

AGENDA ITEM 8

UPDATE ON STUDENT LOANS HELD BY ISAC/IDAPP

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Update on Student Loans Held by ISAC/IDAPP

Submitted for: Information

Summary: Operational Impact on Student Loans from COVID-19

ISAC has been in the student loan business for over fifty years and currently administers the following student loan portfolios funded by either the Federal Government, the State of Illinois, bonds that were previously issued or a private bank credit facility. All these portfolios have been in wind down for many years with no new loans being issued.

Federal Funding – Federal Family Education Loan Program (FFELP)

FFELP was a Department of Education (ED) funded program designed to stimulate the making of educational loans by commercial lenders by guaranteeing repayment of defaulted loans to lenders. The program was/is administered by guarantee agencies, like ISAC, on behalf of the Ed working in conjunction with private lenders. ISAC has been a FFELP guarantor since 1965.

The Illinois Designated Account Purchase Program (IDAPP), was created as an arm of ISAC by the State of Illinois in 1977 to increase participation of eligible lenders in ISAC's Student Loan Programs by purchasing guaranteed FFELP student loans from private lenders. Capital to support IDAPP was funded through the sale of revenue notes and bonds or borrowing from a bank with the guaranteed FFELP student loans as collateral.

As a result of the Student Aid and Fiscal Responsibility Act (SAFRA), which was part of the Health Care and Education Reconciliation Act, FFELP was terminated in 2010 and all new loan disbursements since then have been made through the federal Direct Loan Program.

Since the end of the FFELP program, there have been no new guarantees for ISAC as the guarantor and no new disbursements of loans from IDAPP. The agency is managing the wind-down of the existing portfolio both as a guarantor and a lender.

The federal Coronavirus Aid, Relief, and Economic Security (CARES) Act, passed on March 27, 2020, provides flexibility and relief for many student loan borrowers during the Coronavirus Outbreak. The CARES Act provisions, however, do not apply to the federal loans under the FFELP program which are held and managed by ISAC or other FFELP lenders or guarantors. ISAC has sought, but has not received, any comprehensive guidance from ED.

Federal regulations and audit requirements that govern ISAC-managed federal loans make it difficult for ISAC to offer any extended benefit or relief to borrowers over and beyond what is specifically allowable under the existing regulations.

Highlights of relief measures offered to borrowers due to COVID-19 is detailed below:

Guarantor of Federal Family Education Loan Program (FFELP):

Currently ISAC services the balance of its current FFELP guaranty loan portfolio of \$2.2 billion with 102,000 borrowers and a FFELP defaulted student loan portfolio of \$335 million with over 15,000 borrowers.

- All outgoing collection calls to borrowers who are not already working towards debt resolution voluntarily have been suspended.
- All new initiations of Administrative Wage Garnishment (AWG) have been stopped, and existing ones have been suspended.
- Treasury offsets have been suspended and current year offsets are being refunded.
- The eligibility time for rehabilitation of defaulted loans has been expanded from ten months to sixteen months to help borrowers complete their payments on time.
- Borrower outreach will be done to inform borrowers whose AWGs have been suspended.
- Borrower outreach will continue for those in the process of rehabilitating their loans and for customer service-related questions etc.

FFELP Lender - Illinois Designated Account Purchase Program (IDAPP):

Currently IDAPP manages a FFELP student loan portfolio of non-defaulted student loan borrowers of over \$183 million with over 11,000 borrowers.

- A 90-day Natural Disaster forbearance is offered to borrowers, if requested.
- The interest will still be accrued but will not be capitalized at the end of the forbearance.
- If the borrower is delinquent, the forbearance will also cover the delinquent period
- All late fees charged will be waived.
- Borrowers will be contacted by their preferred mode of communication to inform them of relief measures available under this if they have been impacted by Covid-19.

Private Funding:

Private Student Loan Portfolio

ISAC also manages a private student loan portfolio. The portfolio was primarily funded through a Credit Facility with Citibank. The size of the Citibank student loan portfolio is approximately \$111 million with over 7,000 borrowers.

In addition, IDAPP has a small portfolio of approximately \$10 million with almost 1,000 borrowers.

