Sunset Advisory Commission

Texas Guaranteed Student Loan Corporation

Staff Report
October 2004

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SUMMARY

Summary

Texas Guaranteed Student Loan Corporation

The Texas Guaranteed Student Loan Corporation (TG), created by the Legislature in 1979, guarantees loans on behalf of the federal government to help students and their parents pay for college or other postsecondary education. Sunset staff evaluated the need for, and benefits of, continuing the Corporation as the administrator of the Federal Family Education Loan Program (FFELP) in Texas. Overall, Sunset staff found that TG's structure and operations work well, providing significant benefits to both Texas and the students who obtain loans through this program.

In approaching this review, Sunset staff encountered several unique circumstances. Unlike most entities under Sunset review, TG is a public, nonprofit corporation – not a state agency; TG operates off fees from the federal government – not a state appropriation; and TG's operations are driven largely by federal law – not its state enabling statute. In addition, the Higher Education Act – the federal law that governs TG's administration of FFELP – is currently undergoing reauthorization by the U.S. Congress, and changes are anticipated that could affect both TG's funding and operations.

TG's structure and operations work well, providing significant benefits to Texans.

Recognizing the need to avoid conflicts with federal law, staff focused on examining TG's accountability as an entity that operates outside many of the State's standard oversight processes, and on activities governed under state, rather than federal, law. The recommendations in this report are designed to make changes in state law to improve TG's accountability to its Board; and its interaction with state agencies in two areas: educating students about financial aid opportunities, and collecting defaulted student loans.

A summary of these recommendations follows.

Issues/Recommendations

Issue 1

Texas Has a Continuing Need for the Texas Guaranteed Student Loan Corporation, but the Current Size of TG's Board Does Not Comply with the Texas Constitution.

Key Recommendations

- Continue the Texas Guaranteed Student Loan Corporation for 12 years.
- Reduce the size of the Texas Guaranteed Student Loan Corporation's Board from ten to nine members.

Issue 2

TG's Internal Auditor Lacks a Direct Link to the Board.

Key Recommendation

- Require the Internal Auditor to report to the Board of Directors.

Issue 3

Texas Lacks a Structure for Maximizing Its Resources, in Conjunction with TG's, to Increase Awareness About Higher Education and Financial Aid Opportunities.

Key Recommendation

- Require the P-16 Council to coordinate higher education and financial aid outreach activities in Texas, and to ensure TG's inclusion in these coordination efforts.

Issue 4

Problems with Identifying and Exchanging Data with Licensing Agencies Limit TG's Ability to Collect From Licensees with Defaulted Student Loans.

Key Recommendations

- Require licensing agencies to provide TG with a written or electronic list of licensees for use in identifying individuals who have defaulted student loans, rather than requiring licensing agencies to identify these individuals.
- Direct TG to compile a more comprehensive list of licensing agencies for inclusion in its search for professional and occupational licensees with defaulted student loans.

Fiscal Implication Summary

The recommendations offered in this report would have no fiscal impact to the State or TG.

ISSUES

Issue 1

Texas Has a Continuing Need for the Texas Guaranteed Student Loan Corporation, but the Current Size of TG's Board Does Not Comply with the Texas Constitution.

Summary

Key Recommendations

- Continue the Texas Guaranteed Student Loan Corporation for 12 years.
- Reduce the size of the Texas Guaranteed Student Loan Corporation's Board from ten to nine members.

Key Findings

- The Legislature created the Texas Guaranteed Student Loan Corporation (TG) to administer the Federal Family Education Loan Program in Texas.
- Texas has a clear and continuing interest in having a guaranty agency to administer the Federal Family Education Loan Program (FFELP) for the State.
- TG functions effectively in its role as FFELP administrator, with the State benefitting from TG's commitment to Texas students, schools, and lenders.
- No benefit would result from changing TG's organizational structure, or having any other agency perform TG's functions.
- The size of TG's Board does not comply with the Texas Constitution.

Conclusion

The Legislature created the Texas Guaranteed Student Loan Corporation as a public, nonprofit corporation in 1979, to administer the Federal Family Education Loan Program in Texas. As a FFELP administrator, TG issues guarantees to private lenders on behalf of the federal government, so that lenders will make low-interest loans available to students and their families to help pay for the cost of postsecondary education. In addition, TG conducts delinquency and default prevention activities, reimburses lenders when borrowers fail to meet their loan obligations, collects on defaulted student loans, and ensures schools and lenders comply with federal regulations.

The Sunset review evaluated the continuing need for an independent agency to administer FFELP in Texas, and whether TG should remain a public, nonprofit corporation. The review concluded that TG is an effective FFELP administrator and the State of Texas benefits from the services TG provides. Further, because TG is federally funded and receives no state appropriations, no benefit would result from changing the current organizational structure or transferring TG's functions to any other agency. However, Sunset staff found that the current size of TG's Board does not comply with the Texas Constitution. Sunset staff concluded that the Legislature should continue TG as a public, nonprofit corporation for 12 years, but reduce the size of TG's Board by one member.

Support

The Legislature created the Texas Guaranteed Student Loan Corporation to administer the Federal Family Education Loan Program in Texas.

FFELP encourages private lenders to make low-interest loans to students and their parents to help pay for the cost of education.

- In 1965, the United States Congress enacted the Higher Education Act, creating federal student aid programs, such as the Federal Family Education Loan Program (FFELP). Administered by the Department of Education, FFELP is a unique, public-private partnership that encourages private lenders to make low-interest loans to students and their parents to help pay for the cost of postsecondary education. The Department of Education protects lenders from financial loss by guaranteeing the repayment of the loans in the event of the borrower's death, disability, or default.

  Initially, the participation of lenders did not keep up with the demand for student loans, due in part to the program's high degree of centralization at the federal level. In response, in 1976, Congress amended the Higher Education Act to include financial incentives for states to create guaranty agencies. The guaranty agencies would insure the repayment of student loans to lenders on behalf of the federal government, and would also aid in the collection of defaulted loans from borrowers. The textbox, *FFELP Process,* outlines the major characteristics of this partnership.

  > ***FFELP Process***
  >
  > Major characteristics of the Federal Family Education Loan Program:
  >
  > - schools determine students' and parents' eligibility for loans;
  > - private lenders, such as financial institutions, originate and service the loans;
  > - TG reviews loan applications and issues guarantees to lenders;
  > - the federal government subsidizes and reinsures the loans; and,
  > - students pay back the loans.

  After conducting an interim study on the options available for a student loan guarantee program, the Texas Legislature created the Texas Guaranteed Student Loan Corporation (TG) in 1979, as a public, nonprofit corporation, to serve as the FFELP administrator in Texas. To fund TG's initial start-up costs, the Legislature approved a one-time appropriation of $1.5 million, derived from federal funds paid by the Department of Education to the Texas Higher Education Coordinating Board. The federal government also contributed approximately $10 million in federal advances.

The Legislature created TG in 1979 to serve as the FFELP administrator in Texas.

- As the FFELP administrator in Texas, TG issues guarantees for three types of FFELP loans: Stafford loans, Parent Loans for Undergraduate Students (PLUS loans), and Consolidation Loans. In addition, TG helps borrowers avoid loan delinquency and default, reimburses lenders for loans that are not paid in full by the borrower, collects from borrowers who default on their loans, and oversees schools and lenders participating in FFELP to ensure compliance with federal regulations. TG also performs outreach activities to increase awareness of postsecondary education and financial aid opportunities.

- Because TG is not a state agency, it receives no state appropriations. Instead, it receives fees from the federal government for the loans it guarantees and services. In fiscal year 2003, TG's revenues from the Department of Education totaled more than $128 million. That same year, TG operated on a budget of $80 million and with a staff of 578 employees.

- TG is governed by a ten-member Board, nine of whom are appointed by the Governor. Of the nine Governor appointees, five members have knowledge or experience in finance; three members are from the faculty or administration of a postsecondary educational institution; and one member is a full-time student enrolled at a postsecondary institution. The Comptroller of Public Accounts serves as a permanent, ex officio, voting member of the Board. The chart, *TG Board of Directors*, shows the Corporation's current Board members.

TG receives fees from the Department of Education for the loans it guarantees and services.

TG Board of Directors

Member Name	Term Expiration	Qualification	Residence
Ruben Esquivel, Chair	2009	School	Dallas
Tommy J. Brooks	2009	Finance	Houston
Albon Head, Jr.	2007	Finance	Fort Worth
Morgan Howard	2005	Student	Bryan
Jorja Kimball	2005	School	College Station
James Langabeer	2007	School	Edinburg
Jerry Don Miller, Ph.D.	2007	Finance	Canyon
Jane Phipps	2005	Finance	San Antonio
Grace Shore	2009	Finance	Longview
Carole Keeton Strayhorn	Permanent Member	Comptroller of Public Accounts	Austin

Texas has a clear and continuing interest in having a guaranty agency to administer FFELP for the State.

- With the increasing cost of attending postsecondary education, Texas students rely heavily on FFELP loans to fund their education. In the 2002-2003 school year, TG issued $2.3 billion in student loan guarantees, helping approximately 416,000 students pursue their education beyond high school. That same year, FFELP loans represented the largest single source of student aid awarded in the state, about 59 percent. Since TG's inception, TG has issued guarantees for more than $32.5 billion in FFELP loans to 2.5 million students.

- TG's loan guarantees on behalf of the federal government help to encourage lenders' participation in FFELP. Absent a guarantee of repayment, lenders would be unlikely to make capital available to students, who rarely have collateral or an established credit history. TG-backed loans afford lenders a level of security that would not otherwise be present, and in the event a borrower defaults, TG reimburses the

Texas students rely heavily on FFELP loans to fund their education.

lender, in most cases, between 98 to 100 percent of the outstanding loan amount and accrued interest.

TG's delinquency and default prevention programs assist students in successfully repaying their student loans.

- Other functions performed by TG contribute to the financial health and stability of FFELP. TG's delinquency and default prevention programs assist students in successfully repaying their student loans by providing information about debt management and helping students to understand their loan repayment obligations. Further, TG is proactive in averting loan delinquencies and defaults by encouraging students to consider re-enrolling in school if they have dropped out or stopped attending mid-semester, as those borrowers are at the highest risk of defaulting on their student loans. When borrowers default on their student loans, TG attempts to recover the funds from the borrower. These efforts ensure that FFELP borrowers satisfy their student loan obligations so that the program can continue to be available to the next generation of students.
- TG also serves as an important source of information for Texas students and schools. TG sponsors educational awareness events throughout Texas, answers financial aid-related questions through its Customer Assistance call center, distributes college awareness posters and brochures, and provides financial aid training and assistance to schools, lenders, and community organizations. In addition, TG operates the Texas Financial Aid Information Call Center on behalf of the Texas Higher Education Coordinating Board, at no cost to the State. TG's outreach efforts ensure that Texans are aware of the costs of obtaining a postsecondary education, the types of schools and programs available, and ways to finance their educational and career goals.
- The Department of Education relies on TG's oversight of FFELP participants to protect the integrity of the federal financial aid program. Since 1988, federal law has charged TG with ensuring that FFELP participants comply with federal laws and regulations. TG ensures that only eligible borrowers receive FFELP loans, and schools and lenders administer the loans as required by the Higher Education Act and federal regulations. In the event a school or lender commits serious violations of federal requirements, federal law requires TG to take action to revoke FFELP eligibility, and to initiate a referral to the Department to revoke all federal student aid eligibility.

TG has consistently met or exceeded the Department of Education's performance goals for administering FFELP.

TG functions effectively in its role as FFELP administrator, with the State benefitting from TG's commitment to Texas students, schools, and lenders.

- TG has successfully and consistently met or exceeded the Department of Education's performance goals for administering FFELP. In fact, in March 2001, the Department of Education selected TG as one of only four guaranty agencies to participate in a pilot project to explore the potential benefits of alternative funding mechanisms. Under terms of the new contract, the Department of Education afforded TG greater program management flexibility over FFELP and tied its funding to performance. TG's specific agreement increased its focus on preventing loan delinquencies and defaults, rather than the more standard approach that focused on the collection of defaulted loans.

