11

Information Item

California Student Aid Commission

EDFUND President's Report

Enclosed is a written report from the President of EDFUND.

Recommended Action: For information only. No action is required.

Responsible Person: Sam Kipp, EDFUND President

President's Quarterly Report to the Board of Directors
For January 1- March 31, 2008

Submitted April 2008

2007 ushered in unprecedented change in the student loan industry and the Federal Family Education Loan Program that will continue to be felt throughout 2008. Deep budget cuts and turmoil in the credit markets have placed significant stress on the Federal Family Education Loan Program and threaten some students' access to federal loans. EDFUND shares a commitment with the U.S. Department of Education (ED) and Congress to ensure that students continue to receive the necessary loan funds to pursue postsecondary education and training.

Lender of Last Resort

Historically, EDFUND has had a Lender of Last Resort (LLR) capability in place to serve the needs of the occasional, individual borrower who could not get a loan from regular FFELP lenders. This program has used a limited number of lenders to provide these loans, with some services provided by EDFUND. It was available for borrowers in California, the only state where we are the designated Guarantor.

Early this year, as indications of potential interruptions in FFELP loan availability began to surface; EDFUND started an LLR renewal project, aimed to provide for much higher volume LLR possibilities.

As a result of this advance work, EDFUND joined in a significant industry-wide effort that has produced an NCHELP proposal to ED for a broader approach to LLR. In this model an LLR program would be available to meet the loan needs of a complete school, partial school (by loan type or grade level, for example), or even a group of schools, for LLR loans. That proposal is now with the Department and a series of meetings and conference calls with the Secretary of Education and Department officials have displayed a cooperative willingness to move forward quickly.

Meanwhile, when the Department reissued its Dear Colleague Letter asking all guaranty agencies to submit plans for a broad-based LLR program, EDFUND was prepared. The plan we will be submitting to ED on May 16 will present an attractive approach for any schools having difficulty finding lenders willing to lend to their students. The Department has committed to complete their review of our plan within 30 days and implementation is targeted for no later than July 1.

Business Planning Initiatives

<u>Budget & Business Plan</u>: EDFUND management is actively engaged in its 2008-09 budget and business planning process. Uniquely challenging this year is developing the business plan and budget with EDFUND as a single-entity company, consistent with the state's plan to sell EDFUND. However, until the sale is final EDFUND and CSAC will continue adhering to the business planning process outlined in the operating agreement. This includes reviewing the budget and business plan components during May and June and submitting to the Board and Commission for final approval in late summer 2008.

Legislative Issues

Activity in Washington, DC during the first quarter of 2008 focused in four main areas: the federal budget process, reauthorization of the Higher Education Act, negotiated rulemaking for the College Cost Reduction and Access Act, and, most recently, Congressional efforts to deal with problems in the credit markets that are spilling into the student loan programs.

Budget

Both the House and Senate completed their respective Budget Resolutions prior to leaving Washington on March 14 for the Spring District Work Period. Upon their return in early April Congress began negotiations on a compromise proposal that, by Congressional standards, passed relatively quickly. On the education front, thankfully, there does not seem to be any more “unpleasant surprises” for the student loan programs and Congress wants to spend approximately $20 billion more on domestic programs than the President proposed in his FY09 spending plan. Approximately $5 billion will go toward education programs.

The next step will be the appropriations process, where the overall spending allocations contained in the Budget Resolution are translated into spending authorizations for specific programs. Student loans are, for the most part, immune from this process because the programs fall under “mandatory spending”. Student aid programs subject to the annual appropriations process include Pell Grants, the Perkins Loan Program, Federal Work-Study, SEOG and the campus-based programs. Due to the highly volatile political climate in Washington and the very slim majority the Democrats hold in the Senate, we may not see final appropriations bills until after the election.

Reauthorization

Staff began initial meetings early in the year to start to hammer out differences between the House and Senate reauthorization proposals. Despite long hours at the staff level, several major sticking points between the two bills have held up the process. Differences on “maintenance of effort” (where states are required to maintain a certain level of support for higher education or risk losing federal funding), college costs, student loan “sunshine-type” issues, and simplification of the FAFSA and the application process have delayed a final bill until at least May.

Congress had hoped to have the process wrapped up by March 14 (when they left for Spring Break) but these four issues have taken longer to sort out than expected and have delayed the process. As a result, Congress passed another extension of the Higher Education Act through May 31, despite the 10 AM – 7 PM daily meetings between House and Senate education staff and significant progress on reconciling the 700 page Senate and 900 page House reauthorization proposals. Some quietly admit that even May might be a stretch, bringing into question whether a final bill can move this session at all. Heavy floor calendars and the unofficial Memorial Day kick off of many Congressional re-election campaigns would likely mean that if a bill is not agreed before the end of May a (new) one-year extension would be necessary.

