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Information Item

GRANT ADVISORY COMMITTEE

Executive Director's Report

The Executive Director will give an oral update on the recent activities of the Commission including the Commission's response to the California Performance Review (CPR) report and related developments in regards to the 2005-06 State Budget.

Responsible Staff: Diana Fuentes-Michel
Executive Director

CALIFORNIA STUDENT AID COMMISSION

CALIFORNIA STUDENT AID COMMISSION

September 3, 2004

Dear Members of the California Performance Review (CPR) Commission:

On behalf of the California Student Aid Commission, we would like to thank you for your willingness to enhance California through your service on the CPR Commission. The task before you is no simple one. Collectively, you possess a wealth of knowledge and experience that qualifies you to help the Governor focus not only on how to improve efficiencies, but to continue to meet the policy goals that have been previously outlined by the Legislature.

As one of the only California state agencies whose operations are self-funded, the Student Aid Commission administers the state financial aid grant program and also serves as the designated guarantee agency for state-administered federal student loans. The Student Aid Commission has been in existence since 1955, and in 1997, it was granted the authority to establish a non-profit, public benefit auxiliary company to perform its loan servicing functions. Since then, as you will see from this document, the Student Aid Commission and its auxiliary, EDFUND, have proven successful in numerous ways and have provided hundreds of millions of dollars in public benefits back to the state.

The mission of the Student Aid Commission is to "make education beyond high school financially accessible to all Californians." In reviewing the CPR recommendations, this mission has remained foremost in our minds. As you will see in the attached document, the "California Student Aid Commission's Response to the California Performance Review," our positions on the issues that affect us always focus on the best interests of students and their families. At the same time, we are fully aware of the need for improvement in some of California's state services and we stand ready to assist in ways that both benefit California and maintain services to students in need.

We would like to extend our best wishes to you in undertaking the challenge ahead. We hope that you find this document helpful in analyzing the effect of the CPR recommendations on California's neediest students. If we can be of any further assistance to you, please do not hesitate to call us at 916.526.8271. Thank you.

Sincerely,

David Roth
Chair

Diana A. Fuentes-Michel
Executive Director

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EXECUTIVE SUMMARY

The California Student Aid Commission (CSAC) commends Governor Schwarzenegger for launching the California Performance Review initiative, a comprehensive review of State government operations.

CSAC shares the Governor's goal of increasing government efficiency, reducing taxpayer costs and eliminating bureaucratic red tape. To do so will result in better public services and benefits for the students, families and postsecondary institutions served by CSAC.

As you know, CSAC was first established in 1955 as the "State Scholarship Commission." Today, CSAC is responsible for administering the $800 million Cal Grant Program, the State's basic financial aid program that awards grants to more than 60,000 needy students. In addition, since 1977, CSAC has served as the guaranty agency in California for the nation's largest federal student loan program, now called the Federal Family Education Loan (FFEL) Program.

In launching the California Performance Review, the Governor said he wanted to "blow up the boxes." CSAC believes it happens to be one box that was already blown up seven years ago, during the administration of former Republican Governor Pete Wilson.

In 1997, the California Legislature and Governor Wilson authorized CSAC to establish EDFUND as a non-profit, public benefit auxiliary corporation to handle CSAC's participation in the FFEL Program.

CSAC is pleased to report that the CSAC/EDFUND enterprise has been a major success and today is a generator of millions of dollars of revenue for the State. For example, the 2004-05 Budget Act includes a one-time transfer of $146.5 million from the Student Loan Operating Fund (SLOF) to fund Cal Grant awards, providing a major savings in General Fund spending. What's more, CSAC's administrative budget is currently funded entirely by the Student Loan Operating Fund – at no cost to the State General Fund. The Student Aid Commission is truly a bargain for the State of California.

CSAC also is pleased to report that the 2004-05 Budget Act recently signed by Governor Schwarzenegger gives CSAC and EDFUND the authority to develop diversified financial aid services and products. Revenue generated from those new services and products will sustain CSAC's ability to provide public benefits to students and institutions in the future.

It is against this backdrop that the CPR's proposals have been put forward as they relate to CSAC and EDFUND. They are summarized as follows:

1) To dismantle CSAC's grant and loan operations and place its policy functions within a proposed Higher Education Division of a new Department of Education and Work Force Preparation;

2) To disband the Cal Grant Program and instead amend existing law to create a college fee waiver program for financially needy students attending the University of California and the California State University;
3) To outsource CSAC's federal student loan guaranty services now performed by EDFUND.

CSAC respectfully opposes these specific recommendations. Adoption of the CPR proposals as submitted will lead to:

- Elimination of a State agency that has generated more than $399 million in revenue for the State for public service initiatives since 1997 ($198 million of which would have otherwise been General Fund expenditures).
- Loss of potential future revenues generated by CSAC and EDFUND to continue to provide direct public benefits to students and institutions, such as Cal-SOAP, Cal Grant public awareness and outreach programs.
- Greatly increased costs to state taxpayers. The estimated taxpayer cost for decentralization of the Cal Grant program alone ranges from $1 million to $4 million – thereby negating any costs savings from the reorganization proposed by the CPR.
- Loss of at least $12 million in matching federal financial aid funds.
- Loss of direct public accountability and oversight by the elimination of a Commission directly responsible and responsive to the public.
- Imposition of a more complex and less reliable financial aid system for students, due to a lack of uniformity in determining program eligibility.
- Increased, ongoing workloads at each UC and CSU campus at an unknown cost.
- A greater demand for institutional aid at the UC and CSU in the face of budgetary cuts.
- The rollback of legislation recently signed by Governor Schwarzenegger giving CSAC and EDFUND the authority to develop diversified financial aid services and products to generate more revenue for student and public benefits.

