A Report to the Montana Legislature

Financial Audit

Montana Guaranteed Student Loan Program

For the Fiscal Year Ended June 30, 2013

December 2013

Legislative Audit Division

13-06

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Financial Audits

Financial audits are conducted by the Legislative Audit Division to determine if the financial statements included in this report are presented fairly and the agency has complied with laws and regulations having a direct and material effect on the financial statements. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) licenses.

Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these requirements and is therefore not intended for distribution to federal grantor agencies for these purposes. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2011, was issued March 29, 2012. The Single Audit Report for the two fiscal years ended June 30, 2013, will be issued by March 31, 2014. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
Room 277, State Capitol
P.O. Box 200802
Helena, MT 59620-0802

Legislative Audit Division
Room 160, State Capitol
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Helena, MT 59620-1705

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LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Deborah F. Butler, Legal Counsel

Deputy Legislative Auditors
Cindy Jorgenson
Angus Maciver

December 2013

The Legislative Audit Committee
of the Montana State Legislature:

This is our report on the fiscal year 2013 financial audit of the Office of the Commissioner of Higher Education's Montana Guaranteed Student Loan Program.

We reviewed the program's operations and compliance with selected federal regulations. Our audit resulted in an unmodified opinion and no recommendations.

We thank the Office of the Commissioner of Higher Education, the Montana Guaranteed Student Loan Program Director of Operations\CFO, and their staff for their assistance and cooperation throughout the audit.

Respectfully submitted,

/s/ Tori Hunthausen

Tori Hunthausen, CPA
Legislative Auditor

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Appointed and Administrative Officials

Office of the Commissioner of Higher Education	Clayton Christian, Commissioner of Higher Education
	Mick Robinson, Deputy Commissioner for Fiscal Affairs/Chief of Staff
	Frieda Houser, Director of Accounting and Budgeting
	Robin Graham, Director of Operations\CFO, Montana Guaranteed Student Loan Program

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Montana Legislative Audit Division

Financial Audit
Montana Guaranteed Student Loan Program
For the Fiscal Year Ended June 30, 2013

December 2013 13-06 Report Summary

At the end of fiscal year 2013, the Guaranteed Student Loan Program had an outstanding guaranteed loan balance of $1.5 billion. Since a change in federal regulations resulted in no further guarantees as of fiscal year 2011, the program will end when no guaranteed loan balances remain outstanding.

Context

Guaranteed Student Loan Program (GSL) operates under the guidance of the Board of Regents. It provides access to post-secondary education through guaranteed student loans.

As the guaranteed loan balances decrease, there will be less revenue to fund GSL's operations. When operating costs exceed revenues, GSL needs to use the assets in its operating fund to provide its required loan guarantee services. During fiscal years 2012 and 2013, the legislature funded over $5 million in scholarships out of the GSL operating fund. As a result, the asset balance in the operating fund was $4.3 million at June 30, 2013, as compared to $8.8 million at June 30, 2011. When no assets remain, another funding source will be required, because federal regulations require GSL to service all the loans it guaranteed.

GSL purchases loans as a result of borrowers defaulting, filing bankruptcy, becoming disabled, or dying. During fiscal year 2013, GSL purchased over $26 million of these guaranteed student loans from the financial institutions. This is about a $1.6 million increase in loans purchased from the previous year.

In the same time period, GSL recovered $7.3 million from borrowers on outstanding loans. In accordance with Federal Family Education Loan Program regulations, GSL remitted $5.4 million of the amounts collected to the U.S. Department of Education, and retained net revenue of $1.9 million.

Results

During our audit we tested compliance with federal regulations governing the GSL. We also focused our audit effort on financial activity related to payments from the federal government, claims paid to lenders, and cost of loan collections and the related control systems. Our audit did not result in any recommendations. We issue an unmodified opinion on the GSL financial statements.

(continued on back)

Recommendation Concurrence	
Concur	0
Partially Concur	0
Do Not Concur	0
Source: Agency audit response included in final report.	

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Call toll-free 1-800-222-4446, or e-mail **ladhotline@mt.gov**.