Under this funding model, TG successfully decreased the number of loan defaults and claims paid to lenders, while increasing its collections on defaulted loans. Specifically, TG assisted in resolving 91 percent of loan delinquencies reported by lenders in fiscal year 2003, while decreasing the number of claims paid on defaulted loans by 11.5 percent, saving the federal government $37 million.[1] TG also recovered more than $291.5 million in defaulted loans – the fourth time in TG's history it surpassed the $200 million mark.[2] As a result of its high performance, TG increased its program revenues from the Department of Education almost 19 percent, or $20 million, to more than $128 million in fiscal year 2003.

TG has decreased defaults overall, while increasing its collections on loans that have defaulted.

- TG has experienced significant growth as a guaranty agency, both in terms of market share and customers served. As shown in the chart, *Top Guaranty Agencies in the Nation,* TG is one of the leading guaranty agencies in the nation, holding the fifth largest market share of the 36 state and regional guaranty agencies. TG has steadily increased its loan guarantee volume over the past several years, averaging 12 percent annual growth since 1998. Despite fierce competition among guaranty agencies to secure market share in Texas, TG currently serves 81.2 percent of the Texas market. In addition, TG has made significant strides in guaranteeing loans for schools outside of Texas, with more than $263 million in new loan volume guaranteed for out-of-state schools in fiscal year 2003. Out-of-state loan guarantees currently represent approximately 6 percent of TG's annual volume.

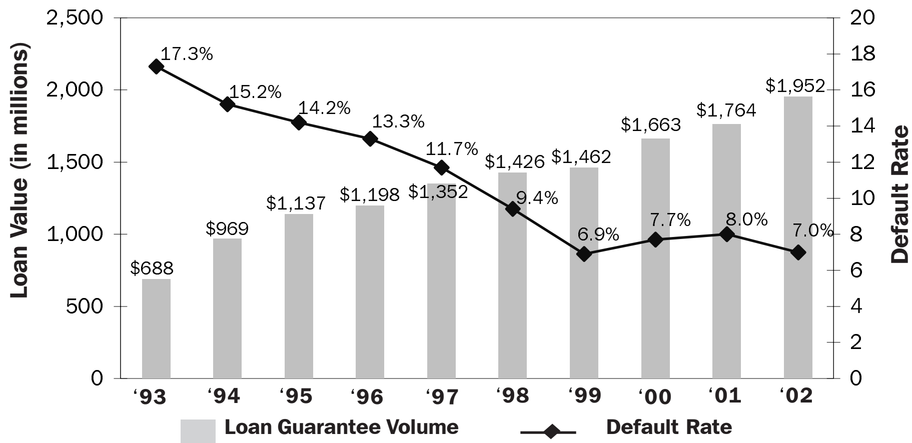
Top Guaranty Agencies in the Nation

Guaranty Agency	Loan Volume (in billions)	Market Share
1. United Student Aid Funds	$8.8	18.4%
2. EdFund	$4.0	8.5%
3. Great Lakes Higher Education Corporation	$2.7	5.5%
4. Pennsylvania Higher Education Assistance Agency	$2.6	5.4%
5. Texas Guaranteed Student Loan Corporation	$2.3	4.8%

TG has also steadily increased the number of borrowers, schools, and lenders participating in FFELP through TG. The number of TG borrowers increased to 416,000 in fiscal year 2003, a 24 percent increase from the previous fiscal year. During that same period, the number of schools participating in FFELP with TG also slightly increased to 774 schools, including 289 four-year private institutions, 160 four-year public institutions, 148 career schools, 102 two-year institutions, and 75 other institutions. Lender participation with TG grew to 303 lenders in fiscal year 2003 – an 8 percent increase from the previous fiscal year.[3]

- Despite TG's significant growth over the past several years, TG has kept its default rate low – one of the most significant measures of success for a guaranty agency. As shown in the chart, *TG Loan Guarantees and Default Rates*, while TG's loan guarantee volume has risen significantly, TG's default rate has declined.

TG Loan Guarantees and Default Rates



TG's default rate of 7 percent is down significantly from 17.3 percent in 1993.

In fiscal year 2002 – the latest statistics available – the Department of Education calculated TG's default rate at 7 percent, down from 17.3 percent in 1993. TG attributes its declining default rate to its enhanced default prevention efforts and program reviews of schools and lenders.

- TG also helps schools keep their default rates low, thereby ensuring the schools' continued participation in federal student aid programs. For example, in 1999, certain Historically Black Colleges and Universities (HBCUs) in Texas were at risk of losing their eligibility for financial aid due to multiple, consecutive years of high default rates above the Department of Education's allowable threshold of 25 percent. With services and technical assistance provided by TG, HBCUs were able to significantly reduce cohort default rates within the allowable range, thereby maintaining their FFELP eligibility. As another example, TG successfully helped the University of Texas – Pan American to reduce its default rate by nearly 15 percentage points, down to 6.5 percent, by using a training model on effective default prevention strategies.

- TG shares the benefits of its financial success with Texas students and schools. Since 1999, TG has waived its guarantee fee for FFELP borrowers of Stafford and PLUS loans. The fee, of up to one percent of a borrower's requested loan amount, is authorized by the Higher Education Act. However, TG has waived this fee for all student and parent borrowers, saving the borrowers about $90 million dollars over the past six years. As another example, in 2000, TG established the Charley Wootan Grant Program, providing grants to Texas postsecondary institutions. The schools in turn award the funds to needy students. Between 2001 and 2003, TG awarded more than $1.7 million in grants to Texas schools.

- TG's progressive use of technology has made the financial aid process more efficient for FFELP participants. Due to technological enhancements TG implemented in fiscal year 2003, TG now processes loan guarantees for Stafford and PLUS loans in less than one minute, a particularly important factor during TG's peak season when it processes an average of 4,800 loan guarantees per day. To make loan processing more efficient for schools and lenders, TG offers reliable, Web-based tools, such as an online loan application and tracking process, and an electronic funds transfer system. In fiscal year 2003, TG facilitated 865,000 electronic disbursements, eliminating paperwork for schools and making $1.6 billion in loans available to borrowers in less time. That same year, about 93 percent of loan applications that TG guaranteed were submitted electronically by borrowers.

TG's progressive use of technology makes the financial aid process more efficient for FFELP participants.

- TG's customers – borrowers, schools and lenders – give TG high marks in customer service. On its most recent external customer satisfaction survey, conducted by an independent research firm, TG scored its best corporate-wide score to date, 4.28 out of a possible 5.0. About 94 percent of schools and lenders gave TG favorable marks in customer support, and rated TG as among the best, or better than most, when comparing TG's financial aid information to other sources. Some of the highest ratings among borrowers showed that borrowers perceive TG as courteous, knowledgeable, and available to answer calls.

No benefit would result from changing TG's structure, or having any other agency perform TG's functions.

- In 1978, an interim committee of the Legislature examined the range of alternatives available to the State for a student loan guarantee program. The Committee's final report recommended that the State create a public, nonprofit corporation to guarantee loans on behalf of the federal government, as that structure would relieve the State from the liabilities associated with a guaranty agency, while providing the agency with the administrative flexibility necessary for effective program administration.[4] That same rationale still holds true today. TG's structure as a nonprofit corporation has served the State well, creating a unique role for TG as it competes for business in the competitive financial aid market, yet promotes its broader social mission of increasing access to postsecondary education. Further, TG performs these functions at no cost to the State.

- Although the organizational structures of other guaranty agencies across the nation vary widely, nonprofit structures have enjoyed the most success. About half of the 36 guaranty agencies nationwide operate as state agencies, while the remaining operate as either public or private nonprofit corporations. However, the top four guaranty agencies in the nation operate as nonprofit corporations.

TG competes for business in the financial aid market, yet promotes a broader social mission of increasing access to higher education.

- No clear benefit exists for transferring TG's functions to a state agency. Although the Texas Higher Education Coordinating Board administers the Hinson-Hazlewood College Student Loan Program, which includes federal Stafford Loans, that agency's loan program operates differently and handles significantly less volume than TG's FFELP-related functions. The Hinson-Hazlewood loan program, which annually provides about $50 million in loans to 8,000 students, is funded through the sale of general obligation bonds that are authorized by the Texas Legislature and subsequently approved by Texas voters.[5] Requiring the Coordinating Board to assume TG's FFELP administrator functions would require a significant increase in the Coordinating Board's staff and additional training at a substantial cost to the State.

- Guaranty agencies in other states could perform TG's functions for the State of Texas, but no distinct advantages were identified to justify such action. Technological advances in guaranteeing and servicing loans have eliminated the need for a guaranty agency in every state. However, most guaranty agencies serve as the guarantor for a single state, while other states contract with guaranty agencies in neighboring states or with a national guarantor, such as United Student Aid Funds, Inc.[6] As a result, Texas could abolish TG and leave postsecondary educational institutions to use an out-of-state guaranty agency, but doing so would most likely result in the loss of the many outreach, awareness, and training programs TG currently performs.

- The federal government operates the William D. Ford Direct Loan Program (Direct Loan Program), providing Stafford, PLUS, and consolidation loans to students. However, under the Direct Loan Program, the federal government fronts the capital for the student loans, bypassing the guaranty agency and the private lender. Since 1992, the Direct Loan Program has gained about 26 percent of the U.S. market share of student loans.

  The Direct Loan Program presently serves as a competitor to, rather than a substitute for, TG. If the Legislature were to abolish TG, postsecondary institutions would ultimately determine whether they would participate in the Direct Loan Program or continue FFELP participation through an out-of-state guaranty agency. TG believes that the competition from the Direct Loan Program has benefitted the financial aid industry as a whole, requiring guaranty agencies to provide better services to FFELP participants to retain their business.

The federal Direct Loan Program serves as a competitor to, rather than a substitute for, TG.

The size of TG's Board does not comply with the Texas Constitution.

- In 1999, Texas voters approved a constitutional amendment that required state boards and commissions created by the Legislature to have an odd number of members. Because the constitutional amendment did not allow boards created before the amendment to continue under their current composition, a temporary provision of the amendment required the Legislature to recreate nonconforming boards to meet the new requirements by September 1, 2003.

- In 2003, in an omnibus bill, the 78th Legislature changed the composition of boards and commissions with an even number of voting members to comply with changes made to the Texas Constitution.[7] Although TG's Board was included in that bill, a drafting error in the bill has resulted in some confusion over the number of Governor appointees on TG's Board. The bill called for TG's Board to be reduced from ten to nine members, by removing one of the five Board members with experience or knowledge in finance who was appointed by the Governor. However, the bill did not reduce the total number of Governor appointees, and as a result, still requires the Governor to appoint nine members. The Comptroller of Public Accounts, who serves as a permanent, ex officio, voting member, is the tenth member.

Recommendations

Change in Statute

1.1 Continue the Texas Guaranteed Student Loan Corporation for 12 years.

This recommendation would continue the Texas Guaranteed Student Loan Corporation as the entity responsible for administering the Federal Family Education Loan Program in Texas.

1.2 Reduce the size of the Texas Guaranteed Student Loan Corporation's Board from ten to nine members.

This recommendation would reduce TG's ten-member Board to a nine-member Board to comply with the Texas Constitution. The Governor would appoint eight members, including four members with knowledge or experience in finance, three members who are on the faculty or administration of an eligible postsecondary educational institution, and one member who is a full-time student enrolled at a postsecondary educational institution. The Comptroller of Public Accounts would continue to serve as a permanent, ex officio, voting member.

Impact

This recommendation would continue the Texas Guaranteed Student Loan Corporation as a public, nonprofit corporation responsible for administering the Federal Family Education Loan Program in Texas. By continuing TG, Texas would retain its administrator of the Federal Family Education Loan Program, thereby helping to remove financial barriers to postsecondary education and increasing students' awareness of postsecondary education and financial aid opportunities. This recommendation would also reduce the size of TG's board from ten to nine members to conform it with the Texas Constitution.

Fiscal Implication

Because TG is federally funded and receives no state appropriations, continuing TG would have no fiscal impact to the State.

