A Report
to the
Montana
Legislature

Financial Audit

Montana Guaranteed Student Loan Program

For the Two Fiscal Years Ended June 30, 2017

December 2017

Legislative Audit Division

17-06

Legislative Audit Committee

Fraud Hotline
(Statewide)
1-800-222-4446
(in Helena)
444-4446
ladhotline@mt.gov

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) certificates.

The Single Audit Act Amendments of 1996 and the Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards 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 reporting requirements. 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, 2015, was issued March 29, 2016. The Single Audit Report for the two fiscal years ended June 30, 2017, will be issued by March 31, 2018.

Audit Staff

Jeane Carstensen-Garrett   Mary Currin
Jennifer Erdahl

Reports can be found in electronic format at:
http://leg.mt.gov/audit

LEGISLATIVE AUDIT DIVISION

Angus Maciver, Legislative Auditor
Deborah F. Butler, Legal Counsel

Deputy Legislative Auditors
Cindy Jorgenson
Joe Murray

December 2017

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, 2017.

The Office of the Commissioner of Higher Education prepares the program financial statements and related notes to the financial statements for the Montana Guaranteed Student Loan Program. The financial statements and related notes are located on pages A-3 through A-16.

As part of our audit, we reviewed the program's operations and compliance with selected federal regulations. Our audit resulted in an unmodified opinion, and the report does not include any recommendations to the office.

We thank the Commissioner of Higher Education and his staff for their assistance and cooperation throughout the audit.

Respectfully submitted,

/s/ Angus Maciver

Angus Maciver
Legislative Auditor

Room 160 • State Capitol Building • PO Box 201705 • Helena, MT • 59620-1705
Phone (406) 444-3122 • FAX (406) 444-9784 • E-Mail lad@mt.gov

Table of Contents

Figures and Tables

Tables

Appointed and Administrative Officials

Office of the Commissioner of Higher Education

Clayton Christian, Commissioner of Higher Education

Tyler Trevor, Deputy Commissioner for Budget & Planning/Chief of Staff

Frieda Houser, Director of Fiscal Affairs

Robin Graham, Director of Operations/CFO, Montana Guaranteed Student Loan Program (through July 2017)

Ron Muffick, Director of Operations & Administration/Student Affairs

Jamie Dushin, Accounting Manager

For additional information concerning the Montana Guaranteed Student Loan Program, contact:

Ron Muffick
Director of Operations & Administration/Student Affairs
Office of the Commissioner of Higher Education
P.O. Box 203201
Helena, MT 59620-3201
(406) 444-0369

e-mail: rmuffick@montana.edu

Montana Legislative Audit Division

Financial Audit

Montana Guaranteed Student Loan Program

For the Two Fiscal Years Ended June 30, 2017

December 2017 | 17-06 | Report Summary

As of October 1, 2017, the loan servicing portion of the Montana Guaranteed Student Loan Program was transferred to a federally-approved national education loan servicing provider, as approved by the Board of Regents in May 2017. The full-time equivalent positions remaining as of October 1, 2017, were 5.5. The Montana Guaranteed Student Loan Program will continue to offer other student financial aid-related activities.

Context

The Montana Guaranteed Student Loan Program (MGSLP) is administered by the Office of the Commissioner of Higher Education. MGSLP guarantees federal loans that were granted prior to 2011. The last borrowers to receive loans by MGSLP received loans in 2008 and 2009. MGSLP purchases loans as a result of borrower default, bankruptcy, disability, or death.

At the end of fiscal year 2017, the MGSLP had loans outstanding of approximately $1.1 billion. The program's guaranteed loans have decreased by over $100 million annually for the past six years. A change in federal regulations resulted in no further guarantees of new loans as of fiscal year 2011. However, as of fiscal year-end 2017, the program was the guarantor of the existing loans.

During fiscal year 2017, MGSLP purchased over $17 million guaranteed student loans from financial institutions. MGSLP purchased over $15 million loans in fiscal year 2016.

MGSLP keeps a percentage of payments made on purchased loans, loans bought back by lenders after completion of a successful rehabilitation plan, and payments made as part of federal direct consolidations.

MGSLP also administers a variety of scholarship programs and assists in administering the Montana Family Education Savings Program.