Chapter I – Introduction

Introduction

We performed a financial audit of the Commissioner of Higher Education's Montana Guaranteed Student Loan Program (GSL) for the fiscal year ended June 30, 2013. The objectives of our audit were to:

1. Determine if GSL's financial statements present fairly the financial position and results of operations for the fiscal year ended June 30, 2013.
2. Obtain an understanding of GSL's control systems to the extent necessary to support our audit of GSL's financial statements and, if appropriate, make recommendations for improvements in management and internal controls.
3. Determine whether GSL complied with selected federal laws and regulations.

We addressed the above objectives by reviewing and testing compliance primarily with federal regulations governing the GSL. We also focused our audit effort on financial activity related to payments from the federal government, claims paid to lenders, and cost of loan collections and the related control systems.

Background

GSL is part of the Office of the Commissioner of Higher Education. Working under the guidance of the Montana Board of Regents, GSL's primary goal is to improve access to postsecondary education in Montana. This goal is accomplished by working collaboratively with schools, colleges, lenders, and other trading partners.

GSL provides a variety of guarantee support services including single point of contact for schools, lenders and borrowers, outreach and financial literacy, and in-house default prevention and collections.

Through management of the Federal Family Education Loan Program, GSL has been able to administer a variety of state and federal grant and scholarship programs, such as:

- The Montana University System Honor Scholarship, a renewable merit scholarship that covers the cost of tuition at qualifying Montana colleges
- The Governor's Postsecondary Scholarship Program
- The Montana Family Education Savings Program
- GSL Essay Scholarship Contest

GSL tracks the outstanding loan balances by the loan's origination amount. The balance does not reflect the current value of the loans due to decreases for amounts paid or increases for accrued interest.

As of June 30, 2013, the original principal balance of guaranteed loans outstanding was $1,517,827,352. The federal government will reimburse GSL for defaulted loans at varying rates. Based on GSL's performance, it is receiving the highest reimbursement at the following rates: 98 to 100 percent for loans issued prior to October 1, 1998, and 95 percent for loans issued on or after October 1, 1998.

Effective July 1, 2010, Congress changed the Federal Family Education Loan Program and moved to the William D. Ford Direct Loan Program. GSL ceased guaranteeing new student loans as of June 30, 2010. Table 1 shows the outstanding guaranteed loan balance as of June 30, 2010, the last fiscal year it guaranteed new student loans, through June 30, 2013. GSL is required to service these student loans and will cease operations when there are no outstanding loans guaranteed.

Table 1

History of Outstanding Guaranteed Loan Balance

Subject	Outstanding Loan Balance
June 30, 2010*	$2,052,149,661
June 30, 2011	$1,756,727,435
June 30, 2012	$1,635,014,002
June 30, 2013	$1,517,827,352

Source: Compiled by the Legislative Audit Division from Guaranteed Student Loans records.

*This is the last year the Guaranteed Student Loan Program guaranteed student loans.

Independent Auditor's Report and Program Financial Statements

LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Deborah F. Butler, Legal Counsel

Deputy Legislative Auditors
Cindy Jorgenson
Angus Maciver

Independent Auditor's Report

The Legislative Audit Committee
of the Montana State Legislature:

Introduction

We have audited the accompanying Balance Sheet of the Office of the Commissioner of Higher Education Montana Guaranteed Student Loan Program – Federal Special Revenue Fund as of June 30, 2013, and related Statement of Revenues, Expenditures, and Changes in Fund Balance – Budget and Actual, for the fiscal year then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this responsibility includes designing, implementing, and maintaining internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the program's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the program's internal control, and accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as the overall presentation of the financial statements.

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We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the program as of June 30, 2013, and the changes in fund balance for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements of the Montana Guaranteed Student Loan Program present the financial position and the changes in financial position of only that portion of the reporting entity of the state of Montana that is attributable to the transactions of the program. They do not purport to, and do not, present fairly the financial position of the state of Montana as of June 30, 2013, or the changes in its financial position for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Emphasis of Matter

As discussed in Note 7 to the financial statements, the program has elected to change its method of accounting for activity occurring between the agency operating and federal funds. In fiscal year 2012, the program reported a transfer. In fiscal year 2013, the program reported the activity to the applicable revenue and expenditure accounts. Our opinion is not modified with respect to this matter.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

October 31, 2013

Office of the Commissioner of Higher Education
Montana Guaranteed Student Loan Program
Federal Special Revenue Fund
Balance Sheet
As of June 30, 2013