Clearly, there would be harmful consequences for students, institutions and taxpayers if the CPR proposals were to be implemented. The CPR proposals fail to recognize that CSAC is the cornerstone to sustaining and improving a college-going culture in California, enabling more students to access quality postsecondary training and education. If there is a single State agency that plays a critical and daily role to make work force preparation happen, it is the California Student Aid Commission.

It should also be noted that CSAC functions optimally as an independent entity overseen by a diverse group of Commissioners appointed by the Legislature and Governor. These Commissioners – drawn from various professions, geographical regions and ethnic backgrounds – represent the broad diversity of California students and institutional stakeholder groups. Eliminating the Student Aid Commission and consolidating it with other education agencies would greatly diminish the State's ability to set and implement effective policies to ensure access and affordability in the current era of rising college costs.

CSAC, however, supports the overall CPR goal of achieving increased government efficiencies and better customer service. With that in mind, CSAC believes it would be well-suited to absorb some of the research functions of the California Postsecondary Education Commission (CPEC). Such a consolidation would allow the State to better coordinate policy decision-making in the current era of increasing college fees but decreasing financial aid, which is in ever greater demand.

Thus, CSAC has prepared this response to the CPR in the spirit of exploring ways to streamline the State's higher education agencies while ensuring college access and affordability for all eligible students.

INTRODUCTION

Since its creation by the Legislature as the State Scholarship Commission in 1955, the primary purpose of the California Student Aid Commission has been to make higher education financially accessible to all California students. Over the years, CSAC has evolved from a small State scholarship agency with a handful of employees into a multidimensional financial aid organization. Today, CSAC administers more than $800 million in grants and specialized programs to more than 255,000 California students. Through its non-profit, public benefit auxiliary, EDFUND, CSAC issues new loan guarantees under the Federal Family Educational Loan (FFEL) Program totaling more than $4.4 billion to over 980,000 students nationwide.

In making policy decisions, the Student Aid Commission receives advice and recommendations from its staff and various advisory committees, including the following: the Grant Advisory Committee; the Loan Advisory Council; the Cal-SOAP Advisory Committee; and ad hoc committees comprising individuals representing colleges and universities, secondary schools, student groups, the business community, lending institutions and various levels of government. CSAC's strong tradition of public participation stems from its commitment to continuous improvement and responsiveness in the development and delivery of its financial aid programs and services.

Grant Program Duties as Established by Law

Existing law establishes CSAC as the primary State agency for the administration of State-authorized student financial aid programs available to students attending all segments of postsecondary education. Under existing law, CSAC administers various programs, including: the Cal Grant A, B, C, and T Programs; the California Student Opportunity and Access Program; the Assumption Program of Loans for Education; the Graduate Assumption Program of Loans for Education; the California State Work-Study Program; the Foster Youth Chafee award program; the federal Robert C. Byrd Scholarship program; and the Child Development Grant Program.

Prior to 2001, the Cal Grant programs were designed to provided undergraduate students attending postsecondary education with financial aid that was both merit- and need-based and that would provide them with the ability to attend a post-secondary academic program at a public or private institution of choice. To serve the diverse need of students and encompass the varied postsecondary education academic programs available, three separate grant programs were created. Those programs evolved into the Cal Grant A, B, and C programs. The Cal Grant A serves low- to middle-income students by providing tuition and fee assistance for academic programs of not less than two academic years.

The Cal Grant B serves low-income students by providing a living allowance and tuition and fee assistance for instructional programs of not less than one academic year. The Cal Grant C serves low-income students attending a postsecondary educational occupational or vocational program by providing tuition and fee assistance, as well as an amount for books, equipment, and tools. The selection and award of the Cal Grant to students was based on the funding provided in the budget and became a competitive program where awards were rationed to only the neediest students based upon criteria recommended by the educational community and approved by the Student Aid Commission. This approach often resulted in a large number of qualified and needy students not receiving an award.

To address the deficiencies of the program, the Legislature in September 2000 passed and the Governor signed Senate Bill 1644, which authorized an educational grant entitlement program. Under the entitlement program, every high-school graduate with sufficient financial need and an eligible Grade Point Average (GPA), and who enrolls in a California qualifying institution, is entitled to a Cal Grant A or B award. SB 1644 also significantly modified the competitive Cal Grant A and B program for non-traditional students. The new Cal Grant competitive program includes a merit component (GPA), financial need, and new special considerations categories. In addition, competitive Cal Grant awards are capped at 22,500 annually – even though the number of students eligible for a competitive grant is more than 100,000 statewide. The competitive program also has two award cycles. The first competitive deadline is March 2 for all public and private institutions; the second deadline is September 2 and is reserved for community college students only.

The Student Aid Commission's Exceptional Performance in Grant Administration

Cal Grant Program

The changes in the Cal Grant program required extensive modification of CSAC's automated Grant Delivery System (GDS) to include the programs above and incorporate other requirements of the entitlement statute. A short four-month deadline for the first major operational deadline, the entitlement awards and the following operational deadlines dictated a "just-in-time" implementation of critical application changes to an already complex system. The major program objectives, the entitlement awards and the revised competitive awards, were completed and successfully implemented on time and under estimated costs. This was a major achievement considering the short time frame and the complexities of changes required. It is an accomplishment that is only possible in a centralized system.

Chafee Grant Program

In October 2003, CSAC staff received a request from the California Department of Social Services asking if CSAC would be able to assist with the administration of the new Chafee Education Training Voucher Program (later named the California Chafee Grant Program). The Chafee program is a federally funded program that provides grants to eligible foster youth to help pay for the cost of post-secondary training and/or education. Because CSAC administers similar programs and has expertise in this area, it was a logical and well-placed request. An interagency agreement was drafted and signed off by both agencies in April 2004. CSAC staff was able to develop on-line resources, printed materials, training programs and internal systems within a 60-day time frame. In just a few months time, this program has provided resources in excess of $4 million to more than 1,000 students.