[1] Texas Guaranteed Student Loan Corporation, *TG Annual Report 2003*, p. 13. Online. Available: www.tgslc.org/pdf/2003annualrpt.pdf. Accessed: September 17, 2004.

[2] Texas Guaranteed Student Loan Corporation, *State of Student Aid in Texas*, by Robin McMillion et.al., (Round Rock, Texas, April 2004), page 89.

[3] Texas Guaranteed Student Loan Corporation, *State of Student Aid in Texas*, by Robin McMillion et.al., (Round Rock, Texas, April 2004), page 64.

[4] The Texas Legislature, *Special Interim Study Committee on State Involvement in and Administration of Student Loan Programs for Texas,* (Austin, Texas, January 9, 1978), Section I, Committee Recommendation 3.

[5] Texas Higher Education Coordinating Board, *Draft 2005-2009 Agency Strategic Plan*, Prepared at the Request of the Joint Interim Select Committee on Higher Education, (Austin, Texas, May 18, 2004 Hearing), p. 16.

[6] USA Funds, Inc., is the designated guaranty agency for eight states, including Arizona, Hawaii, Indiana, Kansas, Maryland, Mississippi, Nevada, and Wyoming.

[7] Texas Senate Bill 287, 78th Legislature (2003).

Issue 2

TG's Internal Auditor Lacks a Direct Link to the Board.

Summary

Key Recommendation

- Require the Internal Auditor to report to the Board of Directors.

Key Findings

- TG's Chief Executive Officer has direct authority over the Internal Auditor.
- Without a direct link to the Board, the effectiveness of TG's Internal Auditor could be weakened.
- State law requires internal auditors at state agencies to report to their governing boards.
- Emerging standards in the private sector call for auditors to report to the audit committee of the board of directors.

Conclusion

State law requires TG to employ an Internal Auditor to examine the corporation's system of internal controls. Sunset staff examined the structure and current practices of TG's internal audit function and found that it serves as an effective resource to TG as an early identifier of problems within the organization. However, staff also found that state law requires the Internal Auditor to report to TG's Chief Executive Officer (CEO), giving the CEO direct authority over the Internal Auditor. Although TG's CEO and senior management team currently support the internal audit function, the existing reporting structure could pose a conflict if the Internal Auditor was to uncover problems directly associated with the CEO or senior management. By changing the reporting structure to require the Internal Auditor to report to the Board, or a designated subcommittee of the Board, the Legislature would ensure that the Internal Auditor has the independence necessary to carry out required functions, absent the support of management. This change would also align TG with both state agency requirements and private sector best practices, which, over the past several years, have moved toward requiring the Internal Auditor to report to the governing board or a subcommittee of the board.

Support

TG's Chief Executive Officer has direct authority over the Internal Auditor.

TG's Internal Auditor completed 21 audits and 36 investigations in FY 2003.

- TG employs an Internal Auditor to evaluate and improve TG's risk management and internal control processes. The Internal Auditor performs audits and investigations with a team of six auditors and an annual budget of $520,000.
- The Internal Auditor conducts annual assessments on all aspects of TG's operations to identify areas of high risk and, based on the results, develops an audit plan, subject to Board approval. The Internal Auditor reports audit and investigation results, and associated recommendations, to TG's CEO. In addition, state law requires the Internal Auditor to meet with the Board on a regular basis and submit reports to the Board upon request. Currently, the Internal Auditor provides summaries of audit results to the Board and is present at all Board meetings. In fiscal year 2003, the Internal Auditor completed 21 audits and conducted 36 investigations.
- In accordance with statute, TG's CEO appoints the Internal Auditor with the approval of the Board.[1] TG's CEO maintains direct authority over the Internal Auditor, including budget and staff size, and conducts annual evaluations of the Internal Auditor.

Without a direct link to the Board, the effectiveness of TG's Internal Auditor could be weakened.

With annual revenues exceeding $128 million, TG has a clear need for strong internal controls.

- The Internal Auditor currently reports audit findings and recommendations to the CEO, who is the sole person responsible for hiring, firing, and evaluating the Internal Auditor. The reporting relationship has worked well in the past, as TG's CEO fully supports the Internal Auditor. However, under different circumstances, the reporting structure could pose inherent conflicts, for example, if the Internal Auditor uncovered evidence of fraud or fiscal mismanagement by TG's CEO or senior management team.
- TG's status as a federally funded, nonprofit corporation with annual revenues exceeding $128 million makes the need for strong internal controls particularly important. Because TG does not receive state funds, TG is not subject to many of the state's oversight processes, such as the legislative appropriations process. Although TG is subject to federal oversight, the State retains an interest in ensuring proper controls are in place to account for federal tax dollars and the services TG provides to Texas students. The Legislature recognized the importance of minimizing TG's risks in 1989 when it statutorily required TG to employ an Internal Auditor. However, the current reporting structure may not allow the Internal Auditor to operate effectively, absent the support of management.

State law requires internal auditors at state agencies to report to their governing boards.

- The Texas Internal Auditing Act requires internal auditors at state agencies to report directly to the agency's governing board, if the agency has a governing board.[2] Only in the absence of a governing board may the internal auditor report to the executive director. The Act also requires that the board appoint the internal auditor, and maintain oversight of the internal auditor's staffing levels and audit plans. The standards in the Texas Internal Auditing Act reflect changes in best practices made since Sunset's last review of TG in 1989, when it was common practice for the internal auditor to report to the administrator of the agency. Similarly, the Office of the Governor recommended that internal auditors at state agencies report directly to their governing bodies' audit committee, to express any concerns that may exist over management's commitment to internal controls or to report allegations of fraud involving management.[3]

State agency boards oversee internal audit plans and staffing levels.

Emerging standards in the private sector call for auditors to report to the audit committee of the board of directors.

- In response to several well publicized corporate and accounting scandals, the federal government enacted the Sarbanes-Oxley Act of 2002 in an effort to strengthen corporate accountability, improve the quality and transparency of financial reporting, and reduce the likelihood of fraud by corporate executives. The Act requires publicly held corporations to strengthen their internal controls, including requiring external auditors to report to the company's audit committee, and not to management. The Act also mandates other requirements aimed at ensuring the objectivity and independence of audits. Although the Act does not directly address the reporting structure of internal auditors, emerging best practices now call for the internal auditor to report to the audit committee as well.[4] This reporting relationship is becoming increasingly common in the private sector.[5]

- The New York Stock Exchange requires listed corporations to have both an internal audit function and an audit committee. The Exchange also requires the audit committee to assist the board in overseeing the internal auditor.[6]

Corporate scandals in the private sector have resulted in requirements to strengthen internal controls.

- While no legal standards exist for the relationship between the board and internal auditors in public, nonprofit corporations, many nonprofits are examining ways to avoid potential problems with their internal controls. In the wake of recent corporate scandals, elected officials in Congress and several states have expressed an interest in mandating stronger internal controls in nonprofit organizations similar to those mandated on publicly traded corporations by the Sarbanes-Oxley Act.[7]

Recommendation

Change in Statute

2.1 Require TG's Internal Auditor to report to the Board of Directors.

This recommendation would change the current reporting structure, which requires the Internal Auditor to report to TG's CEO, to instead require the Internal Auditor to report to the Board. The Board could also opt to have the Internal Auditor report to a designated subcommittee of the Board. The Internal Auditor should report on the progress and results of audits at Board meetings, which occur at least twice a year. Under this recommendation, TG's Board would have the authority to hire and fire the Internal Auditor and would approve the Internal Auditor's budget, staffing level, and audit plans. TG's CEO would continue to provide administrative day-to-day support. The Internal Auditor would also continue to work closely with TG's CEO and senior management team to address audit related activities.

Impact

This recommendation would provide a structure that better ensures TG's Board is informed of areas of high risk or weaknesses in internal controls at TG. Although the Internal Auditor would continue to work closely with TG's CEO and senior management, eliminating the CEO's direct oversight over the Internal Auditor would help ensure the objectivity of the Internal Auditor's work. Establishing a direct reporting line between the Internal Auditor and the Board of Directors would align TG's reporting structure with the corporate and state agency standards emerging in the post Sarbanes-Oxley environment. Although no serious problems were found with TG's current operations, this recommendation would ensure that an appropriate structure is in place to identify potential problems in the future.

Fiscal Implication

This recommendation would not result in any fiscal impact to the State or TG.

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[1] Texas Education Code, sec. 57.761.

[2] Texas Government Code, sec. 2102.007.

[3] Office of the Governor, *Best Practices for the Prevention and Detection of Fraud*, p.17. Online. Available: www.governor.state.tx.us/divisions/bpp/files/fraud_best_practices.doc. Accessed: August 25, 2004.

[4] Protiviti Independent Risk Consulting, *Guide to the Sarbanes-Oxley Act: Internal Control Reporting Requirements – Frequently Asked Questions Regarding Section 404, 2nd Edition,* p. 96.

[5] Deloitte Development, LLC. *The Evolving Relationship between the Audit Committee and the Internal Audit Function*, p.2. Online. Available: www.deloitte.com/dtt/cda/doc/content/us_assur_ACBriefApril04.pdf. Accessed: August 25, 2004.

[6] New York Stock Exchange, *NYSE Listed Company Manual,* Section 303A.07(c). Online. Available: www.nyse.com/lcm/lcm_section.html. Accessed: August 25, 2004.

[7] U.S. Congress, Senate Finance Committee, *Senate Finance Committee Staff Discussion Draft*, pp. 9-15. Online. Available: www.senate.gov/~finance/hearings/testimony/2004test/062204stfdis.pdf. Accessed: August 25, 2004.

Issue 3

Texas Lacks a Structure for Maximizing Its Resources, in Conjunction with TG's, to Increase Awareness About Higher Education and Financial Aid Opportunities.

Summary

Key Recommendation

- Require the P-16 Council to coordinate higher education and financial aid outreach activities in Texas, and to ensure TG's inclusion in these coordination efforts.

Key Findings

- TG performs many outreach activities to increase awareness about higher education and financial aid opportunities.
- The Coordinating Board and TEA also conduct higher education and financial aid outreach.
- Despite these outreach efforts to help increase awareness of financial aid opportunities, most Texas students still rank cost as the major barrier to higher education.
- Texas lacks a structure for maximizing its resources, in conjunction with TG's, to increase awareness about higher education and financial aid opportunities.

Conclusion

In addition to administering the Federal Family Education Loan Program, state law charges TG with coordinating with the Texas Higher Education Coordinating Board and the Texas Education Agency on activities designed to increase awareness of higher education and financial aid. Sunset staff reviewed TG's current outreach activities in relation to the State's goal of increasing college participation in Texas, and concluded that while TG's outreach efforts offer a valuable resource to the State, the Coordinating Board, TEA, and TG lack a clear mechanism to coordinate on higher education and financial aid outreach. Staff determined that requiring the P-16 Council – the State's structure for addressing education issues – to coordinate higher education and financial aid outreach activities in conjunction with TG would reduce the potential for duplication of existing outreach activities; and create opportunities for further collaboration, potentially increasing participation in higher education.

Support

TG performs many outreach activities to increase awareness about higher education and financial aid opportunities.

- As a FFELP administrator, TG's primary mission is to guarantee low-interest student loans on behalf of the federal government. State law also requires TG to actively engage in and support programs designed to increase awareness about postsecondary education and financial aid availability. Further, the law requires TG to coordinate its outreach efforts with the Texas Higher Education Coordinating Board (the Coordinating Board), the Texas Education Agency (TEA), and other educational associations and institutions.[1]

In fiscal year 2003, TG spent about $4.5 million on outreach efforts to educate people about higher education and financial aid opportunities.

- TG performs many outreach functions aimed at students, parents, schools, and community organizations. TG's outreach efforts educate people about financial aid availability and higher education opportunities, as well as responsible borrowing and debt management. Typical outreach efforts include presentations for students and parents, providing and distributing brochures, and conducting workshops. The table, *Selected TG Outreach Activities*, provides some examples of the activities TG supports. TG spent about $4.5 million in fiscal year 2003 on these and other outreach related activities.