	Agency Operating Fund	Federal Student Loan Reserve Fund	Essay Scholarship Fund
Assets			
Cash in Treasury	$ 244,890	$ 2,056,352	$ -
Cash Collateral - SI	9,883	8,730	413
Interest Receivable	575	789	24
Short Term Investments (Note 2)	3,842,715	4,085,322	149,088
Long Term Investments (Note 2)	50,558	53,750	1,962
Prepaid Expense	1,549	-	-
Accounts Receivable	-	-	-
Due From Federal Government (Note 3)	224,810	756,486	-
Total Assets	$ 4,374,980	$ 6,961,429	$ 151,487
Liabilities and Fund Balance			
Liabilities			
Accounts Payable	$ 734,564	$ 1,722	$ -
Deferred Revenue	3,583	-	-
Property Held in Trust	1,583	-	-
Liab. Under Securities Lend	9,883	8,730	413
Due to Federal Government (Note 4)	-	707,491	-
Total Liabilities	$ 749,613	$ 717,943	$ 413
Total Fund Balance - Restricted	3,625,367	6,243,486	151,074
Total Liabilities and Fund Balance	$ 4,374,980	$ 6,961,429	$ 151,487

The accompanying notes are an integral part of this financial statement.

Office of the Commissioner of Higher Education
Montana Guaranteed Student Loan Program
Federal Special Revenue Fund
Statement of Revenues, Expenditures, and Changes in Fund Balance
Budget and Actual
For the Fiscal Year Ended June 30, 2013

	Agency Operating Fund			Federal Student Loan Reserve Fund			Essay Scholarship Fund		
	Budget	Actual	Variance	Budget	Actual	Variance	Budget	Actual	Variance
Revenue									
Account Maintenance Fees (Note 5)	$ 1,020,000	$ 951,887	$ (68,113)	$ -	$ -	$ -	$ -	$ -	$ -
Default Aversion Fees (Note 6)	500,000	408,305	(91,695)	100,000	235,008	135,008	-	-	-
Defaulted Loan Collections (Note 7)	2,233,200	1,941,065	(292,135)	-	-	-	-	-	-
Reinsurance from Department of Education (Note 8)	-	-	-	27,700,000	32,230,620	4,530,620	-	-	-
Non-Reinsured Loan Recoveries (Note 10)	-	-	-	182,000	269,420	87,420	-	-	-
Investment Earnings (Note 2)	20,000	13,092	(6,908)	20,000	12,280	(7,720)	-	393	393
STIP Security Lending Gross Earnings	5,000	49	(4,951)	3,000	50	(2,950)	-	2	2
Miscellaneous	15,000	15,017	17	-	51	51	-	-	-
Total Revenue	3,793,200	3,329,415	(463,785)	28,005,000	32,747,429	4,742,429	-	395	395
Expenditures									
Administrative Costs	$ 3,489,980	$ 3,294,403	$ 195,577	$ -	$ -	$ -	$ -	$ -	$ -
Cost of Loan Collections (Note 7)	-	-	-	5,700,000	5,406,862	293,138	-	-	-
Claims Paid to Lenders (Note 8)	-	-	-	25,440,015	26,762,839	(1,322,824)	-	-	-
Claims Paid to Lenders -uninsured (Note 10)	-	-	-	750,000	894,672	(144,672)	-	-	-
Default Aversion Fees (Note 6)	400,000	235,008	164,992	500,000	408,305	91,695	-	-	-
STIP Security Lending Expense	-	16	(16)	-	16	(16)	-	-	-
Scholarships (Note 9)	2,500,000	2,517,761	(17,761)	-	-	-	-	14,700	(14,700)
Total Expenditures	6,389,980	6,047,188	342,792	32,390,015	33,472,694	(1,082,679)	-	14,700	(14,700)
Excess (Deficiency) of Revenues Over Expenditures	(2,596,780)	(2,717,773)	(120,993)	(4,385,015)	(725,265)	3,659,750	-	(14,305)	(14,305)
Fund Balance - Restricted 06/30/12	6,343,140	6,343,140	-	6,968,751	6,968,751	-	165,379	165,379	-
Fund Balance - Restricted 06/30/13	$ 3,746,360	$ 3,625,367	$ (120,993)	$ 2,583,736	$ 6,243,486	$ 3,659,750	$ 165,379	$ 151,074	$ (14,305)

The accompanying notes are an integral part of this financial statement.