This is just one example of how CSAC, by virtue of its efficient operations and streamlined processes, was able to assist another State agency to deliver funds to students in the most efficient and timely manner.

Establishment of EDFUND

In the early 1990s, the demand for student loans in California grew substantially due to factors such as the increase in the cost of education, the failure of other sources of financial aid to keep pace with growing demand, and federal expansion of loan eligibility requirements. CSAC's loan portfolio began growing at a rapid pace.

In 1993, the Federal Direct Student Loan Program was created in the Omnibus Budget Reconciliation Act. The program was marketed heavily by the U.S. Department of Education. As a result, UC and CSU campuses and other California schools began switching their loan business from CSAC's FFEL Program to the Federal Direct Lending program.

The loss of business to direct lending raised the competition level among FFEL Program participants. To minimize their losses, other participants moved quickly to improve their services and began heavily marketing a wide range of services to California schools. Out-of-state guaranty agencies began "cherry picking" the schools in California.

CSAC was limited to providing services within the State of California and was hampered from making improvements to its services and systems within the confines of a state bureaucracy. It was unable to respond quickly to market forces. As a result, its market share loss was dramatic, and it faced extinction as a provider of loan guarantees.

To counter this, CSAC in 1995 proposed that its loan program operations be shifted from a State agency to a non-profit, public benefit corporation operating under the auspices of the Student Aid Commission.

The auxiliary would provide CSAC with the ability to be more competitive by freeing it from the processes of State government, specifically, the State controls over personnel, procurement, financial management and technology matters. AB 3133, Statutes of 1996 authorized the creation of the CSAC auxiliary, EDFUND.

Today, EDFUND is the nation's second-largest guaranty agency in the FFEL Program. Annual loan volume now totals more than $4.4 billion, and it oversees assets totaling more than $21 billion.

In closing, it should be noted that CSAC for almost 50 years has been the State agency known as the distributor of State grants for needy students, while EDFUND in the past seven years has gained a national reputation for providing superior loan guaranty services in the FFEL Program.

CSAC and EDFUND are the cornerstone to sustaining and improving a college-going culture in California, enabling more students to access quality postsecondary training and education. For many students, CSAC is *the bridge* to workforce participation because they view the Cal Grant award letter from CSAC as their ticket to college.

CSAC and EDFUND have a single mantra: “Students First.” The goal is to put the best interests of students first. The CPR proposals run counter to those interests and should be rejected.

What follows is a critical analysis of each of the CPR proposals as they relate to CSAC and EDFUND.

ETV 03: Consolidate Selected State Higher Education Agencies

CPR Recommendation: *The California Community College Chancellor's Office, the California Postsecondary Education Commission, the California Student Aid Commission(CSAC) and the Bureau for Private Postsecondary and Vocational Education should be restructured and consolidated into a single, unified Higher Education Division. The Governor should appoint a Deputy Secretary of Higher Education who will be responsible for the effective management of the Higher Education Division. The Deputy Secretary of Higher Education should report to the Secretary for Education, or his or her successor.*

CSAC ANALYSIS:

Summary: Dismantling CSAC operations will increase, not decrease, bureaucratic red tape and will dramatically reduce college access and affordability for middle- and low-income students. Among the reasons:

- Statewide and campus-based financial aid assistance programs will either be eliminated or revert to General Fund expenditures (in all, EDFUND-generated revenues have financed at least $32 million for such efforts in the past three years).
- CSAC workshops to assist students with completion of the requisite federal financial aid application form to determine financial aid eligibility will be eliminated.
- CSAC's first-in-the-nation policy to provide students a 1% discount on federal student loans, which has saved EDFUND's student borrowers $163 million to date, could be reversed. <u>CSAC's chief competitor recently announced it's re-instituting the fee, costing students more.</u>
- Reduced public accountability and oversight over financial aid policymaking and practices.

KEY ISSUES

- **Loss of Accountability to the Public and the Legislature**

CSAC is a 15-member governing body with a diverse membership that reflects broad public representation. Eleven members are appointed by the Governor, and two each by the Senate Rules Committee and the Assembly Speaker.

Currently, the membership of CSAC includes: a high school counselor with more than 35 years of experience in teaching and counseling; a retired president of California State University, Pomona; an educator with over 30 years' experience who serves as trustee of a local community college; a retired CSU professor with decades of teaching experience; two members who serve in student affairs for two campuses within the University of California; a retired private college administrator who also holds a law degree and sits on numerous boards and commissions; an attorney with more than 30 years' experience and a history of supporting higher education for underprivileged students; two members who currently work for independent postsecondary institutions; a successful information technology business executive; and slots for two student members.

All members serve as volunteers, receive only per diem and travel costs, and give hundreds of hours per year in their roles as Commissioners. Members are appointed because of their demonstrated commitment to ensuring that *all* California students have access to quality higher education.

Consolidation of CSAC with three other agencies would eliminate this public accountability component of the State's financial aid system.

Furthermore, the Legislature would have limited oversight over the CSAC-successor operations if such operations are under the sole purview of the Office of the Secretary for Education. Since the Legislature passed SB 1644, the groundbreaking legislation establishing the Cal Grant Entitlement Program in 2000, it is highly unlikely that the Legislature would favor the relinquishing of its authority over Cal Grant and other State financial aid programs.