Selected TG Outreach Activities

Program	Objective
Free Application for Federal Student Aid (FAFSA) Teleconference	TG holds an annual teleconference, in English and Spanish, that provides students and parents with information on how to complete the FAFSA, which determines a student's financial aid package, including federal and state loan, scholarship, work-study, and grant aid. Last year, 156 sites showed the teleconference live, and TG distributed more than 1,200 tapes of the teleconference.
Ambassador Program	TG trains volunteers from within TG to conduct FAFSA and general financial aid training. Working with community organizations, TG's ambassadors participated in more than 100 events last year.
Texas Financial Aid Information Center	Working with the Coordinating Board, TG supports a toll-free hotline offering assistance, in English and Spanish, on financial aid, college opportunities, career exploration, and other aspects of the higher education experience. In fiscal year 2003, TG received about 15,000 calls on the hotline number.
College Bound Newsletter Publication	In collaboration with the Coordinating Board, TG produces the semi-annual *College Bound* newsletter that provides information about higher education and financial aid opportunities. The newsletter goes to more than 600,000 students in high schools with high minority enrollment.
Council for the Management of Educational Finance	Supported by TG, the Council develops and distributes publications and posters; and administers public service announcements and workshops to help inform high school and middle school students about financial aid opportunities, default prevention, and debt management.
College Planning Web sites	TG supports many Web sites that provide prospective students with information about college planning and financial aid. A textbox in the Agency Information section of this report describes these Web sites.

The Coordinating Board and TEA also conduct higher education and financial aid outreach.

- The Coordinating Board performs outreach activities to ensure students and parents realize the benefits of higher education and the necessary steps to prepare academically and financially for college.[2] The Coordinating Board provides many of its outreach activities through its College for Texans Campaign (the Campaign), a public awareness campaign mandated by state law that aims to get 500,000 new students to enroll in college by 2015.[3] To spread these messages, the Campaign uses television, radio, and print advertisements; college recruiting centers located in schools; training workshops; and other campaign events. The Campaign seeks to coordinate with existing programs rather than duplicate efforts.

The Coordinating Board aims to enroll 500,000 new students in college by 2015.

- As the agency that oversees primary and secondary education, TEA also plays a role in higher education and financial aid outreach. State law requires TEA and the Coordinating Board to work with school districts that have low postsecondary education enrollment percentages to increase the number of students that go to college.[4] Plans must include initiatives to get more high school students to fill out the Free Application for Federal Student Aid (FAFSA). The law also requires high school counselors to provide students with information about higher education and financial aid availability at the beginning of high school and during their senior year.[5]

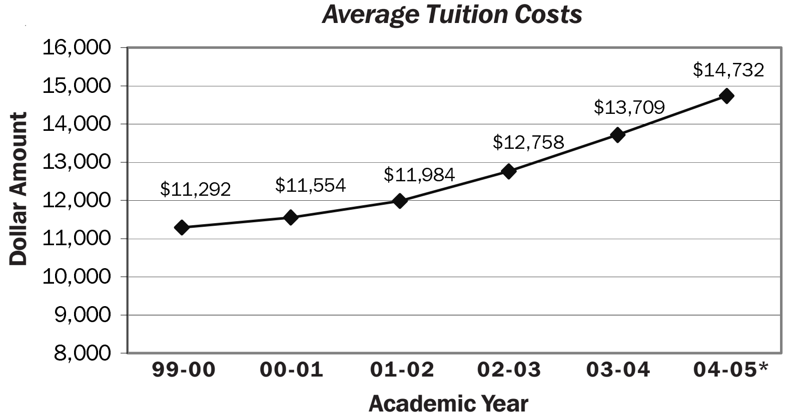
Tuition costs have increased 30 percent over the last five years in Texas.

Despite these outreach efforts to help increase awareness of financial aid opportunities, most Texas students still rank cost as the major barrier to higher education.

- A study by the Coordinating Board shows that most students rank cost as the biggest barrier to higher education.[6] Many students may not understand that financial aid, including grants, scholarships, work-study programs, and loans, is available to help pay for higher education, or how to go about applying for financial aid. Sharing information about the benefits of higher education and how to prepare, both academically and financially, is crucial to getting more students to enroll.

Rising tuition costs pose additional obstacles to enrolling more Texans in college. The graph, *Average Tuition Costs*, shows the average increase in tuition costs over the last five years for a four-year public institution in Texas, as reported to the Coordinating Board.[7] From 1999 to 2004, tuition costs increased 30 percent in Texas. Nationally, economists estimate that the number of new students that enroll in college drops by three to four percentage points for every $1,000 increase in tuition.[8]

Average Tuition Costs



*Tuition cost for 2004-2005 is an estimate made by the Coordinating Board, based on information provided by schools.

- According to the Coordinating Board, to meet its goal of increasing college enrollment by 500,000 students, 300,000 new students must be recruited from families that have not historically gone to college.[9] Meeting this goal depends on the ability of the State to educate these students about the possibility of attending college and obtaining financial aid.

Meeting the State's goal of increasing college participation depends on educating students about higher education and financial aid opportunities.

Texas lacks a structure for maximizing its resources, in conjunction with TG's, to increase awareness about higher education and financial aid opportunities.

- Due to recent state budgetary constraints, the Coordinating Board and TEA, like other state agencies, have less money available for outreach and awareness purposes. Limited resources challenge the success of such initiatives as the College for Texans Campaign and require greater coordination between all agencies involved in education access.

- TG has resources to contribute to many different outreach and educational initiatives, and federal law authorizes TG to spend money on financial aid-related activities in addition to standard FFELP-related activities, as determined by TG. In addition to its broader social mission, as a public nonprofit corporation, TG must reinvest profits into worthwhile and appropriate activities that are within federal guidelines.

  For example, TG's Board recently adopted a plan designed to support the State in improving access and participation in postsecondary education, college retention, and student success, with an emphasis on students from low- to moderate-income families. Under this plan, the Board will approve contributions for outreach programs on a case by case basis, not to exceed a specified percentage of TG's available funds. For fiscal year 2005, TG estimates it will have about $4.75 million in available funds to spend on public benefit activities, as determined by the Board.

No current structure exists for the Coordinating Board, TEA, and TG to coordinate outreach activities.

- Currently, no structure exists for the Coordinating Board, TEA, and TG to discuss or coordinate their different higher education and financial aid outreach activities. TG coordinates on outreach with the Coordinating Board through a memorandum of understanding, but does not include TEA. TG and TEA had a memorandum of understanding, but it has since expired, and the two entities have not collaborated in recent years. The lack of a formal structure for these three entities to coordinate outreach functions increases the potential for duplication or gaps, does not maximize limited resources, and could contribute to an unclear message about education access, ultimately impacting the ability of the State to increase participation in higher education.

- To achieve better interagency coordination between TEA, the Coordinating Board, and other state agencies regulating workforce and education in Texas, the Legislature created the P-16 Council (the Council), but TG has no formal involvement with the Council. The textbox, *P-16 Council Composition*, describes who serves on the Council. State law charges the Council with advising the Coordinating Board and the State Board of Education on such things as coordinating postsecondary activities, teacher retention and recruitment programs, and preparation of high school students for postsecondary study.[10] However, the Council is not charged with coordinating higher education and financial aid outreach, although, in the past, the Council has addressed issues such as aligning high school curriculum with college admission requirements and the progress of the College for Texans Campaign.

> ***P-16 Council Composition***
>
> The P-16 Council is composed of the Commissioner of Education, the Commissioner of Higher Education, the Executive Director of the Texas Workforce Commission, and the Executive Director of the State Board for Educator Certification. These members may appoint additional members, as deemed neccessary.

Recommendation

Change in Statute

3.1 Require the P-16 Council to coordinate higher education and financial aid outreach activities in Texas, and to ensure TG's inclusion in these coordination efforts.

This recommendation would require the P-16 Council to add higher education and financial aid awareness programs to its current areas of coordination, and to include TG on these issues. This recommendation would not add TG as a permanent member of the Council, but would ensure TG's inclusion for purposes of coordinating outreach activities.

Impact

As the existing structure in the State to coordinate education activities, expanding the P-16 Council's charge to include higher education and financial aid outreach will provide a mechanism for TG, the Coordinating Board, and TEA to discuss outreach. Creating a formal mechanism for the three entities to discuss financial aid outreach should help reduce gaps and duplication in outreach activities, allow them to maximize limited resources, and provide a unified message to Texans about higher education and financial aid. Given the increasing costs of tuition, these outreach efforts will likely play a key role in Texas' efforts to increase participation in higher education and assist in reaching the goal of adding 500,000 students to the system by 2015.

Fiscal Implication

This recommendation would have no fiscal impact to the State. However, the recommendation could result in an unidentifiable savings to the Coordinating Board and TEA, as TG could potentially contribute to some outreach activities that would otherwise be funded by the State.

[1] Texas Education Code, sec. 57.21.

[2] Texas Higher Education Coordinating Board, *Closing the Gaps: The Texas Higher Education Plan*, (Austin, Texas, October 2000), p. 1.

[3] Texas Education Code, sec. 61.9701 to 61.9705.

[4] Texas Education Code, sec. 29.904.

[5] Texas Education Code, sec. 33.007.

[6] Sherry Matthews Advocacy Marketing – Texas Higher Education Coordinating Board, *Texas Higher Education Awareness and Motivation Campaign Research* (Austin, Texas, September 2002), p.88.

[7] Tuition costs are for a nine-month period for full-time students who are residents living off campus. The costs include tuition and fees, books and supplies, room and board, transportation, and personal expenses.

[8] June Kronholz, "Who Can Fix Higher (Cost) Education?" *The Wall Street Journal* (August 1, 2004).

[9] Texas Higher Education Coordinating Board, *Preparing for the Emerging Texas: Report on the Effectiveness and Efficiency of State Financial Aid Programs to Help Close the Gaps in Participation and Success* (Austin, Texas, August 2004), p.1.

[10] Texas Education Code, sec. 61.076(b).

Problems with Identifying and Exchanging Data with Licensing Agencies Limit TG's Ability to Collect From Licensees with Defaulted Student Loans.

Summary

Key Recommendations

- Require licensing agencies to provide TG with a written or electronic list of licensees for use in identifying individuals who have defaulted student loans, rather than requiring licensing agencies to identify these individuals.
- Direct TG to compile a more comprehensive list of licensing agencies for inclusion in its search for professional and occupational licensees with defaulted student loans.

Key Findings

- To assist TG in collecting on defaulted student loans, state law authorizes TG to work with state agencies to deny the renewal of professional and occupational licenses until licensees enter into repayment with TG.
- Current law places the burden of identifying licensees with defaulted student loans on the licensing agencies instead of TG, even though TG has a greater interest in, and resources for, administering the data matches.
- Some agencies may not be participating in this program because TG has not identified them as having a licensing function.

Conclusion

The Texas Guaranteed Student Loan Corporation collects on defaulted student loans on behalf of the federal government. To assist in its collection efforts, the Legislature has authorized TG to work with state agencies to identify professional and occupational licensees who have defaulted on their student loans, and to deny the renewal of their licenses until they enter into a repayment agreement with TG. The Sunset review evaluated TG's use of this collection tool and found that current law inappropriately places the burden of identifying licensees with defaulted student loans on the licensing agencies, instead of TG. Additionally, staff found TG has not identified all potential state licensing functions for inclusion in its search for licensees with defaulted loans. This results in missed opportunities for collections and unfairly applies this tool to some professions, but not to others. Staff concluded that requiring agencies to provide TG with a list of licensees, and directing TG to update its list of agencies for inclusion in its search, would increase the effectiveness of this collection tool.

Support

To assist TG in collecting on defaulted student loans, state law authorizes TG to work with state agencies to deny the renewal of professional and occupational licenses until licensees enter into repayment with TG.

TG works with 34 state agencies to deny the license renewal of licensees with defaulted student loans.