Office of the Commissioner of Higher Education
Montana Guaranteed Student Loan Program
Federal Special Revenue Fund
Notes to the Financial Statements
For the Fiscal Year Ended June 30, 2013

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Description of Program

The State of Montana's Guaranteed Student Loan Program (MGSLP) is located in the Office of the Commissioner of Higher Education, the state-level administrative organization of the Montana University System (MUS). The Montana Constitution, Article X, Section 9, grants governance authority over the MUS to the Board of Regents. MGSLP was established by the Office of the Commissioner of Higher Education in fiscal year 1981 to coordinate and administer the federally insured student loans issued by various lending institutions. Montana's Federal Family Education Loan Program (FFELP) operates in compliance with and pursuant to agreements between the Montana Board of Regents and the U.S. Department of Education (DE), pursuant to Section 428 of the Higher Education Act of 1965, as amended. On February 8, 2006, President Bush signed the Higher Education Reconciliation Act of 2005 (the “HERA”), PUB. L. 109-171, which made changes to the Higher Education Act of 1965, as amended. These changes became effective during the fiscal year ended June 30, 2008.

B. Basis of Accounting

The financial statements were prepared using the modified accrual basis of accounting, and are presented in a budget to actual format. Under the modified accrual basis of accounting, revenues are recognized when they are realizable, measurable, earned and available. They are considered realizable and measurable if the transaction has been completed or there is enough information to reasonably estimate the revenue to be received. The revenue is considered earned when the services have taken place. Available means that the revenue is collectable within the current accounting period or will be received within sixty days after the end of the fiscal year. The expenditures are recorded when the department incurs the related liability and it is measurable.

C. Descriptions of Federal Special Revenue Funds

As a Federal Special Revenue Fund, MGSLP accounts for the proceeds of revenue sources that are legally restricted to expenditures for specified purposes. Pursuant to the Higher Education Act of 1965, as amended, MGSLP accounts for its operations in two separate funds: the Federal Student Loan Reserve Fund (FSLRF) and the Agency Operating Fund (AOF). Use of the FSLRF is limited to payment of lender claims and payment of default aversion fees or other DE fee payments as directed. MGSLP is required to deposit claim reimbursements from DE into the FSLRF, as well as the following: DE’s equitable share of defaulted loan recoveries, the portion of default recoveries that equals the complement of the reinsurance rate which is not reimbursed to MGSLP by DE, and student loan insurance premiums (guarantee fees). The AOF is the property of MGSLP and is used for a variety of FFELP activities and for other student aid related activities. Payments received by MGSLP for account maintenance, default aversion activities, and MGSLP’s share of defaulted loan collections is all deposited into the AOF. MGSLP also maintains a fund to account for funds held in trust for recipients of MGSLP’s essay scholarship contest. Funds are invested in the Montana Short Term Investment Pool (STIP).

2. INVESTMENTS

Short and Long Term investments are units purchased in the State of Montana's STIP and are recorded at a unit cost of $1. All securities in STIP are held in the name of the Montana Board of Investments or were registered in the nominee name for the Montana Board of Investments and held by the Board's custodial bank. STIP credit quality is not rated. The Board of investments employs the "Prudent Expert Rule" in managing the State's investment portfolio. At June 30, 2013, MGSLP owned 8,183,395 units valued at $8,183,395. MGSLP does not have a formal policy for credit risk. As directed by the Department of Administration, MGSLP classified $106,270 of STIP as Long Term Investments to reflect MGSLP pro rata share of STIP Investments that are not readily salable at June 30, 2013.

3. DUE FROM FEDERAL GOVERNMENT

MGSLP pays individual lending institutions for any loans that have defaulted or are unpaid due to the death, permanent disability, or bankruptcy of the borrower. The agency then seeks reimbursement from the DE in accordance with reinsurance agreements between the agency and DE. Claim payments and subsequent reinsurance payments are paid from and deposited into the FSLRF. MGSLP's claims for reinsurance payments not received as of June 30, 2013, are included here. In addition, the receivable Due From Federal Government includes amounts MGSLP had not yet received for Account Maintenance Fee (Note 5) for the last quarter of fiscal year 2013. The extent of the outstanding reinsurance activity and other pending reimbursements from DE as of June 30, 2013, is shown below.