- **California vs. Other States: Comparing Apples to Oranges**

The CPR Report cites examples of thirteen states that have consolidated their agencies for higher education planning and coordination, administration of student financial aid, and licensing of non-public postsecondary education institutions. However, none of the states cited are comparable to California in terms of population, student enrollment, diversity of the public school population, and the number of postsecondary schools. California has the largest number of students enrolled in postsecondary education compared with all other states, and only Arkansas and Michigan have grant programs that compare to California's in size and scope. California has approximately 3,000 private postsecondary institutions and 141 public colleges and universities. None of the states cited in the CPR report has nearly as many schools. According to the CPR report, these out-of-state consolidations have taken place within the past seven years. The CPR report, however, does not indicate whether or not these consolidations in other states are considered successful.

- **Increase in Bureaucracy and Red Tape**

Finally, CSAC believes that a consolidation of these four agencies will add to, not eliminate, the layers of state bureaucracy that students and institutions must navigate to obtain desired results. Under the CPR proposal it is conceivable that each UC and CSU campus would have to verify individual student eligibility for a waiver of system-wide fees in lieu of a Cal Grant award. Also, students might qualify for a fee waiver at one segment but not another. For example, a student attending a community college would be limited by the availability of funds at each individual campus.

<u>CSAC RECOMMENDATION</u>: CSAC recommends that its Commission be maintained in its current form, rather than be consolidated with other agencies under the Office of the Secretary for Education. Because of the complexity of CSAC's programs, and the need to maintain representation of Californians' diverse interests through a governing body with multiple appointing authorities, CSAC should remain a separate State agency that will continue to provide public benefits to California at a minimal cost. Additionally, since CSAC's administrative functions are funded by the Student Loan Operating Fund, which may not be the case under a consolidated agency, it is more fiscally sound to leave CSAC as a separate, independent agency.

That said, CSAC acknowledges that numerous agencies that deal with higher education issues can be confusing for Californians and CSAC supports the CPR goal of improving government efficiency and customer service.

CSAC is open to alternative methods of consolidation that would better serve Californians. For example, CSAC would be well-suited to absorb some of the research functions of the California Postsecondary Education Commission (CPEC). CSAC is willing to collaborate with CPR and/or the Administration on exploring ways to streamline the State's higher education agencies to produce greater efficiency and savings to the State.

ETV 16: Provide a Fee Waiver in Lieu of a Cal Grant Award

CPR Recommendation:

A. The Governor should work with the Legislature to amend relevant Education Code sections replacing portions of the State's current Cal Grant A and Cal Grant B programs with a new fee waiver program at the State's public universities.

Specifically, the Education Code should be amended to provide a waiver of the system-wide student fees for all financially needy California resident undergraduates attending the University of California and the California State University. Under the amended law, these financially needy undergraduates should receive a waiver of system-wide fees in lieu of a Cal Grant award.

B. Beginning in 2006–2007, Cal Grant funds for financially needy students at California community colleges should be appropriated directly to the community colleges.

The Community College Chancellor's Office should allocate these funds to the community college districts based on the number of financially needy students enrolled in each district. Campuses should disburse these funds to financially needy students consistent with eligibility criteria outlined in California Education Code Section 69538.

CSAC ANALYSIS:

Summary: Decentralizing the Cal Grant program and reinventing it as a "fee waiver" system would run counter to the Legislature's passage of SB 1644 and would be detrimental to students, institutions and the State in a number of ways:

- Increased Costs to California Taxpayers, not Less
- A more complex and less reliable financial aid system for students
- Increased Workload at UC, CSU and Community College Campuses
- A Potential Loss of matching federal funds, resulting in increased demands for financial aid provided by institutions

KEY ISSUES

- **Negative Fiscal Impact on California Taxpayers, the State and Institutions**

Contrary to the CPR report's assertion, costs to the State will likely not decrease. It is anticipated that some type of administrative allowance would be required to help campuses offset the cost of the increased workload. An Assembly Appropriations Committee analysis last year estimated it would cost taxpayers at least $1 million to implement decentralization of the Cal Grant program, with undetermined, ongoing workload increases at each campus. One CSAC staff estimate in April 2003 outlined decentralization costs totaling at least $4 million.

Perhaps most telling is that an Assembly bill that would have implemented decentralization of Cal Grants (AB 1323; Jackson) failed to garner support during the first year of the 2003-04 legislative session.

In addition, the projected savings in CSAC administrative operations appear to be overstated, as well.

The CPR recommendation indicates an annual savings of $6.6 million in operations and 77 fewer positions based on an estimate that 60% of CSAC's operations budget supports administration of the Cal Grant awards for students attending the State's public colleges and universities. The CPR report presumably used 2001-02 data. That year was the first year of the new Cal Grant A & B Entitlement and Competitive programs, so the segmental date primarily represents the old Cal Grant A & B programs. The segmental distribution has changed significantly with the implementation of the new Cal Grant Programs. The Cal Grant A & B Entitlement and Competitive programs system wide fee funding for students attending UC and CSU is projected to be approximately 38% of the Cal Grant Program portion of CSAC's total 2004-05 local assistance budget.

Using the CPR methodology, a 38% reduction would account for $4.2 million in savings of CSAC's approximate $11 million budget for non-loan programs and a reduction of 48 positions. Further analysis is needed to determine if this methodology is appropriate as CSAC administers many different programs, most of which are not as automated as the Cal Grant Programs and do not provide the economies of scale that the Cal Grant Programs do.

The CPR report also states that the existing Cal Grant aid levels coupled with a relatively small portion of undergraduate institutional grant aid would be sufficient to fully fund the proposed fee waivers at UC. CSAC's calculations indicate that a significant amount of undergraduate institutional aid or General Fund resources would be required to fund the Fee Waiver program. The CPR report is silent on the Cal Grant Program for private/independent institutions and Cal Grant C. Therefore, CSAC's calculations do not include the associated funding in its calculations of funding available for a Fee Waiver program at the UC and CSU. Also not included is the Cal Grant Entitlement and Competitive Program funding for the Cal Grant B access awards as renewal recipients would presumably continue to receive these funds until their eligibility ran out.