- As an administrator of the Federal Family Education Loan Program (FFELP), TG insures loans against default for the federal government. To accomplish this, TG reimburses lenders for defaulted student loans, and in turn is reimbursed by the federal government. TG must then collect on the defaulted loans on behalf of the federal government.
- To assist TG in collecting from borrowers who have defaulted on their student loans, state law requires agencies that issue professional and occupational licenses to deny the renewal of licenses belonging to persons with defaulted loans.[1] The law requires TG to identify and notify the agencies that are subject to this law. Before denying a license renewal application, the licensing agency must afford the licensee an opportunity to contest the denial. TG currently works with 34 state agencies, listed in the textbox, *Agencies that Work with TG on Loan Defaults*, to deny the license renewal of licensees with defaulted loans.[2] In fiscal year 2003, TG identified 23,792 state licensees with defaulted student loans.

  Once a licensee enters into a repayment agreement with TG, the licensing agency may release the hold on the license renewal. In fiscal year 2003, about 550 licensees with defaulted student loans entered into repayment agreements with TG based on the effective use of this collection tool.

Agencies that Work with TG on Loan Defaults

The following agencies work with TG to identify licensees who have defaulted on their student loans.

Board of Public Accountancy
Department of Agriculture
Board of Architectural Examiners
State Bar of Texas[3]
Board of Barber Examiners
Board of Chiropractic Examiners
Cosmetology Commission
Court Reporters Certification Board
Commission for the Deaf and Hard of Hearing[4]
Board of Dental Examiners
Board of Professional Engineers
Commission on Environmental Quality
Funeral Service Commission
Department of Health[5]
Department of Housing and Community Affairs
Department of Human Services[6]
Department of Insurance
Board of Professional Land Surveying
Commission on Law Enforcement Officer Standards and Education
Department of Licensing and Regulation
Board of Medical Examiners[7]
Board of Nurse Examiners
Optometry Board
Board of Pharmacy
Executive Council of Physical Therapy and Occupational Therapy Examiners
Board of Plumbing Examiners
Board of Podiatric Examiners
Polygraph Examiners Board
Private Security Board
Board of Examiners of Psychologists
Real Estate Commission
Structural Pest Control Board
Board of Tax Professional Examiners
Board of Veterinary Medical Examiners

Current law places the burden of identifying licensees with defaulted student loans on the licensing agencies instead of TG, even though TG has the greater interest in, and resources for, administering the data matches.

- Although TG has a vested interest in gaining licensee information to use in its collections efforts, state law places the burden of administering the matches on the licensing agencies. The statute requires TG to identify persons whose loans are in default and provide a list of those names to licensing agencies. The licensing agencies must then match the information against their licensee lists. While many licensing agencies cooperate with TG in this effort, matching this data is not a high priority for them, and can be very burdensome, as TG had about 90,700 individuals with defaulted loans at the end of fiscal year 2003. In fact, all participating agencies have opted to send information to TG to let them perform the matching process.

All participating state agencies have opted to send information to TG to perform the matching process.

- While TG possesses the technological and administrative resources to efficiently conduct the data exchange and matching process, many state licensing agencies do not. TG indicated that some agencies have difficulty producing an electronic list of licensees, and cannot effectively take TG's list of defaulted borrowers and compare it to their own. With limited funds, many agencies simply have difficulty dedicating the staff and resources required for conducting these matches.

Some agencies may not be participating in this program because TG has not identified them as having a licensing function.

- Since implementing the program in 1989, TG has never updated its list of licensing agencies subject to these requirements. Only agencies that TG identifies, and provides written notice to, are required to deny license renewals. By not updating its list of agencies, TG is missing the opportunity to work with agencies that have been recently created by the Legislature, or those that have a broader function beyond licensing. For example, in 2000, the Texas Savings and Loan Department began licensing more than 27,000 mortgage brokers and loan officers, in addition to its broader function of regulating savings banks. As another example, in 2003, the Legislature created the Texas Residential Construction Commission, and required the Commission to certify about 15,000 builders. However, TG does not work with either of these agencies. The table, *Selected Agencies Not Participating with TG on Loan Defaults*, provides some

Selected Agencies Not Participating with TG on Loan Defaults

Agency	Licensing Function	Estimated Number of Licensees
State Board for Educator Certification	Certifies educators	118,000[8]
Texas Savings and Loan Department	Licenses mortgage brokers and loan officers	27,000
Texas Residential Construction Commission	Certifies registered builders	15,000
Railroad Commission of Texas	Certifies individuals that handle liquified petroleum gas and compressed natural gas/liquified natural gas	10,000
Texas Board of Professional Geoscientists	Licenses geologists, geophysicists, and soil scientists	6,700
Texas Appraiser Licensing and Certification Board	Regulates real estate appraisers	6,500
Texas Commission on Alcohol and Drug Abuse[9]	Regulates licensed chemical dependency counselors	4,800

examples of licensing agencies that could be included in TG's annual match, but currently are not participating.

Since implementing this program, TG has never updated its list of licensing agencies, resulting in missed opportunities to increase collections.

- By not taking a more comprehensive approach to identifying agencies that could be participating in this program, TG misses opportunities to increase its collections on defaulted loans. For example, because TG does not work with the Savings and Loan Department, it cannot identify whether any of the 27,000 licensed mortgage brokers and loan officers have defaulted student loans.
- In addition, TG's inconsistent application of this collection tool means some state licensees with defaulted loans are held accountable for entering into repayment with TG, and are subject to losing their ability to practice their professions; while other licensees, whose agencies do not participate, are not held accountable. For example, real estate agents, licensed by the Real Estate Commission, could lose their ability to renew their licenses, while real estate appraisers, licensed by the Texas Appraiser Licensing and Certification Board, face no such sanction.

Recommendations

Change in Statute

4.1 Require licensing agencies to provide TG with a written or electronic list of licensees for use in identifying individuals who have defaulted student loans, rather than requiring licensing agencies to identify these individuals.

This recommendation would require licensing agencies to prepare a list, in written or electronic format, of licensees and provide that list to TG annually. TG should use the list to identify individuals with defaulted student loans guaranteed by TG. It would then notify the appropriate agency of any matches so that the licensing agency would deny the license renewal application of any licensee with a defaulted student loan.

Management Action

4.2 Direct TG to compile a more comprehensive list of licensing agencies for inclusion in its search for professional and occupational licensees with defaulted student loans.

This recommendation would direct TG to develop a more comprehensive list of agencies with licensing functions that are subject to this requirement including, but not limited to, the additional agencies identified in this issue. To effectively identify agencies with licensing functions, TG should conduct periodic searches of state statutes that provide for the licensure of individuals, and determine if any new licensing functions have been created that could be subject to this collection tool. Once identified, TG should provide the agencies with written notice of this requirement and work with them to effectively implement it. TG should update its list at least biennially, which would capture any agencies or licensing functions that have been created or reorganized by the Legislature.

Impact

These recommendations would increase TG's ability to collect on defaulted student loans on behalf of the federal government. Requiring licensing agencies to provide TG with a list of licensees would ensure that the burden of performing data matches rests with the agency with primary responsibility for collecting on defaulted student loans. In addition, requiring TG to regularly update its list of agencies with licensing functions would afford TG additional opportunities to identify licensees with defaulted student loans, and ensure that all the State's licensees are held equally accountable.

Fiscal Implication

These recommendations would not have a fiscal impact to the State, but could potentially increase collections made by TG on behalf of the federal government.

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[1] Texas Education Code, sec. 57.491.

[2] Under the Texas Government Code, section 411.172, TG also receives information on concealed handgun licenses issued by the Department of Public Safety.

[3] Although not required by state law, the Supreme Court of Texas has independently required the State Bar of Texas to suspend the licenses of attorneys who have defaulted student loans.

[4] As of September 1, 2004, the Commission for the Deaf and Hard of Hearing is now part of the Department of Assistive and Rehabilitative Services.

[5] Information received from the Texas Department of Health includes information from the individual licensing boards administratively housed at the Department, as well as from the individual licenses issued by the Department. As of September 1, 2004, the Department of Health is now the Department of State Health Services.

[6] As of September 1, 2004, the Department of Human Services is now part of the Department of Aging and Disability Services.

[7] Licensee information from the Board of Medical Examiners includes information from the Board of Acupuncture Examiners and the Board of Physician Assistant Examiners.

[8] Prior to 1999, educators were certified for life. That year, the Legislature required all new educators to be certified for five year periods. Therefore, only those newly certified educators would be subject to denial of license renewal for loan default through TG, or approximately 118,000 of the total 292,000 active certified educators in Texas. Educators include teachers, principals, superintendents, counselors, educational diagnosticians, and learning resource specialists.

[9] As of September 1, 2004, the Texas Commission on Alcohol and Drug Abuse is now part of the Department of State Health Services.

Across-the-Board Recommendations

Texas Guaranteed Student Loan Corporation	
Recommendations	**Across-the-Board Provisions**
Do Not Apply	1. Require public membership on the agency's policymaking body.
Update	2. Require provisions relating to conflicts of interest.
Update	3. Require unbiased appointments to the agency's policymaking body.
Apply	4. Provide that the Governor designate the presiding officer of the policymaking body.
Update	5. Specify grounds for removal of a member of the policymaking body.
Modify	6. Require training for members of the policymaking body.
Update	7. Require separation of policymaking and agency staff functions.
Already in Statute	8. Provide for public testimony at meetings of the policymaking body.
Update	9. Require information to be maintained on complaints.
Apply	10. Require the agency to use technology to increase public access.
Do Not Apply	11. Develop and use appropriate alternative rulemaking and dispute resolution procedures.

Agency Information

Agency Information

Agency at a Glance

The Federal Family Education Loan Program (FFELP), administered by the Department of Education, encourages private lenders to make loans to students and their parents to help pay for the cost of postsecondary education. To encourage lenders to participate in the program without requiring collateral or proof of creditworthiness from the student, the Department of Education protects the lender from financial loss by guaranteeing the repayment of the loan. The Texas Guaranteed Student Loan Corporation (TG) serves as the FFELP administrator in Texas, guaranteeing loans on behalf of the federal government. Established by the Legislature as a public, nonprofit corporation in 1979, TG's major functions include:

- issuing guarantees to private lenders for the repayment of FFELP loans;
- helping borrowers avoid loan delinquency and default through up-front education and awareness of loan repayment obligations;
- reimbursing lenders for loans that are not paid in full by the borrower;
- collecting from borrowers who have defaulted on their loans;
- overseeing schools and lenders participating in FFELP to ensure compliance with federal regulations; and,
- serving as the central clearinghouse for FFELP student loan and financial aid information for students, parents, schools, and lenders in Texas.

On the Internet: Information about TG is available at www.tgslc.org.

Key Facts

- **Funding.** As a public, nonprofit corporation, TG receives no state funding. In fiscal year 2003, TG generated $131.6 million in operating revenue, mostly derived from administrative fees paid by the Department of Education for FFELP loan guarantee functions. Of this amount, TG spent about $80 million on student loan activities and related administrative functions.
- **Staffing.** TG has a staff of 578 employees, most of whom are based in its corporate headquarters in Round Rock.
- **Loan Guarantee Operations.** In fiscal year 2003, TG guaranteed 416,000 FFELP loans totaling more than $2.3 billion. On average, loans guaranteed by TG that year totaled $2,963 for undergraduates, and $6,459 for graduate borrowers. Since its creation, TG has guaranteed more than $32.5 billion in FFELP loans that were issued to 2.5 million postsecondary education students.

- **Default Prevention Activities.** The typical student leaving school has a median student loan debt of $8,125. TG provides borrowers with a variety of resources to help them track loan balances, manage debt, and understand and meet their loan repayment obligations. In fiscal year 2003, TG helped to resolve more than 91 percent of all loan delinquencies reported by lenders.
- **Claim Payments.** When a borrower does not repay a loan in full to the lender, TG reimburses the lender for most of its loss. In fiscal year 2003, TG paid 59,696 claims to lenders totaling $285 million. These claims were for bankruptcy, disability or death, as well as default. TG's loan default rate is currently 7 percent, down from 17 percent ten years ago.
- **Collections.** In fiscal year 2003, TG collected $291.5 million in defaulted loans on behalf of the federal government, and assisted another 2,615 borrowers in rehabilitating their defaulted loans.
- **Outreach**. TG serves as a resource to students and their parents, schools, lenders, and the public. Last year, TG's Customer Assistance call center received about 130,000 telephone inquiries, and fielded more than 15,000 calls to the Texas Financial Aid Information Center hotline.
- **Compliance.** TG approves schools and lenders for FFELP participation at TG, and conducts reviews to ensure their continued compliance with federal regulations. Currently, TG works with about 775 schools and 300 lenders.

