



A REPORT
TO THE
MONTANA
LEGISLATURE

FINANCIAL AUDIT

Montana Guaranteed Student Loan Program

*For the Two Fiscal Years Ended
June 30, 2015*

DECEMBER 2015

LEGISLATIVE AUDIT
DIVISION

15-06

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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.

The Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports in addition to those reports required by Government Auditing Standards. This individual agency audit report is not intended to comply with these requirements and is therefore not intended for distribution to federal grantor agencies. 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, 2013, was issued March 28, 2014. The Single Audit Report for the two fiscal years ended June 30, 2015, will be issued by March 31, 2016. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
Room 277, State Capitol
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Deborah F. Butler, Legal Counsel



Deputy Legislative Auditors:
Cindy Jorgenson
Angus Maciver

December 2015

The Legislative Audit Committee
of the Montana State Legislature:

This is our report on the Office of the Commissioner of Higher Education's Montana Guaranteed Student Loan Program for the two fiscal years ended June 30, 2015.

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

TABLE OF CONTENTS

Tables	ii
Appointed and Administrative Officials	iii
Report Summary	S-1
CHAPTER I – INTRODUCTION.....	1
Introduction	1
Background.....	1
INDEPENDENT AUDITOR’S REPORT AND PROGRAM FINANCIAL STATEMENTS	
Independent Auditor’s Report	A-1
Federal Special Revenue Fund Balance Sheet as of June 30, 2014.....	A-3
Federal Special Revenue Fund Statement of Revenues, Expenditures, and Changes in Fund Balance-Budget and Actual for the Fiscal Year Ended June 30, 2014	A-4
Federal Special Revenue Fund Balance Sheet as of June 30, 2015.....	A-5
Federal Special Revenue Fund Statement of Revenues, Expenditures, and Changes in Fund Balance-Budget and Actual for the Fiscal Year Ended June 30, 2015	A-6
Federal Special Revenue Fund Notes to the Financial Statements for the Fiscal Year Ended June 30, 2014, and June 30, 2015.....	A-7
REPORT ON INTERNAL CONTROL AND COMPLIANCE	
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government</i> <i>Auditing Standards</i>	B-1
PROGRAM RESPONSE	
Montana Guaranteed Student Loan Program	C-1

TABLES

Tables

Table 1	History of Outstanding Guaranteed Loan Balance	2
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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 Two Fiscal Years Ended June 30, 2015

DECEMBER 2015

15-06

REPORT SUMMARY

At the end of fiscal year 2015, the Montana Guaranteed Student Loan Program guaranteed loans of approximately \$1.3 billion. This is down from \$1.4 billion in fiscal year 2014 and \$1.5 billion in fiscal year 2013. A change in federal regulations resulted in no further guarantees of new loans as of fiscal year 2011, however, the program is still the Guarantor of the existing loans. Based on current federal policy, in 2018 or 2019, the program will begin winding down until no guaranteed loan balances remain.

Context

The Montana Guaranteed Student Loan Program (GSL) is administered by the Administrative & Fiscal Affairs Division of the Office of the Commissioner of Higher Education. GSL guarantees federal loans that were given out prior to 2011. GSL purchases loans as a result of borrowers defaulting, filing bankruptcy, becoming disabled, or dying. During fiscal year 2014, GSL purchased over \$25 million guaranteed student loans from the financial institutions. GSL purchased over \$17 million loans in fiscal year 2015.

The GSL program is able to keep a percentage of payments made on purchased loans (collection recoveries), loans bought back by lenders after completion of a successful rehabilitation plan (rehab), and payments made as part of federal direct consolidations.

The GSL program also administers a variety of scholarship programs and assists in administering the Montana Family Education Savings Program. Funding for administration of the above programs will need to come from

another source when the GSL program ceases operations.

Our audit focused on financial activity related to payments from the federal government, claims paid to lenders, cost of loan collections, and administrative costs.

We also examined documentation related to the history of guaranteed loan amounts. The original amount of loans outstanding has decreased from over \$2 billion in June 30, 2010, to \$1.3 billion in June 30, 2015.

The last borrowers to receive loans guaranteed by GSL received loans in 2008 or 2009. GSL estimates they will have diminished operations in 2018 or 2019, based on the last borrowers making 10 years of fully amortized payments.