Finally, changing portions of the Cal Grant Program to a fee waiver would also result in the loss of $12 million in federal funding as the State would no longer have a grant program that meets the federal matching requirements. (The affected federal programs are the Special Leveraging Educational Assistance Partnership or SLEAP, and the Leveraging Educational Assistance Partnership or LEAP.) As these federal funds are part of the Cal Grant funds issued to the UC and CSU, either the General Fund or the institutional aid contribution would have to be increased to cover the loss of these funds, thereby resulting in a loss of savings proposed by the consolidation.

- **<u>The Burden on Students</u>**

Bureaucratic Red Tape Likely to Increase, not Decrease

For students, a fee waiver program would mean that any student who applied at more than one institution would need to qualify separately at each of those institutions. This means the eligibility determination would *still* be duplicated, possibly many times over, making the State's financial aid system more complex, not simpler for students.

The CPR report assumes that fee waivers will reduce unnecessary application and paperwork requirements but that is far from certain.

That assumption ignores the reality that the current process for a Cal Grant requires completion and submission of two key documents – the Free Application for Federal Student Aid (FAFSA) form, and a GPA verification form. Even with fee waivers, the FAFSA will still be required of any student applying for a Pell Grant or various other forms of federal aid, and more than likely the proposed fee waiver program. If the FAFSA is not used for the proposed fee waiver program, then in all likelihood an additional form would be required, thereby adding an additional form for students to complete and submit. The FAFSA form, while complex, is a federal form and can be completed online. CSAC has a variety of programs aimed at assisting students and parents with completion of the FAFSA (these programs would be eliminated if the CPR proposals are enacted). The GPA verification forms are often submitted in bulk electronically by high schools, or can be completed by a student who visits his or her high school office for verification and mails the form.

Another uncertainty is how these fee waivers will be renewed. Will the process be automatic or will students be required to have their eligibility determined every year? If the eligibility requirements were to change from one year to the next, it is possible that a student could find themselves ineligible for a waiver midway into their college career. Under the current program students are not penalized if program changes are made; they are simply grandfathered in and allowed to finish their course of study.

Students Lose Portability of Cal Grant Award and "Choice"

The Cal Grant Entitlement program is remarkable for a number of reasons, but arguably the biggest advantage of a Cal Grant is its "portability." A student who receives a Cal Grant can apply it to any accredited postsecondary institution in the state, including the UC, the CSU, California community colleges, private institutions and vocational or technical schools. Students choosing to attend non-public institutions would lose the waiver. Furthermore, if the Cal Grant program is kept intact for independent institutions, students might not learn they are eligible to apply for a competitive award until it is too late in the application process.

Therefore, a student who wants to explore attendance at more than one institution will be faced with even more confusion and different types of awards, whereas under the current program a Cal Grant award is in the hands of an individual student early and can be applied uniformly at any institution.

In addition, having one agency whose specialty is Cal Grant administration ensures that students receive accurate and consistent information with regard to Cal Grants on behalf of the State. A system whereby each campus is responsible for determining a student's eligibility for a fee wavier will lead to a more complex and less reliable financial aid system due to a lack of uniformity in determining program eligibility.

Another problem with fee waivers is the ability of students to have time to make a decision about which school to attend. The Cal Grant letters from CSAC begin to reach students in January, informing them of an award at the institution(s) of their choice. Another advantage of the current program is that sometimes the award notice can be the catalyst that encourages students to explore other education options or to follow up with schools that they may have thought were out of their reach. Under the CPR proposal, students will have to wait to hear from each college campus as to whether or not they will qualify for a waiver of student fees at that particular UC or CSU campus.

The current Cal Grant B program contains an access component or subsistence award that can be used by students to pay for additional expenses outside of tuition. This may include expenses such as campus-based fees, books and supplies, and even room and board costs. Under a fee waiver program, the loss of a subsistence award would be devastating to the neediest of students. The loss of these funds could limit access and choice and may force students to seek other lower-cost alternatives, attend school on a part-time basis, increase student work/loan burden, or forfeit college altogether.

Students Attending Independent Colleges and Private Institutions at Risk

Alarmingly, the CPR fee waiver proposal is silent on private/independent postsecondary institutions. Currently, an eligible student who wishes to attend a private institution would receive a Cal Grant award amount that is typically greater than those issued for public institutions due to the significant difference in cost of attendance. Although these award amounts are higher, they allow the student to choose an institution, not based on the limitations of their family income, but on their individual academic needs and goals. As stated previously, the Legislature clearly intended for all eligible students to have this broad access to any accredited postsecondary institution in the State. Further, private institutions usually provide matching institutional aid when a student uses a Cal Grant award. Depriving the State's most financially needy students of the opportunity to choose a private institution means that those institutions will only be available to those with substantial financial resources. The resulting drop in private college enrollments could also be a detriment to the California economy in various ways.

➢ **Burden On Institutions**

The Fee Waiver proposal would shift the entire workload to the campus level financial aid office. Determining eligibility, documentation, reconciliation and State reporting would all become the responsibility of each individual campus. Changes in computer systems would be required, standards would have to be established, maintained and audited. It is likely that additional staffing would be required to maintain program integrity and meet student demand.