Negotiated Rulemaking

Miracles were in the air in the nation’s capitol this week, evidenced by the arrival of Pope Benedict XVI and an announcement from the Department of Education that negotiators had reached consensus on a proposed set of rules for the loan programs related to the College Cost Reduction and Access Act. Shortly after convening the extra fourth negotiation session in early April, negotiators agreed to accept the Department’s proposed regulatory language. The new provisions provide the regulatory framework for the new Income-Based Repayment program, economic hardship deferments, public service loan forgiveness, HEROS waivers/military deferments and the definition of not-for-profit holder. The Department will now develop a Notice of Proposed Rulemaking using the agreed-upon language which will then be followed by a an opportunity for public comment leading to the publication of a Final Rules package on or before November 1, 2008. The Final Regulations will then take effect on July 1, 2009.

Student Loan Credit Crisis
For more than a year now we've heard about problems in the sub-prime mortgage industry and how a number of factors, including higher interest rates and correction in prices in an inflated housing market, contributed to the situation. While there is generally no direct connection to mortgages and student loans, many non-profit, private and state-based lenders in the student loan programs use similar financing vehicles in order to raise the capital to make student loans. Because investors have become fearful of purchasing almost any type of securitized asset investments, they also became resistant to purchasing student loan assets and demanded higher rates of return from the student loan companies trying to sell the investments.

At the same time, lenders were dealing with two back-to-back years of significant cuts in the subsidies they receive from the federal government resulting from the Higher Education Reconciliation Act (HERA) and the College Cost Reduction and Access Act (CCRAA). The combination of the increased costs of securing capital in the credit markets (or an inability to secure capital at all) and the cuts in federal subsidies have made operating margins in the student loan market not only less profitable but in some cases even a losing proposition for lenders.

While most students have only felt the impact of these problems in the form of fewer borrower benefits and discounts, it is anticipated that the impacts of continued problems in the credit markets could eventually touch students in all sectors. For students attending higher priced institutions, lenders have already begun to tighten credit requirements and raise interest rates on private label (non federal) loans. Students who attend schools with lower graduation rates, short-term programs and/or higher cohort default rates are facing problems finding lenders that are willing to make even federal loans available.

Legislative Action
As news of the problems in the credit market began to reach Washington, Congressional leaders began to take notice. From the education policy perspective, House Education and Labor Committee Chairman, George Miller (D-CA), and Senate Health, Education, Labor and Pensions Chairman, Ted Kennedy (D-MA), held hearings in early spring to learn from the education community and the Department of Education the extent of the problem. The series of hearings resulted in both Chairmen introducing legislation that, while not "fixing" the problem, would provide some band-aid provisions for borrowers who may have problems finding willing lenders in the upcoming peak loan cycle. Mr. Miller's bill, HR 5715, was approved in committee in early April, on the House floor on April 17 and would:

- raise federal loan limits by $2,000 for most students;
- clarify the Secretary's authority to provide federal funds to guaranty agencies under the Lender of Last Resort program;
- give the Secretary the authority to act as a "secondary market of last resort" in cases where attempts to auction securitized loan portfolios fail; and
- temporarily prevent lenders from looking at negative credit reports resulting from medical expenses or mortgage default/foreclosure when considering credit eligibility for a PLUS loan.

Mr. Kennedy's bill contains some similar provisions, but when it passed the Senate, it contained provisions that closely paralleled the House-passed Miller bill. The final bill is now headed for signature by the President.

On the financial policy side, Representative Paul Kanjorski (D-PA) and Senator John Kerry (D-MA) have both introduced legislation that would provide what many analysts see as more of a solution to the core of the problem by giving state-based Federal Home Loan Banks the authority to step out of their role as financial facilitators for the mortgage markets to provide liquidity assistance to student lenders. Both sets of proposals have received bi-partisan support in both the House and the Senate and are moving through the legislative process.

Department of Education and Industry Actions

While lawmakers looked at legislative measures, the Department of Education was also working hard and fast within its scope of authority. As part of her testimony before the House Education and Labor Committee, Education Secretary Margaret Spellings assured Members that she is in talks with Treasury Secretary Paulson and will continue to explore possibilities working together. She also informed the Committee that the Department had some additional immediate capacity in the Direct Loan program should schools choose to switch to that program. Finally, she discussed the Department's efforts on preparing the LLR program for large-scale implementation, should it become necessary.

Since that time the Secretary has held a meeting with the guaranty agency community to discuss LLR and what the Department and the industry can do to put the infrastructure in place for a large-scale LLR program. All 35 guaranty agencies have joined the Secretary with a commitment to ensure a strong, streamlined LLR program is in place and that students who need LLR loans have them available in the coming academic year. EDFUND is actively engaged in this process and in discussions with the Department and our industry colleagues to ensure our customers and the students we serve receive the high level of service they have come to expect from EDFUND.

Default Fee

All four of the Client Solutions and Services regions are experiencing very positive reactions to our recently introduced default fee program. This program is helping us retain volume and is responsible for helping us get new loan volume, either at schools new to EDFUND or at schools that want to expand their lender list with the EDFUND guarantee. Many schools that don't qualify for the 0% default fee are choosing to remain with EDFUND because of the default aversion program and other services we provide.