- Borrowers who call due to hardship will be granted up to 90 days of natural disaster forbearance.
- The interest will still be accrued, but will not be capitalized at the end of the forbearance.
- All negative consequences of non-payment including negative credit reporting, late fees and assignment of delinquent loans to collection agencies will be suspended.
- All outbound collection calls have been suspended for delinquent borrowers.
- No new AWGs or State offsets will be initiated and for delinquent borrowers on forbearance, existing AWGs will be suspended for the 90-day period.
- Servicers will continue to take inbound calls from borrowers for customer service-related questions and adding the above forbearance options to the priority of solutions.

State Funding:

State Funded Teacher Scholarships Converted into loans:

ISAC administered teacher programs have specific teaching requirements that must be fulfilled as a condition to receiving the financial aid. If the specific teaching requirements are not met by the student, the financial aid received converts to a loan. Recipients must repay the entire amount of the scholarship(s), plus interest. Size of the portfolio is over \$32 million with over 3,000 borrowers.

- Borrowers who call due to hardship will be granted up to 90 days of natural disaster forbearance.
- The Interest will still be accrued but will not be capitalized at the end of the forbearance.
- All outbound collection calls have been suspended for delinquent borrowers.
- All new initiations of AWGs have been stopped, and existing ones have been suspended.
- Servicers will continue to take inbound calls from borrowers for customer service-related questions and adding the above forbearance options to the priority of solutions.

Financial Impact on the Agency due to Covid-19

The primary impact of Covid-19 and the borrower relief measures that have been implemented, will be on revenues earned by ISAC as the guarantor of FFELP. The Student Loan Operating Fund (SLOF) which funds over 40% of the administrative costs of the agency primarily earns its revenues from collection activities related to the FFELP defaulted portfolio.

Collection activities on the defaulted portfolio have been suspended over the next six months. Automatic wage garnishments have also been suspended. This will decrease collection revenues significantly and more importantly, it will also result in a decrease in the pipeline for rehabilitated borrowers.

A previously defaulted borrower who qualifies for a rehabilitation does not actually receive the rehabilitation until the rehabilitated loan is sold to another lender. Also, ISAC is not paid rehabilitation revenue until the loan is sold.

Due to the volatility in the financial markets and liquidity risk, the lender market to purchase rehabilitated loans has slowed down. One of our main lenders to whom we have been selling rehabilitated loans has paused purchasing rehabilitated loans for the next quarter. Also, the market discount rate, from other lenders, for purchasing rehabilitated loans has also increased. ISAC is closely monitoring the situation and exploring other options to ensure that borrowers who are eligible and have made their required payments are rehabilitated timely.

Although IDAPP is in winddown, IDAPP is a FFELP lender and may repurchase FFELP loans from Guarantors as a part of its regular operations. As we did, during the 2009 recession when the rehabilitation market dried up, ISAC may have IDAPP purchase rehabilitated loans from ISAC as and when necessary.

Overall, this will result in significant decreases in revenues coming into SLOF. How much of a decrease is yet to be determined and will depend upon how long the current crisis lasts. The agency will monitor the decrease in revenue going forward. ISAC currently has unused capacity to draw upon State General Revenue Funds and will adjust the cost allocation to the State General Revenue Fund as necessary.

The impact of COVID-19 on IDAPP is a decrease in the cash flows collected on the underlying student loan portfolios which support the outstanding debt. The payments required on the debt is linked directly to these cash flows and will adjust downward based on the decreased cash flow. This has the effect of stretching out the time it will take to repay the outstanding debt.