Account Maintenance Fee	$228,789	AOF
IRS Offset Overpayment	($3,979)	AOF
	$224,810	
Reinsurance Claims	$642,736	FSLRF
Teacher Loan Forgiveness	$103,147	FSLRF
Status Changes	$3,167	FSLRF
Repurchase	$7,436	FSLRF
	$756,486	
Total Due From Federal Government	$981,296	

4. DUE TO FEDERAL GOVERNMENT

After assignment to the guaranty agency, MGSLP seeks collection of student loans that have defaulted. A portion of the recoveries of loans reinsured by the DE is owed back to DE (Note 7). At June 30, 2013, the amount owed to DE was $707,491.

5. ACCOUNT MAINTENANCE FEE

The Higher Education Amendments of 1998 authorized the payment of an Account Maintenance Fee (AMF) beginning October 1, 1998. Under this Act, each guaranty agency is paid an account maintenance fee, to be deposited into the AOF. For federal fiscal years beginning 2007, the fee is .06% of the original principal balance of guaranteed loans outstanding during the year. During fiscal year 2013, AMF revenue totaled $951,887 which includes $228,789 accrued for reimbursements that were not received until after June 30, 2013.

6. DEFAULT AVERSION FEES

The Higher Education Amendments of 1998 authorized the payment of a Default Aversion Fee (DAF) beginning October 1, 1998. Upon receipt of a completed lender request for assistance (LRA) not earlier than the 60th day of delinquency, a guaranty agency must engage in default aversion activities designed to prevent a default by the borrower. Department of Education regulations provide for payment of a fee equal to 1% of the loan balance at the time an LRA is submitted, regardless of whether or not the loan is brought current. The default aversion fees are to be transferred from the FSLRF to the AOF no more frequently than monthly. If the agency receives a default aversion fee and the account later defaults, the agency must rebate 1% of the claim amount to the FSLRF. The fee may be paid only once on any loan. During fiscal year 2013, DAF paid to the AOF was $408,305 and $235,008 was returned to the FSLRF, for net revenue of $173,297 to the AOF.

7. DEFAULTED LOAN COLLECTIONS

MGSLP pursues collection, from the borrower or other responsible party, of defaulted loans held by the agency. The U.S. Secretary of Education is entitled to an equitable share of any recoveries, as determined by the rate of reinsurance on the defaulted loans less an allowance for collection cost reimbursement. Beginning October 1, 2003, the Higher Education Amendments (HEA) of 1998 authorize guaranty agencies to deposit an amount equal to 23% of the payments made by or on behalf of a defaulted borrower into its AOF. Beginning October 2007, this changed to 16%. The HEA also stipulates that the agency shall remit 81.5% of the total outstanding principal collected on rehabilitated loans to the Secretary and the agency shall deposit 18.5% of the principal, 100 % accrued interest and 18.5 % of the outstanding balance. In addition, the Secretary provides the agency with collection costs amounting to 18.5% of the outstanding balance of any defaulted loan held by the agency which is consolidated by the borrower into a Federal Consolidation Loan through either FFELP consolidation or FDSLP consolidation. HERA requires that on or after October 1, 2006, the guaranty agency shall remit directly to the Secretary that portion of the collection charge equal to 8.5 % of the outstanding balance of the defaulted loan. For the fiscal year ended June 30, 2013, the net revenue retained by MGSLP of $1,941,065 is reported in the AOF and the federal share of $5,406,862 is reported in the FSLRF as revenue with corresponding expenditures of $5,406,862. Previously, the reporting of the federal share of collections on defaulted loans was recorded as a transfer-out from the AOF into the FSLRF as a transfer-in. The current method of accounting increases revenues and expenditures in the FSLRF to clearly present the revenue and expense activity between funds for the payments owed to the federal government. The change does not affect the amount of funds retained by the federal government in the FSLRF and by MGSLP in the AOF.