Results

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

Our audit did not result in any recommendations, and we issued an unmodified opinion on the MGSLP financial statements. This means the financial statements and related notes presented in this report can be relied upon.

For a complete copy of the report (17-06) 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**
Report Fraud, Waste, and Abuse to the Legislative Auditor's FRAUD HOTLINE
Call toll-free 1-800-222-4446, or e-mail **lad@mt.gov.**

Chapter I – Introduction

Introduction

We performed a financial audit of the Office of the Commissioner of Higher Education's Montana Guaranteed Student Loan Program (MGSLP) for the two fiscal years ended June 30, 2017. The objectives of our audit were to:

1. Determine whether MGSLP's financial statements present fairly the financial position and results of operations for the two fiscal years ended June 30, 2017.
2. Obtain an understanding of MGSLP's control systems to the extent necessary to support our audit of MGSLP's financial statements and, if appropriate, make recommendations for improvements in management and internal controls.
3. Determine whether MGSLP complied with selected regulations recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements.

We focused our audit effort on financial activity related to payments from the federal government, claims paid to lenders, cost of loan collections, administrative costs, and the related control systems. Our audit did not result in any recommendations.

This audit is completed to satisfy financial reporting requirements established by the U.S. Department of Education.

Background

The Office of the Commissioner of Higher Education administers the MGSLP. MGSLP's primary goal is to improve access to postsecondary education in Montana by working collaboratively with schools, colleges, lenders, and other trading partners. MGSLP has authorized 41.02 full-time equivalent (FTE) positions. As of June 30, 2017, 16.52 FTE were vacant.

Through management of the Federal Family Education Loan Program, MGSLP 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. As of October 1, 2017, the loan servicing portion of MGSLP was transferred to a federally-approved national education loan servicing provider, as approved by the Board of Regents in May 2017. The FTE remaining as of October 1, 2017, were 5.5. MGSLP will continue to offer other student financial aid-related activities. The transfer is disclosed in Note 16 of the Notes to the Financial Statements.

Effective July 1, 2010, Congress changed the Federal Family Education Loan (FFEL) Program and moved to the William D. Ford Direct Loan Program. As a result, MGSLP ceased guaranteeing new student loans. Table 1 shows the original guaranteed loan amounts of loans outstanding as of June 30, 2012, through June 30, 2017. MGSLP 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.

Table 1

History of Outstanding Guaranteed Loan Balance

Original Principal Balance of Loans Outstanding	
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
June 30, 2016	$1,194,864,477
June 30, 2017	$1,090,537,475

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

Since July 1, 2010, MGSLP continued to administer the FFEL program and provide loan guaranty services. Revenue to sustain the program was generated from servicing loans within the FFEL program. By 2017, the program was deemed by the Office of the Commissioner of Higher Education no longer capable of sustaining its operations without suffering annual financial losses. The annual financial losses were expected to worsen with each successive year due to a shrinking guaranty portfolio. Transferring the guaranty responsibilities was deemed necessary by the office to avoid future liabilities that MGSLP could not cover.

Independent Auditor's Report and Program Financial Statements

LEGISLATIVE AUDIT DIVISION

Angus Maciver, Legislative Auditor
Deborah F. Butler, Legal Counsel

Deputy Legislative Auditors
Cindy Jorgenson
Joe Murray

Independent Auditor's Report

The Legislative Audit Committee
of the Montana State Legislature:

Introduction

We have audited the accompanying Federal Special Revenue Fund Balance Sheets of the Office of the Commissioner of Higher Education's Montana Guaranteed Student Loan Program as of June 30, 2017, and 2016, 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, 2017, and 2016, 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 Matters

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, 2017, and 2016, 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.

