1]		Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares That May Yet Be Purchased Under the Plans or Programs[2]
Period:					
April 1 - April 30, 2006	2.1	$	54.70	2.1	13.2
May 1 - May 31, 2006	.4		49.25		10.9
June 1 - June 30, 2006					10.9
Total second quarter	2.5	$	53.93	2.1	

(1) The total number of shares purchased includes: i) shares purchased under the stock repurchase program discussed above, and ii) shares purchased in connection with the exercise of stock options and vesting of performance stock to satisfy minimum statutory tax withholding obligations and shares tendered by employees to satisfy option exercise costs (which combined totaled .4 million shares for the second quarter of 2006).

(2) Reduced by outstanding equity forward contracts.

Item 3. Defaults Upon Senior Securities

Nothing to report.

Item 4. Submission of Matters to a Vote of Security Holders

At the Company s annual meeting of shareholders held on May 18, 2006, the following proposals were approved by the margins indicated:

1. To elect 14 directors to serve on the Company s Board of Directors for one-year terms or until their successors are elected and qualified:

	Number of Shares	
	Votes For	Votes Withheld
Ann Torre Bates	363,780,517	2,481,411
Charles L. Daley	356,206,952	10,054,976
William M. Diefenderfer, III	363,713,812	2,548,116
Thomas J. Fitzpatrick	356,393,788	9,868,140

Diane Suitt Gilleland	356,335,359	9,926,569
Earl A. Goode	363,817,037	2,444,891
Ronald F. Hunt	330,148,606	36,113,322
Benjamin J. Lambert, III	356,331,661	9,930,267
Albert L. Lord	356,248,185	10,013,743
Barry A. Munitz	363,689,275	2,572,653
A. Alexander Porter, Jr.	356,265,780	9,996,148
Wolfgang Schoellkopf	363,601,920	2,660,008
Steven L. Shapiro	356,345,578	9,916,350
Barry L. Williams	359,247,674	7,014,254

2. To ratify the appointment of PricewaterhouseCoopers LLP as the independent registered public accounting firm for 2006:

Number of Shares		
Votes For	**Votes Against**	**Abstain**
363,594,771	471,061	2,196,096

Item 5. Other Information

The diluted EPS of $1.52 reported in this Form 10-Q for the quarter ended June 30, 2006, reflects a change in the calculation of diluted shares under the reverse treasury stock method and corrects the information previously reported in the Company s second quarter 2006 press release filed on Form 8-K on July 20, 2006, as described in Note 7 to the Notes to Consolidated Financial Statements in Part I Item 1 of this Form 10-Q.

Item 6. Exhibits

The following exhibits are furnished or filed, as applicable:

31.1	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

SLM CORPORATION
(Registrant)

By: /s/ C.E. Andrews

C.E. Andrews
Executive Vice President and
Chief Financial Officer
(Principal Accounting Officer and
Duly Authorized Officer)

Date: August 8, 2006