

Action/Information Item

***Joint California Student Aid Commission
and EDFUND Board of Directors Workshop***

**Implementation of Commission's Response to
Bureau of State Audits (BSA) Audit**

A status update as of July 19, 2006 on progress in implementing the recommendations made by BSA in their recent performance review is provided in the agenda materials. Two items referenced in the update are also included. One is a draft request for proposal for consulting services to assist the Special Committee in delineating roles and responsibilities (see topic 5). The other is an analysis prepared by Sally Furay, Co-Chair of the Special Committee, of the recommendations presented in the 2005 performance review of EDFUND (see topic 10).

Recommended Action: Approval to engage a consultant to provide legal and financial advice to support the Commission in delineating the roles and responsibilities of the Commission and EDFUND.

Responsible Staff:

Diane Manning, VP of Audit Services

**Status Update for the Commission and EDFUND Board
Joint Workshop Held on July 26, 2006
(Update is as of July 19, 2006)**

1.	<p>Topic: Higher Education Reconciliation Act</p> <p><i>BSA Finding:</i> The federal Higher Education Reconciliation Act of 2005 could make it difficult for the FFEL Program to generate an operating surplus.</p> <p><i>BSA Recommendation:</i> Student Aid should continue to reassess the fiscal impact on the FFEL Program caused by changes in the federal Higher Education Act and the recent announcements made by some large guaranty agencies that they will pay the federal default fee for borrowers.</p> <p><i>Commission Chair's Summary Response on April 10, 2006:</i> ...given the potential impact on the market of anticipated federal default fee decisions, the Student Aid Commission intends to monitor EDFUND's forecasts and market assumptions closely.</p> <p><i>Commission Process Established on April 21, 2006:</i> Request the EdFund Board to require at its quarterly meetings explicit information on the effectiveness of EdFund forecasts and market assumptions from its Finance and Budget Committee, such reports to be forwarded to the Chair of the Commission's Fiscal Policy Committee and the Chair of the Commission.</p> <p><i>Status as of June 16, 2006 (required 60 day update to BSA):</i> The EDFUND Chief Financial Officer (CFO) will report in closed session on the effectiveness of EDFUND forecasts and market assumptions at the July 2006 Commission and Board workshop. The CFO will begin reporting such information as a standing agenda item at each subsequent Finance and Budget Committee meeting and quarterly Board meetings. Reports from such meetings will be forwarded to the Chair of the Commission's Fiscal Policy Committee and Chair of the Commission.</p> <p>Status as of July 19, 2006 for Commission/Board Workshop: Same status as of June 16.</p>
2.	<p>Topic: Other Federal Changes</p> <p><i>BSA Finding:</i> Other federal changes caused EDFUND to shift its strategy for collecting on defaulted student loans.</p> <p><i>BSA Recommendation:</i> Student Aid should monitor EDFUND's progress toward reducing its reliance on defaulted loan consolidations.</p> <p><i>Commission Chair's Summary Response on April 10, 2006:</i> EdFund has already adapted its collection strategies to conform to the HERA (Higher Education Reconciliation Act of 2005) even though the Act's new collection provisions take effect on October 1, 2006 and then later in 2009...., and the Student Aid Commission will monitor the actual collection revenues and the financial impact upon the Student Loan Operating Fund.</p> <p><i>Commission Process Established on April 21, 2006:</i> Request the EdFund Board to require at its quarterly meetings specific information on EdFund default collections from its Finance and Budget Committee, such reports to be forwarded to the Chair of the Commission's Fiscal Policy Committee.</p> <p><i>Status as of June 16, 2006 (required 60 day update to BSA):</i> The Vice President of Default Management will report in closed session on EdFund default collections at the July 2006 Commission and Board workshop. The Vice President will begin reporting such information as a standing agenda item at each subsequent Finance and Budget Committee meeting and quarterly Board meetings. Reports from such meetings will be forwarded to the Chair of the Commission's Fiscal Policy Committee.</p> <p>Status as of July 19, 2006 for Commission/Board Workshop: Same status as of June 16.</p>

<p>3.</p>	<p>Topic: Voluntary Flexible Agreement</p> <p><i>BSA Finding:</i> Student Aid may have lost the opportunity to receive millions in federal revenue because it failed to renegotiate its Voluntary Flexible Agreement promptly.</p> <p><i>BSA Recommendation:</i> Student Aid should ensure that critical tasks, including the renegotiation of its Voluntary Flexible Agreement with the U.S. Department of Education ...are completed.</p> <p><i>Commission Chair's Summary Response on April 10, 2006:</i> The ability to successfully conclude negotiations is to a large degree determined by the U.S. Department of Education...</p> <p><i>Commission Process Established on April 21, 2006:</i> Await action by the U.S. Department of Education, while keeping in touch with federal officials. If necessary, involve California administration officials once the Voluntary Flexible Agreement is forwarded by the Department's staff to the U.S. Secretary of Education. EdFund management will report immediately to the Board and Commission any new developments in the negotiations.</p> <p><i>Status as of June 16, 2006 (required 60 day update to BSA):</i> The EDFUND President and Acting CFO met with Department staff in Washington D.C. on May 5, 2006 to discuss the proposed Voluntary Flexible Agreement (VFA). No requests were made by the Department at that time, or subsequent to the meeting, to revise the agreement. Department staff is continuing to analyze the Commission's proposed VFA. To date, USED has not finalized the pending new agreements with the other three guaranty agencies which also maintain VFA's with the Department.</p> <p>Status as of July 19, 2006 for Commission/Board Workshop: EDFUND's President Kipp was informed by USED staff on June 29, 2006 that key management staff scheduled an internal meeting for July 7, 2006 to further discuss the proposed renegotiated VFAs of the four guaranty agencies. Staff also informed President Kipp that a recent reorganization within USED had redirected the Department's focus and that these individuals were now getting back to discuss the proposed VFAs. Since the June 29 discussion, EDFUND has been informed that USED staff expects to complete their review of all renegotiated VFAs by the end of July 2006 and will then present their analysis to the Secretary of Education for further consideration and public comment.</p>
<p>4.</p>	<p>Topic: Business Diversification</p> <p><i>BSA Finding:</i> Efforts to increase revenue through business diversification have not succeeded.</p> <p><i>BSA Recommendation:</i> Student Aid should ensure that critical tasks, including ...the development of a diversification plan, are completed.</p> <p><i>Commission Chair's Summary Response on April 10, 2006:</i> The Student Aid Commission intends to work with EDFUND to accomplish its business diversification objectives while taking into consideration the current financial position of the Student Loan Operating Fund and the limitations placed in the 2004 state law.</p> <p><i>Commission Process Established on April 21, 2006:</i> Delegate diversification exploration to the EdFund Chief Financial Officer. The CFO will report to the EdFund Board, Commission, and Executive Director at each regularly scheduled meeting with the goal of developing a diversification plan.</p> <p><i>Status as of June 16, 2006 (required 60 day update to BSA):</i> EDFUND's vacant CFO position was filled effective June 1, 2006. The CFO will make his first report on developing a diversification plan at the August 2006 Board meeting. The CFO will then report such matter as a standing agenda item to the EdFund Board, Commission, and Executive Director at each subsequent regularly scheduled meeting.</p> <p>Status as of July 19, 2006 for Commission/Board Workshop: Same status as of June 16, however, the CFO will also make a brief presentation at the July 26 workshop.</p>