As disclosed in Note 16, the loan servicing portion of the Montana Guaranteed Student Loan Program was transferred to a federally-approved national education loan servicing provider, effective October 1, 2017. 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 13, 2017, 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 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 13, 2017

Office of the Commissioner of Higher Education
Montana Guaranteed Student Loan Program
Federal Special Revenue Fund
Balance Sheet
As of June 30, 2017

	Agency Operating Fund	Federal Student Loan Reserve Fund
Assets		
Cash in Treasury	$ 605,736	$ 1,156,063
Interest Receivable	3,193	4,697
Short Term Investments (Note 3)	3,418,721	4,184,875
Accounts Receivable	2,202	-
Due From Federal Government (Note 4)	170,131	2,578,301
Total Assets	$ 4,199,983	$ 7,923,936
Liabilities and Fund Balance		
Liabilities		
Accounts Payable	$ 163,231	$ 705
Due to Federal Government (Note 5)	11,324	1,427,910
Total Liabilities	$ 174,555	$ 1,428,615
Total Fund Balance - Restricted	$ 4,025,428	6,495,321
Total Liabilities and Fund Balance	$ 4,199,983	$ 7,923,936

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, 2017

	Agency Operating Fund			Federal Student Loan Reserve Fund		
	Budget	Actual	Variance	Budget	Actual	Variance
Revenue						
Account Maintenance Fees (Note 7)	$ 805,000	$ 699,515	$ (105,485)	$ -	$ -	$ -
Default Aversion Fees (Note 8)	200,000	170,961	(29,039)	100,000	106,847	6,847
Defaulted Loan Collections (Note 9)	2,000,000	2,435,688	435,688	-	-	-
Reinsurance from Department of Education (Note 10)	-	-	-	25,600,000	26,745,500	1,145,500
Non-Reinsured Loan Recoveries (Note 12)	-	-	-	400,000	386,894	(13,106)
Investment Earnings (Note 3)	13,000	29,533	16,533	15,000	35,910	20,910
STIP Security Lending Gross Earnings	-	92	92	-	126	126
Allocated STIP Earnings/Agency	-	2,245	2,245	-	7,500	7,500
Miscellaneous	20,000	19,030	(970)	-	155	155
Transfers In-General (Note 11)	-	117,878	117,878	-	-	-
Total Revenue	3,038,000	3,474,942	436,942	26,115,000	27,282,933	1,167,933
Expenditures						
Administrative Costs	$ 3,600,000	$ 3,688,204	$ (88,204)	$ -	$ -	$ -
Capital Leases-Equipment (Note 6)	-	-	-	-	-	
Cost of Loan Collections (Note 9)	-	-	-	9,100,000	8,762,776	337,224
Claims Paid to Lenders (Note 10)	-	-	-	16,500,000	17,969,038	(1,469,038)
Claims Paid to Lenders -uninsured (Note 12)	-	-	-	400,000	(64,360)	464,360
Default Aversion Fees (Note 8)	100,000	106,847	(6,847)	185,000	170,961	14,039
STIP Security Lending Expense	-	41	(41)	-	57	(57)
Scholarships (Note 11)	-	200	(200)	-	-	-
Total Expenditures	3,700,000	3,795,292	(95,292)	26,185,000	26,838,472	(653,472)
Excess (Deficiency) of Revenues Over Expenditures (Note 15)	(662,000)	(320,350)	341,650	(70,000)	444,461	514,461
Fund Balance - Restricted 06/30/16	4,707,766	4,345,778	-	5,692,652	6,050,860	-
Fund Balance - Restricted 06/30/17	$ 4,045,766	$ 4,025,428	$ 341,650	$ 5,622,652	$ 6,495,321	$ 514,461

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, 2016

	Agency Operating Fund	Federal Student Loan Reserve Fund
Assets		
Cash in Treasury	$ 575,045	$ 1,743,289
Cash Collateral - SI	15,816	11,369
Interest Receivable	1,811	2,224
Short Term Investments (Note 3)	3,753,241	2,697,995
Accounts Receivable	1,078	-
Due From Federal Government (Note 4)	195,384	2,711,368
Total Assets	$ 4,542,375	$ 7,166,245
Liabilities and Fund Balance		
Liabilities		
Accounts Payable	$ 167,968	$ 5,714
Liab. Under Securities Lend	15,816	11,369
Due to Federal Government (Note 5)	12,812	1,098,302
Total Liabilities	$ 196,596	$ 1,115,385
Total Fund Balance - Restricted	$ 4,345,779	6,050,860
Total Liabilities and Fund Balance	$ 4,542,375	$ 7,166,245

