

AGENDA ITEM 6.

FY2006 APPROPRIATED FUNDS BUDGET REQUEST

Submitted for: Action

Summary: The Commission submits a budget request each year to the Illinois Board of Higher Education (IBHE), indicating the amount of funding necessary to support student aid programs for which ISAC has administrative responsibility. Historically, the Commission has acted on its budget request at the September meeting. This year, however, given the uncertainty in economic projections, consideration of the request was deferred for several months to allow using updated revenue projections to provide a context for requested funding.

For FY2006, staff is recommending a budget request based on one priority: continuing support for need-based aid to promote affordability and access.

Staff recommends that the Commission approve an FY2006 budget request totaling \$668.5 million, which represents an 18.2 million increase (2.6 percent) compared to FY2005. Staff recommends seeking an increase of \$11.8 million in state General Funds in FY2006; all of this recommended increase is for the Monetary Award Program. The recommended request shifts funding for several administrative activities from state General Funds to the federal Student Loan Operating Fund (SLOF). The recommended General Funds Administrative request totals \$2.6 million, which is a reduction of \$2.0 million from the FY2005 appropriation. The recommended SLOF request totals \$67.8 million, which is nearly \$2.7 million or approximately four percent greater than the FY2005 appropriation. When all administrative funding sources are combined, the recommended increase for Administration and Outreach is \$621,900 or approximately one percent more than the FY2005 appropriation. The programmatic components of the FY2006 request are summarized below:

- \$369.3 million for need-based aid;
- \$37.3 million for special purpose state and federal scholarship and grant programs; and,
- \$257.8 million in aggregate spending authority from the Federal Student Loan Fund and the Student Loan Operating Fund.

In addition, \$875,000 in spending authority is being sought for the MAP Reserve Fund to address unforeseen, and therefore unbudgeted, increases in MAP claim rates.

Action requested: That the Commission approve an FY2006 budget request totaling \$668.5 million as detailed in Table 1.

By source of funds, this request consists of \$403.4 million in state General Funds, \$257.8 million in federal Student Loan Funds, \$875,000 from the MAP Reserve Fund, \$5.5 million in federal scholarship and grant funds, \$570,000 in other state funds, and \$400,000 in other federal funds.

ILLINOIS STUDENT ASSISTANCE COMMISSION
FY2006 APPROPRIATED FUNDS BUDGET REQUEST

Introduction

In developing the Fiscal Year 2006 budget request, staff considered a number of environmental and economic factors, which will significantly affect ISAC's programmatic and administrative funding needs. The budget request also embraces the Illinois Board of Higher Education's FY2006 budget priority of college affordability.

While economic factors point to a slightly improving Illinois economy, forecasts seem to suggest that difficult economic times will continue to overshadow the state's budget for FY2006. The Illinois Economic and Fiscal Commission (IEFC) recently reported an expected four percent growth in the revenue base for FY2006. However, when all other factors are considered, net revenue growth is anticipated to be only \$325 million. A number of non-education funding issues such as pension obligations, group insurance increases, and human services programs will continue to require the State's fiscal attention in FY2006. It is, therefore, unlikely that the growth in state revenue will be sufficient to meet the needs of Illinois higher education. In fact, the stark reality is that little, if any, new funding can be anticipated to address growing higher education programmatic needs.

Given the current economic outlook, this agenda item addresses one programmatic priority for the FY2006 budget request: continuing support for need-based aid to promote affordability and access.

In terms of administrative initiatives, staff is recommending that ISAC once again reduce its GRF administrative funding request for FY2006. This flexibility is provided to the agency via current federal legislation governing the administration of the agency's Student Loan Operating Fund (SLOF). The next federal Reauthorization of the Higher Education Act is scheduled to occur in calendar year 2005. Staff will closely monitor this legislation as it advances as changes to the student loan programs and the guaranty agency financial structure may be necessary in state fiscal year 2006 and beyond.

The following agenda item presents the FY2006 Appropriated Funds Budget Request in five separate sections: I) Need-Based Grant Programs; II) Special Purpose Programs; III) Administrative Support and Outreach; IV) Federal Student Loan Fund Expenditures; and, V) Other Federal Funds activities.

The following table -- Table 1 -- provides a summary of the FY2006 recommended budget request, and compares the recommended request to FY2005 appropriations.