5. Topic: Operating Agreement

BSA Finding: Student Aid and EDFUND have been unable to agree on a new operating agreement for the FFEL program that delineates their respective roles.

BSA Recommendation: Student Aid should ensure that the roles and responsibilities it delineates for itself and EDFUND do not inappropriately cede its statutory responsibilities to EDFUND.

Commission Chair's Summary Response on April 10, 2006: The Student Aid Commission decided to renew the existing single-year operating agreement until it makes a final determination about the appropriate roles and responsibilities of both organizations. The Commission believes the two issues – the operating agreement and the roles and responsibilities upon which it must be crafted – are inextricably intertwined.

Beginning with a more detailed clarification of the respective roles and responsibilities of the Commission and EDFUND, the Student Aid Commission will work to develop policies and definitions to ensure that its own oversight mandate and EDFUND's operational role are managed effectively under both with state and federal law.

Commission Process Established on April 21, 2006: Establish a Special Committee co-chaired by Commissioners James Sandoval and Sally Furay. This committee is responsible for developing a final draft of roles and responsibilities and a new draft Operating Agreement for review and approval by the Board and Commission. This Special Committee is also responsible for overseeing completion of the 2005 Performance Review tasks (see Topic 10). Additionally, this Special Committee is responsible for overseeing the establishment of appropriate verification and reporting processes and expectations of the oversight division (see Topic 9). The Special Committee may appoint subcommittees to assist in carrying out its responsibilities.

Status as of June 16, 2006 (required 60 day update to BSA): The Special Committee met on May 25, 2006 to discuss an initial process for addressing the responsibilities assigned by the Commission described above. The Committee requested CSAC and EdFund staff to provide certain information for the Committee which is currently being collected. Further direction and assignments will be made at the next meeting scheduled for June 19, 2006. The Special Committee is currently co-chaired by Commissioners Sally Furay and Dean Johnston. This effort is expected to be ongoing for the next few months until completion.

Status as of July 19, 2006 for Commission/Board Workshop: The Special Committee met via teleconference on June 19, 2006 to discuss the information requested at the last meeting held on May 25. The Special Committee determined that sufficient information had been provided by Commission and EDFUND staff to support hiring an outside consultant with legal and financial expertise to assist the Committee in further delineating the roles and responsibilities. The work performed by the consultant is needed by the Committee in drafting a new Operating Agreement. The Special Committee recommended to the Commission on June 23 that the Committee move forward to develop a request for proposal (RFP) for such consulting services. The Commission approved the recommendation and asked to see the RFP once developed. The RFP is included in the workshop materials.

<p>6.</p>	<p>Topic: Concerns Raised Regarding Accomplishment of Performance Goals</p> <p><i>BSA Finding:</i> Student Aid has not fully addressed concerns raised by an assessment of EDFUND's accomplishment of performance goals.</p> <p><i>BSA Recommendation:</i> Student Aid should follow through on issues raised by its staff regarding EdFund's operations.</p> <p><i>Commission Chair's Summary Response on April 10, 2006:</i> The Student Aid Commission's executive director and the EdFund president are working to review the methodology for measuring year-end performance under the performance goals and metrics agreed to by the Student Aid Commission and EDFUND. Meetings to discuss the measurement standards are already scheduled for April 2006 and the Commission will await the results of those meetings before developing its actions related to the assessment of EDFUND's performance goals.</p> <p><i>Commission Process Established on April 21, 2006:</i> The Executive Director of the Commission and the EdFund President will set policy on performance goals, methodology, and metrics for the 2006-2007 federal fiscal year. This information will be provided to the Commission by June 1, 2006.</p> <p><i>Status as of June 16, 2006 (required 60 day update to BSA):</i> Discussions are ongoing between the Executive Director and President. The Commission's Fiscal Policy and Long-Range Planning Committee or a special committee may be tasked to work with the Executive Director and President on remaining areas of divergence in order to finalize the policy within the next few weeks.</p> <p>Status as of July 19, 2006 for Commission/Board Workshop: The Commission Chair, Executive Director, and President met on July 11 to discuss and agree upon certain aspects of the performance goal calculation for FY 05-06. The Executive Director is drafting the 05-06 policy for performance goals, methodology, and metrics for review by the EDFUND President before presenting the policy to the Commission. The final policy approved by the Commission for 05-06 and input from Watson Wyatt (see Topic 11) may influence the policy for 06-07 which should be established prior to the beginning of the new federal fiscal year (October 1, 2006).</p>
<p>7.</p>	<p>Topic: Relinquishing Oversight Circumvented State Law</p> <p><i>BSA Finding:</i> Student Aid circumvented state law by erroneously relinquishing a key oversight responsibility to the EDFUND Board.</p> <p><i>BSA Recommendation:</i> Student Aid should rescind its delegation of the approval authority of EDFUND's detailed operating budget to the EDFUND board.</p> <p><i>Commission Chair's Summary Response on April 10, 2006:</i> To the extent that the Commission's action has been interpreted as delegating the approval of the budget to EDFUND, such delegation was not the Commission's intent. Consequently, the chair will schedule action for the Commission to clarify its intent.</p> <p><i>Commission Process Established on April 21, 2006:</i> At the Commission's June meeting, the Chair of the Commission will schedule action to clarify the Commission's intent.</p> <p><i>Status as of June 16, 2006 (required 60 day update to BSA):</i> At the June 22, 2006 Commission meeting, the Commission will formally make it clear that it retains its approval authority of the EDFUND budget.</p> <p>Status as of July 19, 2006 for Commission/Board Workshop: On June 22 the Commission rescinded the Commission's delegation of the approval authority of EdFund's detailed operating budget to the EdFund Board. Implementation of BSA's recommendation is now complete.</p>