AGENDA ITEM 8A

ILLINOIS DESIGNATED ACCOUNT PURCHASE PROGRAM (IDAPP) STATEMENT OF INVESTMENT POLICY REVIEW

Submitted for: Action

Summary: The Statement of Investment Policy represents the investment plan that applies to all funds held by IDAPP (IDAPP Funds), including without limitation, any proceeds of ISAC Debt, or escrowed funds held under any trust indenture or bond resolution. The Policy represents the formal document governing the investment of Fund assets and identifies a set of investment objectives, policies, authorized investments and guidelines for the investment of the assets of the Fund. The Illinois Sustainable Investing Act, which became effective on January 1, 2020, requires:

1. Every “public agency” and “governmental unit” to develop, publish and implement sustainable investment policies applicable to the management of all “public funds” under its control; and
 - The sustainable investment policy should include material, relevant, and decision-useful sustainability factors to be considered by the public agency or governmental unit as one component of its overall evaluation of investment decisions. Such factors may include but are not be limited to: (1) corporate governance and leadership factors; (2) environmental factors; (3) social capital factors; (4) human capital factors; and (5) business model and innovation factors.
 - "Public funds" means current operating funds, special funds, interest and sinking funds, and funds of any kind or character belonging to or in the custody of any public agency.
2. Every public agency to prudently integrate “sustainability factors” into its investment decision-making, investment analysis, portfolio construction, due diligence and investment ownership in order to maximize financial returns, minimize projected risks and more effectively execute its fiduciary duty.

The Illinois Sustainable Investing Act at (30 ILCS 238) is attached hereto, in its entirety, as Exhibit A.

A summary of the proposed changes is listed below, and an annotated draft copy of Statement of Investment Policy is attached hereto for reference as Exhibit B.

- Page 2, Section 3.5, add Sustainability Policy to Section 3 Objectives and Policies.

Action requested: For the Commission to approve the attached proposed revisions to the Statement of Investment Policy for the Illinois Designated Account Purchase Program (IDAPP).

EXHIBIT A

THE ILLINOIS SUSTAINABLE INVESTING ACT

FINANCE

(30 ILCS 238/) Illinois Sustainable Investing Act. (30 ILCS 238/1)

Sec. 1. Short title. This Act may be cited as the Illinois Sustainable Investing Act.

(Source: P.A. 101-473, eff. 1-1-20.)

(30 ILCS 238/5)

Sec. 5. Findings and purpose.

(a) The General Assembly finds that consideration of factors relevant to the environmental impact, social impact, and governance of investments is vital for maximizing the safety and performance of public funds. Such sustainability factors are indicative of the overall performance of an investment and are strong indicators of its long-term value. Public agencies and governments have a duty to recognize and evaluate these materially relevant factors.

(b) It is the purpose of this Act to prudently integrate sustainability factors into the investment decision-making, investment analysis, portfolio construction, due diligence, and investment ownership of public funds to maximize anticipated financial returns, minimize projected risks, more effectively execute fiduciary duties, and contribute to a more just, accountable, and sustainable State of Illinois.

(Source: P.A. 101-473, eff. 1-1-20.)

(30 ILCS 238/10)

Sec. 10. Definitions. As used in this Act:

"Financial institution" means a bank, savings bank, or credit union established under the laws of the State of Illinois, another state, or the United States of America.

"Governmental unit" has the same meaning as in the Local Government Debt Reform Act.

"Investment policy" means a written investment policy adopted by a public agency or governmental unit which addresses safety of principal, liquidity of funds, and return on investment and which requires the investment portfolio be structured in such a manner as to provide sufficient liquidity to pay obligations as they come due.

"Public agency" means the State of Illinois, the various counties, townships, cities, towns, villages, school districts, educational service regions, special road districts, public water supply districts, fire protection districts, drainage districts, levee districts, sewer districts, housing authorities, the Illinois Bank Examiners' Education Foundation, the Chicago Park District, and all other political corporations or subdivisions of the State of Illinois, now or hereafter created, whether herein specifically mentioned or not.

"Public funds" means current operating funds, special funds, interest and sinking funds, and funds of any kind or character belonging to or in the custody of any public agency.

"Sustainability factors" means factors that may have a material and relevant financial impact on the safety or performance of an investment and which are complementary to financial factors and financial accounting.

(Source: P.A. 101-473, eff. 1-1-20.)

(30 ILCS 238/15)

Sec. 15. Development of sustainable investment policies.

(a) Any public agency or governmental unit should develop, publish, and implement sustainable investment policies applicable to the management of all public funds under its control. The sustainable investment policy may be incorporated in existing investment policies developed, published, and implemented by a public agency or governmental unit.