	Revenues	Expenses	Net
Collection Recoveries	$2,896,567	$2,433,274	$463,293
Rehabilitations	$4,117,000	$2,827,451	$1,289,549
Federal Direct Consolidations	$334,360	$146,137	$188,223
Total	$7,347,927	$5,406,862	$1,941,065

8. CLAIMS PAID TO LENDERS AND REINSURANCE FROM DEPARTMENT OF EDUCATION

MGSLP records amounts paid to lenders for claims and subsequent amounts received from the DE as expenses and revenues respectively. For fiscal year 2013, MGSLP paid claims to lenders totaling $26,762,839 and received reinsurance revenue from DE totaling $32,230,620. The reinsurance includes $26,823,758 from claim purchases and $5,406,862 from default collections as detailed in Note 7.

9. SCHOLARSHIP FUNDS

In fiscal year 2013, MGSLP paid $1,947,500 to Montana students who were recipients of the Governor's Post-Secondary Scholarship and $570,261 Montana teachers who were selected for loan forgiveness through the Quality Educator Loan Forgiveness Program. This is a result of a House Bill 2 funding switch from general fund to federal special revenue, approved by the 2011 Legislature, in program 2-student assistance. The funding switch required MGSLP to fund the Governor's Post-Secondary Scholarship Program and the Quality Educator Loan Forgiveness Program for the biennium ended June 30, 2013.

MGSLP sponsored an essay competition from 1999 to 2008 which was open to students in Gaining Early Awareness and Readiness for Undergraduate Programs (GEAR UP) schools. The recipients were awarded scholarships worth $150 - $250. MGSLP will hold the scholarship in the recipient's name until he or she enters an eligible postsecondary education institution or until the eligibility to use the scholarship run out. If the student doesn't enroll in the time frame allotted, the funds will revert back to MGSLP.

10. CONTINGENCIES

The original principal balance of guaranteed loans outstanding held by MGSLP as of June 30, 2013 was approximately $1,517,827,352. This amount excludes bad debt, death, disability, and bankruptcy claims which have been previously purchased by the agency. MGSLP has entered into agreements with the DE, dated June 13, 1980, for reinsurance and supplemental reinsurance of loans, in accordance with the Higher Education Act of 1965, as amended. These agreements allow for 100% reimbursement by DE for claims due to the death, disability, or bankruptcy of the borrower. Claims paid due to defaulted loans may be reimbursed by DE for up to 100%. The percent of reimbursement on defaulted loans payable to the agency is dependent upon MGSLP's annual default rate and date of the loan's first disbursement. Annual default rates are calculated as the ratio of year-to-date default purchases divided by the original guaranteed amount of loans in repayment status at the beginning of the federal fiscal year.

The following schedule reflects the federal reinsurance rates on defaulted student loans. In the event of extreme future adverse loss experience, MGSLP could be liable for up to 25% of the outstanding loan volume. During fiscal year 2013, MGSLP paid $894,672 in claims, or portions of claim eligible loans, which were not reinsured by DE. During fiscal year 2013, MGSLP recovered $269,420 of the total outstanding balance of non-reinsured claims held by the agency.

RATE OF ANNUAL DEFAULTS	FEDERAL REINSURANCE On loans made prior to 10/01/93	FEDERAL REINSURANCE On loans made on or after 10/01/93 and prior to 10/01/98	FEDERAL REINSURANCE On loans made after 10/01/98
Less than 5%	100%	98%	95%
5% or greater but less than 9%	90% of claims 5% or greater but less than 9%	88% of claims 5% or greater but less than 9%	85% of claims 5% or greater but less than 9%
9% or greater	80% of claims 9% or greater	78% of claims 9% or greater	75% of claims 9% or greater

11. COMMITMENTS

MGSLP is bound by Guarantee Reserve Agreements with the lending institutions participating in the FFELP in Montana. These agreements require MGSLP to maintain an amount in the guarantee reserve fund equal to at least 0.25% of the unpaid principal balance of all outstanding loans guaranteed by the agency.

The Guarantee Reserve Agreement ensures that MGSLP will have sufficient cash available to carry out its reasonably expected obligations on guaranteed claim eligible student loans. As of June 30, 2013, MGSLP was in compliance with all Guarantee Reserve Agreements.

12. RELATED PARTY TRANSACTIONS

The Montana Board of Regents, which governs MGSLP, guarantees loans owned by the Montana Higher Education Student Assistance Corporation (MHESAC), a nonprofit corporation operating exclusively for the purpose of acquiring student loans. MHESAC has no employees. It's business operations are managed by the Student Assistance Foundation (SAF). Approximately 76.19%, or $1,156,483,026, of MGSLP's outstanding loan volume is held by MHESAC.