Major Events in Agency History

Congress created FFELP to remove financial barriers to postsecondary education.

In 1965, the United States Congress created the Guaranteed Student Loan Program, later renamed the Federal Family Education Loan Program. Administered by the Department of Education, the program was created to remove financial barriers to postsecondary education by ensuring students had access to low-interest loans made by private lenders. The Department of Education offered federal subsidies to lenders that made loans under the program, insured the loans against default, and encouraged states to create nonprofit guaranty agencies to administer the program. Several years later, in 1979, the Texas Legislature created the Texas Guaranteed Student Loan Corporation as a public, nonprofit corporation to administer FFELP in Texas.

Although federal law and regulations primarily govern TG's administration of FFELP, the Texas Legislature has also passed laws affecting TG's operations. In 1989, the Legislature reviewed and continued TG through the Sunset process, authorizing TG to engage in alternative revenue generating activities, and requiring state licensing agencies to deny the license renewals of licensees with defaulted student loans. In 1995, the Legislature authorized TG to guarantee FFELP loans in other states, and required the State Lottery to withhold winnings to individuals with defaulted student loans. More recently, in 1999, the Legislature directed TG to coordinate postsecondary education outreach and awareness efforts within the state, and directed TG to work with the Texas Higher Education Coordinating Board to establish the Texas Financial Aid Information Center.

Organization

Policy Body

TG is governed by a ten-member part-time Board, nine of whom are appointed by the Governor for six year terms. Of the nine Governor appointees, five members have knowledge or experience in finance, three members are from the faculty or administration of an eligible postsecondary educational institution, and one member is a full-time student enrolled at a postsecondary educational institution. In addition, the Comptroller of Public Accounts serves as a permanent, ex officio voting member. The chart, *Texas Guaranteed Student Loan Corporation, Board of Directors*, provides information about the Board.

Texas Guaranteed Student Loan Corporation
Board of Directors

Member Name	Term Expiration	Qualification	Residence
Ruben Esquivel, Chair	2009	School	Dallas
Tommy J. Brooks	2009	Finance	Houston
Albon Head, Jr.	2007	Finance	Fort Worth
Morgan Howard	2005	Student	Bryan
Jorja Kimball	2005	School	College Station
James Langabeer	2007	School	Edinburg
Jerry Don Miller, Ph.D.	2007	Finance	Canyon
Jane Phipps	2005	Finance	San Antonio
Grace Shore	2009	Finance	Longview
Carole Keeton Strayhorn	Permanent Member	Comptroller of Public Accounts	Austin

The key functions of the Board include approving the budget, setting policies, and providing long-term direction for TG. Although only required to meet twice annually, the Board generally meets at least four times per year. To accomplish its work, the Board breaks into four subcommittees: the Executive Committee, the Budget/Finance/Audit Committee, the Personnel Committee, and the Planning Committee. The subcommittees do not have binding authority but make recommendations to the entire Board. In addition, as required by law, TG has established a School and Lender Advisory Committee, consisting of representatives from postsecondary education institutions and the student lending industry, to advise TG on industry issues. Advisory committee members are appointed by TG's Board of Directors, upon the recommendation of TG's Chief Executive Officer, and serve two-year, staggered terms. The Board appoints and delegates powers to the President of TG, who serves as Chief Executive

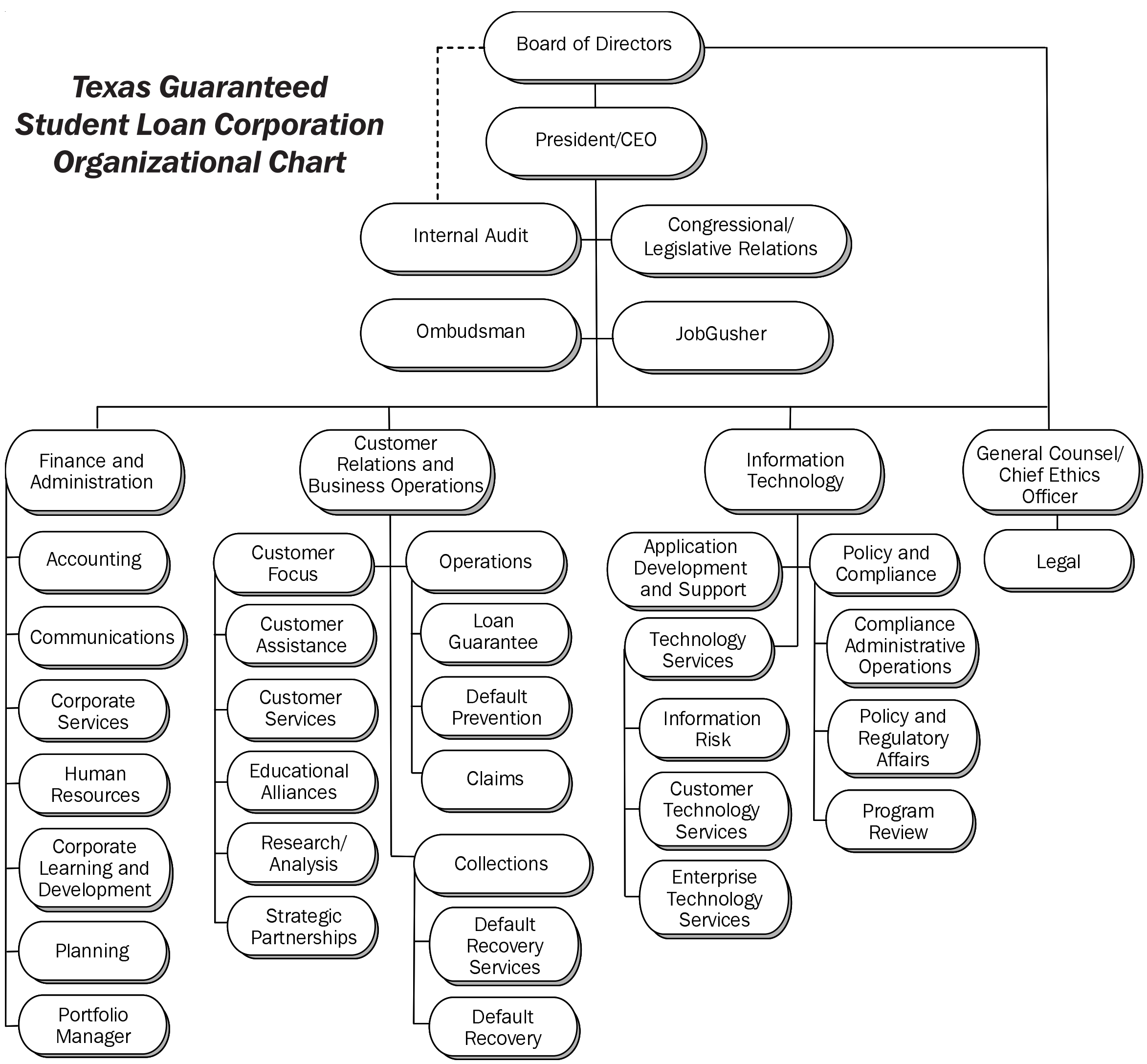
Officer in administering the daily operations of the agency and coordinating the activities of staff.

Staff

TG has a staff of 578 employees, most of whom work in TG's corporate headquarters in Round Rock. TG also has 12 employees who are located around the country supporting TG marketing activities. The *Texas Guaranteed Student Loan Corporation Organizational Chart* depicts the organization of TG's staff. TG's General Counsel and Chief Ethics Officer serves a dual role, reporting to the Chief Executive Officer in his capacity as Chief Ethics Officer, and also serving as General Counsel to the Board.

TG employs a team of six internal auditors who conduct reviews of TG's operations and procedures to improve internal controls and reduce risk. In fiscal year 2003, Internal Audit staff completed 21 audits, which primarily focused on information technology, administration, and customer service.

Texas Guaranteed Student Loan Corporation Organizational Chart



Because TG is not a state agency, TG does not submit information about its employment of minorities and females to the Texas Workforce Commission's civil rights division. Instead, state law requires TG to file an annual policy statement with the Office of the Governor that details TG's Equal Employment Opportunity policies and an analysis of TG's compliance with federal and state guidelines.

Funding

Revenues

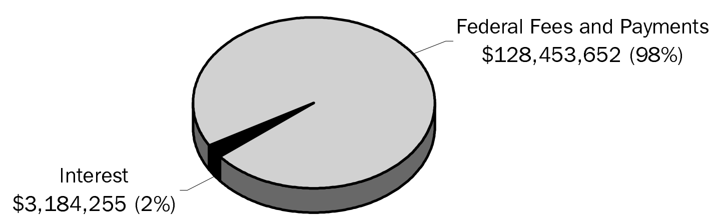
Because TG operates as a public, nonprofit corporation, its budget works differently than a typical state agency. TG receives no state appropriations; instead, the U.S. Department of Education (the Department) pays TG for the FFELP loans TG guarantees and services.

TG is federally funded and receives no state appropriations.

As part of a pilot program initiated by the Department, TG entered into a Voluntary Flexible Agreement (VFA) with the Department in 2001. Through VFA, the Department exempts a guaranty agency from certain statutory and regulatory requirements so that it may pursue more efficient and effective means of managing FFELP. The Department uses VFAs as a means of testing new and innovative methods for carrying out required activities. Under the terms of TG's VFA, TG receives variable rate fees from the Department based on its performance in guaranteeing loans, keeping borrowers' loan payments current and out of default, and collecting on defaulted loans. The VFA shifted the focus of TG's funding from back-end collections on defaulted loans to prevention of student loan delinquencies and defaults.

Consistent with federal requirements, TG maintains two funds: an operating fund and a federal fund.[1] TG uses the operating fund for all of its loan guarantee and administrative operations. At the beginning of fiscal year 2003, TG had $85,920,903 in cumulative net revenue in the operating fund. Also, as depicted in the pie chart, *Operating Fund Revenue,* in fiscal year 2003, TG had about $131.6 million in new revenue. Performance-based fees paid by the Department to TG for administering the loan guarantee program accounted for almost all of the revenue received in the operating fund.

Operating Fund Revenue FY 2003



Total: $131,637,907

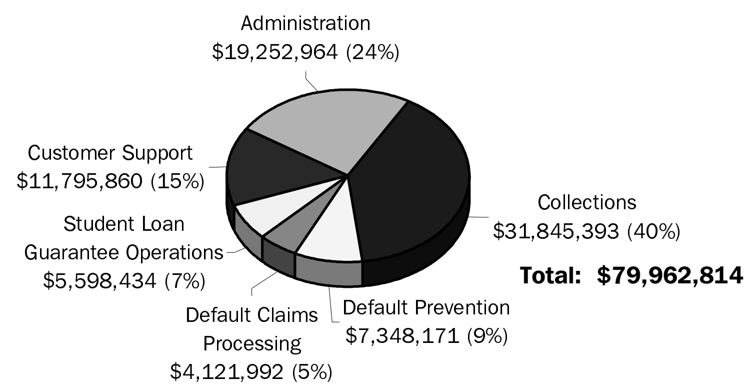
As part of the VFA, TG also maintains a federal fund. The federal fund is the property of the United States government, and only the Department can spend the money in the fund. At the beginning of fiscal year 2003, TG had a net balance of $9,034,252 in its federal fund. That same year, federal fund revenues totaled $5,398,454, primarily derived from interest accrued and recoveries on loans that defaulted before the VFA started in 2001. TG also maintains an escrow account for the federal government, described in the textbox, *Escrowed Assets*.