(b) The sustainable investment policy should include material, relevant, and decision-useful sustainability factors to be considered by the public agency or governmental unit as one component of its overall evaluation of investment decisions. Such factors may include, but are not be limited to: (1) corporate governance and leadership factors; (2) environmental factors; (3) social capital factors; (4) human capital factors; and (5) business model and innovation factors.

(Source: P.A. 101-473, eff. 1-1-20.)

(30 ILCS 238/20)

Sec. 20. Consideration of sustainable investment factors in decision-making.

(a) A public agency shall prudently integrate sustainability factors into its investment decision-making, investment analysis, portfolio construction, due diligence, and investment ownership in order to maximize anticipated financial returns, minimize projected risk, and more effectively execute its fiduciary duty.

(b) Sustainability factors may include, but are not limited to, the following:

(1) Corporate governance and leadership factors, such as the independence of boards and auditors, the expertise and competence of corporate boards and executives, systemic risk management practices, executive compensation structures, transparency and reporting, leadership diversity, regulatory and legal compliance, shareholder rights, and ethical conduct.

(2) Environmental factors that may have an adverse or positive financial impact on investment performance, such as greenhouse gas emissions, air quality, energy management, water and wastewater management, waste and hazardous materials management, and ecological impacts.

(3) Social capital factors that impact relationships with key outside parties, such as customers, local communities, the public, and the government, which may impact investment performance. Social capital factors include human rights, customer welfare, customer privacy, data security, access and affordability, selling practices and product labeling, community reinvestment, and community relations.

(4) Human capital factors that recognize that the workforce is an important asset to delivering long-term value, including factors such as labor practices, responsible contractor and responsible bidder policies, employee health and safety, employee engagement, diversity and inclusion, and incentives and compensation.

(5) Business model and innovation factors that reflect an ability to plan and forecast opportunities and risks, and whether a company can create long-term shareholder value, including factors such as supply chain management, materials sourcing and efficiency, business model resilience, product design and life cycle management, and physical impacts of climate change.

(c) Sustainability factors may be analyzed in a variety of ways, including, but not limited to: (1) direct financial impacts and risks; (2) legal, regulatory, and policy impacts and risks; (3) against industry norms, best practices, and competitive drivers; and (4) stakeholder engagement.

(d) Nothing in this Act prohibits a public agency or governmental unit from integrating additional factors into its investment decision-making, investment analysis, portfolio construction, due diligence, and investment ownership of public funds. This Act shall not apply to financial institution time deposits or financial institution processing services.

ILLINOIS STUDENT ASSISTANCE COMMISSION - IDAPP STATEMENT OF INVESTMENT POLICY

1 Background

The Illinois Designated Account Purchase Program (“IDAPP”) of the Illinois Student Assistance Commission (the “Commission”) operates under the provisions of the Education Loan Purchase Program Law which is described in sections 125 through 170 of the Higher Education Student Assistance Act, 110 ILCS 947 (the “Act”). It was created to improve Illinois residents’ access to higher education by creating a secondary market for certain loans to reduce lender administrative costs, facilitate the early identification and treatment of delinquent loan accounts, and reduce potential student loan default losses to encourage commercial lenders to make student loans.

Pursuant to authority contained in section 145 of the Act, the Commission, by resolution, has the power to issue bonds (1) to make or acquire eligible loans, (2) to refund the bonds of the Commission, or (3) for a combination of such purposes. Proceeds from the sale of the bonds may be used for various purposes identified by the Act. Such purposes include (1) funding the reserves required under any bond issuance and investing them in accordance with the terms of the resolution and as the Commission from time to time may provide, in order to fulfill the stated public policy goal of encouraging student loan lending. Additional guidance and limitations with respect to the investment of funds is provided by Section 160 of the Act (Moneys of the Commission) and Section 2 (Authorized Investments) of the Public Funds Investment Act, 30 ILCS 235. Section 2.5 of the Public Funds Investment Act stipulates certain requirements for this investment policy.

2 Scope

This Investment Policy applies to all funds held by IDAPP (IDAPP Funds), including without limitation, any proceeds of ISAC Debt, or escrowed funds held under any trust indenture or bond resolution. These IDAPP Funds are accounted for in IDAPP’s assets as shown on IDAPP’s annual financial statements.