Bear in mind that CSAC performs a number of tasks related to the administration of the Cal Grant program, including the following:

- Establish policies regarding the awarding and use of Cal Grant funds, including scoring criteria and income and asset ceilings
- Approve schools participating in the Cal Grant programs
- Perform fiscal and administrative reviews of schools and institutions distributing Cal Grant funds
- Provide fiscal projections to the Department of Finance
- Compile detailed reports on the Cal Grant programs
- Assign federal SLEAP (Special Leveraging Educational Assistance Partnership)/LEAP (Leveraging Educational Assistance Partnership) funds to eligible Cal Grant recipients

The ability to continue to perform these duties would be either eliminated or severely hampered by this proposal. In order to continue with these tasks, schools would have the increased workload of sending detailed information to CSAC in a timely manner or providing the information to the State, or compiling the data individually by campus or sending the data to a central location for compilation. Federal SLEAP/LEAP matching funds, which totaled over $12 million for the 2002-03 year, would be eliminated.

Furthermore, under the current Cal Grant program, verified GPAs are submitted directly to CSAC, either by schools or the student. Under a fee waiver program, individual institutions would have to establish criteria by which GPAs are calculated for the fee waiver program. The GPAs currently used by UC and CSU include weighted courses, a process by which Advanced Placement courses are counted in the calculation. The inclusion of weighted courses could disadvantage students who come from schools with limited access to these kinds of programs. If a separate GPA calculation were to be required, this would increase the institutions' workload even further. California community colleges currently do not require students to submit transcripts when applying for enrollment and therefore they do not have the systems in place to calculate GPAs for students. To add the burden of GPA collection for students receiving Cal Grant funds at a California community college could be overwhelming and also could be a deterrent to students by further complicating the enrollment process.

If the competitive program continues to exist for students attending non-public institutions as it is currently written, the State would still be required to continue collecting GPAs for all eligible applicants in order to make awards. The workload for schools would not be reduced or eliminated. This could add to student confusion if they are awarded a Cal Grant but excluded from using it at a public institution.

Finally, CSAC currently serves as an inter-segmental advocate for students in all segments of higher education on financial aid-related issues. If funds were to become restricted for the fee waiver program, this could eliminate the balanced approach to distributing financial aid, and could pit segment against segment. The unanswered questions about private segment school participation in the program further expand the potential for fragmentation.

Loss of State Oversight/Role on Financial Aid

CSAC is currently responsible for developing policies regarding the Cal Grant programs. Issues or policy decisions are brought to the Grant Advisory Committee (GAC), whose members include representatives from all segments of education. The makeup of this committee ensures that changes to the programs are student-centered and do not favor one segment over any other. Once a recommendation is made by GAC, the item is brought to the Student Aid Commission for further discussion and approval. The fee waiver program would serve only the public segment students without direct control of the State over the program.

CSAC RECOMMENDATION: CSAC opposes the CPR proposal to establish a fee waiver system because it will create a more complex and less reliable State financial aid delivery system than what exists today. Notwithstanding the fact that the CPR report contains no explanation of how the proposed fee waiver program would work, implementation of fee waivers would be a bigger expense to the State, a larger workload for the State’s public colleges and universities, and will apparently lock financially needy students out of private/independent institutions. CSAC recommends that it continue to be responsible for the Cal Grant program, as established by current law, providing college opportunity and access for all eligible California students, as intended by the Legislature.

ETV 22: Reduce the Cost of the State's Student Loan Guarantee Function

CPR Recommendation:

A. The Secretary of Education, or his or her successor, should ensure that the California Student Aid Commission, or its successor, issues a Request for Proposals to solicit competitive bids for the delivery of student loan guarantee administrative services required under the Federal Family Education Loan (FFEL) Program.

B. The Governor should work with the Legislature to amend Education Code Sections 69522–69529.5 to allow the State's public benefit auxiliary corporation to compete as a provider of student loan guarantee services.

Existing civil service State employees now assigned to work for EdFund should return to CSAC and should be reintegrated into the workforce. All State assets held by EdFund should also be returned to the State.

CSAC ANALYSIS:

Summary: The CPR proposal to outsource student loan guarantee services failed to present any analysis of CSAC's current market success, ignoring the fact that CSAC generates hundreds of millions of dollars in revenue for the State by operating through its non-profit auxiliary, EDFUND, and that CSAC's entire administrative budget today is funded without the use of California taxpayer dollars. In addition, the CPR proposal is largely based on "unknown" or speculative assumptions and "informal inquiries" rather than rigorous analysis.

KEY ISSUES

EDFUND'S Record of Success

The Student Aid Commission is the student loan guaranty agency for the FFEL Program in California (Educ. Code §69761.5(a)). To this end, California law requires the Student Aid Commission to administer the FFEL Program and to adopt rules and regulations to implement the Program (Educ. Code §69763; 69764, 69765). The Student Aid Commission is designated by California law as the only entity to receive federal funds for administrative costs and payment of insurance obligations under the FFEL Program. In addition, statute authorizes CSAC to use an auxiliary organization for operational and administrative services to accomplish its responsibilities under the FFEL Program, but expressly directs CSAC to maintain its responsibility for policy leadership, financial aid program administration, program evaluation and information development and coordination.

EDFUND is a non-profit public benefit corporation that was established by the California Student Aid Commission in 1997 as its auxiliary to administer its duties as a guaranty agency under the FFEL Program. The federal government delegates most administrative responsibilities for the program to 36 individual guaranty agencies, and reimburses those agencies based on terms set in the federal Higher Education Act.

Colleges and universities select the guaranty agency of their choice based on who they believe will deliver the best service to their students and campus(es). The Student Aid Commission (the guaranty agency) and EDFUND (its guaranty services provider) have grown to the second-largest such agency in the nation based on the quality of services and products delivered to students and schools.

There have been no performance issues. In fact, EDFUND recently achieved superior results in audits by the State auditor (the annual single State audit) and the U.S. Department of Education (an approximately five-year comprehensive review). Moreover, the track record speaks for itself. Since 1997, the FFEL Program grew by 10 percent nationally; CSAC programs' rate of growth was 19 percent. During the same period, it cut its student loan default rate in half, from 14.4 percent to 6.7 percent.