> **_Escrowed Assets_**
>
> When TG and the Department of Education entered into a Voluntary Flexible Agreement in 2001, the Department required TG to deposit all cash, cash equivalents, and investments of the federal fund into an escrow account. The escrowed assets are the property of the Department, cannot be spent on TG's operations, and are not part of TG's fund balances. Only the Department can authorize a transfer of funds from the escrowed account to TG's operating account. At the end of fiscal year 2003, TG held about $151 million in escrowed assets for the federal government.

Expenditures

TG uses its operating fund for administrative purposes, limited by federal agreement to financial aid-related activities. In fiscal year 2003, TG spent $79,962,814 from its operating fund, primarily on the corporation's operations, as shown in the pie chart, *Operating Fund Expenditures*. TG's highest category of spending was on collection activities, totaling about $31.8 million. At the end of fiscal year 2003, TG's ending balance in its operating fund was about $138.5 million.

Operating Fund Expenditures
FY 2003



TG reimburses lenders for loans that are not paid in full by the borrower.

As a FFELP administrator, TG reimburses lenders for loans that are not paid in full by the borrower. In most cases, TG pays lenders between 98 to 100 percent of the outstanding principal and interest owed on defaulted loans. These reimbursements represent TG's biggest disbursement each year, totaling about $285 million in fiscal year 2003. Under provisions of the VFA, the Department fully reimburses TG for all claims paid. Because the reimbursement occurs on a real time basis, TG does not reflect the pass-through funds in its revenues and expenditures.

Through terms of the VFA, only the Department has access to TG's federal fund, and rarely expends money from the fund. However, in fiscal year 2003, the Department authorized a transfer of $147,000 from the federal fund to TG's operating fund to support delinquency and default prevention programs. The federal fund also expended about $755,000 in depreciation. At the end of fiscal year 2003, TG's federal fund had a balance of about $13.5 million.

Although state law does not require TG to use Historically Underutilized Businesses in purchasing goods and services, TG voluntarily maintains a Vendor Inclusion Program.

Agency Operations

TG administers FFELP loan guarantees on behalf of the federal government, and acts as a resource for information about postsecondary educational opportunities and the availability of student financial aid. TG's key functions, as described in the sections below, include processing and issuing loan guarantees to lenders, helping borrowers to fulfill their loan repayment obligations by avoiding loan delinquency and default, reimbursing lenders for eligible loan claims, collecting money from borrowers who default on their loans, and ensuring schools and lenders comply with federal regulations. In carrying out these functions, TG interacts with borrowers, schools, lenders, and secondary markets as described in the textbox, *TG's Key Customers*.

TG's Key Customers

TG primarily interacts with the four following types of customers.

- **Borrowers.** Typically a student; however, TG also guarantees PLUS loans for parents.
- **Schools.** Institutions of higher education, including career schools, junior colleges, community colleges, and four-year colleges and universities, whose students have loans guaranteed by TG.
- **Lenders.** Financial institutions, such as commercial banks, savings banks, or credit unions, that provide the money for FFELP loans guaranteed by TG. For example, in 2003, Wells Fargo was Texas' largest originating lender in the program.
- **Secondary Markets.** An organization, such as the Student Loan Marketing Association, that purchases student loans from lenders and collects on the loans, thus providing the lenders with additional funds to make available to other students.

Financial Aid Awareness

FFELP loans represent a significant portion of the financial aid distributed to Texas students – about 59 percent. In addition to TG's primary role guaranteeing FFELP loans, the Legislature has also charged TG with disseminating postsecondary educational awareness information, including information about financial aid. As such, TG acts as the central clearinghouse for FFELP student loan and financial aid information for students and their parents, schools, and lenders. One of the primary tools that TG uses to answer financial-aid related questions is its Customer Assistance inbound call center. In fiscal year 2003, TG's call center received approximately 130,000 calls, the majority of which came from borrowers and their parents.

FFELP loans represent about 59 percent of the financial aid distributed in Texas.

TG's call center also fields incoming calls for the Texas Financial Aid Information Center, a toll-free hotline established by the Legislature in 1999, that offers assistance, in English and Spanish, on such topics as financial aid, college opportunities, career exploration, and other aspects of the higher education experience. TG staff operate the hotline at no cost to the State on behalf of the Texas Higher Education Coordinating Board. In fiscal year 2003, TG received about 15,000 calls on the hotline number.

TG performs other outreach initiatives aimed at educating prospective students about higher education and financial aid opportunities. For example, TG works with middle schools, high schools, postsecondary schools, and independent organizations to provide financial aid presentations and training to students, parents, and administrators. Additionally, TG broadcasts a yearly video conference available in English and Spanish that helps students complete the Free Application for Federal Student Aid.

TG also produces many publications, including the semi-annual *College Bound* newsletter, which provides information about higher education and financial aid opportunities. Produced in collaboration with the Texas Higher Education Coordinating Board, the newsletter goes to more than 600,000 students in high schools with high minority enrollment. Finally, TG supports many different Web sites that act as a resource for prospective students and their parents. The textbox, *TG Web Sites,* offers some examples.

TG Web Sites

TG maintains or helps support the following Web sites for providing information and assistance on financial aid opportunities to parents, students, and schools.

- **www.AdventuresInEducation.org.** Offers college and career planning tools in English and Spanish, scholarship searches, tips for preparing for higher education, and resource information and lesson plans for educators and counselors.
- **www.TexasMentor.com.** Prepares students for higher education opportunities in Texas, focusing on private universities and colleges. TG administers the Web site in collaboration with the Independent Colleges and Universities of Texas.
- **www.Mapping-Your-Future.org.** A college and career planning Web site sponsored by all of the nation's guaranty agencies.

Loan Origination and Guarantee

TG guarantees three types of student loans, described in the textbox, *FFELP Loan Types*. To receive any type of federal aid, including a FFELP loan, a student must complete the Free Application for Federal Student Aid (FAFSA). Based on the information provided in the FAFSA, the Department calculates the amount the student's family will be expected to contribute to the student's educational costs for a given year. Schools then develop individualized financial aid packages for the students, which may include a combination of grants, scholarships, work-study, and loans. Because Stafford loans represent 62 percent of the FFELP loans guaranteed by TG, the material below describes TG's functions in relation to Stafford loans. Consolidation loans, while popular because of the current, low-interest rates, are used by students only after graduation or departure from school; and PLUS loans, which go to parents, represent only 8 percent of TG's guarantees.

Eighty-one percent of the postsecondary schools in Texas use TG's guarantee services.

FFELP Loan Types

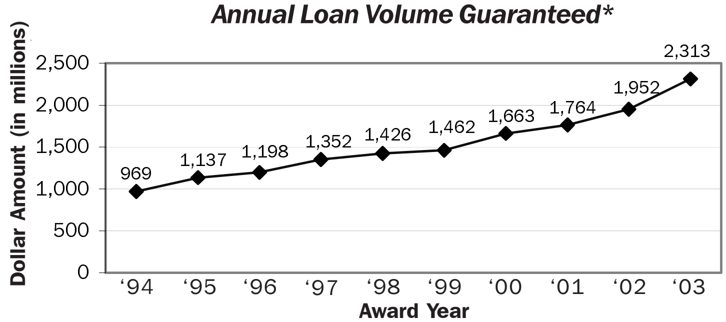
The Federal Family Education Loan Program includes the following three types of loans.

- **Stafford Loans.** Low-interest loans given to eligible students enrolled in postsecondary education. If the student demonstrates financial need and qualifies for a subsidized loan, the federal government pays the interest while the student is in school, during the six-month grace period, and during authorized periods of deferment. For unsubsidized Stafford loans, the student pays the interest on the loan.
- **PLUS Loans.** Loans offered to parents of dependent students enrolled in postsecondary education. PLUS borrowers are subject to credit evaluation and must begin repaying the loans within 60 days of the final disbursement.
- **Consolidation Loans.** Loans available to students who, after leaving school, want to consolidate their student loans into one loan, with one payment and one fixed interest rate.

When applying for a FFELP loan, students work with their school's financial aid office to select a lender. If the school uses TG's guarantee services, as do 81 percent of the postsecondary schools in Texas, the lender submits the student's application to TG for loan guarantee approval. The lender advises the school once the loan has been guaranteed by TG. During peak season, TG processes an average of 4,800 loan guarantee applications per day, guaranteeing most loans in a matter of minutes. In fiscal year 2003, TG guaranteed a total of 416,000 loans totaling $2.3 million. These loans averaged $2,963 for undergraduates, and $6,459 for graduate borrowers.[2]

The graph, *Annual Loan Volume Guaranteed*, shows how TG's loan portfolio has grown significantly over the last ten years. In addition to guaranteeing loans for students attending schools in Texas, TG also guarantees loans for students attending schools in other states and countries. Currently, TG's out-of-state loan guarantees account for 6 percent of its loan guarantee volume.

Annual Loan Volume Guaranteed*



*Excluding Consolidation Loan Volume

Loan Repayment and Default Prevention

Students are responsible for repaying their FFELP loans once they leave school, cease to be enrolled at least half-time, or graduate. The typical student leaving school in fiscal year 2003 had a median student loan debt of $8,125, which for the standard 10-year repayment term resulted in an average monthly payment of $80.[3] FFELP provides for a six-month grace period in which the student does not have to repay the loan.[4] During the grace period, TG contacts borrowers to explain repayment options, acts as a resource for finding jobs, and attempts to get students who have dropped out of school to re-enroll. The textbox, *JobGusher*, provides information on one of the tools TG uses to assist borrowers.

> ***JobGusher***
>
> JobGusher is an online recruitment service targeted at first-time job seekers in Texas. JobGusher matches job seekers and employers, and provides support, such as résumé building and interviewing tips. TG maintains this Web site to assist students in getting jobs, which gives them the financial capacity neccessary to repay their student loans. JobGusher can be accessed at www.jobgusher.com

The typical student leaving school in fiscal year 2003 had student loan debt of $8,125.

Once the grace period has expired, the student must begin to repay the FFELP loan to the lender. At this point, TG works with borrowers, schools, and lenders to help borrowers successfully repay their loans, and keep them from becoming delinquent in loan payments. If, however, a borrower fails to make a loan payment for more than 60 days, the lender notifies TG of the loan delinquency, and both the lender and TG begin an aggressive campaign to contact and work with the borrower to avoid a loan default.

TG's default prevention activities include telephone calls and letters that explain the consequences of defaulting on a student loan and attempt to get the borrower back into repayment. TG provides borrowers with a wide variety of options that allow them to bring their account into good standing, including alternatives like deferment or forbearance, which allow a borrower to skip payments for valid reasons such as unemployment, economic hardship, or enrollment in school.[5] During this same period, federal law requires lenders to exert similar efforts to reduce loan defaults, or risk financial penalties or loss of the loan guarantee.

In fiscal year 2003, about 30 percent of the $9.3 billion loans in repayment were delinquent at some point during the year. Of these delinquent loans, TG was able to bring more than 91 percent into repayment, thereby avoiding default.

Loan Defaults and Claims

Ideally, borrowers will make all loan payments as scheduled and repay their loans in full. However, in the event a loan is not paid in full by the borrower, TG reimburses the lender for its loss. Lenders submit requests for reimbursement, called claims, to TG for loans that have defaulted, and in some instances, for loans that have not defaulted but qualify for reimbursement under special circumstances; for example, in the event of the borrower's death or disability.

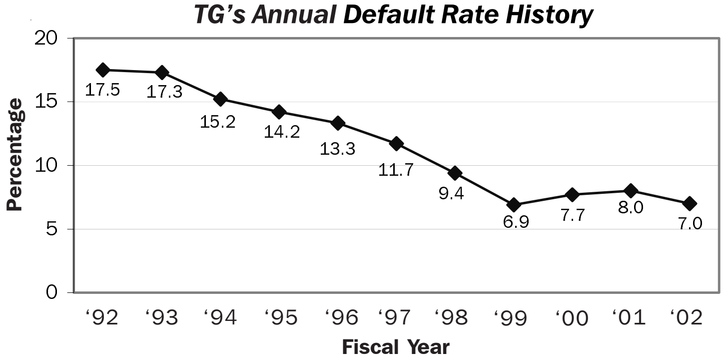
Federal law deems a loan to be in default if the borrower has failed to make payments for 270 days.