13. GOING CONCERN

As of July 1, 2010 all new Federal student loans are made through the Federal Direct Student Loan Program (FDSLP). MGSLP no longer receives income from Loan Processing and Issuance Fee, Disbursement Service, or Guarantee Fees.

14. EMPLOYEES' RETIREMENT SYSTEM

As an employee of MGSLP, benefits eligible employees must participate in a retirement system under section §19-3-402 of the Montana Code Annotated (MCA), MGSLP classified employees may choose to participate in the Montana Public Employees' Retirement System (PERS) or the Montana University System Retirement Plan (MUS-RP) (§19-21-213 MCA). PERS offers both a Defined Benefit Plan (PERS-DB) and a Defined Contribution Plan (PERS-DC) for employees to choose from. Certain professional employees under contract with the Board of Regents who were are already active or inactive members of PERS can choose to remain in their current retirement plan or transfer to the MUS-RP. If these employees are not already active, inactive or retired members of PERS, they must enroll in the MUS-RP.

Public Employees' Retirement System

<u>PERS-Defined Benefit Plan</u>

The PERS-DB is a public pension plan for employees of the state, university system and local government. Established by the 1945 Legislature and governed by Title 19, Chapters 2 and 3, MCA, the PERS-DB was created to grant service retirement, disability retirement, or survivor benefits to plan members and their beneficiaries. Unless another state plan covers the position, PERS covers all state and university workers. PERS-DB is considered a typical, cost-sharing multiple-employer pension plan where the employee and employer contribute to a pension trust. The Montana Public Employees' Retirement Board (MPERB) is the trustee of all money collected for the retirement systems and has exclusive control of the administration of the pension trust funds. The state treasurer is custodian of the pension trust funds, subject to the exclusive control of the board for administration and the board of investment for the investment of the funds (§19-2-503, MCA). Contribution rates for the plan are required and determined by State law (§19-3-315 and §19-3-316, MCA).

Members are "vested" after completing five years of membership service. After the employee is vested, they are entitled to any retirement benefits for which they are eligible.

Members hired before July 1, 2011 are eligible to retire at age 60 with at least five years of service; at age 65 regardless of length of service; or at 30 years of service regardless of age. The PERS-DB retirement benefit is based on the employee's highest consecutive 36 months of compensation (§19-3-901 and §19-3-108, MCA). The formula for a monthly service retirement benefit in the PERS-DB depends on the employee's years of membership service and service credit (§19-3-904, MCA). Effective January 1, 1989, if the employee has less than 25 years membership service, monthly retirement benefits are calculated by taking 1/56 (1.7857%) times the years of service times the highest average compensation. If the employee has more than 25 years of membership service, the monthly retirement benefits are calculated by taking 1/50 (2%) times the years of service times the highest average compensation.

Members hired after July 1, 2011 are eligible to retire at age 65 with at least five years of service; or at age 70 and in active service. The PERS-DB retirement benefit is based on the employee's highest consecutive 60 months of compensation. The formula for a monthly service retirement benefit in the PERS-DB depends on the employee's years of membership service and service credit (§19-3-904, MCA). Effective July 1, 2011, if the employee has less than 10 years membership service, monthly retirement benefits are 1.5% times the years of service times the highest average compensation. If the employee has more than 10 years of membership service, but less than 30 years of membership service, the monthly retirement benefits 1.7857% times the years of service times the highest average compensation. If the employee has more than 30 years membership service, the monthly retirement benefit is 2% times the years of service time the highest average compensation.

PERS- Defined Contributions Plan

The PERS-DC is a retirement plan for employees of the state and the university system. Both the employee and employer contribute to the employee's individual account. The employee then chooses how the contributions are invested from the available investment options. The benefit will depend on the size of the individual account balance at retirement. The account balance depends on the contributions and the investment earnings. Investment earnings may be either positive or negative during any period of time. The employee assumes the investment risk in the PERS-DC, but is also entitled to all of the investment returns. Contribution rates for the plan are required and determined by State law (§19-3-315 and §19-3-316, MCA).