Results

Our audit did not result in any recommendations, and we issued an unmodified opinion on the GSL financial statements.

For a complete copy of the report (15-06) or for further information, contact the Legislative Audit Division at 406-444-3122; e-mail to lad@mt.gov; or check the web site at <http://leg.mt.gov/audit>

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Chapter I – Introduction

Introduction

We performed a financial audit of the Office of Commissioner of Higher Education's Montana Guaranteed Student Loan Program (GSL) for the two fiscal years ended June 30, 2015. The objectives of our audit were to:

1. Determine whether GSL's financial statements present fairly the financial position and results of operations for the two fiscal years ended June 30, 2015.
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.

We focused our audit effort on financial activity related to payments from the federal government, claims paid to lenders, cost of loan collections, and the related control systems.

We also examined documentation related to the history of outstanding guaranteed loan balance. The outstanding loan balance has decreased from over \$2 billion in June 30, 2010 to \$1.3 billion in June 30, 2015.

Background

The Office of the Commissioner of Higher Education administers the Montana Guaranteed Student Loan Program. 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, in-house default prevention, and collections. Default prevention includes sending letters and calling borrowers who are in danger of defaulting. Collections include accepting borrower payments. GSL purchases loans as a result of borrowers defaulting, filing bankruptcy, becoming disabled, or dying. During fiscal years 2014 and 2015, GSL purchased over \$25 million in loans and \$17 million in loans, respectively.

The GSL program is able to keep a percentage of payments made on purchased loans (Collection Recoveries), loans bought back by lenders after completion of a successful rehabilitation plan (Rehabs), and payments made as part of Federal Direct Consolidations. Rehabs are more common than in prior years due to changes in

federal regulations that allow borrowers to qualify for lower payments on their loans. GSL educates borrowers on payment options that could rehabilitate the defaulted loan.

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, as well as assist in administering the Montana Family Education Savings Program, Montana's 529 savings plan that allows families to save for higher education. Another program will have to administer the scholarships and Montana Family Education Savings Program when the GSL program winds down.

GSL tracks the outstanding loans 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, 2014, the original principal balance of guaranteed loans outstanding was \$1.4 billion, and \$1.3 billion as of June 30, 2015. 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. As a result, GSL ceased guaranteeing new student loans. Table 1 shows the original guaranteed loan amounts of loans outstanding as of June 30, 2010, the last fiscal year GSL guaranteed new student loans, through June 30, 2015. GSL is required to service these student loans and will cease operations when there are no outstanding loans guaranteed, which is expected to be in 2018 or 2019. The last borrowers to receive loans guaranteed by GSL received loans in 2008 or 2009. The estimate above is based on the last borrowers making 10 years of fully amortized payments. Therefore, GSL estimates they will have diminished operations in 2018 or 2019, based on the last borrowers making 10 years fully amortized payments.

Table 1
History of Outstanding Guaranteed Loan Balance

Original Principal Balance of Loans Outstanding	
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
June 30, 2014	\$1,411,974,799
June 30, 2015	\$1,307,054,147

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 sheets of the Office of the Commissioner of Higher Education Montana Guaranteed Student Loan Program-Federal Special Revenue Fund as of June 30, 2014, and 2015, and related Statements of Revenues, Expenditures, and Changes in Fund Balance-Budget and Actual, for the fiscal years 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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.

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, 2014, and 2015, and the changes in fund balance for the fiscal years 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, 2014, or 2015, or the changes in its financial position for the fiscal years 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.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 4, 2015, on our consideration of the program's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the program's internal control over financial reporting and compliance.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

November 4, 2015

**Office of the Commissioner of Higher Education
Montana Guaranteed Student Loan Program
Federal Special Revenue Fund
Balance Sheet
As of June 30, 2014**