TABLE 1 - UPDATED 01/24/05

**ILLINOIS STUDENT ASSISTANCE COMMISSION
STATE FISCAL YEAR 2006 BUDGET REQUEST**

| | FY2005 APPROPRIATION | FY2006 COMMISSION ACTION | FY2005 -- FY2006 DOLLARS | CHANGE PERCENT |
|--|-------------------------|--------------------------------|-----------------------------|-------------------|
| NEED-BASED GRANTS | \$346,919,800 | \$369,319,800 | \$22,400,000 | 6.5% |
| Monetary Award Program (MAP) | 338,699,800 | 361,099,800 | 22,400,000 | 6.6 |
| State General Funds | 338,699,800 | 357,399,800 | 18,700,000 | 5.5 |
| Allocated MAP Reserve Funds | 0 | 0 | 0 | 0.0 |
| Federal LEAP/SLEAP Funds | 0 | 3,700,000 | 3,700,000 | 100.0 |
| Silas Purnell Illinois Incentive for Access (IIA) Grants | 7,200,000 | 7,200,000 | 0 | 0.0 |
| Student to Student Grants | 950,000 | 950,000 | 0 | 0.0 |
| Higher Education License Plate (HELP) Grants | 70,000 | 70,000 | 0 | 0.0 |
| SPECIAL PURPOSE GRANT PROGRAMS | \$42,130,000 | \$37,260,000 | (\$4,990,000) | (11.8%) |
| State General Funds | 40,200,000 | 35,330,000 | (4,870,000) | (12.1) |
| Illinois Future Teacher Corps Scholarships * | 4,160,000 | 4,160,000 | 0 | 0.0 |
| Minority Teacher Scholarships | 3,100,000 | 3,100,000 | 0 | 0.0 |
| Teacher/Child Care Provider Loan Repayment | 500,000 | 500,000 | 0 | 0.0 |
| Illinois Scholars Program | 3,020,000 | 2,900,000 | (120,000) | (4.0) |
| Dependents Grant Programs | 350,000 | 350,000 | 0 | 0.0 |
| Illinois Veteran Grants** | 19,250,000 | 19,250,000 | 0 | 0.0 |
| National Guard Grants*** | 4,500,000 | 4,500,000 | 0 | 0.0 |
| Merit Recognition Scholarships | 5,400,000 | 0 | (5,400,000) | (100.0) |
| Optometric Education Scholarship Program | 50,000 | 50,000 | 0 | 0.0 |
| Bonus Incentive Grants | 0 | 650,000 | 650,000 | 100.0 |
| Federal Robert C. Byrd Scholarships | 1,800,000 | 1,800,000 | 0 | 0.0 |
| MAP RESERVE FUND (UNALLOCATED) | \$875,000 | \$875,000 | \$0 | 0.0% |
| ADMINISTRATION AND OUTREACH | \$4,921,000 | \$370,000 | (\$4,551,000) | (92.5%) |
| General Revenue Fund | 4,551,000 | 0 | (4,551,000) | (100.0) |
| State Accounts Receivable Fund | 300,000 | 300,000 | 0 | 0.0 |
| Contracts and Grants Fund | 70,000 | 70,000 | 0 | 0.0 |
| FEDERAL STUDENT LOAN PROGRAM | \$255,146,600 | \$260,419,100 | \$5,272,500 | 2.1% |
| Student Loan Fund Operating Expenses | 36,146,600 | 44,084,700 | 7,938,100 | 22.0 |
| Federal Loan Systems Development & Maintenance | 5,000,000 | 5,000,000 | 0 | 0.0 |
| Lender Reimbursements | 160,000,000 | 156,000,000 | (4,000,000) | (2.5) |
| Return of FSLF Reserves to U.S. Treasury | 0 | 4,000,000 | 4,000,000 | 100.0 |
| Collections Payments to SLOF | 25,000,000 | 25,000,000 | 0 | 0.0 |
| Default Aversion Fee | 5,000,000 | 5,000,000 | 0 | 0.0 |
| Default Aversion Fee Reversals | 2,000,000 | 2,000,000 | 0 | 0.0 |
| SLOF Outside Collection Agency Activities | 22,000,000 | 19,334,400 | (2,665,600) | (12.1) |
| OTHER FEDERAL FUNDS | | | | |
| Return of Paul Douglas Collections to ED | 400,000 | 400,000 | 0 | 0.0 |
| GRAND TOTAL, ALL PROGRAMS | \$650,392,400 | \$668,643,900 | \$18,251,500 | 2.8% |
| State General Funds | \$391,600,800 | \$400,879,800 | \$9,279,000 | 2.4% |
| General Revenue Fund | 391,600,800 | 400,879,800 | 9,279,000 | 2.4 |
| Education Assistance Fund | 0 | 0 | 0 | 0.0 |
| Other Funds | | | | |
| Federal S&G Program Funds | 1,800,000 | 5,500,000 | 3,700,000 | 205.6 |
| Federal Student Loan Funds | 255,146,600 | 260,419,100 | 5,272,500 | 2.1 |
| MAP Reserve Fund | 875,000 | 875,000 | 0 | 0.0 |
| Other Federal Funds | 400,000 | 400,000 | 0 | 0.0 |
| Other State Funds | 570,000 | 570,000 | 0 | 0.0 |

*\$60,000 in appropriation authority for this program is from the Future Teacher Corps Scholarship Fund.

**\$20,000 in FY2006 appropriation authority for this program would be from the National Guard Grant Fund.

***\$20,000 in FY2005 appropriation authority for this program is from the National Guard Grant Fund.

I. Need-Based Grant Programs

The Commission is responsible for administering four need-based grant programs, the Monetary Award Program (MAP), the Silas Purnell Illinois Incentive for Access (IIA) Grant Program, the Student to Student (STS) Program of Matching Grants, and the Higher Education License Plate (HELP) Grant Program. FY2002 through FY2005 appropriation levels, as well as staff's recommendations for the FY2006 budget request, are summarized in Table 2.

Table 2: Need-Based Scholarship and Grant Programs FY2002 through FY2005 Appropriations and ISAC Staff Recommended FY2006 Budget Request

| NEED-BASED GRANT PROGRAMS | FY2002 | FY2003 | FY2004 | FY2005 | RECOMMENDED FY2006 REQUEST |
|---|----------------------|----------------------|----------------------|----------------------|-------------------------------|
| Monetary Award Program (MAP) | \$375,628,300 | \$333,222,800 | \$338,699,800 | \$338,699,800 | \$361,974,800 |
| Silas Purnell Illinois Incentive for Access (IIA) | 7,200,000 | 7,200,000 | 7,200,000 | 7,200,000 | 7,200,000 |
| Student to Student (STS) | 1,000,000 | 950,000 | 950,000 | 950,000 | 950,000 |
| Higher Education License Plate (HELP) | 70,000 | 70,000 | 70,000 | 70,000 | 70,000 |
| Total | \$383,898,300 | \$341,442,800 | \$346,919,800 | \$346,919,800 | \$369,319,800 |

This table shows that the overall recommended FY2006 budget request for ISAC's need-based scholarship and grant programs is \$369.3 million. This represents an increase of \$22.4 million, or 6.5 percent over FY2005 funding levels, but less than FY2002 levels. The remainder of this section discusses each need-based program.

Monetary Award Program

Most state programs sustained large cuts in FY2003, and MAP was no exception. The final FY2003 appropriation totaled \$333.2 million, a reduction of more than \$38.0 million from the FY2002 appropriation. Included within this reduction was the elimination of \$20.0 million for awards to students who have already used MAP to pay for the equivalent of 8 semesters or 12 quarters of full-time enrollment, i.e., fifth-year recipients. In FY2004, \$6.0 million was added to help restore eligibility for fifth-year students. As a result, the FY2004 MAP appropriation totaled \$338.7 million where it remained in FY2005.

ISAC did not qualify for approximately \$3.7 million in federal Leveraging Educational Assistance Partnership (LEAP) and Special Leveraging Educational Assistance Partnership (SLEAP) funds for the 2003-04 or 2004-05 school year. Increasing matches in state appropriations is the main requirement for these funds, and Illinois became ineligible due to the \$38.0 million reduction in the MAP appropriation in FY2003 and relatively stable funding in FY2004 and FY2005. Unless new State funding of at least \$8.0 million is provided for MAP in the FY2006 budget cycle, LEAP/SLEAP money will not be forthcoming for the 2005-06 award year either.

Regaining College Affordability

The final FY2005 recompute formula recognized college costs based on FY2003 tuition and fee figures assessed at 95 percent and further reduced all MAP grants by at least ten percent. For the third consecutive year, actual tuition and fees were not covered for any student at any institution. Award announcements were suspended in mid-August and after the reduction factor, the actual paid maximum award will be equivalent to that of FY1999.

Tuition and Fees

The Commission has not received funding to cover tuition and fee increases in MAP since FY2002. In FY2003, the Commission calculated awards using 2001-02 tuition and fee figures. This meant that no matter how needy a student was determined to be, awards were not calculated based upon actual costs and no student received full tuition and fees. In FY2004, due to internal reallocations, the Commission was able to incorporate 2002-03 tuition and fees but only at 95 percent of their value. The Commission continued to use 95 percent of 2002-03 tuition and fees to calculate MAP eligibility in FY2005. The costs of recognizing 100 percent, rather than 95 percent, of 2002-03 tuition and fees is projected at \$8.4 million.