<p>8.</p>	<p>Topic: Business Plans and Budget Unaddressed Concerns</p> <p><i>BSA Finding:</i> Student Aid approved EDFUND's federal fiscal years 2005 and 2006 business plans and budget despite several unaddressed concerns.</p> <p><i>BSA Recommendation:</i> Student Aid should follow through on issues raised by its staff regarding EdFund's operations.</p> <p><i>Commission Chair's Summary Response on April 10, 2006:</i> The chair of the Student Aid Commission intends to direct the Commission's Fiscal Policy Committee to establish a process and appropriate dates for the evaluation of Commission staff recommendations on the EDFUND business plan and budget to ensure the timely submission and consideration of these recommendations.</p> <p><i>Commission Process Established on April 21, 2006:</i> The Commission's Fiscal Policy Committee will seek recommendations from EdFund management and CSAC staff and propose to the Commission a schedule to ensure timely submission and consideration of EdFund's business plan and budget. This proposed schedule will be submitted to the Commission by June 1, 2006.</p> <p><i>Status as of June 16, 2006 (required 60 day update to BSA):</i> To address BSA's recommendation to follow through on issues raised by staff regarding EDFUND's business plans and budget for federal fiscal years 2005 and 2006, EDFUND fully analyzed CSAC staff's recommendations. The issues were then discussed in detail by the Board, CSAC staff responsible for EDFUND oversight, and EDFUND staff at the May 2006 Board workshop. A final schedule for submission and consideration of EDFUND's federal fiscal year 2007 business plan and budget has not yet been finalized. However, EDFUND's draft business plan and budget have been provided to Commission staff for review.</p> <p>Status as of July 19, 2006 for Commission/Board Workshop: Commission staff has received EdFund's 06-07 draft business plan and budget. The EDFUND Finance and Budget Committee will review the documents and input from Commission staff at their August 3 meeting and will make a recommendation to the Board at the August 18 meeting. The Commission's Fiscal Policy and Long-Range Planning Committee will meet soon after August 18 to review and approve EDFUND's business plan and budget and then make a recommendation to the Commission at the September 7 – 8 meeting.</p>
<p>9.</p>	<p>Topic: Independently Verify Reports</p> <p><i>BSA Finding:</i> Student Aid does not independently verify the reports submitted by EDFUND.</p> <p><i>BSA Recommendation:</i> Student Aid should require staff to independently verify the accuracy of the reports submitted by EDFUND.</p> <p><i>Commission Chair's Summary Response on April 10, 2006:</i> The Student Aid Commission concurs with the Report's recommendation and will establish appropriate verification and reporting processes, including examining whether the operating agreement needs to address such processes.</p> <p>In light of the finding posed in this audit, the Commission is committed to revising and clarifying its roles and responsibilities, including the expectations of the oversight division.</p> <p><i>Commission Process Established on April 21, 2006:</i> These issues will be addressed by the Special Committee described in Topic 5.</p> <p><i>Status as of June 16, 2006 (required 60 day update to BSA):</i> These issues have been assigned to the Special Committee. See status under Topic 5.</p> <p>Status as of July 19, 2006 for Commission/Board Workshop: Same status as of June 16.</p>

10. Topic: Acting Upon Key Tasks in Performance Review

BSA Finding: Student Aid has not acted upon key tasks identified in its performance review of EDFUND.

BSA Recommendation: Student Aid should complete key tasks outlined in the June 2005 mandated performance review of EDFUND.

Commission Chair's Summary Response on April 10, 2006: The chair of the Student Aid Commission intends to request the members of the Commission to convene a committee to oversee the timely development of a new operating agreement. The operating agreement is the means by which the vast majority of the Commission's actions with respect to the performance review recommendations are to be adopted. To inform that process, the Commission will review the key tasks outlined in the June 2005 performance review and direct its staff and EDFUND to develop action plans in accordance with its conclusions.

Commission Process Established on April 21, 2006: This issue will be addressed by the Special Committee described in Topic 5.

Status as of June 16, 2006 (required 60 day update to BSA): This issue has been assigned to the Special Committee. See status under Topic 5.

Status as of July 19, 2006 for Commission/Board Workshop: Sally Furay, Co-Chair of the Special Committee, prepared an analysis dated May 30, 2006 of the recommendations presented in the 2005 Performance Review of EDFUND. The analysis is included in the workshop materials.

11. Topic: Executive Salary Determination

BSA Finding: EDFUND's policy does not meet federal requirements for executive salary determination; nor does it comply with its own policy.