	Agency Operating Fund	Federal Student Loan Reserve Fund
Assets		
Cash in Treasury	\$ 1,148,499	\$ 2,917,841
Cash Collateral - SI	2,828	2,203
Interest Receivable	388	432
Short Term Investments (Note 2)	3,772,282	2,939,236
Long Term Investments (Note 2)	41,810	32,577
Prepaid Expense	-	-
Accounts Receivable	-	-
Due From Federal Government (Note 3)	216,560	7,436
Total Assets	<u>\$ 5,182,367</u>	<u>\$ 5,899,725</u>
 Liabilities and Fund Balance		
Liabilities		
Accounts Payable	\$ 159,414	\$ 9,707
Property Held in Trust	\$ 3,822	-
Liab. Under Securities Lend	\$ 2,828	2,203
Due to Federal Government (Note 4)	\$ -	108,379
Total Liabilities	<u>\$ 166,064</u>	<u>\$ 120,289</u>
Total Fund Balance - Restricted	<u>\$ 5,016,303</u>	<u>5,779,436</u>
Total Liabilities and Fund Balance	<u>\$ 5,182,367</u>	<u>\$ 5,899,725</u>

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, 2014**

	Agency Operating Fund			Federal Student Loan Reserve Fund		
	Budget	Actual	Variance	Budget	Actual	Variance
Revenue						
Account Maintenance Fees (Note 5)	\$ 884,000	\$ 891,595	\$ 7,595	\$ -	\$ -	\$ -
Default Aversion Fees (Note 6)	375,000	339,320	(35,680)	275,000	222,214	(52,786)
Defaulted Loan Collections (Note 7)	3,547,000	3,850,346	303,346	-	-	-
Reinsurance from Department of Education (Note 8)	-	-	-	30,400,000	34,564,742	4,164,742
Non-Reinsured Loan Recoveries (Note 10)	-	-	-	270,000	425,932	155,932
Investment Earnings (Note 2)	5,000	5,702	702	13,000	6,337	(6,663)
STIP Security Lending Gross Earnings	-	6	6	-	9	9
Miscellaneous	40,000	49,077	9,077	-	83	83
Total Revenue	<u>4,851,000</u>	<u>5,136,046</u>	<u>285,046</u>	<u>30,958,000</u>	<u>35,219,317</u>	<u>4,261,317</u>
Expenditures						
Administrative Costs	\$ 3,655,164	\$ 3,668,070	\$ (12,906)	\$ -	\$ -	\$ -
Cost of Loan Collections (Note 7)	-	-	-	8,664,308	8,838,434	(174,126)
Claims Paid to Lenders (Note 8)	-	-	-	23,100,000	25,726,334	(2,626,334)
Claims Paid to Lenders -uninsured (Note 10)	-	-	-	700,000	779,278	(79,278)
Default Aversion Fees (Note 6)	275,000	222,214	52,786	375,000	339,320	35,680
STIP Security Lending Expense	-	0	(0)	-	1	(1)
Scholarships (Note 9)	-	5,900	(5,900)	-	-	-
Total Expenditures	<u>3,930,164</u>	<u>3,896,184</u>	<u>33,980</u>	<u>32,839,308</u>	<u>35,683,367</u>	<u>(2,844,059)</u>
Excess (Deficiency) of Revenues Over Expenditures	920,836	1,239,862	319,026	(1,881,308)	(464,050)	1,417,258
Fund Balance - Restricted 06/30/13	3,776,441	3,776,441	-	6,243,486	6,243,486	-
Fund Balance - Restricted 06/30/14	<u>\$ 4,697,277</u>	<u>\$ 5,016,303</u>	<u>\$ 319,026</u>	<u>\$ 4,362,178</u>	<u>\$ 5,779,436</u>	<u>\$ 1,417,258</u>

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
Balance Sheet
As of June 30, 2015**

	Agency Operating Fund	Federal Student Loan Reserve Fund
Assets		
Cash in Treasury	\$ 876,652	\$ 2,003,769
Cash Collateral - SI	8,813	9,239
Interest Receivable	656	843
Short Term Investments (Note 2)	3,778,771	3,961,274
Long Term Investments (Note 2)	32,729	34,310
Prepaid Expense	-	-
Accounts Receivable	-	-
Due From Federal Government (Note 3)	201,371	1,900,107
Total Assets	<u>\$ 4,898,992</u>	<u>\$ 7,909,542</u>
 Liabilities and Fund Balance		
Liabilities		
Accounts Payable	\$ 178,590	\$ 7,374
Property Held in Trust	\$ 3,822	-
Liab. Under Securities Lend	\$ 8,813	9,239
Due to Federal Government (Note 4)	\$ 1	2,200,277
Total Liabilities	<u>\$ 191,226</u>	<u>\$ 2,216,890</u>
Total Fund Balance - Restricted	<u>\$ 4,707,766</u>	<u>5,692,652</u>
Total Liabilities and Fund Balance	<u>\$ 4,898,992</u>	<u>\$ 7,909,542</u>