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, 2016

	Agency Operating Fund			Federal Student Loan Reserve Fund		
	Budget	**Actual**	**Variance**	**Budget**	**Actual**	**Variance**
Revenue						
Account Maintenance Fees (Note 7)	$ 805,000	$ 761,107	$ (43,893)	$ -	$ -	$ -
Default Aversion Fees (Note 8)	200,000	183,908	(16,092)	100,000	100,325	325
Defaulted Loan Collections (Note 9)	2,000,000	2,287,229	287,229	-	-	-
Reinsurance from Department of Education (Note 10)	-	-	-	25,600,000	24,340,130	(1,259,870)
Non-Reinsured Loan Recoveries (Note 12)	-	-	-	400,000	442,227	42,227
Investment Earnings (Note 3)	13,000	16,946	3,946	15,000	17,474	2,474
STIP Security Lending Gross Earnings	-	74	74	-	98	98
Allocated STIP Earnings/Agency	-	1,052	1,052		3,510	
Miscellaneous	20,000	17,774	(2,226)	-	73	73
Inception of Lease (Note 6)	-	14,688	14,688	-	-	-
Total Revenue	3,038,000	3,282,778	244,778	26,115,000	24,903,838	(1,211,163)
Expenditures						
Administrative Costs	$ 3,510,000	$ 3,532,746	$ (22,746)	$ -	$ -	$ -
Capital Leases-Equipment (Note 6)	-	14,688	(14,688)	-		
Cost of Loan Collections (Note 9)	-	-	-	9,100,000	8,979,660	120,340
Claims Paid to Lenders (Note 10)	-	-	-	16,500,000	15,374,807	1,125,193
Claims Paid to Lenders -uninsured (Note 12)	-	-	-	400,000	7,216	392,784
Default Aversion Fees (Note 8)	100,000	100,325	(325)	200,000	183,908	16,092
STIP Security Lending Expense	-	29	(29)	-	39	(39)
Scholarships (Note 11)	-	800	(800)	-	-	-
Total Expenditures	3,610,000	3,648,588	(38,588)	26,200,000	24,545,630	1,654,370
Excess (Deficiency) of Revenues Over Expenditures (Note 15)	(572,000)	(365,810)	206,190	(85,000)	358,208	443,208
Fund Balance - Restricted 06/30/15	4,707,766	4,707,766	-	5,692,652	5,692,652	-
Prior period adjustment (Note 2)	3,822	3,822				
Restated Fund Balance-Restricted 06/30/15		$ 4,711,588				
Fund Balance - Restricted 06/30/16	$ 4,139,588	$ 4,345,779	$ 206,190	$ 5,607,652	$ 6,050,860	$ 443,208

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, 2016 and June 30, 2017

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. ACCOUNTING CHANGES

The fund balance-restricted for the period ended June 30, 2015 has been restated to reflect a prior period adjustment. An amount of $3,822 returned to MGSLP in a prior period were misclassified as property held in trust. The monies received should have been treated as an abatement to the expenditure incurred at the time of disbursement. As a result, the fund balance for June 30, 2015 was understated. The beginning fund balance for June 30, 2016 has been adjusted to reflect the increase.

3. INVESTMENTS

Short Term Investment Pool (STIP) is managed and administered under the direction of the MBOI as authorized by the Unified Investment Program. Funds may be invested for one or more days and provides a 24-hour liquidity for state agency participants. It is a commingled pool for investment purposes and requested redemptions from the pool are redeemed the next business day. The fair values of the investments in this category have been determined using the Net Asset Value (NAV) per share (or its equivalent) of the investment.

The STIP portfolio may include asset-backed securities, commercial paper, corporate, U.S. Government direct obligations, U.S. Government agency securities, repurchase agreements, institutional money market funds, certificates of deposit, and variable-rate (floating-rate) instruments. Investments must have a maximum maturity of 397 days or less unless they are a variable rate security.

STIP as of June 30, 2016 and June 30, 2017, respectively, are shown below.