BSA Recommendation: Student Aid should ensure that EDFUND complies fully with federal regulations and its policy governing salary setting for its executives, including modifying its policy to address board members who have a conflict of interest and ensuring that its consultants compile comparable compensation data solely from similar financial related organizations.

Commission Chair's Summary Response on April 10, 2006: Consistent with the findings in this Report, the Commission will request the EDFUND Board of Directors to evaluate the compensation comparison methodology and to employ expert counsel to advise it on whether the comparison methodology it adopts satisfies federal requirements for tax-exempt organizations.

We agree that EDFUND should comply with its policy requirement that the executive committee of the Board maintain detailed minutes describing the salary determination process, including the avoidance of a conflict of interest by any board member, as required by its Bylaws and corporate policy.

Commission Process Established on April 21, 2006: Officially request the EdFund Board to seek advice of outside legal counsel on the adequacy of the compensation comparison methodology used by EdFund in meeting federal requirements for nonprofit tax-exempt organizations. The Board's minutes described above will be available to the Commission.

Status as of June 16, 2006 (required 60 day update to BSA): A request for proposal was provided to eight compensation consulting firms on May 26, 2006 to assist the Board in reviewing the existing salary policy and process and recommend modifications, if needed, to ensure that EDFUND complies with federal and state requirements for nonprofit tax-exempt organizations. A firm will be selected by June 23, 2006 and the work is expected to begin by July 3, 2006. The firm will be required to provide preliminary draft policies to the Board's Personnel and Nominations (PEN) Committee by August 4, 2006. Additionally, a legal firm will be retained to provide a written legal opinion that the proposed compensation policies would fully comply with all applicable federal and state regulations. The legal firm will be required to provide this opinion on proposed policies by August 18, 2006. The PEN Committee will recommend policies for Board approval at the August 2006 Board meeting. The Board will recommend policies to the Commission's PEN Committee and Commission at their September 2006 meetings.

Status as of July 19, 2006 for Commission/Board Workshop: The consulting firm of Watson Wyatt was selected in June 2006 to assist the EDFUND Personnel and Nominations (PEN) Committee in reviewing the existing salary policy and process and recommend modifications to ensure that EDFUND complies with federal and state requirements for nonprofit tax-exempt organizations. Watson Wyatt will provide preliminary draft policies to PEN at the Committee's August 2006 meeting. Additionally, legal counsel will be retained to provide a written legal opinion that the proposed compensation policies fully comply with all applicable federal and state regulations. The PEN Committee will recommend policies to the Board and the Board will then present its recommendations to the Commission's PEN Committee which in turn will present recommendations to the Commission.

12. Topic: Incentive Compensation

BSA Findings:

- Student Aid's policy regarding EDFUND executive incentive compensation is flawed. Student Aid allows EDFUND's Executive Management Team to receive substantial bonuses even with an operating deficit. The policy specifically excludes certain loan program revenues and expenses.
- The board's determination of the total bonus amount for vice presidents appears inconsistent.
- EDFUND uses high-level organizational metrics to measure its performance and award incentive compensation to non-executive employees.

BSA Recommendations:

Student Aid should:

- Ensure that EDFUND determines bonuses for its president in accordance with Student Aid's policy.
- Modify its policy statement and guidelines memorandum entitled "EDFUND incentive Compensation Plans" to ensure that EDFUND's executive management team does not receive a bonus if the FFEL Program or Operating Fund realizes a deficit.
- Ensure that EDFUND includes all FFEL Program revenues and expenses in its calculation of the program's operating surplus or deficit.
- Ensure that it and EDFUND's board establish guidelines to use when approving the total bonus pool amount of EDFUND's executive management team.
- Direct its executive director and EDFUND's president to resolve outstanding issues related to the methodology used to measure EDFUND's performance which affects the bonuses for its non-executive employees.

Commission Chair's Summary Response on April 10, 2006: The chair of the Student Aid Commission will schedule meetings for the Commission to examine its policy for the approval of incentive compensation and make corresponding changes in the Operating Agreement.

Commission Process Established on April 21, 2006: In the light of the BSA comments, request the EdFund Board to review, with its management, all aspects of the incentive compensation policy approved by the Commission in August, 2002, and propose appropriate adjustments to the Commission's PEN Committee and the Commission for their review and approval before the end of the fiscal year, so that any changes may become effective in fiscal 2006-2007.

Status as of June 16, 2006 (required 60 day update to BSA): The request for proposal provided to the eight compensation consulting firms described in Topic 11 above also requests the selected firm to review the existing Commission policy on EDFUND incentive compensation plans and recommend changes to the policy. The same schedule described in Topic 11 applies to addressing incentive compensation. The Executive Director and President have been directed to discuss and resolve the outstanding issues related to the methodology used to measure EDFUND's performance which affects bonuses for non-executive employees. This discussion is currently in process.

Status as of July 19, 2006 for Commission/Board Workshop: As indicated above, Watson Wyatt will review the Commission's existing policy on EDFUND's compensation plans and recommend any changes.