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, 2015

	Agency Operating Fund			Federal Student Loan Reserve Fund		
	Budget	Actual	Variance	Budget	Actual	Variance
Revenue						
Account Maintenance Fees (Note 5)	\$ 884,000	\$ 831,760	\$ (52,240)	\$ -	\$ -	\$ -
Default Aversion Fees (Note 6)	375,000	228,393	(146,607)	275,000	120,488	(154,512)
Defaulted Loan Collections (Note 7)	1,944,000	2,008,982	64,982	-	-	-
Reinsurance from Department of Education (Note 8)	-	-	-	27,400,000	26,503,892	(896,108)
Non-Reinsured Loan Recoveries (Note 10)	-	-	-	400,000	431,152	31,152
Investment Earnings (Note 2)	5,000	5,786	786	6,500	5,981	(519)
STIP Security Lending Gross Earnings	-	17	17	-	20	20
Miscellaneous	40,000	6,000	(34,000)	-	91	91
Total Revenue	<u>3,248,000</u>	<u>3,080,938</u>	<u>(167,062)</u>	<u>28,081,500</u>	<u>27,061,624</u>	<u>(1,019,876)</u>
Expenditures						
Administrative Costs	\$ 3,412,000	\$ 3,268,385	\$ 143,615	\$ -	\$ -	\$ -
Cost of Loan Collections (Note 7)	-	-	-	9,256,000	8,809,147	446,853
Claims Paid to Lenders (Note 8)	-	-	-	19,115,714	17,694,933	1,420,781
Claims Paid to Lenders -uninsured (Note 10)	-	-	-	610,654	415,933	194,721
Default Aversion Fees (Note 6)	275,000	120,488	154,512	375,000	228,393	146,607
STIP Security Lending Expense	-	2	(2)	-	2	(2)
Scholarships (Note 9)	-	600	(600)	-	-	-
Total Expenditures	<u>3,687,000</u>	<u>3,389,475</u>	<u>297,525</u>	<u>29,357,368</u>	<u>27,148,408</u>	<u>2,208,960</u>
Excess (Deficiency) of Revenues Over Expenditures	(439,000)	(308,537)	130,463	(1,275,868)	(86,784)	1,189,084
Fund Balance - Restricted 06/30/14	5,016,303	5,016,303	-	5,779,436	5,779,436	-
Fund Balance - Restricted 06/30/15	<u>\$ 4,577,303</u>	<u>\$ 4,707,766</u>	<u>\$ 130,463</u>	<u>\$ 4,503,568</u>	<u>\$ 5,692,652</u>	<u>\$ 1,189,084</u>

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 Years Ended June 30, 2014 and June 30, 2015

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Description of Program

The State of Montana's Guaranteed Student Loan Program (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 cash is received or when receipts are realizable, measurable, earned and available to pay current liabilities. The expenditures are recorded when MGSLP 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. 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 are all deposited into the AOF.

2. INVESTMENTS

Short and long term investments are units purchased in the State of Montana's Short Term Investment Pool (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 (Board) or were registered in the nominee name for the Board and held by the Board's custodial bank. STIP credit quality is not rated. The Board employs the "Prudent Expert Rule" in managing the State's investment portfolio. MGSLP does not have a formal policy for credit risk. At June 30, 2014, MGSLP owned 6,785,905 units valued at \$6,785,905. At June 30, 2015, MGSLP owned 7,807,084 units

valued at \$7,807,084. As directed by the Department of Administration, MGSLP classified \$74,387 of STIP at June 30, 2014 and \$67,039 at June 30, 2015 as long term investments to reflect MGSLP pro rata share of specific STIP Investments that are not readily salable at fiscal year-end.

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. MGSLP then seeks reimbursement from the DE in accordance with reinsurance agreements. 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, 2014 and June 30, 2015, are included here. In addition, the receivable Due From Federal Government includes amounts MGSLP had not yet received for the Account Maintenance Fee (AMF) (Note 5) for the last quarter of each fiscal year 2014 and 2015. The extent of the outstanding reinsurance activity and other pending reimbursements from DE as of June 30, 2014 and June 30, 2015, respectively, are shown below.