By the end of the current fiscal year, annual new loan volume is projected to have doubled in just three years. This performance is derived from CSAC's and EDFUND's student-centered, customer service-oriented approach to student loan guarantee services, delivered through a close technology relationship with educational institutions and their student loan program lenders. A change in guaranty service provides, as proposed by the CPR, would have the outcome of driving institutions that have choices to competitors, likely resulting in a net loss of income for the State from student loan program operations. Remaining institutions would incur the cost of migrating services to a new technology platform with the State's new guaranty services provider.

Public Benefits to Students and the State

As a non-profit auxiliary of the State's leading student financial aid policy body, EDFUND furthers State policy interests by providing direct benefits to students and schools. These include:

- waiving of the 1 percent guarantee fee, generating more than $23 million per year in savings to student borrowers;
- extensive outreach and consumer education for students and families about financial aid options;
- regular notifications to student borrowers regarding their accumulated loan debt;
- direct support services for college financial aid offices;
- training and professional development for college financial aid staff;
- a borrower contact management system to assist financial aid staff in preventing student loan defaults;
- $5 million annually in public service, outreach and borrower education initiatives and programs.

To date, revenue generated by CSAC through EDFUND operations has funded more than $399 million in public service initiatives, including at least $198 million for programs or spending that otherwise would have been General Fund expenditures. The $198 million includes such key programs as the Cal Grant public awareness program, the California Student Opportunity and Access Program (Cal-SOAP), campus-based financial assistance programs, and backfilling General Fund monies to fund part of the Cal Grant Program in 2004-05. That includes CSAC's administrative budget, which since July 2003 has been funded entirely by revenue generated by EDFUND.

And for the first time, revenue generated by CSAC through EDFUND operations will fund Cal Grant awards in fiscal year 2004-05. The recently signed State budget includes a one-time usage of $146.5 million from the Student Loan Operating Fund to cover what had been proposed reductions in the Cal Grant program.

At CSAC and EDFUND, the mantra is *Students First*. That approach is best exemplified by CSAC's first-in-the-nation policy decision to waive the 1% guarantee fee paid by students taking out loans in the FFEL Program. CSAC has waived this fee as a matter of policy since before EDFUND was created. Through this fee waiver, CSAC and EDFUND have saved student borrowers $163 million since July 1996.

One of CSAC/EDFUND's key competitors recently reinstated the fee, costing students more. Some of EDFUND's chief competitors have argued that EDFUND's waiving of the fee is an unfair advantage. CSAC rejects that contention because other guarantors have the same option; the only advantage CSAC provides is to students.

CSAC and EDFUND also provide a positive economic benefit to the State economy. As of August 1, 2004, EDFUND employed 660 people at its Rancho Cordova headquarters (including 71 civil servants), generating approximately $90 million in regional impact dollars. Eliminating CSAC's contract with EDFUND would terminate almost 600 private sector jobs.

Finally, the CPR recommends that EDFUND be allowed to compete as a provider of student loan guarantee services. However, without an active contract with a guaranty agency to perform guaranty functions, EDFUND would have no authority to administer federal student loans. The only options available to it would be to immediately find another guaranty agency to affiliate with – unlikely, given that most already have the systems and personnel in place to meet their needs – or begin a wind-down process resulting in the loss of 660 jobs and a California-based public benefit organization.

CPR Outsourcing Proposal is Based on Faulty, Tenuous Assumptions

The CPR report recommends that the services now provided by EDFUND be contracted out through an RFP process. The CPR assumes that by soliciting competitive bids for the administrative services required under the FFEL Program, the State should be able to reduce administrative costs. The CPR proposal states that the "overall fiscal impact of outsourcing California's student loan guarantee administrative services is unknown, but will likely generate significant cost savings."

There is no quantifiable savings amount in the CPR report, which only offers that "informal inquiries of other providers of student loan guarantee administrative services suggest that these services could likely be provided at a significantly lower cost."

Furthermore, outsourcing the FFEL Program administrative functions to another entity that does not have the same high quality of service and policy goals may result in significantly lower revenues, offsetting any potential savings.

The CPR report also fails to note CSAC's history and experience with outsourcing. Prior to the establishment of EDFUND, CSAC contracted out for guarantee services. The contracting process and rebidding of the contract was lengthy and costly. Costs and the quality of the work performed by the vendor could not be controlled.

If a new contractor was selected through the State rebidding process, the conversion to a new system could create errors in data or borrower records and could result in audit findings with financial liability. Managing the contract to ensure that all the federal and State requirements were being met by the vendor required increased resources and diligence.

The CPR proposal to cut ties with EDFUND, a thriving California-based operation, should not be based on factors that are "unknown," "likely," and the result of "informal inquiries" rather than rigorous analysis. The CPR proposal focuses only on the cost of guarantee services, not on the relationship between investments in the enterprise and revenue that provides public benefits to students, institutions and the State. Past experience is contrary to the CPR's conjecture. CSAC operated the student loan program in a low-bid State environment for almost two decades, and as a result the program was nearing federal termination before CSAC created EDFUND.

CPR Proposal Will Result in Loss of Public Accountability

Another important consideration is policy oversight and accountability. Under current law and company by-laws, the entire EDFUND Board of Directors serves at the pleasure of the Student Aid Commission, and the company is contracted for services by the CSAC under an annually-reviewed operating agreement. EDFUND is additionally subject to annual federal, State and independent financial audits, and an annual reporting requirement to the State Legislature. Few, if any, of these protections would be left in place if the State instead contracted with an outside service provider.