<p>13.</p>	<p>Topic: Spending Practices</p> <p><i>BSA Finding:</i> EDFUND's imprudent spending practices</p> <p><i>BSA Recommendations:</i></p> <p>Student Aid should:</p> <ul style="list-style-type: none"> ▪ Closely monitor EDFUND expenses paid out of the Operating Fund for conferences, workshops, all-staff events, travel, and the like. Discontinue using Operating Fund money to pay for expenses related to non-employees attending its company functions. ▪ Ensure that reimbursements to commissioners for their expenses are not excessive. <p><i>Commission Chair's Summary Response on April 10, 2006:</i> The Commission will request the EDFUND Board of Directors to propose for the Commission's consideration a policy that governs the expenses and scope of the employee conferences, employee recognition events, and the appropriate costs of annual Board of Director workshops.</p> <p><i>Commission Process Established on April 21, 2006:</i> Commission process is already identified in the Chair's Summary Response above.</p> <p><i>Status as of June 16, 2006 (required 60 day update to BSA):</i> At the time of the BSA report in April 2006, President Kipp directed all EDFUND Vice Presidents to employ cost conscious practices for employee conferences, Board meetings, and the like. Guidelines for spending are currently being reviewed and will be proposed to the Board and Commission when completed.</p> <p>Status as of July 19, 2006 for Commission/Board Workshop: Draft spending guidelines will be presented to the EDFUND Finance and Budget Committee at the August 3 meeting. Decisions made by the Committee will then be presented to the Board and Commission for further consideration.</p>
<p>14.</p>	<p>Topic: Travel Policy</p> <p><i>BSA Finding:</i> Student Aid did not ensure that EDFUND's travel policy was fiscally conservative; in some instances, EDFUND and Student Aid did not comply with their travel policies.</p> <p><i>BSA Recommendation:</i> Student Aid should amend its operating agreement to require EDFUND to establish a travel policy that is consistent with the State's policy.</p> <p><i>Commission Chair's Summary Response on April 10, 2006:</i> The findings and recommendations in the Report with respect to EDFUND's travel policies will be reviewed and deliberated by the Commission. In that review, the Commission intends to consider EDFUND's status as a nonprofit corporation and its competitive role in the marketplace. Additionally, the chair of the Commission and the chair of the EDFUND Board will direct management in each organization to establish processes to ensure compliance with the travel policy exceptions noted in the Report.</p> <p><i>Commission Process Established on April 21, 2006:</i> The Commission will request of the EdFund Board a complete review of all aspects of the current travel policy, with current practice and any adjustments or changes to be fully explained and documented prior to submission to the Commission for its review and approval.</p> <p><i>Status as of June 16, 2006 (required 60 day update to BSA):</i> The directive from President Kipp cited in Topic 13 above also focused on fully enforcing the existing travel policy. The current travel policy is under review with results to be proposed to the Board and Commission when completed.</p> <p>Status as of July 19, 2006 for Commission/Board Workshop: A draft travel policy will be presented to the EDFUND Finance and Budget Committee on August 3. Decisions made by the Committee will then be presented to the Board and Commission for further consideration.</p>

<p>15.</p>	<p>Topic: Contracting Policies</p> <p><i>BSA Finding:</i> EDFUND contracting policies are vague and lead to frequent non-compliance.</p> <p><i>BSA Recommendations:</i></p> <p>Student Aid should:</p> <ul style="list-style-type: none"> ▪ Ensure that EDFUND follows through on its efforts to revise its contracting policies. ▪ Amend its operating agreement to require purchases of goods and services incurred by EDFUND to be reimbursed pursuant to procurement and contracting policies approved by the executive director of Student Aid. <p><i>Commission Chair's Summary Response on April 10, 2006:</i> EDFUND is in the process of improving its contracting policy to require documentation to be maintained by contract officers, to improve the quality of information provided for sole source justifications and cost-benefit analysis, and to ensure that work is not initiated or approved in advance of obtaining signed contract documents. The chair will request a report to be submitted to the Commission with respect to actions taken by EDFUND.</p> <p><i>Commission Process Established on April 21, 2006:</i> The Commission will request the EdFund Board to revise and tighten EdFund's contracting policies in the immediate future, and submit a report to the Commission by its September, 2006 meeting that this has been accomplished and reviewed by the EdFund Board.</p> <p><i>Status as of June 16, 2006 (required 60 day update to BSA):</i> A new policy has been drafted. EDFUND's General Counsel and CFO will review and further refine the policy before presenting a final draft to the Board at their August 2006 meeting. The Board will then submit a report to the Commission by its September 2006 meeting for review and approval.</p> <p>Status as of July 19, 2006 for Commission/Board Workshop: Same status as of June 16.</p>
<p>16.</p>	<p>Topic: Closed Session Meetings</p> <p><i>BSA Finding:</i> The EDFUND Board has violated state law governing closed session meetings.</p> <p><i>BSA Recommendations:</i> Student Aid should ensure that EDFUND complies with the Bagley-Keen Act record-keeping requirements by maintaining a confidential minute book of the business discussed during its closed sessions. In addition, Student Aid and EDFUND should establish policies and procedures to help ensure that closed sessions are conducted within the board's authority as required by state law. These policies and procedures should provide the board and staff with clear guidelines in defining trade secrets and business proprietary information that can be discussed during closed sessions so that no further violations of state law occur.</p> <p><i>Commission Chair's Summary Response on April 10, 2006:</i> We agree that the EDFUND Board should have been maintaining a confidential minute book of the matters discussed in its closed sessions. The EDFUND Board started complying with that requirement with its 2006 meetings.</p> <p><i>Commission Process Established on April 21, 2006:</i> EdFund has already begun to keep minutes of closed sessions, as of the beginning of 2006. The confidential minute-book will be available for monitoring by the Commission.</p> <p><i>Status as of June 16, 2006 (required 60 day update to BSA):</i> Completed.</p>

17. Topic: Internal Audit

BSA Finding: The independence of the internal audit functions at Student Aid and EDFUND may be compromised.

BSA Recommendations:

Student Aid should:

- Replace its current chief of internal audits with an individual who is free from the appearance of organizational and personal impairments to independence.
- Ensure that it complies with IIA (Institute of Internal Auditors) and government auditing standards that require an external assessment of its internal audits unit.

Commission Chair's Summary Response on April 10, 2006: The internal auditor was temporarily placed in charge of the Legal Division's invoices and employee timesheets while the search for a replacement vice president of legal services is underway. Because of BSA's concern that this might create a potential impairment of the internal auditor's independence, EDFUND discontinued that practice.

The Report also finds that the internal auditor should not have an executive management role in either the Student Aid Commission or EDFUND. While the internal auditor's participation as an executive management team member could enhance executives' awareness of essential compliance issues, we will evaluate whether it would be more appropriate for this role to be advisory and non-voting. The Student Aid Commission must also examine whether it requires its own separate internal auditor.