Overall, the 2003-04 weighted-mean tuition and fees increased 5.7 percent to total \$6,964 for all institutions. By sector, weighted-mean tuition and fees totaled \$17,077 at private and proprietary institutions representing an increase of 5.4 percent over the previous year. Tuition and fee amounts increased 5.7 percent to \$1,830 at community colleges and increased 9.2 percent to \$5,298 at public universities. The projected cost of incorporating 2003-04 tuition and fees over the 2002-03 costs is \$16.4 million.

The weighted-mean increase in 2004-05 tuition and fees ranged from 6.3 percent at private and proprietary institutions to 13.0 percent at public universities for an overall average of 9.2 percent. The projected cost of incorporating 2004-05 tuition and fees over 2003-04 costs is \$15.2 million. The total cost of incorporating 2004-05 tuition and fees into the MAP formula in place of the 2002-03 amounts is projected to be \$40.0 million.

Reduction Factors

In response to an increase in application volume in FY2003, the Commission opted to reduce the amount of all MAP grants by five percent in order to continue to announce awards to mid-August. The Commission increased the reduction factor to ten percent in FY2004 in response to an eight percent increase in application volume. This allowed the Commission to continue to announce awards into early August. The FY2005 recompute formula maintained the ten percent award reduction factor for students with a Federal Expected Family Contribution (EFC) under \$3,000 but increased the reduction factor to eleven percent for those students with EFCs over \$3,000. All students from all types of institutions would benefit from the removal of this reduction factor. The cost to remove the ten / eleven percent reduction factors is projected to be \$44.5 million.

Application Volume

Announced application volume, or applications from Illinois residents attending MAP-approved institutions, has increased significantly over the last several years. Year-end application volume rose by 7.2 percent in FY2002, 6.1 percent in FY2003, and 6.7 percent in FY2004. Over the past several weeks, FY2005 application volume has been between three and four percent over the same points last year. Most of the increase is attributed to the state's current economic condition and the resulting loss of employment opportunities. During economic downturns, many individuals pursue education and training as a means to enhance their employability.

The continued increase in applications has forced the Commission to reduce award amounts as well as suspend award announcements in early to mid-August over the past several years. For FY2006, staff projects overall application volume to continue to increase at a similar rate as experienced this year, approximately three to four percent. The projected cost to cover a four percent application volume increase in FY2006 and suspend award announcements at a similar date as in FY2005 is \$14.0 million.

MAP Reserve Fund

In 1995, legislation was enacted to create a MAP Reserve Fund in the State Treasury. By statute, the amount in the Reserve Fund cannot exceed two percent of the annual state appropriation for MAP. The purpose of the MAP Reserve Fund is to provide ISAC with additional management flexibility in administering the MAP Program by providing a means to address contingencies. At the end of FY2004, the fund balance totaled \$875,000.

Staff recommends that the Commission seek \$875,000 in spending authority for FY2006. Staff also recommends that the Commission authorize staff to seek authority to transfer up to two percent of the MAP appropriation into the Reserve Fund in FY2006. In the event that economic conditions improve during FY2006 and regular MAP funding remains unexpended at the end of the year, funding could be then transferred to the Reserve Fund to address contingencies in future fiscal years.

Staff Recommendations for MAP

The estimated cost of incorporating all of the formula changes described above is approximately \$150 million. Considering the erosion of college affordability and the decline in the portion of tuition and fees covered by MAP, it would be ideal to address all of these formula improvements. However, with the State's current economic outlook and limited available funds, staff is recommending the Commission request \$22.4 million in additional MAP funding in FY2006. More specifically, staff recommends that the Commission request:

- \$8.4 million to incorporate 2003 tuition and fees at 100 percent; and,
- \$14.0 million to address application volume increases.

By funding source, \$18.7 million of this additional funding would be GRF funding and \$3.7 million would be LEAP/SLEAP funding received from the federal government.

Other Need-Based Programs

Silas Purnell Illinois Incentive for Access (IIA) Program

In FY1997, the Commission first received funding for a new initiative designed to direct additional grant aid to students classified as freshmen with no family resources to pay for college. The purpose of the Illinois Incentive for Access (IIA) Grant Program was to promote access and retention for a targeted group of students. IIA is a need-based grant program, which provides a one-time \$500 award to freshmen applicants who have no financial resources for college, i.e., a zero EFC. The program was intended to supplement, rather than supplant, funding for existing need-based grant programs for this group of students, much like the federal Student Educational Opportunity Grant Program supplements the federal Pell Grant Program.

Effective July 1, 2004, the Illinois Incentive for Access Grant Program was renamed the Silas Purnell Illinois Incentive for Access Grant Program. The award amounts were increased from \$500 up to \$1,000 for freshman college students who have a \$0 EFC, and the program was expanded to allow grants of up to \$500 to be given to freshmen with an EFC between \$1 and \$500, contingent upon adequate funding. To fully fund the program, it is projected that approximately \$18 million would be needed for zero EFC freshmen applicants and \$5 million for \$1 to \$500 EFC applicants for a total of \$23 million. Due to the State's current financial situation, staff is recommending that the Commission choose to secure additional funding for MAP as its first priority and request level funding, \$7.2 million, for IIA in FY2006.

Student to Student (STS) Program of Matching Grants

The Student to Student (STS) Program of Matching Grants provides matching funds for need-based grant assistance to students who attend participating public universities and community colleges. Students at participating institutions pay a voluntary fee and the total of the collected funds is matched by the State to provide grants of up to \$1,000 to financially needy students. The \$1,000 maximum grant is limited by statute, and the maximum fee which institutions can charge is limited by ISAC Rules. Public institutions are required to receive approval via a student referendum before increasing mandatory fees.

In FY2004, ISAC fully utilized its appropriation and provided matching funds for awards to about 3,000 students. Paying full STS claims received from institutions would have exceeded available funding, and thus, claims were prorated. The funding which would have been required to fully pay all claims for FY2004 is estimated at \$1.17 million, suggesting FY2005 claims will exceed the FY2005 appropriation of \$950,000.

Full funding for STS for FY2006 is estimated at \$1.2 million. Given limited state funding, the recommended FY2006 request for STS is \$950,000.

Higher Education License Plate Grant Program

Working through the Secretary of State, participating public universities, community colleges, and not-for-profit private colleges and universities in Illinois can have specialized collegiate license plates issued for their schools. ISAC annually seeks spending authority to disburse funds collected from the sales of these plates to the participating private schools. According to the Secretary of State's Office, calendar year 2003 sales generated \$51,650 in scholarship funds for distribution in academic year 2005.

Final calendar year 2004 sales figures are not yet available, but year-to-date sales are only slightly higher than sales in 2003. Thus, the recommended FY2006 budget request of \$70,000 in spending authority is projected to be sufficient to cover any increase in license plate sales.