	FY 2014		FY 2015	
Account Maintenance Fee	\$212,876	AOF	\$197,687	AOF
IRS Offset Overpayment	\$3,684	AOF	\$3,684	AOF
	<u>\$216,560</u>		<u>\$201,371</u>	
Claims			\$1,787,667	FSLRF
Discharges			\$98,814	FSLRF
Status Changes			\$6,190	FSLRF
Repurchase	\$7,436	FSLRF	\$7,436	FSLRF
	<u>\$7,436</u>		<u>\$1,900,107</u>	
Total Due From Federal Government	<u>\$223,996</u>		<u>\$2,101,478</u>	

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, 2014, the amount owed to DE was \$108,379 and at June 30, 2015, the amount owed to DE was \$2,200,278.

5. ACCOUNT MAINTENANCE FEE (AMF)

The Higher Education Amendments of 1998 authorized the payment of AMF beginning October 1, 1998. Under this Act, each guaranty agency is paid an AMF, 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 2014, AMF revenue totaled \$891,595 which includes \$212,876 accrued for reimbursements that were not received until after June 30, 2014. During fiscal year 2015, AMF revenue totaled \$831,760 which includes \$197,687 accrued for reimbursements that were not received until after June 30, 2015.

6. DEFAULT AVERSION FEES (DAF)

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 sixtieth day of delinquency, a guaranty agency must engage in default aversion activities designed to prevent a default by the borrower. DE 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 DAF is to be transferred from the FSLRF to the AOF no more frequently than monthly. If MGSLP receives DAF 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 2014, the DAF payment to the AOF was \$339,320 and \$222,214 was returned to the FSLRF, for net revenue of \$117,106 to the AOF. During fiscal year 2015, the DAF payment to the AOF was \$228,393 and \$120,488 was returned to the FSLRF, for net revenue of \$107,905 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. Effective July 1, 2014, on a rehabilitated loan, MGSLP may charge the borrower an amount not to exceed 16% of principal and interest, in order to defray collection costs. MGSLP may retain this amount from the proceeds of the loan sale and return 100% of the principal to the Secretary. 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 FDSLSP 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, 2014, the net revenue retained by MGSLP of \$3,850,346 is reported in the AOF and the federal share of \$8,838,434 is reported in the FSLRF as revenue with corresponding expenditures of \$8,838,434. For the fiscal year ended June 30, 2015, the net revenue retained by MGSLP of \$2,008,982 is reported in the AOF and the federal share of \$8,809,147 is reported in the FSLRF as revenue with corresponding expenditures of \$8,809,147.

8. CLAIMS PAID TO LENDERS AND REINSURANCE FROM DE

MGSLP records amounts paid to lenders for claims and subsequent amounts received from the DE as expenditures and revenues respectively. For fiscal year 2014, MGSLP paid claims to lenders totaling \$25,726,334 and received reinsurance revenue from DE totaling \$34,564,742. For fiscal year 2015, MGSLP paid claims to lenders totaling \$17,694,932 and received reinsurance revenue from DE totaling \$26,503,892. The reinsurance includes \$25,726,309 from claim purchases and \$8,838,434 from default collections for fiscal year

2014 and \$17,694,745 from claim purchases and \$8,809,147 from default collections for fiscal year 2015 as detailed in Note 7.

9. SCHOLARSHIP FUNDS

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 ranging from \$150 - \$250 in value. 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. For fiscal year 2014 and 2015, \$5,900 and \$600 were disbursed, respectively to MUS campuses on behalf of the scholarship recipients. If the student doesn't enroll in the time frame allotted, the funds will revert back to MGSLP when the last essay award expires December 2016. The activity in the Essay Scholarship Fund is combined with the AOF for presentation purposes.

10. CONTINGENCIES

The original principal balance of guaranteed loans outstanding held by MGSLP as of June 30, 2014 was approximately \$1,411,974,799 and as June 30, 2015 was approximately \$1,307,054,147. This amount excludes bad debt, death, disability, and bankruptcy claims which have been previously purchased by the agency. MGSLP's agreement with the DE 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. MGSLP's current three year cohort default rate is 4.8%.