CPR Proposal Relies on Outdated Material

The CPR report also asserts that the "relationship between CSAC and EDFUND has often been strained." The report cites five-year-old legal action taken between CSAC and the EDFUND Board of Directors. The origin of this legal action is as follows: the original management structure envisioned for CSAC and EDFUND was one in which the same person would serve as chief executive of both organizations. However, in 1998, the State auditor issued a report expressing disapproval of this arrangement and the two organizations' joint management structure was disrupted. The installation of separate CEOs for the two organizations created inevitable tensions that devolved into a legal battle in which CSAC prevailed. Neither of the two executives involved in the litigation is associated with either organization today, and the relationship between the two organizations over the past five years has been one of steadily growing cooperation and coordination, as evidenced by the performance results cited above.

In summary, lower costs for guaranty agency operations are not in any way demonstrated by the CPR analysis. And assuming lower costs are feasible, they do not automatically result in a greater net gain from revenues. The change proposed by CPR would likely result in a net loss of income from student loan program operations as current customer schools abandon the new guaranty services provider for competitor agencies.

CSAC RECOMMENDATION: CSAC has repeatedly expressed its willingness to explore alternative models for administering the FFEL Program in California in ways that protect the services and benefits currently provides to California students and schools. CSAC, however, is strongly opposed to the idea of issuing an RFP to find a new contractor to service the FFEL loan program. CSAC recommends instead that the CPR Commission endorse the action taken by the Legislature, and approved by the Governor, to expand CSAC's authority to enter into new income-producing activities.

ETV 24: Use a Portion of the Student Loan Operating Fund Surplus to Fund Cal Grant Awards

CPR Recommendation*: The Governor should instruct the Department of Finance, or its successor, to transfer $134 million from the Student Loan Operating Fund to the Cal Grant Program. The Department of Finance, or its successor, should annually examine the Student Operating Loan balance and determine if a portion of that balance can be used to help fund the Cal Grant Program.*

CSAC ANALYSIS:

Summary: The current 2004-05 Budget includes a provision that will take $146.5 million from the Student Loan Operating Fund to backfill CSAC operations including the Cal Grant program. This is even more than the CPR report recommended taking. The first part of this recommendation is therefore moot.

KEY ISSUES

Student Loan Operating Fund

The federal 1998 Reauthorization of the Higher Education Act changed the funding model for guaranty agencies. Most importantly, in addition to a Federal Fund, it allowed for the creation of an Operating Fund, the contents of which are the property of the guaranty agency rather than the federal government. SB 1031, Statutes of 1999, formally established the Student Loan Operating Fund (SLOF) in the State Treasury as a State fund within the custody and control of CSAC. (SB 1031 also permitted CSAC to provide FFEL services out of state.)

The SLOF is used to cover typical guaranty agency related activities. The SLOF provides additional flexibility to CSAC because it can also be used to fund “other student financial aid-related activities for the benefit of students, as selected by the guaranty agency.”

A significant amount of revenue into the SLOF in the past two years has come from income derived by EDFUND through a “Voluntary Flexible Agreement” or VFA with the U.S. Department of Education.

The 1998 reauthorization of the Higher Education Act established authority for the U.S. Secretary of Education to enter into VFAs with guaranty agencies. (CSAC was one of the four GA’s originally selected for a VFA in 2001.) The VFA agreement can be cancelled by the Secretary with 90 days’ notice, or it can be renegotiated. Under the program, the Department is authorized to negotiate individually with guaranty agencies the performance measures for which each agency is compensated, with the aim of creating incentives for high performance, efficiency and innovation. The CSAC/EDFUND VFA includes provisions tying federal compensation to our default rate and collections performance.

The CSAC VFA generated a significant portion of loan program revenue in the 2002-03 federal fiscal year. CSAC, however, has been notified that its VFA will be renegotiated by USED for the 2004-05 federal fiscal year. CSAC anticipates that revenues from the existing VFA will be reduced under a renegotiated agreement. In addition, the next Reauthorization of the Higher Education Act scheduled for 2005 may put constraints on the Secretary that affect VFA performance-based payments to guaranty agencies.

CPR is misinformed on CSAC's business diversification efforts

The CPR report states that "the huge surplus [in the Student Loan Operating Fund] suggests that CSAC has not been actively taking advantage of [business diversification] opportunities during the last three years." To the contrary, CSAC and EDFUND throughout 2004 have worked with the Department of Finance and the Legislature on legislation and budget language that will allow the shifting of funds so that business diversification can begin.

The 2004 Budget Act signed by Governor Schwarzenegger includes the funds necessary ($70 million from the Student Loan Operating Fund) to pursue alternative financial aid products and services, as outlined in the provisions in SB 1108 (Chapter 216, Statutes of 2004).

The transfer of $146.5 million from the SLOF, along with the uncertainty over the future of VFA agreements, makes it imperative that CSAC receive the necessary authority to continue to provide valuable benefits to California students and families through diversified financial aid services and products.

Finally, the CPR recommends that the "Department of Finance…should annually examine the Student Operating Loan balance and determine if a portion of that balance can be used to help fund the Cal Grant Program." The current State budget makes clear that this use of funds is a one-time occurrence.
In fact, the additional amounts used by the State to fund Cal Grant awards, the need to fund business diversification efforts and the ongoing requirements to fund CSAC operations and loan program operations make it highly unlikely that surplus funds will be available in the next few years.

CSAC RECOMMENDATION: The CPR-recommended action of transferring funds from the Student Loan Operating Fund to backfill expenditures usually covered by the General Fund already has taken place. CSAC's recommendation is that the Student Loan Operating Fund not be considered a source of General Fund replacement monies in the future. These funds already are earmarked for CSAC operations, loan program operations, and diversification efforts to produce long-term income for student and institutional public benefits.