3 Objectives and Policies

The primary objectives, in priority order, of IDAPP’s investment activities shall be:

3.1 Safety

Safety of principal is the foremost objective with respect to the investment of IDAPP Funds. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital.

3.2 Liquidity

IDAPP’s investment portfolio should remain sufficiently liquid to enable the payment of all obligations as they come due.

3.3 Return

The program shall seek a modest positive return subject to safety and liquidity objectives detailed above. Performance shall be evaluated in comparison to overnight Treasury repurchase agreements.

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3.4 Simplicity and Low Cost

IDAPP's investment portfolio shall be designed to simplify administration of IDAPP's investments to minimize operational risks and administrative costs.

3.5 Sustainability Policy

This policy is designed to allow for the sufficient flexibility in the execution of sustainability investment responsibilities while executing the IDAPP Funds' investment goals.

Pursuant to the Illinois Sustainable Investing Act (30 ILCS 238), the Commission and Investment Staff shall prudently consider sustainability factors into its investment decision-making, investment analysis, portfolio construction, due diligence and investment ownership in order to maximize anticipated financial returns, minimize projected risk, and more effectively execute its fiduciary duty.

Sustainability analysis will include additional reviews of investment accounts and funds' performance on material factors likely to impact its long-term value. The analysis will also consider other relevant factors such as financial, legal and regulatory risks that contribute to an optimal risk management framework and are necessary to create long-term investment value.

4 Roles and Responsibilities of Fiduciaries

4.1 Standard of Care

All fiduciaries to IDAPP Funds shall conduct their responsibilities with the care, skill, prudence, and diligence under the circumstances then prevailing which a prudent person familiar with these matters and acting in a like capacity would use in the conduct of an activity of like character and purpose. Fiduciaries, their employees, agents, and designees shall discharge their duties with respect to IDAPP Funds solely in the interest of the beneficiaries of IDAPP.

4.2 Illinois Student Assistance Commission

In this Investment Policy, the Commission refers to the governing fiduciaries appointed as commissioners to the Illinois Student Assistance Commission by the Governor with the advice and consent of the Senate in accordance with section 15 of the Higher Education Student Assistance Act, 110 ILCS 947/15. (In this document, the agency organization will be referred to as ISAC or the Agency.) The Commission has ultimate responsibility for the success and safety of the IDAPP program. Specific responsibilities of the Commission include, but are not limited to, the following.

1. Adopting a sound investment policy. The Policy may be reviewed, modified, and adopted by action of the Commission as necessary, but shall be adopted at least every three years.
2. Monitoring and evaluating the structure and performance of IDAPP Funds with an emphasis on ensuring the risk profile is consistent with Policy objectives.

4.3 IDAPP Chief Investment Officer

ISAC's -Chief Investment Officer (CIO) will also serve as IDAPP's CIO unless otherwise specified by the ISAC Executive Director. Specific responsibilities of the CIO are as follows.

1. Investing funds in accordance with this Investment Policy.

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2. Establishing the internal controls and written procedures for the operation of the investment program for IDAPP Funds.
3. Monitoring and evaluating applicable investment guidelines.
4. Protecting IDAPP Funds against fraud, error, misrepresentation by third parties and imprudent actions by employees and IDAPP Funds agents or delegates.

4.4 ISAC Chief Financial Officer

The Chief Financial Officer of ISAC shall provide quarterly written reports of investment activities to the Executive Director and the Commission. The reports shall include information regarding securities in the portfolio by class or type, book value, income earned, and market value as of the report date.

5 Authorized Investments

Investment of IDAPP Funds is limited to those investments authorized by Section 2 of the Public Funds Investment Act, 30 ILCS 235/2, as may be further restricted by this Investment Policy. Authorized investments include the following:

5.1 Guaranteed United States Obligations

Bonds, notes, certificates of indebtedness, treasury bills or other securities now or hereafter issued, which are guaranteed by the full faith and credit of the United States of America as to principal and interest.

5.2 Non-guaranteed United States Obligations

Bonds, notes, debentures, or other similar obligations of the United States of America, its agencies, and its instrumentalities.