Commission Process Established on April 21, 2006: The Commission's Audit Committee will review all aspects of the current roles and responsibilities of the internal auditor, and recommend to the Commission whether there should be separate internal auditors for the Commission and EdFund.

Status as of June 16, 2006 (required 60 day update to BSA): The Commission's Audit Committee is scheduled to meet on June 20, 2006 to discuss the BSA findings regarding the internal audit function. The Committee will present the results of their initial discussions to the Commission at the June 22, 2006 Commission meeting.

Status as of July 19, 2006 for Commission/Board Workshop: On June 22, the Commission Audit Committee recommended to the Commission, which the Commission approved, separation of the internal audit function between the Commission and EDFUND and to hire a new internal auditor for the Commission.

The Commission was informed that the Audit Committee intends to engage an outside audit firm to perform an assessment of the internal audit function in fiscal year 07-08 following the Institute of Internal Auditors standards as recommended by BSA.

18. Topic: Composition of EdFUND Board

BSA Finding: The composition of the EDFUND Board could impair Student Aid's decision making.

BSA Recommendations:

Student Aid should:

- Consider removing Student Aid commissioners from the EDFUND board.
- Consider changing the Student Aid executive director's role on the EDFUND board from a voting member to a non-voting member.

Commission Chair's Summary Response on April 10, 2006: In the context of the findings in this Report that Student Aid Commission members or the executive director serving as EDFUND Board of Directors may impact their independent decision-making roles, the Commission will evaluate the appropriate composition of the EDFUND Board.

Commission Process Established on April 21, 2006: The Commission's PEN Committee, with outside assistance as needed, will review all aspects of the composition of the board of a nonprofit corporation, the issue of a state agency with an auxiliary entity, and the needs of the Commission itself for both oversight and information - then offer a recommendation to the Commission.

Status as of June 16, 2006 (required 60 day update to BSA): Initial discussions regarding the composition of the EDFUND Board is planned for the June 22, 2006 Commission workshop. The PEN Committee will then work through the issue and present a recommendation to the full Commission by the September 2006 Commission meeting.

Status as of July 19, 2006 for Commission/Board Workshop: At the June 22, 2006 Commission meeting, the Commission voted and approved a change in the composition of the Edfund Board of Directors to include only one Commissioner and to change the Executive Director's role on the EdFund Board from a voting member to a non-voting member. The EdFund bylaws must be revised to incorporate these changes.



**REQUEST FOR PROPOSAL
FOR
CONSULTING SERVICES
RFP #xxxxx**

Contract Manager: (person), (title)
(division/dept.)
Phone: 916-526-xxxx
E-mail: [XXXXXXXXX](#)

Proposal due: August xx, 2006
No later than 5:00 P.M.

Number of copies: Original plus five copies

**California Student Aid Commission
10834 International Drive, Rancho Cordova, CA 95670**

I. Background

The California Student Aid Commission (Commission) has been serving California students and families with financial aid services for more than 50 years. The Commission is the principal state agency responsible for administering state grants.

In 1977, the Commission's responsibilities significantly expanded when it became California's designated guaranty agency for the Federal Family Education Loan (FFEL) Program. The Commission's role changed in 1996, however, when the Legislature enacted AB 3133 authorizing the Commission to establish an auxiliary organization for the purpose of administering the FFEL Program on its behalf. The Commission sought the authority to create an auxiliary to resolve conditions that threatened to force the Commission out of the FFEL Program altogether, including: inadequate customer service; deficient and unstable technology systems; and substantial unresolved federal and state audit issues.

The Commission created EDFUND, a nonprofit public benefit corporation, in 1997 as a result of AB 3133. Ever since, the state has relied on this two-entity model of the Commission administering the state grant programs and EDFUND administering the FFEL Program on behalf of the Commission. A remarkable aspect of AB 3133 is that the Commission/EDFUND enterprise has become the second largest FFEL Program guaranty agency nationally.

This new structure became a successful example of converting a program administered totally within the state system to one administered as a business enterprise in a nonprofit corporate structure linked to the state. The Commission retains responsibility for financial aid policy leadership and FFEL Program oversight. Additionally, the Legislature granted the Commission custody and control of operating funds generated through the FFEL Program. EDFUND's functions are limited to activities consistent with the Commission's mission, goals, and provisions within an operating agreement. (See Exhibit 1 – Operating Agreement in effect since 2002.)

As a guaranty agency, the Commission through EDFUND is responsible for ensuring that federally-insured loans are issued to eligible students attending eligible postsecondary educational institutions and that loans are borrowed through an approved FFEL Program lender. A guarantor also has specific responsibilities relating to the maintenance of borrower account information, for securing borrower repayment of delinquent and defaulted loans, and for payment of claims submitted by lenders when a borrower defaults. A guarantor may be either a state agency or a nonprofit corporation and is authorized to contract with third-party services for program administration. The U.S. Department of Education (USED) designates a guarantor for each state. The designation as a guarantor for a state is non-exclusive; that is, an educational institution may choose to work with any participating guarantor. The Commission through EDFUND is the designated state guarantor for California and also provides guarantee services nationwide.

The Commission and EDFUND have separate governing bodies. The California Student Aid Commission is governed by a 15-member commission which is entrusted with nominating and appointing a Board of Directors for EDFUND. This organizational structure has, at times, caused tension since the Board is given substantial operational responsibilities but no ultimate authority.

The Legislature placed relatively few constraints on the management of the FFEL Program and EDFUND as an auxiliary of the Commission. Instead, the Legislature granted broad powers to the Commission and the EDFUND Board. Consistent with the statutory constraints placed on it, the Commission has generous flexibility to govern EDFUND and the loan program.