II. Special Purpose Scholarship and Grant Programs

For FY2006, the Commission will administer funds for eleven special purpose scholarship and grant programs. This section of the budget request presents the recommended FY2006 budget request for each of the current programs. In recognition of the need to identify and prioritize ISAC program funding and spending authority requirements, staff recommends the FY2006 budget request for special purpose scholarship and grant programs include funding in the following priority order:

- 1) **Entitlement Programs and State Obligations.** Entitlement programs include the Dependents Grant Programs, the Illinois Veteran Grant (IVG) Program, and the Illinois National Guard (ING) Grant Program. The Bonus Inventive Grant (BIG) program is not an entitlement by law because awards are subject to appropriation by the General Assembly, but the program has been identified as a state obligation to purchasers of college savings bonds.
- 2) **Teacher Assistance.** Teacher assistance programs include the Illinois Future Teacher Corps (IFTTC) Scholarship Program, the Minority Teachers of Illinois (MTI) Scholarship Program, the Illinois Scholars Program, and the Teacher/Child Care Provider Loan Repayment Program. The Special Education Teacher Tuition Waiver (SETTW) Program, administered by ISAC, waives tuition incurred by recipients at public universities, and no appropriation is needed for this program.
- 3) **Merit Programs and Targeted Aid.** Merit and achievement programs making monetary awards include the Merit Recognition Scholarship (MRS) Program and the federally funded Robert C. Byrd

Honors Scholarship Program. The Optometric Education Scholarship Program targets graduate optometry students and is funded from the Optometric Licensing and Disciplinary Board Fund.

As shown in Table 3, the overall recommended FY2006 budget request for ISAC's special purpose scholarship and grant programs is \$37.26 million, which represents a decrease of \$4.67 million, or 11.6 percent, from the FY2005 appropriation. The largest recommended increase in funds is \$650,000 to restore funding for the BIG program. The largest decrease is a recommended \$5.4 million reduction in MRS funding. Following Table 3, a discussion of each program is provided. The program discussions are presented and grouped according to recommended funding priority.

**Table 3: ISAC Special Purpose Scholarship and Grant Programs
FY2004 and FY2005 Appropriations, Recommended FY2006 Request**

| Special Purpose Scholarship and Grant Programs | FY2004 Appropriation | FY2005 Appropriation | FY2006 Recommended Request |
|---|---------------------------------|---------------------------------|---|
| Entitlement Programs and Obligations | | | |
| Dependents Grant Programs | \$275,000 | \$350,000 | \$350,000 |
| Illinois Veteran Grant | 19,250,000 | 19,250,000 | 19,250,000 |
| National Guard Grant | 4,500,000 | 4,500,000 | 4,500,000 |
| Bonus Incentive Grant | 650,000 | 0 | 650,000 |
| Teacher Assistance Programs | | | |
| Illinois Future Teacher Corps Scholarship | 7,050,000 | 4,160,000 | 4,160,000 |
| Minority Teachers of Illinois Scholarship | 3,100,000 | 3,100,000 | 3,100,000 |
| Illinois Scholars | 3,514,300 | 3,020,000 | 2,900,000 |
| Teacher/Child Care Provider Loan Repayment | 2,700,000 | 500,000 | 500,000 |
| Merit Programs and Targeted Aid | | | |
| Merit Recognition Scholarship | 5,400,000 | 5,400,000 | 0 |
| Robert C. Byrd Honors Scholarship (Federal) | 1,800,000 | 1,800,000 | 1,800,000 |
| Optometric Education Scholarship | 50,000 | 50,000 | 50,000 |
| TOTAL | \$48,289,300 | \$42,130,000 | \$37,260,000 |
| Sub-Total General Revenue Fund | \$46,389,300 | \$40,200,000 | \$35,330,000 |
| Sub-Total Federal Funds | \$1,800,000 | \$1,800,000 | \$1,800,000 |
| Sub-Total Other State Funds | \$100,000 | \$130,000 | \$130,000 |

Entitlement Programs and Obligations

Illinois Veteran Grant (IVG) Program

The Illinois Veteran Grant (IVG) Program provides grants for qualified veterans at Illinois public universities and community colleges. Because the IVG Program is an entitlement program, public institutions are required to cover any funding shortfalls which occur at their campuses by waiving the portion of a student's tuition and fees not paid by the grant. In FY2004, 11,800 veterans received more than \$19.2 million in assistance; however, claims by institutions were prorated and could not be paid fully. The funding which would have been required to fully pay all claims for FY2004 is estimated at \$23.7 million. Based on FY2004 claim levels, ISAC expects to fully utilize the FY2005 appropriation of \$19.25 million. With limited state funding, the recommended FY2006 IVG request is for level funding of \$19.25 million.

Illinois National Guard (ING) Grant Program

The Illinois National Guard (ING) Grant Program provides grants for qualified members of the Illinois National Guard at Illinois public universities and community colleges. Because the ING Grant Program is an entitlement program, public institutions are required to cover any funding shortfalls which occur at their campuses by waiving the portion of a student's tuition and fees not paid by the grant. For FY2004, ING provided 2,000 students with assistance totaling approximately \$4.5 million. The FY2005 appropriation represents level funding from FY2004 and should be fully expended. The recommended FY2006 request of \$4.5 million continues level funding and does not allow for tuition and fee increases for FY2005 or FY2006.

Dependents Grant Programs

The Dependents Grant Programs include the Grant Program for Dependents of Police or Fire Officers and the Grant Program for Dependents of Correctional Officers. Although these programs are not entitlement programs, the state has historically attempted to fully fund them because they provide grant assistance to the spouse and children of Illinois police officers, fire officers, or correctional officers killed or permanently disabled in the line of duty. In FY2004, ISAC made awards to 74 students totaling approximately \$270,000. The funding which would have been required to fully pay all claims for FY2004 is estimated at \$330,000, suggesting the FY2005 appropriation of \$350,000 will be fully expended. The recommended FY2006 request of \$350,000 represents level funding. Because usage for these programs is difficult to predict, staff will continue to monitor FY2005 claims to determine what additional funding may be needed to fully fund these programs in FY2006.

College Savings Bond Bonus Incentive Grant (BIG) Program

The Baccalaureate Savings Act allows for supplemental grants under the College Savings Bond Bonus Incentive Grant (BIG) Program, subject to annual appropriation by the General Assembly, to holders of Illinois College Savings Bonds who use their bond proceeds to pay for educational expenses at an Illinois college or university. The FY2004 appropriation of \$650,000 was fully expended to provide 1,252 awards. The funding which would have been required to fully pay all claims for FY2004 is estimated at \$753,000. Given the State's financial difficulties, and important needs in other ISAC programs, the FY2005 appropriation for BIG was \$0. It is estimated that \$910,000 would be required to fully fund the program in FY2006. The recommended FY2006 request of \$650,000 restores funding for the program at the FY2004 funding level.