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. In order to receive maximum reimbursement, a guaranty agency's trigger rate must not exceed 5%. The trigger rate is calculated by dividing the defaulted loan balance during the federal fiscal year by the loan balance in repayment at the beginning of the same fiscal year. MGSLP's current trigger rate is .90%. During fiscal year 2014, MGSLP paid \$779,278 in claims, or portions of claim eligible loans, which were not reinsured by DE. During fiscal year 2014, MGSLP recovered \$425,932 of the total outstanding balance of non-reinsured claims held by the agency. During fiscal year 2015, MGSLP paid \$415,933 in claims, or portions of claim eligible loans, which were not reinsured by DE. During fiscal year 2015, MGSLP recovered \$431,152 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. For the periods ended June 30, 2014 and June 30, 2015, 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 73.90%, or \$1,047,918,090, of MGSLP's outstanding loan volume was held by MHESAC for fiscal year 2014 and approximately 71.89%, or \$939,577,597 was held for fiscal year 2015.

13. 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) as per §19-21-213 (MCA). PERS offers both a Defined Benefit Plan (PERS-DB) and a Defined Contribution Plan (PERS-DC) for employees to choose. Certain professional employees under contract with the Board of Regents who were 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

Defined Benefit Plan (PERS-DB)

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 employees. 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 is 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.

Defined Contributions Plan (PERS-DC)

The PERS-DC is a retirement plan for employees of the state and the university system, in which 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 (MUS-RP)

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: 1-866-842-2442

According to state law, MGSLP, as a part of the MUS, remits additional employer contributions, for contract employees 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
 Montana Teachers' Retirement System
 PO Box 200139
 Helena, MT 59620-0139

Retirement plan information for MGSLP as of June 30, 2015, is as follows.

	PERS	MUS-RP Staff
Covered Payroll	\$1,026,885	\$121,574
Employer Contributions	\$88,194	\$12,197
Percent of Covered Payroll	8.27%	8.27%
Employee Contribution	\$81,124	\$9,320
Percent of Covered Payroll	7.90%	7.90%

Retirement plan information for MGSLP as of June 30, 2014, is as follows.

	PERS	MUS-RP Staff
Covered Payroll	\$1,053,253	\$113,822
Employer Contributions	\$90,972	\$9,306
Percent of Covered Payroll	8.17%	8.17%
Employee Contribution	\$83,207	\$8,791
Percent of Covered Payroll	7.90%	7.90%

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%

Report on Internal Control and Compliance

LEGISLATIVE AUDIT DIVISION

B-1

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



Deputy Legislative Auditors:
Cindy Jorgenson
Angus Maciver

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

The Legislative Audit Committee
of the Montana State Legislature:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Office of the Commissioner of Higher Education Montana Guaranteed Student Loan Program-Federal Special Revenue Fund for the two fiscal years ended June 30, 2014, and 2015, and the related notes to the financial statements, which collectively comprise the program's financial statements, and have issued our report thereon dated November 4, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the program's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the program's internal control. Accordingly, we do not express an opinion on the effectiveness of the program's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal controls was for the limited purposes described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify

any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the program's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination on financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the program's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the program's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

November 4, 2015

MONTANA GUARANTEED
STUDENT LOAN
PROGRAM

PROGRAM RESPONSE

**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 4, 2015

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

RECEIVED
DEC 07 2015
LEGISLATIVE AUDIT DIV.

Dear Ms. Hunthausen:

This letter acknowledges receipt of the results of the audit for the two fiscal years ending June 30, 2015 and we consider the audit complete. I understand that the audit resulted in an unmodified opinion and there are no findings or recommendations contained in the report.

I would like to take this opportunity to provide clarification on the wind down of the operations of the Montana Guaranteed Student Loan Program (GSL). The timeline of 2018 or 2019 presented in the report is based on the current financial position of the program operating under current federal policy. GSL will not cease to exist on this date, but the guaranteed loan portfolio will be significantly diminished and there will be less demand on the program's resources. It is important to note that any change in the federal policy could impact GSL's operations and alter the timeline.

I appreciate the professional manner in which the audit was conducted. The staff was helpful and very thorough in their review.

Sincerely,

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