STATE OF ILLINOIS
OFFICE OF THE
AUDITOR GENERAL
William G. Holland, Auditor General

SUMMARY REPORT DIGEST

ILLINOIS STUDENT ASSISTANCE COMMISSION - ILLINOIS DESIGNATED ACCOUNT PURCHASE PROGRAM

FINANCIAL AUDIT
For the Year Ended: June 30, 2013

Release Date: February 6, 2014

Summary of Findings:

Total this audit:	**2**
Total last audit:	**2**
Repeated from last audit:	**1**

INTRODUCTION

This report covers our financial audit of the Illinois Student Assistance Commission (Commission) - Illinois Designated Account Purchase Program (IDAPP) as of June 30, 2013 and for the year then ended.

SYNOPSIS

- IDAPP was not in compliance with two of the covenants relating to the Commission's revolving line of credit agreement.
- IDAPP depository accounts with funds in excess of the Federal Deposit Insurance Company's coverage amount were not properly collateralized.

{Financial information is summarized on the reverse page.}

ILLINOIS STUDENT ASSISTANCE COMMISSION
ILLINOIS DESIGNATED ACCOUNT PURCHASE PROGRAM
FINANCIAL AUDIT
For the Year Ended June 30, 2013 (in thousands)

STATEMENT OF NET POSITION	2013	2012
Unrestricted assets		
Cash and investments	$ 16,857	$ 16,352
Capital assets, net	-	4
Restricted assets		
Cash and cash equivalents	21,927	48,672
Student loans receivable, net	644,232	809,410
Accrued interest	12,488	15,212
Other	3,600	6,367
Total	699,104	896,017
Liabilities		
Accounts payable and accrued expenses	398	617
Accrued interest payable	940	1,523
Federal special allowance and interest subsidy	1,745	2,174
Revolving credit line	240,607	275,957
Notes payable, net	429,388	590,704
Due to other ISAC funds	2,420	3,396
Compensated absences	206	202
Total	675,704	874,573
Net Position		
Net investment in capital assets	-	4
Restricted	9,567	9,303
Unrestricted	13,833	12,137
Total	$ 23,400	$ 21,444

REVENUES, EXPENSES AND CHANGES IN NET POSITION	2013	2012
Operating revenues		
Interest - student loans	$ 29,518	$ 35,201
Fees	328	717
Interest - investments	12	343
Total	29,858	36,261
Operating expenses		
Provision for loan losses	8,685	15,475
Interest on revenue bonds	(37)	6,097
Student loan costs and fees	4,144	5,016
External loan servicing	2,658	2,141
Salaries and employee benefits	1,985	1,806
Management and professional services	1,275	1,523
Other	155	288
Total	18,865	32,346
Operating income	10,993	3,915
Federal special allowance and excess interest	(7,434)	(9,422)
Loss on sale of loan portfolio	(1,603)	-
Change in net position	$ 1,956	$ (5,507)

AGENCY EXECUTIVE DIRECTOR
During Examination Period: Mr. Eric Zarnikow
Currently: Mr. Eric Zarnikow

FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

DEBT COVENANT VIOLATION

Noncompliance with debt covenants

The Illinois Student Assistance Commission (Illinois Designated Account Purchase Program) was not in compliance with two of the covenants relating to the agency's revolving line of credit agreement.

Minimum coverage condition ratio not met

During our audits of the agency's June 30, 2009, 2010, 2011, and 2012 financial statements, we noted that IDAPP was in violation of one or more debt covenants related to the agency's revolving credit (loan) agreement. In addition, the facility matured on July 27, 2010 and has not been repaid. Per the agreement, the minimum required coverage condition ratio is 104%, while the ratio as of June 30, 2013 was 101.04%. Also per the agreement, the default ratio is set at a maximum of 6.25%, but at June 30, 2013 this ratio was 7.17%.

Lender has right to call loan but has not communicated any intent to exercise remedies available

As a result of the debt covenant violation and the maturity of the facility, the bank has certain remedies available to it under the terms of the loan agreement, principal of which would be rights to call the loan and take possession of the collateral (the underlying student loan portfolio). The bank has been made aware of the event of default and the maturity of the loan and has not communicated to IDAPP any intent to exercise the remedies available to it under the terms of the loan agreement. The balance of the line of credit with the bank was $240,606,827 at June 30, 2013.

According to Commission management, the coverage condition and default issues are due to the poor performance of the portfolio. The portfolio continues to experience a high level of delinquent accounts. The line of credit has not been refinanced because of the conditions in the private loan credit market. (Finding 1, page 29) **This finding was first reported in 2009.**

Commission agrees with auditors and continues to review on a monthly basis

Commission officials accepted our finding and recommendation to continue to monitor the loan covenant violations and continue seeking remedies from the lender involved. Commission officials indicated the loan covenants are reviewed on a monthly basis and that they continue to talk to Citibank about the portfolio. (For the previous IDAPP response, see Digest Footnote #1.)

INADEQUATE COLLATERAL COVERAGE

Funds not properly collateralized

The Illinois Student Assistance Commission (Illinois Designated Account Purchase Program) did not properly collateralize excess funds over the Federal Deposit Insurance Company (FDIC) coverage amount, in certain of the Agency's depository accounts.

FDIC reduced coverage on January 1, 2013

Prior to December 31, 2012, the FDIC insured all deposits in non-interest bearing accounts. Beginning January 1, 2013, the coverage was reduced to $250,000, per depositor, per institution. IDAPP had funds invested in certain banks that exceed $250,000. As a result, the agency began the process to collateralize these excess deposits. Per review of the provided collateral agreements, the agreements did not go into effect until August 5, 2013, leaving a balance of $5,543,230 uncollateralized as of June 30, 2013.

Collateral agreement process not finalized prior to year end

No loss took place

According to Commission management, they assumed the bank went back to the pre-financial crisis method of collateralizing Commission accounts. When it was determined that they did not, the collateral agreement process was started, but was not finalized prior to year end. While no loss took place, without adequate collateralization of funds, the funds could be susceptible to custodial credit risk losses in the event of a bank failure. (Finding 2, page 30)

Commission agrees with auditors

Commission officials accepted our finding and recommendation to more closely monitor its collateral requirements to ensure that new agreements are approved timely to allow for proper collateralization of all deposits. Commission officials indicated that the existing collateral agreement will be in place until the accounts are closed and collateral requirements will be reviewed on an annual basis.

AUDITORS' OPINION

Our auditors stated the financial statements of IDAPP are fairly presented in all material respects.

WILLIAM G. HOLLAND
Auditor General

WGH:DJB

SPECIAL ASSISTANT AUDITORS

Our special assistant auditors for this audit were McGladrey LLP.

DIGEST FOOTNOTE

#1 - DEBT COVENANT VIOLATION

2012 – ISAC agrees with the recommendation. IDAPP will continue to monitor these loan covenants and will work with our external servicers to try to bring the coverage condition and default ratios back into compliance.

This credit facility matured on July 27, 2010. Due to the tight credit markets for student loans and the performance of the portfolio, neither Citibank nor ISAC have been able to refinance the facility. ISAC management has been in regular contact with the lender and continues to explore options on the refinancing. At this time however, there are no imminent plans to refinance the facility.