Teacher Assistance Programs

Illinois Future Teacher Corps (IFTC) Scholarship Program

The Illinois Future Teacher Corps (IFTC) Scholarship Program encourages academically-talented, financially needy students to pursue preschool, elementary, and secondary school teaching in Illinois. IFTC uses differential award amounts to encourage students to teach in disciplines which have been designated as teacher shortage areas and to teach in schools that have been designated as hard-to-staff. By statute, IFTC recipients may receive up to \$5,000 for agreeing to pursue a teaching degree and teach in Illinois for five years. They may receive up to \$10,000 for agreeing to pursue a teaching degree and teach in a subject shortage discipline or agreeing to teach in a hard-to-staff school for five years. Finally, recipients may receive up to \$15,000 if they agree to pursue a teaching degree, teach in a subject shortage discipline, and teach at a hard-to-staff school for five years. IFTC eligibility is limited to students at or above the junior level, and recipients who do not fulfill their five year commitment are required to repay any assistance received.

As per guidance from the Governor's office, ISAC limited the amount of scholarships awarded to students in FY2004 to \$5,000 scholarships to students pursuing degrees in a subject shortage discipline and \$10,000 scholarships to students pursuing degrees in a subject shortage discipline who also agree to teach for five years in a hard-to-staff school. 1,530 awards were provided in FY2004. For FY2005, staff anticipates providing renewal awards to approximately 260 recipients and new awards to approximately 310 students. Staff expects to provide about 250 \$10,000 awards and about 320 \$5,000 awards. Full funding for the limited \$10,000 and \$5,000 award schedule for FY2006 is estimated at \$9.9 million.

Given state budget limitations, staff recommends that the Commission request level funding of \$4.16 million for IFTC in FY2006, which would allow for about 570 awards, is recommended.

Minority Teachers of Illinois (MTI) Scholarship Program

The Minority Teachers of Illinois (MTI) Scholarship Program annually awards scholarships of up to \$5,000 to minority students who agree to teach at least one year for each year of scholarship assistance at a preschool, elementary, or secondary school where at least 30 percent of the students are minority. In FY2004, 631 students received assistance totaling nearly \$3 million. As the need for qualified teachers increases, funding teacher scholarship programs will remain a high priority for the State. ISAC expects to fully utilize the FY2005 appropriation. The recommended FY2006 level funding request of \$3.1 million would provide for 620 scholarships.

Illinois Scholars Program

ISAC first received funding for the Illinois Scholars line item in FY2004, totaling \$3.514 million for the Golden Apple Foundation. The Golden Apple Foundation recruits students into teaching careers, particularly in urban areas, and provides scholarships as well as mentoring and support services and the opportunity to attend summer institutes on teaching. Students are nominated in their junior year of high school or their sophomore year of college. One hundred new students are selected each year for an award from a pool of 1,200 nominees. Awards are for \$5,000 per year for up to four years and must be repaid if a teaching commitment is not fulfilled.

In FY2005, ISAC received \$2.9 million on behalf of the Golden Apple Foundation, in addition to a first-time appropriation of \$120,000 for the Academy for Urban School Leadership. The recommended request of \$2.9 million would provide level funding to the Golden Apple Foundation.

Teacher/Child Care Provider Loan Repayment Program

In January 2003, ISAC began providing matching grants of up to \$5,000 to teachers who have fulfilled the teaching obligations of the federal Teacher Loan Forgiveness Program and to child care providers who have fulfilled the obligations of the federal Child Care Provider Loan Forgiveness Program in Illinois. To be eligible for the federal programs, teachers must teach full time in a low-income school for five consecutive years and early childcare professionals must work full time in a childcare facility that serves a low-income community for two consecutive years. Recipients of loan forgiveness under these federal programs may be eligible to receive a matching grant from the State. Statute permits ISAC to utilize up to five percent of an appropriation to help fund administrative costs and outreach activities for teacher incentive programs, but staff is recommending that no funding from this appropriation be used to pay administrative costs in FY06. The recommended FY2006 request of \$500,000 would allow for 100 awards and should be sufficient to meet expected program demand.

Merit Programs and Targeted Aid

Merit Recognition Scholarship (MRS) Program

The Merit Recognition Scholarship (MRS) Program rewards the academic achievement of Illinois high school graduates by providing monetary awards to students who, at the end of their sixth semester in high school, are in the top five percent of their high school class or have a score on the ACT Assessment or the SAT I: Reasoning Test at or above the 95th percentile. In FY2004, 4,491 students representing the top 3.5 percent of their class received scholarships totaling \$4.4 million. Based on the FY2005 appropriation of \$5.4 million, ISAC announced MRS awards for the top 4 percent of the high school graduating class of 2004. It is projected that \$6.0 million would have been needed to fund all students in the top 5 percent. Due to limitations in available state funding and the need to prioritize expenditures, staff recommends that no funding be requested for MRS in FY2006.

Federal Robert C. Byrd Honors Scholarship Program

The federally-funded Robert C. Byrd Honors Scholarship Program provides scholarships to academically-exceptional Illinois high school graduates for undergraduate study at approved U.S. colleges and universities. Scholarships are allocated by geographic district to students who graduate in the top two percent of their high school class, based on academic performance and test scores. In FY2004, ISAC made 1,082 awards totaling about \$1.6 million. ISAC received a federal allocation of about \$1.7 million for the program in FY2005 and again anticipates making awards to approximately 1,100 students. The recommended FY2006 budget request of \$1.8 million assumes a continued full federal allocation and allows sufficient authority to handle funds carried over between federal fiscal years.

Optometric Education Scholarship Program

Created by Public Act 92-0569, the Optometric Education Scholarship Program provides up to ten scholarships annually for students pursuing a graduate optometry degree at a qualified Illinois institution. The scholarship is funded from Optometric Licensing and Disciplinary Board fees that are deposited into a special state fund. ISAC annually seeks spending authority to disburse these funds to qualified students. Scholarship recipients are required to practice optometry in Illinois one year for each year of assistance received. The recommended FY2006 request of \$50,000 in spending authority would allow for ten scholarships.

III. Administrative Support and Outreach

Introduction

Each year, ISAC receives a state General Funds appropriation to help pay operating expenses associated with the programs the agency administers. ISAC also derives funding for its federal student loan operations from non-state funding sources. Expenditures of such non-state funds are authorized by the General Assembly through the annual appropriations process in the same manner as state-funded operations and programs. All revenues and expenditures associated with the administration of the Federal Family Education Loan (FFEL) Program are accounted for in the Federal Student Loan Fund (FSLF) and the Student Loan Operating Fund (SLOF).