	FY 2016		FY 2017	
Short Term Investments	$3,752,464	AOF	$3,418,157	AOF
STIP Appr/Depr	$777	AOF	$564	AOF
	$3,753,241		$3,418,721	
Short Term Investments	$2,697,437	FSLRF	$4,184,185	FSLRF
STIP Appr/Depr	$558	FSLRF	$690	FSLRF
	$2,697,995		$4,184,875	

4. 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, 2016 and June 30, 2017, 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 2016 and 2017. The extent of the outstanding reinsurance activity and other pending reimbursements from DE as of June 30, 2016 and June 30, 2017, respectively, are shown below.

	FY 2016		FY 2017	
Account Maintenance Fee	$180,590	AOF	$164,795	AOF
IRS Offset Overpayment	$14,794	AOF	$5,336	AOF
	$195,384		$170,131	
Claims	$2,628,083	FSLRF	$2,544,046	FSLRF
Discharges	$42,530	FSLRF	$29,173	FSLRF
Status Changes	$40,755	FSLRF	$5,082	FSLRF
	$2,711,368		$2,578,301	
Total Due From Federal Government	$2,906,752		$2,748,432	

5. 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, 2016, the amount owed to DE was $1,111,114 and at June 30, 2017, the amount owed to DE was $1,439,234.

6. CAPITAL LEASE OBLIGATION

During FY2016, MGSLP entered into an agreement with Xerox Corporation to lease a Xerox Workcentre 7970 multifunction printer for a cost of $14,688. The lease is a 60-month fair market value lease with a monthly fixed lease cost of $244.80 for the term of the lease. The straight-line depreciation expense at June 30, 2016 is $1,958 and at June 30, 2017 is $2,938.

7. 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 2016, AMF revenue totaled $761,107 which includes $180,590 accrued for reimbursements that were not received until after June 30, 2016. During fiscal year 2017, AMF revenue totaled $699,515 which includes $164,795 accrued for reimbursements that were not received until after June 30, 2017.

8. 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 2016, the DAF payment to the AOF was $183,908 and $100,325 was returned to the FSLRF, for net revenue of $83,583 to the AOF. During fiscal year 2017, the DAF payment to the AOF was $170,961 and $106,847 was returned to the FSLRF, for net revenue of $64,114 to the AOF.

9. DEFAULTED LOAN COLLECTIONS

MGSLP pursues collection, from the borrower or other responsible party, of defaulted loans held by the agency. The U.S. Department of Education (Secretary) 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 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, 2016, the net revenue retained by MGSLP of $2,287,229 is reported in the AOF and the federal share of $8,979,660 is reported in the FSLRF as revenue, in Reinsurance from Department of Education, with corresponding expenditures, in Cost of Loan Collections, of $8,979,660. For the fiscal year ended June 30, 2017, the net revenue retained by MGSLP of $2,435,688 is reported in the AOF and the federal share of $8,762,776 is reported in the FSLRF as revenue, in Reinsurance from Department of Education, with corresponding expenditures, in Cost of Loan Collections, of $8,762,776.

10. 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 2016, MGSLP paid claims to lenders totaling $15,374,807 and received reinsurance revenue from DE totaling $24,340,130. For fiscal year 2017, MGSLP paid claims to lenders totaling $17,969,038 and received reinsurance revenue from DE totaling $26,745,500. The reinsurance includes $15,360,470 from claim purchases and $8,979,660 from default collections for fiscal year 2016 and $17,982,725 from claim purchases and $8,762,776 from default collections for fiscal year 2017 as detailed in Note 9.

11. 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 2016 and 2017, $800 and $200 were disbursed, respectively to MUS campuses on behalf of the scholarship recipients. The last essay awards expired December 2016 with the funds reverting back to MGSLP. The activity in the Essay Scholarship Fund is combined with the AOF for presentation purposes.

12. CONTINGENCIES

The original principal balance of guaranteed loans outstanding held by MGSLP as of June 30, 2016 was approximately $1,194,686,477 and as June 30, 2017 was approximately $1,090,537,475. 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. As of December 1, 2015, claims paid due to defaulted loans are reimbursed by DE at 100%. The percent of reimbursement on defaulted loans payable to the agency prior to December 1, 2015 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 2016, MGSLP paid $183,908 in claims, or portions of claim eligible loans, which were not reinsured by DE. During fiscal year 2016, MGSLP recovered $442,227 of the total outstanding balance of non-reinsured claims held by the agency. During fiscal year 2017, MGSLP was paid $64,360 in claims, or portions of claim eligible loans, which were not reinsured by DE. During fiscal year 2017, MGSLP recovered $386,894 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

13. 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, 2016 and June 30, 2017, MGSLP was in compliance with all Guarantee Reserve Agreements.