State law has not adequately delineated which entity is responsible for which operational functions which have led to disagreements about each entity's appropriate roles and responsibilities. Additionally, no framework has been established which specifies the method by

which the Commission and Commission staff conduct oversight activities over EDFUND operations. Although the operating agreement between the Commission and EDFUND address some delineation of responsibilities, many provisions are subject to competing interpretations. What appears to be vigilant oversight and meaningful accountability from some parties' point of view has appeared as micro-management and counterproductive interference from others' point of view.

II. SCOPE OF WORK AND SERVICE DELIVERY REQUIREMENTS

The Commission is seeking external consulting assistance in collecting data and providing input regarding roles and responsibilities of the two organizations that will help the Commissioners in drafting a new Operating Agreement between the Commission and EDFUND.

The consultant selected must have legal and financial management expertise to assist the Commission in this effort. The consultant must also have extensive knowledge in federal, state and non-profit reporting and oversight regulatory requirements.

The scope of work and service delivery required of the consultant includes, but is not limited to, the following:

1. Review documentation developed by EDFUND staff which identifies current federal, state, and non-profit reporting and information sharing activities made available by EDFUND to Commission staff. (See Exhibit 2.)
2. Review documentation developed by Commission staff of oversight activities performed by Commission staff.
3. Interview key EDFUND and Commission staff, Commissioners, Board members and relevant stakeholders to validate information provided by staff and to identify gaps in reporting and oversight activities.
4. Identify ineffective, inefficient, and redundant reporting and oversight activities.
5. Identify gaps in regulatory reporting and oversight activities.
6. Provide a framework that defines the oversight activities that should be conducted by Commission staff. This framework should include, but not be limited to, the types of information and activities that should be regularly reviewed, the timing of such activities, and the reporting of oversight results to the applicable Commission Committee.
7. Recommend staffing requirements for the oversight function which should include, but not be limited to, number of staff and expected skill sets.

III. KEY DATES

The consultant should consider the following key dates developing a proposed schedule for the project:

- Documentation review and interviews with key staff, Commissioners, Board members, and relevant stakeholders – no later than August xx, 2006
- Identification of ineffective, inefficient, and redundant reporting and oversight activities in addition to gaps in existing activities (deliverable)– no later than September xx, 2006
- Framework and staffing requirements for the oversight function (deliverable) – November xx, 2006

IV. PROPOSAL RESPONSE

The proposal must reflect the consultant's capability to satisfy the requirements of this request for proposal. The written proposal must include the following elements:

1. Background information on the consultant:
 - a. Experience in providing legal and financial analysis in reporting and oversight activities.
 - b. Location of office that will have primary responsibility for the effort.
2. The consultant's approach and management of the services.
3. The consultant's proposed timeline which identifies, but is not limited to, key milestones and deliverables.
4. A statement that the proposed fee is an amount not-to-be-exceeded and that the consultant will obtain written approval from the Commission prior to the incurrence of any additional effort beyond the proposed hours. The consultant will not request payment for additional hours if this process is not followed.
5. Resumes of each engagement team member are to be included in an appendix to the proposal.
6. Reference list of current clients who may be contacted regarding your services. Provide at least three references. Include the name and title of the contact person and telephone number along with a description of the service provided.

V. ADMINISTRATIVE INFORMATION

The Commission intends to award a contract to the bidder who the Commission believes will provide the best quality of services for the best price. The Commission is not bound to "low bid", but will consider all factors which provide the best value for services, including price, references submitted, etc.

The proposal must be submitted to *(name of contract manager)*, no later than August XX, 2006; 5:00 p.m.

For overnight deliveries, and hand deliveries, proposals should be addressed to:

(name of contract manager)
California Student Aid Commission
10834 International Drive
Rancho Cordova, CA 95670

Issuance of the consultant's proposal in no way constitutes a contract or a commitment by the Commission. The Commission reserves the right to reject the proposals and/or request clarification of information submitted by the consultant. The Commission further reserves the right to reject any oral responses or portions thereof received in response to this document if the Commission determines that it is in its best interest to do so. The Commission may reject any consultant's responses which are conditional, incomplete, or that contain any material deviations from the request for proposal requirements. Finally, the Commission reserves the right to modify its requirements based on the consultant's response to this request for proposal.

VI. OWNERSHIP OF REPLIES

All materials supplied in response to this request for proposal become the property of the Commission, and may at any time, subsequent to the notification of the intent to amend the contract, be reviewed and evaluated by any persons. These materials may be returned only at the Commission's option and at the consultant's expense.

VII. CONTRACT REQUIREMENTS

Awarding of a contract will require execution of a contract with the Commission. Standard terms will be included as part of the contract and are not subject to modification or deletion except as necessary to carry out the purpose of the contract. These terms include, but are not limited to the following:

1. This request for proposal shall be incorporated and made a part of the final agreement, and all terms and conditions herein shall be a part of the final contract.
2. Termination/Revocation - Either party may revoke or otherwise terminate this Agreement, upon reasonable cause, by notifying the other party in writing of their intention to take such action. Any such writing shall be sent to the other party by certified mail, return receipt requested, and shall be effective ten (10) days after the date of mailing. The grounds for reasonable cause shall include: material violations of this Agreement, and/or any act exposing the other party to liability for personal injury or property damage. In the event of termination, the Commission shall be obligated to pay the Contractor only for services rendered up to the effective date of termination.

In addition, the Commission may terminate this Agreement immediately without prior notice if the Contractor commits an act of fraud, dishonesty, or any other act of negligent, reckless or willful misconduct in providing services to the Commission.

3. Any necessary travel shall be approved in advance by the Commission's contract manager. Travel shall be reimbursed in accordance with the state Travel and Per Diem Schedule, which will be incorporated and made part of the agreement.
4. Safeguards and Security – All financial, statistical, personal, technical and other data or information relating to EDFUND's operations which is considered confidential as defined by law or is designated as confidential and/or proprietary by EDFUND, and made available to the Contractor in order to carry out this contract, shall be protected by the Contractor from unauthorized use, disclosure or destruction through the observance of all applicable federal and state information security, and confidentiality laws and procedural requirements.