To administer the FFEL Program, ISAC requires an appropriation, or state spending authority, from both of the funds (FSLF and SLOF) to pay programmatic and operating expenses, as well as make interfund transfers and payments to the U.S. Department of Education. This section of the agenda item itemizes staff's

recommendation for the FY2006 budget request related to administrative expenses paid using either state funds or federal funds. The programmatic request for federal programs is discussed in sections IV and V.

Table 4 shows the total administrative funding in the recommended request without respect to funding source, and shows that staff is recommending an increase of less than one percent to the overall appropriated funds administrative budget in FY2006. A more detailed description of the proposed changes is provided following these two tables.

The proposed changes from the FY2005 appropriation to the recommended FY2006 request are summarized by funding source in Table 5. As shown in this table, staff is recommending that ISAC once again reduce its GRF administrative funding request for FY2006 and shift \$2.0 million in administrative costs to SLOF. This flexibility is provided to the agency via current federal statute governing the administration of the agency's Student Loan Operating Fund (SLOF).

It should be noted that the development of internal operating budgets and unforeseen federal requirements may result in slight adjustments to the line item configuration shown for GRF and SLOF in Table 5. The total request, as approved by the Commission, however, will not change.

Table 4: Total Administration and Outreach

| | FY2005 Appropriation | FY2006 Request | CHANGE FY2005 – FY2006 | |
|--|-------------------------|---------------------|------------------------|--------------|
| | | | DOLLAR | PERCENT |
| <i>Line Item Budgets</i> | | | | |
| Personal Services | \$17,188,200 | \$17,617,700 | \$429,500 | 2.5% |
| Employee Retirement | 456,000 | - | -456,000 | -100.0% |
| State Retirement | 2,768,300 | 3,819,000 | 1,050,700 | 38.0% |
| Social Security | 1,315,000 | 1,348,000 | 33,000 | 2.5% |
| Group Insurance | 3,603,100 | 4,833,400 | 1,230,300 | 34.1% |
| Contractual Services | 11,666,900 | 12,666,900 | 1,000,000 | 8.6% |
| Travel | 216,400 | 216,400 | 0 | 0.0% |
| Commodities | 272,800 | 272,800 | 0 | 0.0% |
| Printing | 727,000 | 727,000 | 0 | 0.0% |
| Equipment | 539,000 | 539,000 | 0 | 0.0% |
| Telecommunications | 1,907,000 | 1,907,000 | 0 | 0.0% |
| Operation of Auto | 37,900 | 37,900 | 0 | 0.0% |
| Sub-Total Line Item Budgets | \$40,697,600 | \$43,985,100 | \$3,287,500 | 8.1% |
| <i>Other Administrative Appropriations</i> | | | | |
| Federal Systems Maintenance & Development | 5,000,000 | 5,000,000 | 0 | 0.0% |
| Payments to Outside Collection Agencies | 22,000,000 | 19,334,400 | -2,665,600 | -12.1% |
| Default Aversion Fee Reversals | 2,000,000 | 2,000,000 | 0 | 0.0% |
| Sub-Total Other Administrative Appropriations | \$29,000,000 | \$26,334,400 | -\$2,665,600 | -9.2% |
| <i>Other Funds</i> | | | | |
| State Accounts Receivable Fund | 300,000 | 300,000 | 0 | 0.0% |
| State Contracts and Grants Fund | 70,000 | 70,000 | 0 | 0.0% |
| Sub-Total Other State Funds | \$370,000 | \$370,000 | 0 | 0.0% |
| TOTAL | \$70,067,600 | \$70,689,500 | \$621,900 | 0.9% |

Table 5: Administration and Outreach - Summary by Fund

| | FY2005 Appropriation | | FY2006 Request | | Dollar Change FY2005 – FY2006 | | Percent Change FY2005 – FY2006 | |
|--|-------------------------|---------------------|--------------------|---------------------|----------------------------------|---------------------|-----------------------------------|--------------|
| | GRF | SLOF | GRF | SLOF | GRF | SLOF | GRF | SLOF |
| <i>Line Item Budgets</i> | | | | | | | | |
| Personal Services | \$1,988,000 | \$15,200,200 | \$355,700 | \$17,262,000 | -\$1,632,300 | \$2,061,800 | -81.3% | 13.6% |
| Employee Retirement | - | 456,000 | - | - | - | -456,000 | - | -100.0% |
| State Retirement | 320,200 | 2,448,100 | 77,100 | 3,741,900 | -243,100 | 1,293,800 | -75.9% | 52.8% |
| Social Security | 152,000 | 1,163,000 | 27,300 | 1,320,700 | -124,700 | 157,700 | -82.0% | 13.6% |
| Group Insurance | - | 3,603,100 | - | 4,833,400 | - | 1,230,300 | - | 34.1% |
| Contractual Services | 1,802,600 | 9,864,300 | 1,802,600 | 10,864,300 | 0 | 1,000,000 | 0.0% | 10.1% |
| Travel | 26,400 | 190,000 | 26,400 | 190,000 | 0 | 0 | 0.0% | 0.0% |
| Commodities | 32,800 | 240,000 | 32,800 | 240,000 | 0 | 0 | 0.0% | 0.0% |
| Printing | 100,000 | 627,000 | 100,000 | 627,000 | 0 | 0 | 0.0% | 0.0% |
| Equipment | 10,000 | 529,000 | 10,000 | 529,000 | 0 | 0 | 0.0% | 0.0% |
| Telecommunications | 113,500 | 1,793,500 | 113,500 | 1,793,500 | 0 | 0 | 0.0% | 0.0% |
| Operation of Auto | 5,500 | 32,400 | 5,500 | 32,400 | 0 | 0 | 0.0% | 0.0% |
| Sub-Total Line Item Budgets | \$4,551,000 | \$36,146,600 | \$2,550,900 | \$41,434,200 | -\$2,000,100 | \$5,287,600 | -43.9% | 14.6% |
| <i>Other Administrative Appropriations</i> | | | | | | | | |
| Federal Systems Maintenance & Development | - | 5,000,000 | - | 5,000,000 | - | 0 | - | 0.0% |
| Payment to Outside Collection Agencies | - | 22,000,000 | - | 19,334,400 | - | -2,665,600 | - | -12.1% |
| Default Aversion Fee Reversals | | 2,000,000 | | 2,000,000 | | | | |
| Sub-Total Other Administrative Appropriations | - | \$29,000,000 | - | \$26,334,400 | - | -\$2,665,600 | - | -9.9% |
| <i>Other Funds</i> | | | | | | | | |
| State Accounts Receivable Fund | 300,000 | - | 300,000 | - | 0 | - | 0.0% | - |
| State Contracts and Grants Fund | 70,000 | - | 70,000 | - | 0 | - | 0.0% | - |
| Sub-Total Other Funds | \$370,000 | - | \$370,000 | - | \$0 | - | 0.0% | - |
| TOTAL | \$4,921,000 | \$65,146,600 | \$2,920,900 | \$67,768,600 | -\$2,000,100 | \$2,622,000 | -40.6% | 4.0% |

Recommended Line Item Requests

Personal Services

Changes between the FY2005 appropriation for personal services and the FY2006 request being recommended by staff can be divided into three major categories. The first category is that mentioned previously: a proposed shift in funding from GRF to SLOF. The recommended FY2006 budget request for personal services also provides for a 2.5 percent salary increase for all employees funded entirely through a recommended increase in SLOF. Finally, the recommended request provides for additional funding in the group insurance and employer retirement line items to account for projected increases for FY2006.