Field staff believe we could have experienced even greater upside from this change if we had introduced it into the market sooner. EDFUND will work with the board on our 2009-10 default fee program in the fall, rather than waiting until January as we have in the past. Ideally we would want to announce our 2009-10 strategy by early December.

Customer Feedback

EDFUND was asked for recommendations when providing a response to an RFI. The Director of Financial Aid responded with the following,

> "I would be most happy to recommend EDFUND as a guarantor for any school wishing to add or change guarantors. I know that our university has been associated with EDFUND for around

4 years and in that time we have really enjoyed working with EDFUND from the customer service representatives in California, to our marketing representative, Sid Holloway.

We enjoy seamless guarantee services with the staff in California. If there are problems with a guarantee, the problems are resolved before we get to work the next day. These folks are wonderful!! We have also had opportunities for on-site training at our campus and these workshops have been beneficial to the Office of Financial Aid as well as the staff across our campus. Our marketing representatives have always been there to assist us as the need arises**. I can say without any reservation that EDFUND is a class company, but the people make it that way.** EDFUND always has knowledgeable staff on board, and that cannot be said about all guarantors as I have been in Financial Aid 16 years. EDFUND's website has many useful tools for students, high school counselors, and post-secondary schools. I highly recommend EdFund as a guarantor for any schools FFELP loan program."

Freed Hardeman University, Henderson, TN

Default Prevention Call Center

A borrower commended Loan Repayment Counselor, Julie Long, for her patience and dedication in helping her resolve her delinquency problem. Julie took the time to explain all of her options in order to bring her loan current.

A borrower included this compliment for Loan Repayment Counselor, Jesse Reyes, on their fax cover sheet: "I wanted to take a moment to thank you for all the time, accurate information and help. There are some customer service people that go the extra mile and you are certainly one of those special people."

Lender Relations

Lender Relations piloted an online lender-specific newsletter in the Midwest region this quarter. The newsletter keeps our lenders abreast of EDFUND offerings and service and provides them with local contacts to support their efforts in providing federal loans to students. This customized pilot newsletter is anticipated to expand nationwide over the next year.

Company Initiatives

Default Prevention Initiatives (DPI): EDFUND offers the Student Loan Debt Summary as a borrower benefit to EDFUND borrowers while in-school. This statement provides the borrower with a snapshot of their aggregate loan debt at the time the statement is generated. Effective October 1, we began providing this statement electronically to borrowers. In April we enhanced our ability for EDFUND to email the borrower directly, sending out close to 60,000 emails and increasing our Web site traffic for the two days during scheduled delivery of the email. This truly is a sign of the times and a new way to communicate with our borrowers. The online statement is updated monthly, providing a more accurate picture of a borrower's total indebtedness prior to graduation. This shift from paper to email generates a significant cost savings for EDFUND.

Financial Literacy: EDFUND has always provided education materials beyond the required loan counseling for borrowers but we are happy to report that for April's Financial Literacy Month we announced our newly expanded Building Futures ~ Financial Literacy modules. Spanning three topics, budgeting, savings and credit and offering a 100, 200, 300 or 400 series within the topics we cover something for everyone.

Training Initiatives: Customers continue to respond positively to the application of webinar technology to obtain quality training from EDFUND staff on a wide variety of Financial Aid topics.

New or Updated Publications

New Materials:

Just in time for April's Financial Literacy Month, EDFUND announced our newly expanded Building Futures ~ Financial Literacy modules. The materials are all available via our Web site, complete with a PowerPoint presentation and speaker notes. Schools may also supplement the material with a student workbook also available online. www.edfund.org/buildingfutures

In our desire to continue providing educational information in a cost effective manner, EDFUND converted several of our tri-fold brochures into rack cards, reducing printing and handling costs:

Credit card rack card
Credit Report rack card
Deferment and Forbearance rack card
NSLDS rack card

Conclusion

EDFUND's business and the entire student loan industry have faced a number of challenges over the past year and must be prepared to meet new ones in the years ahead. The sale of EDFUND and the continual changing external environment require EDFUND to review all aspects of its business to ensure that we are competitively positioned for a successful future.

Externally, we have stayed very close to pending legislation in order to be prepared to respond effectively to new demands in our industry. As a result, we have been adjusting our product and service offerings to our schools, lenders, and students. We were successful in obtaining the Department of Education's preliminary determination on a new Voluntary Flexible Agreement, providing Early Withdrawal Counseling to our most at-risk borrowers. We have also implemented our new Federal Default Fee strategy that positions EDFUND well in a highly competitive student loan marketplace. We listen attentively to our customer needs in order to be responsive and build long-term, mutually beneficial relationships.

Internally, we continue to assess our company and make appropriate adjustments so that we are operating in the most efficient and effective manner. After an extensive review of our internal organization, we did a company-wide restructuring to better align our business units, provide greater synergy and further strengthen EDFUND's financial position. This new structure realigns and consolidates the sales and customer servicing functions of our business within one division and the post delinquency functions within another division.

Even in uncertain times, EDFUND remains focused on the value we bring to students and schools and remains committed to providing the consistent levels of service they have come to expect from us.