Federal law deems a loan to be in default status if the borrower fails to make loan payments to the lender for 270 consecutive days. TG also reimburses lenders for non default related claims, such as when the borrower qualifies for one of the Department's loan discharge or forgiveness programs. Generally, loan discharge and forgiveness programs relieve the borrower, in whole or in part, from loan repayment obligations. A loan discharge helps a borrower who is experiencing a very serious life disruption, such as total and permanent disability, while forgiveness programs encourage borrowers to work in certain professions while serving low-income families.

In most cases, TG pays lenders between 98 to 100 percent of the outstanding principal and eligible interest for each claim submitted, provided the lender has complied with all requirements for making, servicing, and collecting the loan. Under provisions of TG's Voluntary Flexible Agreement with the Department, the Department fully reimburses TG for all claims paid to lenders. In fiscal year 2003, TG paid 59,696 claims to lenders totaling $285 million. About 83 percent of the claims were for defaulted loans, with the average default totaling $4,615. The remaining 17 percent were non default related claims. Federal law requires TG to pay all claims within 60 days, and TG is currently averaging 53 days.

For fiscal year 2002 – the most recent statistics available – the Department of Education calculated TG's default rate at 7 percent, down from 17 percent ten years ago, as shown in the chart, *TG's Annual Default Rate History*.[6] This rate represents the second lowest rate in TG history. TG credits its declining default rate to several factors, including TG's program review and default prevention efforts, as well as the Department's increased oversight of schools.[7] The

TG's Annual Default Rate History



Department holds schools, lenders, and guaranty agencies responsible for keeping default rates low, or they face the risk of being suspended or terminated from FFELP, or in TG's case, subject to reduced funding.

The Department of Education holds schools, lenders, and guaranty agencies responsible for keeping default rates low.

Collections

After paying a claim on a defaulted loan, TG attempts to collect the money from the borrower on behalf of the federal government. If the loan default is not resolved within 61 days after default, TG adds a variable rate collection fee – 16.8 percent in 2003 – to the principal of the loan to cover its costs during the collection process. The textbox, *TG Collection Tools,* describes additional means that TG, in partnership with federal and Texas agencies, may use to spur loan repayment.

> ***TG Collection Tools***
>
> TG, working in partnership with federal and state agencies, may encourage loan repayment through several of the following means.
>
> - **Wage Garnishment.** As authorized by federal law, TG may garnish the wages of a defaulted borrower.
> - **Withhold Federal Payments.** Through the Treasury Offset Program, the federal government may withhold funds owed to an individual and apply them to a defaulted loan. For example, the federal government may withhold tax refunds or a percentage of Social Security Administration payments.
> - **Deny Professional/Occupational Licenses.** State law bars the renewal of certain state professional/occupational licenses held by a defaulted borrower.
> - **Withhold Lottery Winnings.** The State of Texas may withhold the lottery winnings of a borrower with a defaulted loan.
> - **Withhold Comptroller Warrants.** The State of Texas may withhold money owed to a state employee that is not part of the employee's wages.

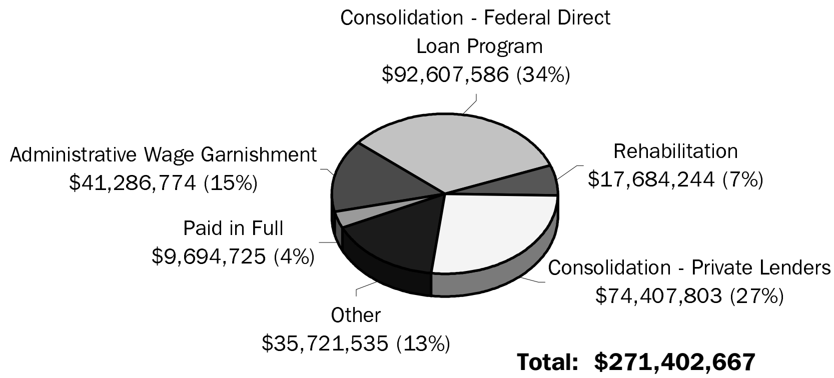
Borrowers have an opportunity to formally object to TG's collection efforts. TG addresses borrower objections through in-house hearings called Claims Administrative Reviews, conducted by designated TG hearing officers. In fiscal year 2003, TG received 301 objections, and after hearing, denied 222, with an average resolution time of 16 days. TG handles wage garnishment disputes differently, referring those disputes to contracted administrative law judges for resolution. About 30 percent of borrowers subject to wage garnishment, or 1,367 borrowers, filed objections in fiscal year 2003. However, only 285 of these borrowers actually pursued the wage garnishment case to hearing, and only one objection was upheld.

TG continues its collection efforts for six months before turning the defaulted loan over to private collection agencies for a period of three years. Ultimately, if both the collection agencies' and TG's efforts fail, TG again attempts to resolve the default for six more months, before it passes the loan on to the Department for any additional collection efforts.

TG attempts to collect on a defaulted loan for four years, before passing the loan to the Department of Education.

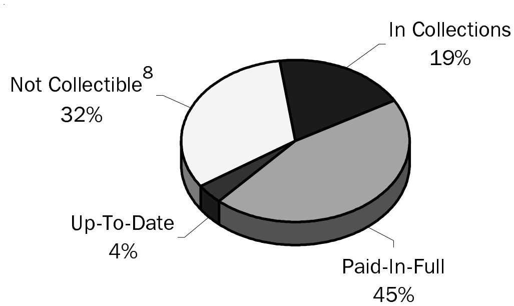
At any point during the collection process, a borrower has several options for getting out of default. The borrower may simply pay off the entire loan; consolidate defaulted loans into a single, new loan; or rehabilitate the loan by making 12 consecutive, timely payments to TG. Rehabilitation removes the default history from the borrower's credit report, while consolidation does not. The pie chart, *Methods of Resolution,* illustrates the methods borrowers most commonly used to remove loans from default in fiscal year 2003.

Methods of Resolution
FY 2003



As shown in the pie chart, *Status of Defaults Since TG's Inception,* of the nearly one million default claims paid by TG since its inception, 45 percent have been satisfactorily repaid by the borrowers; 4 percent of defaulted accounts were up-to-date during the last 90-day repayment period; and 19 percent remained in collection status. The remaining 32 percent were not collectible by TG due to the death, disability, or bankruptcy-discharge of the borrower; or were transferred to the Department of Education.

Status of Defaults Since TG's Inception



Oversight of Schools and Lenders Participating in FFELP

In addition to its loan guarantee functions, TG coordinates with the Department of Education to oversee about 775 schools and 300 lenders participating in FFELP.[9] This oversight includes ensuring that only eligible schools and lenders participate in FFELP, and that all participants comply with the federal Higher Education Act, federal regulations, and TG's policies and procedures.

Oversight of Schools

Schools seeking to participate in FFELP must submit an application to the Department and TG. The Department and TG work together to assess the school's administrative and financial capabilities for properly administering FFELP. For example, schools must employ an adequate number of personnel to administer its loan programs, and must designate an individual to coordinate FFELP with the school's other student aid programs. In fiscal year 2003, TG approved 247 new applications from schools.

TG periodically conducts on-site reviews of schools participating in FFELP. Federal law requires TG to biennially review any Texas school whose overall loan default rate exceeds 20 percent for either of the two most recent years. In addition, TG considers other factors when selecting schools for review, such as high loan volume, number of complaints received, number of claims paid, and the school's default rate for TG-guaranteed loans.

TG oversees schools and lenders to ensure compliance with federal laws and FFELP regulations.

Depending on the results of the review, TG may require the school to take corrective action, including returning FFELP funds. If necessary, TG has the authority to limit, suspend, or terminate a school's FFELP participation, but TG has not had to initiate such action in recent years. In fiscal year 2003, TG conducted 11 reviews of schools, five of which were federally mandated. In addition, schools undergo independent financial and compliance audits on an annual basis and must report the results to the Department.

Oversight of Lenders

Before making FFELP loans to students, lenders must enter into an agreement with TG, and receive the Department's approval to participate in FFELP. In fiscal year 2003, TG approved nine new applications from lenders.

To maintain FFELP eligibility, a lender must administer its loan portfolio in compliance with federal laws and regulations, as well as TG requirements. The Department requires TG to conduct biennial compliance reviews of certain lenders. For example, a lender is subject to review by TG if the lender represents a significant percentage of TG's loan volume, or if its loan volume equals or exceeds $10 million. If a lender delegates the making, servicing, collection, or assignment of its loans to any other party, the lender must ensure the other party meets all requirements. In fiscal year 2003, TG conducted eight lender reviews, all of which were federally required. Lenders also undergo independent financial and compliance audits on an annual basis and must report the results to the Department.

[1] The uses of these funds are defined in the Higher Education Act, sections 422A [20 U.S.C. 1072a] and 422B [20 U.S.C. 1072b].

[2] Federal law limits the amount of Stafford loans borrowers may receive. For example, dependent undergraduates may receive a maximum of $2,625 during their first year of school. Loan limits increase for succeeding years, but cannot exceed $23,000 total. Independent undergraduates, and graduate and professional students have higher limits.

[3] The median debt among students represents typical student debt more accurately than an average, since heavy borrowers such as medical students tend to skew the average indebtedness.

[4] Only Stafford loans have a grace period after the student leaves school. Parents who receive PLUS loans must begin repaying the loans within 60 days of the final disbursement.

[5] A forbearance is an agreement between the borrower and the lender in which a borrower can skip or reduce one or several loan payments, but the loan continues to accrue interest. Alternatively, with a deferment, the borrower can skip payments but interest does not accrue. TG has 16 different types of deferment options. The most common cause for deferment at TG is unemployment.

[6] TG's cohort default rate is the percentage of students with loans entering repayment in a given fiscal year who default on their loan obligations before the end of the next fiscal year. For example, the fiscal year 2002 cohort default rate is based on students who entered repayment during fiscal year 2002 and subsequently fell into default before the end of fiscal year 2003.

[7] Texas Guaranteed Student Loan Corporation, *State of Student Aid in Texas,* by Robin McMillion et al., (Round Rock, Texas, April 2004), p. 80.

[8] This amount includes loans that were transferred to the Department of Education.

[9] The 300 lenders participating in FFELP through TG include secondary markets and servicers.

Appendix

Staff Review Activities

The Sunset staff engaged in the following activities during the review of the Texas Guaranteed Student Loan Corporation (TG).

- Worked extensively with TG's CEO/President, senior management, and staff.
- Attended Board and advisory committee meetings, and interviewed or solicited written comments from Board and advisory committee members.
- Interviewed and received written comments from representatives of postsecondary education institutions, lenders, secondary markets, financial aid associations, and other industry representatives.
- Met with, or interviewed by phone, representatives from the Lower Colorado River Authority, Office of Consumer Credit Commissioner, Texas Comptroller of Public Accounts, Texas Education Agency, Texas Higher Education Coordinating Board, Texas Lottery Commission, and Texas Mutual Insurance Company.
- Conferred with staff from the Governor's Office, Lieutenant Governor's Office, Speaker's Office, State Auditor's Office, Legislative Budget Board, and legislative committees charged with examining higher education and financial aid issues.
- Attended hearings of the Joint Interim Committee on Higher Education, Legislative Oversight Committee on Higher Education, and House Higher Education Committee.
- Met with financial aid administrators at Huston-Tillotson College, University of Texas-Austin, and Southern Methodist University-Dallas.
- Researched past legislation involving financial aid issues.
- Researched the functions of other guaranty agencies, and interviewed representatives from the U.S. Department of Education.
- Reviewed TG documents, reports, and publications.
- Performed background and comparative research using the Internet, and reviewed literature on financial aid issues.

Sunset Review of the Texas Guaranteed Student Loan Corporation

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