In FY2005, ISAC was appropriated \$2,460,200 from GRF and \$22,870,400 from SLOF, or a total of \$25,330,600, for personal services and related expenses. For FY2006, staff is proposing that the funding source for \$2,000,100 in personal services related expenses be shifted from GRF to SLOF. Staff also recommends that the Commission seek an additional \$621,900 in SLOF personal services and related line items to fund a 2.5 percent salary increase for all employees in FY2006.

One of the benefit lines ISAC must pay for SLOF-funded personnel is Group Insurance. Thus, transferring personal services related expenditures from GRF to SLOF will require the Commission to request an increase in the SLOF Group Insurance line item to pay this benefit for the employees whose salaries are being transferred. Staff also recommends that the Commission request additional funding in the Group Insurance line item to pay for anticipated increases in this expense for all employees paid from this fund. Thus far in FY2005, Group Insurance costs have averaged 26 percent of employees' salaries. It is anticipated that Group Insurance rates will increase in January 2005 and yet again in July 2005. Thus, staff is recommending that the Commission request SLOF funding sufficient to pay an average of 28 percent in salary cost for Group Insurance. Overall, the recommended increase for Group Insurance exceeds the FY2005 appropriation by nearly \$1.2 million, or 34.1 percent.

Another benefit line that ISAC must pay for all employees is the state retirement contribution. In FY2005, ISAC was appropriated 16.1 percent of its salary line item to pay this benefit. Recent guidance received from the State Employees Retirement System (SERS) has indicated that the rate required for FY2006 will total 21.675 percent. Staff recommends that the Commission request funding needed to meet this increased contribution rate. Overall, the recommended increase for retirement contribution exceeds the FY2005 appropriation by nearly \$1.1 million, or 38.0 percent.

Contractual Services

In FY2005, ISAC was appropriated \$1,802,600 from GRF and \$9,864,300 from SLOF, or a total of \$12,666,900, for contractual services. For GRF, this appropriation represented a decline of \$210,400 (10.5%) from the FY2004 appropriation of \$2,013,000; for SLOF, this appropriation represented a decline of \$1,877,700 (16.0%) from the FY2004 appropriation; and overall, this appropriation represented a decline of \$2,088,100 (15.2%) from the FY2004 appropriation of \$13,755,000. ISAC staff expected that its SLOF contractual services appropriation would be reduced by \$750,000 to fund the transfer of IS contractors being moved to regular positions, but the additional reduction occurred because of changes in the rates expected for the agency's retirement contribution during the budget request process.

For FY2006, staff is recommending that the Commission request an increase of \$1.0 million (10.1%) in SLOF spending authority for contractual services. This recommended increase will recover approximately two-thirds of the spending authority lost in contractual services between FY2004 and FY2005 due to differences in the expected retirement rate contribution. The recommended increase will provide funding for three purposes. First, in late FY2004, ISAC contracted with XAP Corporation to develop Illinois Mentor™ to

build an integrated information management system that establishes and maintains an Internet-based database of grade school, high school and college students. The product is scheduled to be deployed during FY2006 and costs attributed to SLOF are expected to increase by approximately \$150,000 during FY2006. The recommended increase will also provide funding to contract with an outside vendor to meet ISAC's imaging storage needs in the event it would need to do so. Finally, the recommended increase would provide for cost increases of approximately five percent in other contractual services, such as postage, utilities and leasing of office equipment.

Travel

In FY2005, ISAC was appropriated \$26,400 from GRF and \$190,000 from SLOF, for a total of \$216,400 for travel. Staff is recommending that the Commission request no increase to this line item from GRF or SLOF for FY2006.

Printing

In FY2005, ISAC was appropriated \$100,000 from GRF and \$529,000 from SLOF, or a total of \$629,000 for printing. Staff is recommending that the Commission request no increase to this line item from GRF or SLOF for FY2006.

Equipment

In FY2005, ISAC was appropriated \$10,000 from GRF and \$529,000 from SLOF, or a total of \$539,000 for equipment. Staff is recommending that the Commission request no increase to this line item from either GRF or SLOF for FY2006.

Telecommunications

In FY2005, ISAC was appropriated \$113,500 from GRF and \$1,793,500 from SLOF, or a total of \$1,907,000 for telecommunications. Staff is recommending that the Commission request no increase to this line item from GRF or SLOF for FY2006.

Operation of Auto

In FY2005, ISAC was appropriated \$5,500 from GRF and \$32,400 from SLOF, or a total of \$37,900 for operation of auto. Staff is recommending that the Commission request no increase to this line item from GRF or SLOF for FY2006.

Other Recommended Student Loan Operating Fund Administrative Request

Federal Student Loan Systems Development and Maintenance

The FY2006 budget request recommendation contains \$5.0 million in spending authority to meet the requirements of federal loan systems development and maintenance. These requirements fall into three specific areas. First, Phase I (default prevention) of the Odyssey System, which was implemented in June of 2000, and Phase II (collections, claims, accounting and federal reporting) of the System, which was implemented in October, 2002 have ongoing maintenance and software support requirements which must be met in the coming fiscal year. Second, in FY2004, staff made several enhancements to its federal systems which included becoming a Meteor Access Provider and fully implementing the Total Enrollment Reporting Process (TERP) via the Clearinghouse. Staff has also begun an incremental development effort to improve its

loan guarantee information system. These activities are scheduled to continue through FY2006 and will require expenditures from this recommended request for spending authority. Finally, the Reauthorization of the Higher Education Act is scheduled for completion during calendar year 2005. Securing this recommended spending authority will help ensure that ISAC has the flexibility required to respond to potential initiatives proposed by ISAC's competitors in the student loan industry or by the federal government during this important time.

Transfer Default Aversion Fee Reversals from SLOF to FSLF

While guaranty agencies are encouraged to increase their default prevention efforts through the payment of default aversion fees to their operating funds, these fees are refundable in the event the default prevention activities subsequently fail to avert the loans from default. If a loan on which the default aversion fee was previously collected goes into default, the fee must be returned to the Federal Student Loan Fund from the Student Loan Operating Fund. As with the Default Aversion Fee, Default Aversion Fee Reversals require transferring revenues from one fund to another which requires spending authorization. The recommended request for spending authority for FY2006 is \$2.0 million.