PERS-DC members have access to the vested components of their individual accounts when they terminate their PERS covered employment, retire or die. Members, or their beneficiaries, can take a lump-sum or use their account balance to provide periodic payments for retirement income.

Additional information or a separate PERS financial statement can be obtained from:

State of Montana, Department of Administration
Montana Public Employees' Retirement Administration
P.O. Box 200131
Helena, MT 59620-0131

Montana University System Retirement Plan

The MUS-RP, formerly known as the Optional Retirement Plan (ORP), was established in 1988 (§19-21-101 MCA) and is underwritten by the Teacher's Insurance and Annuity Association – College Retirement Equities Fund (TIAA-CREF). The MUS-RP is a defined-contribution plan established under authority of Title 19, Chapter 21, MCA. Effective July 1, 1993, MUS-RP was made a mandatory retirement plan for new administrative and faculty staff. Combined contributions cannot exceed 13% of participants compensation (§19-21-203, MCA). MGSLP's contributions were equal to the required contribution.

The benefits at retirement depend upon the amount of contributions and amounts of investment gains and losses. Under the MUS-RP, each employee enters into an individual contract with TIAA-CREF. MGSLP records employee/employer contributions and remits monies to TIAA-CREF. Individuals are immediately vested in the plan.

Annual reports that include financial statements and required supplemental information on the plans are available from:

TIAA-CREF
730 Third Ave.
New York, NY 10017-3206
Phone: 1-800-842-2733

According to state law, MGSLP, as a part of the MUS, remits additional employer contributions to the Teachers' Retirement System to amortize past service unfunded liability (§19-20-621 MCA).

Trend information, indicating the progress made toward accumulating assets needed to pay retirement benefits when they are due, is not available on an agency basis. Separately issued financial statements can be obtained from:

State of Montana, Department of Administration
Teacher's Retirement Division
PO Box 200139
Helena, MT 59620-0139

Retirement plan information for MGSLP as of June 30, 2013, is as follows.

	PERS	MUS-RP
		Staff
Covered Payroll	$1,079,021	$109,310
Employer Contributions	$80,592	$7,878
Percent of Covered Payroll	7.17%	7.17%
Employee Contribution	$75,208	$7,542
Percent of Covered Payroll	6.90-7.90%	6.90%

Retirement plan information for MGSLP as of June 30, 2012, is as follows.

	PERS	MUS-RP	MUS-RP
		Professional	Staff
Covered Payroll	$1,054,037	$159,058	$107,010
Employer Contributions	$75,627	$16,981	$7,702
Percent of Covered Payroll	7.17%	10.68%	7.17%
Employee Contribution	$73,466	$11,204	$7,384
Percent of Covered Payroll	6.90%-7.90%	7.04%	6.90%

Retirement plan information for MGSLP as of June 30, 2011, is as follows.

	PERS	MUS-RP Professional	MUS-RP Staff
Covered Payroll	$1,093,944	$93,312	$124,057
Employer Contributions	$79,694	$9,962	$8,912
Percent of Covered Payroll	7.17%	10.68%	7.17%
Employee Contribution	$ 79,248	$6,573	$8,560
Percent of Covered Payroll	6.90-7.90%	7.04%	6.90%

Montana Guaranteed Student Loan Program

Program Response

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LEGISLATIVE AUDIT DIV.

MGSLP

Montana Guaranteed Student Loan Program

2500 Broadway P.O. Box 203101
Helena, MT 59620-3101
Phone: (406) 444-6594 Fax: (406) 444-1869
Customer Assistance: (800) 537-7508
mgslpcustserv@montana.edu www.mgslp.org

December 9, 2013

Tori Hunthausen
Legislative Auditor
Legislative Audit Division
State Capitol, Room 160
P.O. Box 201705
Helena, MT 59620-1705

Dear Ms. Hunthausen:

This letter acknowledges receipt of the results of the audit for the fiscal year ending June 30, 2013 and we consider the audit complete. We understand an unmodified opinion has been issued and that the report contains no findings or recommendations.

We appreciate the efforts of your staff and the professionalism demonstrated while conducting the audit. The efficiency with which they carried out their review allowed our agency to present a complete and accurate report to our federal partners in a timely manner.

Sincerely,

Robin Graham
Director of Operations/CFO
Montana Guaranteed Student Loan Program