14. 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. One Montana Board of Regents member is also a MHESAC Board of Directors member, an OCHE staff member is a MHESAC officer, and the Commissioner of Higher Education is an Ex-Officio member of the board. Approximately 70.44%, or $841,679,269, of MGSLP's outstanding loan volume was held by MHESAC for fiscal year 2016 and approximately 68.36%, or $745,509,155 was held for fiscal year 2017.

15. BUDGETED DEFICIENCY OF REVENUES OVER EXPENDITURES

MGSLP budgeted a deficiency in revenues for both fiscal year 2016 and fiscal year 2017. With the decreasing loan portfolio and required commitments of the agency, MGSLP's revenues were less than expenses. MGSLP has an established fund balance in place to be used for the budgeted deficiency of revenues.

16. SUBSEQUENT EVENT

Effective October 1, 2017, the loan servicing portion of MGSLP will be transferred to a federally approved national education loan servicing provider. This transfer was approved by the Montana Board of Regents in May 2017. MGSLP will continue to exist in the office but at a much smaller level. The program will continue to offer other student financial aid related activities for the benefit of Montana students as determined by the Montana Board of Regents.

After the transfer of the loan servicing portion, MGSLP will be required to return the Federal Student Loan Reserve Fund (FSLRF) to the U.S. Department of Education. As of June 30, 2017, the amount to return was $6,495,320.

17. 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). 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. MGSLP records employee/employer contributions and remits monies to TIAA. Individuals are immediately vested in the plan.

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

TIAA
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, 2017, is as follows.

	PERS	MUS-RP
		Staff
Covered Payroll	$ 949,238	$129,564
Employer Contributions	$78,193	$14,356
Percent of Covered Payroll	8.47%	8.43%
Employee Contribution	$ 74,990	$10,216
Percent of Covered Payroll	7.90%	7.90%

Retirement plan information for MGSLP as of June 30, 2016, is as follows.

	PERS	MUS-RP
		Staff
Covered Payroll	$1,036,637	$129,062
Employer Contributions	$86,348	$13,381
Percent of Covered Payroll	8.37%	8.37%
Employee Contribution	$81,894	$10,196
Percent of Covered Payroll	7.90%	7.90%

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%

Report on Internal Control and Compliance

LEGISLATIVE AUDIT DIVISION

Angus Maciver, Legislative Auditor
Deborah F. Butler, Legal Counsel

Deputy Legislative Auditors
Cindy Jorgenson
Joe Murray

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's Montana Guaranteed Student Loan Program–Federal Special Revenue Fund for each of the two fiscal years ended June 30, 2017, and 2016, and the related notes to the financial statements, which collectively comprise the program's financial statements, and have issued our report thereon dated November 13, 2017.

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 opinion 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 purpose 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

Room 160 • State Capitol Building • PO Box 201705 • Helena, MT • 59620-1705
Phone (406) 444-3122 • FAX (406) 444-9784 • E-Mail lad@mt.gov

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 of 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 13, 2017

Montana Guaranteed Student Loan Program

Program Response

MONTANA UNIVERSITY SYSTEM
OFFICE OF THE COMMISSIONER OF HIGHER EDUCATION

2500 Broadway – PO Box 203201 – Helena, Montana 59620-3201
(406) 444-6570 – FAX (406) 444-1469

December 18, 2017

RECEIVED
DEC 18 2017
LEGISLATIVE AUDIT DIV.

Angus Maciver
Legislative Auditor
State Capitol, Room 160
P.O. Box 201705
Helena MT 59620-1705

Dear Mr. Maciver:

We have reviewed the audit report for the two fiscal years ending June 30, 2017. The office received an unmodified opinion on the Montana Guaranteed Student Loan Program's financial statements and no findings or recommendations were included in the report. We appreciate the professional manner in which the audit was conducted.

Sincerely,

Clayton T. Christian
Commissioner of Higher Education