Outside Collection Agency Activities

As part of ISAC's collection strategy, ISAC contracts with outside collection agencies to assist in collections on the agency's defaulted student loan portfolio. ISAC currently has entered into agreements with four collection agencies to service a portion of its defaulted loan portfolio. Collection agencies typically are assigned borrowers with accounts for which a voluntary payment has not been received for at least 180 days despite intensive in-house collection efforts. Collection agencies retain a contractually-stated portion (ranging from 14 to 18 percent) of payments which they receive from borrowers on such accounts.

Appropriations authority is required to enable ISAC to remit commission fees back to the collection agencies following their transmittal of the total payment amount. The recommended spending authority for this purpose for FY2005 is \$19.3 million, which is equivalent to the level of fees anticipated to be retained by collection agencies in FY2006.

Recommended Requests from Other Administrative Funds

State Accounts Receivable Fund

Staff recommends an FY2006 State Accounts Receivable Fund request of \$300,000, which represents no change from the current year appropriation. In FY2006, the agency plans to continue the aggressive approach to collection activities first undertaken in FY2002 (with the assistance of an outside collection agency) for the teacher scholarship programs covered by this appropriation. These programs include 12 teacher education scholarship programs formerly managed by the Illinois State Board of Education. Although these programs are no longer in existence, collection activities are still required for those students who did not fulfill the teaching obligation of the scholarship. This level of spending authority will allow for the utilization of monies in this fund (which are generated through the repayment of teacher scholarships from students who do not fulfill their teaching requirements) for administrative expenses and related collection agency charges.

State Contracts and Grants Fund

In FY2003, ISAC received legislative approval for creation of this Fund, intended as a repository for monies received from not-for-profit professional associations interested in assisting ISAC with joint outreach, training and research activities. These associations include, but are not limited to, the Illinois Association of Student Financial Aid Administrators (ILASFAA), the Illinois Association of College Admission Counseling

(IACAC), the National Association of State Scholarship and Grant Programs (NASSGAP), and United Student Aid Fund's Lumina Foundation. In FY2005, ISAC received an appropriation of \$70,000 in spending authority from this Fund. Staff recommends an FY2006 spending authority request of \$70,000 for the Contracts and Grants Fund.

IV. Federal Student Loan Fund Expenditures

To administer the FFEL Program, ISAC requires state spending authority from the Federal Student Loan Fund (FSLF) to pay programmatic expenses, as well as make interfund transfers and payments to the U.S. Department of Education. This section of the agenda item itemizes staff's recommendation for the FY2006 budget request related to programmatic expenses paid using this fund.

Federal Student Loan Fund (FSLF)

Lender Reimbursements

Payments are made from the Federal Student Loan Fund to reimburse lenders for defaulted loans, as well as loans that are discharged as a result of the death, disability or bankruptcy of the borrower. In addition, payments are also made for refunds to students or lenders from closed school or false certification accounts, and for refunds to students who have been erroneously subject to Internal Revenue Service offset procedures. To partially offset the cost of lender reimbursements, ISAC receives payments, in the form of federal reinsurance, from the U.S. Department of Education.

The level of spending for lender reimbursements generally corresponds to economic conditions, the volume of loan guarantees made in previous years, and successful default prevention activities. At a time of relatively low unemployment and stable personal income, students are less likely to default on their loan obligations and, as a result, reimbursements to lenders for defaulted loans generally decline. For FY2005, the lender reimbursement appropriation is \$160.0 million, although expenditures are expected to be less than \$120.0 million. A number of lenders have been designated as exceptional lenders by the U.S. Department of Education, which increases the reimbursement rate for these lenders. With the continued uncertainty regarding the overall state of the economy, and the potential that additional lenders will be granted designation as exceptional lenders, staff recommends that the Commission request spending authority of \$156.0 million for lender reimbursements in FY2006.

Return of Recalled Reserves

As part of the Reauthorization of the Higher Education Act of 1998, guaranty agencies were required to return a portion of funds held in the FSLF to the U.S. Treasury. The second installment of this return is due in FY2006. Staff recommends that the Commission seek \$4.0 million in spending authority to complete this federally required transfer in FY2006.

Transfer ISAC's Share of Collections from FSLF to SLOF

ISAC is permitted to retain approximately 23 percent of all collection revenues according to federal law. This rate varies by loan type, with consolidation rates being lower and the retention level for rehabilitated loans being higher. ISAC is required to deposit all collection revenues in the FSLF and to transfer ISAC's retention amount to the SLOF.

The level of spending authority required in FY2006 in order to make such transfers is \$25.0 million, which represents no change from FY2005.

Transfer Default Aversion Fee Revenues from FSLF to SLOF

This fee is intended to encourage guaranty agencies to increase their default prevention efforts. This fee is actually paid from ISAC's Federal Student Loan Fund to ISAC's Student Loan Operating Fund. Transferring revenues from one fund to another requires spending authorization. The recommended request for spending authority for FY2006 is \$5.0 million, which is the same as FY2005.

The recommended request for all expenditures from the Student Loan Operating Fund and the Federal Student Loan Fund are summarized in Table 8.

**Table 8: FY2006 Student Loan Funds
Budget Request by Fund Type (\$ in millions)**

| STUDENT LOAN FUND TYPE | FY2006 BUDGET REQUEST |
|--|----------------------------------|
| Student Loan Operating Fund | |
| Student Loan Operating Fund Expenses | \$41.4 |
| Default Aversion Fee Reversals | 2.0 |
| Outside Collection Agency Activities | 19.3 |
| Federal Loan Systems Development and Maintenance | 5.0 |
| Subtotal: Student Loan Operating Fund | \$67.7 |
| Federal Student Loan Fund | |
| Lender Reimbursements/Reserve Recall | \$160.0 |
| Collections Payments to SLOF | 25.0 |
| Default Aversion Fee | 5.0 |
| Subtotal: Federal Student Loan Fund | \$190.0 |
| Total: FY2006 Student Loan Funds Request | \$257.7 |

V. Other Federal Funds

Federal Student Assistance Scholarship Fund

In addition to the FFEL Program, ISAC will also require an appropriation from the Federal Student Assistance Scholarship Fund to fulfill its administrative responsibilities related to the Paul Douglas Teacher Scholarship Program. The Paul Douglas Teacher Scholarship Program was a federally funded program administered by ISAC which provided undergraduate scholarships to encourage outstanding high school graduates to pursue teaching careers. Similar to the state teacher scholarship programs, the Paul Douglas Scholarship required a teaching commitment. Failure to fulfill the teaching obligation required the student to repay the scholarship with interest. Although federal funding for this program was discontinued after FY1995, repayments on the converted scholarships continue.

In FY2004, ISAC received spending authority of \$400,000 to transfer repayment funds collected under the Paul Douglas Teacher Scholarship Program to the U.S. Treasury. Staff recommends that the Commission request \$400,000 in spending authority for FY2005 to continue the return of these payments to the federal government.