The Commission looks forward to receiving your response. Please contact *(the contract manager)* at 916-526-XXXX or *(email of contract manager)* if you have any questions.

May 30, 2006
SMF

California Student Aid Commission
RECOMMENDATIONS in PERFORMANCE REVIEW OF EDFUND
June, 2005

Recommendations in the California Student Aid's Commission June, 2005 Performance Review of EdFund have been analyzed to ascertain whether there are aspects of those recommendations which have not been included in the BSA Report or the Commission's Process document of April 21, 2006, but which still need attention/action from the Commission and EdFund. Only actual recommendations have been included in this analysis, not narrative points which the Commission chose not to include in the recommendations themselves.

The Bureau of State Audits, in its report of mid-April, 2006 repeated verbatim the first seven bullets (page 65) in the list of recommendations of the June, 2005 Performance Review, as follows (page 2):

- Re-examine the basic assumptions of the current business model.
- Re-evaluate technology and services.
- Re-assess marketing strategies.
- Undertake a thorough organizational risk assessment in relation to the existing portfolio and future growth strategies.
- Renegotiate its Voluntary Flexible Agreement with the U.S. Department of Education.
- Maximize the efficiency and effectiveness of its collection recoveries on student loans that default.
- Continue to explore business diversification options.

All of these items are included in the formal BSA recommendations on page 76 of the BSA Report. Because the BSA Report (page 76) specifies: "Complete key tasks outlined in the June 2005 mandated performance review of EdFund," these 7 bullets are also identified in the Commission's April 21 Process document (#10) to be addressed by the Special Committee set up for this purpose, among other purposes.

In the Analysis portion of the June 2005 Commission Performance Review of EdFund, there are four categories (Fiduciary Responsibilities, Contracting Practices, Compensation, and Operating Efficiencies). Each of these categories contains at the end of the section some recommendations which were adopted by the Commission. *All of these recommendations are included either by reference or specifically in the BSA Report, since the BSA recommendation on page 76 states: "Complete key tasks outlined in the June 2005 mandated performance review of EdFund."* These recommendations are analyzed below – with format slightly changed - to ascertain whether they are specifically included in the Commission's August 21, 2006 process document, or whether they need action by the Commission to deal with them, either itself or through EdFund.

At the end of Fiduciary Responsibilities, "the Commission recommends the following"(page 7):

- A joint planning effort should be reinstated, regular updates on any changes to revenue or expenditure forecast should be examined, and financial reporting should be improved and made more consistent.

The Special Committee, at its teleconference meeting of May 25, 2006 set in motion a process to begin implementation of this recommendation.

- As part of this effort, Commission staff should have on-line access to EdFund financial systems to help monitor cash flow.
- The EdFund Board should reexamine the question of what appropriate amount should be allocated to the contingency fund and should review current policies and practices regarding its use for the purpose of determining if these should be strengthened or changed.

The EdFund Board will do this as part of its development of the 2006-2007 EdFund fiscal year business plan and budget.

At the end of Contracting Practices, “the Commission recommends the following”: (page 9)

- One of the purposes of establishing EdFund as the Commission’s auxiliary organization was to provide more flexibility to respond to competitive business requirements without the highly prescribed contracting processes that may limit the responsiveness of state agencies. Nonetheless, we recommend that the EdFund Board re-examine the organization’s contracting policies and procedures and determine if these should be strengthened or changed.
- This re-examination should address the types of justifications provided before approving competitively bid, single source, and especially sole source contracts and amendments to sole source contracts.
- The process should balance the need for administrative flexibility with the need to ensure accountability.

The Commission already took action on the above bullets in its April 21 process document. That document stated it will request the EdFund Board to revise and tighten these policies. This work is already under way.

At the end of Compensation, “the Commission recommends the following”: (page 10)

- EdFund’s compensation structure has a direct effect on the organization’s effectiveness. The organization’s long term success depends on the performance of staff at all levels, and particularly the executive management team. Decisions about salaries and incentive compensation must be made with a high degree of integrity based on sound salary comparisons and a rigorous review process.
- The EdFund Board of Directors should re-examine the process by which incentive compensation is approved for both regular staff and executive management, and work to ensure that there is mutual understanding on the part of the Commission and EdFund regarding the process by which incentive compensation is determined and approved.

The Commission already took action on the above bullets in its April 21 process document. That document stated it will request the EdFund Board to review, with its management, all aspects of the incentive compensation policy...and proposed appropriate adjustments to the Commission’s PEN Committee and the Commission for their review and approval before the end of the fiscal year, so that any changes may become effective in fiscal 2006-2007. This work is already under way.

At the end of Operating Efficiencies, “the Commission recommends the following”: (page 12)

- The current operating agreement is outdated and needs to be revised. The new operating agreement should accommodate the decisions regarding the roles and responsibilities of the two organizations. The Commission has asked the EdFund Board to make recommendations on the roles and responsibilities of the EdFund Board. The new operating agreement can be multi-year if the basic services provided by EdFund and long term goals are well defined in the agreement. Strategic short-term performance goals, standards and weights and the operating budget should be included in EdFund’s

business plan, which would be approved annually by the EdFund Board and Commission.

The Commission determined in its process document of April 21, 2006 that issues about the operating agreement are the responsibility of the Special Committee.

- Commission and EdFund management need to identify redundancies and operating efficiencies in both organizations in order to lower costs given that Student Loan Operating Fund reserves have been reduced and the business model and revenue streams for the FFEL Program may be changed with the reauthorization of the Higher Education Act. The Commission and the EdFund Board should re-examine allocations within the Capital Utilization Plan. The Commission will also examine the loan program operating budget.

The Special Committee, at its teleconference meeting of May 25, 2006 set in motion a process to begin implementation of parts of this recommendation. It appears that the Capital Utilization Plan was not cited in the BSA Report nor in the Commission's April 21, 2006 process document, so the Commission will need to make a determination on this issue.