5.3 Savings Accounts and Certificates of Deposit

Interest-bearing savings accounts, interest-bearing certificates of deposit, or interest-bearing time deposits or any other investments constituting direct obligations of any bank as defined by the Illinois Banking Act, 205 ILCS 5/1, et seq.

5.4 Short-Term Corporate Obligations

Short term obligations of corporations organized in the United States with assets exceeding \$500,000,000 if all of the following criteria are met: (i) such obligations are rated at the time of purchase at one of the three highest classifications established by at least two SEC registered Nationally Recognized Statistical Rating Organizations (NRSRO) and which mature no later than 180 days from the date of purchase; (ii) such purchases do not exceed 10% of the corporation's outstanding obligations; and (iii) such purchases represent no more than one third (1/3) of IDAPP Funds total investment portfolio.

5.5 Money Market Mutual Funds

Money market mutual funds registered under the Investment Company Act of 1940, 15 USC 80a-1, et seq., provided that the portfolio of investments of any such money market mutual fund is limited to obligations described in 5.1 and/or 5.2 (U.S. Obligations) of this Section.

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5.6 Public Treasurers Investment Pool

A Public Treasurers' Investment Pool created under Section 17 of the State Treasurer Act, 15 ILCS 505.

5.7 Bank Funds

A fund managed, operated, and administered by a bank, subsidiary of a bank, or subsidiary of a bank holding company or use the services of such an entity to hold and invest or advise regarding the investment of any IDAPP Funds.

6 Diversification

IDAPP will diversify its investments by security type and institution. With the exception of obligations backed by the full faith and credit of the United States of America or investments fully collateralized by these obligations, no more than 5% of IDAPP's total investment portfolio shall be invested in the obligations of a single issuer.

7 Internal Controls

The Chief Financial Officer shall establish a system of internal controls, which shall be documented and shall be designed to prevent losses of IDAPP Funds arising from fraud, employee error, and misrepresentation by third parties, or imprudent actions by employees.

8 Ethics and Conflicts of Interest

The Commission and its members, employees and any other persons authorized to make or influence investment decisions must (1) comply with all obligations and requirements of ISAC's Ethics Policy, applicable provisions of the State Officials and Employees Ethics Act and all other applicable laws pertaining to ethics, prohibited acts or gift bans and (2) refrain from personal business activity that could potentially conflict with proper execution of this Investment Policy or impair their ability to make impartial decisions.

Under no circumstances shall a participant in the investment process receive any type of financial gain, either directly or indirectly, from the investment of any Program funds. Any real or perceived conflict of interest shall be reported, in writing, to the CIO and Ethics Officer, who will jointly decide the appropriate steps to be taken under the circumstances, including whether or not to notify the Commission of the actual or perceived conflict at its next scheduled meeting.

9 Authorized Financial Dealers and Institutions

IDAPP Funds may be invested with federal and state financial institutions, or any of their subsidiaries, (provided such institutions have been authorized to conduct business in the State of Illinois and have been specifically approved by ISAC to receive and hold IDAPP Funds).

Commission approval may be granted only if the selection complies with applicable state law, including, without limitation, the Public Funds Investment Act.

10 Collateralization

Collateralization will be required on cash deposits in any institution to the extent the deposit is not fully insured by the Federal Deposit Insurance Corporation or National Credit Unions Administration or other approved share insurer. In order to accommodate market changes and provide a level of security for all funds, the collateralization level will be 102% of market value of principal and accrued interest. The type of investments which may be pledged as collateral

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shall be limited to cash and any classes of securities authorized by Section 6(d) of the Public Funds Investment Act, 30 ILCS 235. Evidence of the pledge of collateral (safekeeping receipt) must be supplied to IDAPP.

11 Safekeeping and Custody

All securities transactions entered into by IDAPP shall be conducted on a delivery-versus-payment (DVP) basis.

12 Investment Policy Adoption

The IDAPP Investment Policy document was originally adopted by the Commission on November 15, 2006 and subsequently approved with revisions by the Commission on November 21, 2008, January 24, 2013, November 18, 2015, December 6, 2018, ~~and~~ April 4, 2019 and April 28, 2020.

DRAFT