

AGENDA ITEM 11.

***COLLEGE ILLINOIS!*
CONTRACT PRICES AND FEES FOR 2003-2004 ENROLLMENT PERIOD**

Submitted for: Action

Summary: The proposed pricing schedule for the 2003-2004 *College Illinois!* enrollment period is set forth in Table A. This pricing schedule has been developed by staff in cooperation with the program's actuary, Richard M. Kaye & Associates, in conjunction with PricewaterhouseCoopers.

The pricing schedule set forth in Table A and proposed for Commission approval reflects an array of conservative assumptions designed to ensure that the financial commitments made by *College Illinois!* to Illinois families remain secure. Prices have been set at a level that will provide revenue from contract sales sufficient not only to fund future contract obligations and current administrative costs, but also to provide for an actuarial reserve. This reserve is created as a hedge against unanticipated large tuition and fee hikes, extended periods of investment under-performance, and future contract sales volatility.

The 2003-2004 *College Illinois!* proposed contract price increases are not as great as those imposed in 2002-2003. *College Illinois!* prices proposed for 2003-2004 average 12.0 percent higher for public university contracts and 8.0 percent higher for community college contracts. The combination plan contract price increases average approximately 11.0 percent. These price increases are needed to recognize the adverse actuarial impact of recent double-digit tuition hikes imposed at many Illinois public universities for 2003-2004, as well as the negative performance within the equities component of the program's investment portfolio. Also, a stabilization reserve factor of approximately 2.5 percent is included in prices proposed for 2003-2004 to further enhance the program's actuarial soundness, and to act as a hedge against the uncertain impact of new legislation on public university tuition increases for 2004-2005 and thereafter.

Table B presents the proposed fee schedule for the *College Illinois!* 2003-2004 enrollment period. For the first time since the program's inception five years ago, an increase in certain fees is requested. Specifically, the recommendation includes an increase in the non-refundable application fee from \$75 to \$85 (for the first contract) and from \$40 to \$50 (for every contract thereafter, by the same purchaser). An increase also is requested from \$15 to \$20 for the monthly late payment fee and non-sufficient funds (NSF) fee. These increases in application, late and NSF fees are recommended to compensate for the impact of inflation during the past five years since the program has been in operation.

The 2003-2004 *College Illinois!* enrollment period during which these prices are in effect will be from October 29, 2003, through March 31, 2004.

Action requested: Staff recommends that the Commission approve the schedule of *College Illinois!* contract prices specified for the 2003-2004 enrollment period in Table A, as well as the schedule of *College Illinois!* fees and charges for the program set forth in Table B.

ILLINOIS STUDENT ASSISTANCE COMMISSION

COLLEGE ILLINOIS!

CONTRACT PRICES AND FEES FOR 2003-2004 ENROLLMENT PERIOD

INTRODUCTION

College Illinois! is a self-sustaining program administered by the Illinois Student Assistance Commission (ISAC) and designed to operate independent of state appropriations and other external financial support. The program recently completed its fifth consecutive enrollment period, during which nearly 7,500 contracts were purchased, an increase of more than 15 percent compared with the previous year. In total, more than 36,000 *College Illinois!* contracts have been purchased and those contracts currently in effect represent a financial commitment by program participants of more than \$600 million.

The program's sixth annual enrollment period is scheduled to begin on October 29, 2003, and continue through March 31, 2004.

PRICING SCHEDULE FOR *COLLEGE ILLINOIS!* CONTRACTS

The proposed pricing schedule for the 2003-2004 *College Illinois!* enrollment period is set forth in Table A. As in prior years, this pricing schedule has been developed by staff in cooperation with the program's actuary.

As in recent years, it is recommended that *College Illinois!* contract prices increase for the 2003-2004 enrollment period, in recognition of four major factors:

- ◆ Tuition and Fee Increases. Tuition and fees at Illinois public universities increased on average by 9.2 percent for the 2003-2004 academic year, including double-digit increases approved for new students at 8 of the state's 12 public university campuses. This 9.2 percent increase is more than the long-term trend rate of 7.0 percent per year (but somewhat less than the 10.0% projected by the program last year at this time when prices were being set for this past 2002-2003 enrollment period). Tuition and fees increased by a more moderate 5.7 percent, on average, at Illinois community colleges, less than the annual 6.5 percent assumed by the program for pricing purposes.
- ◆ Investment Performance. The program's overall investment returns in FY2003 were positive, in contrast to the results posted in the past two years, but still lower than long-term actuarial expectations. Nonetheless, when combined with other factors, investment returns were sufficient to ensure a significant improvement in the program's overall funding ratio. *College Illinois!* will continue to show an actuarial deficit as of June 30, 2003, but this deficit can be diminished partially or entirely by the Commission's contract pricing decisions over time.
- ◆ Investment Return and Tuition Inflation Assumptions. Each year, future investment return and tuition inflation assumptions are incorporated into contract pricing to ensure that the program's long-term fiscal viability remains based on conservative assumptions, rooted in a realistic view of what is achievable and likely to occur within the next ten years. This year, staff recommends that the long-term annual investment return assumption remain unchanged from last year, when it was lowered by

25 basis points, from 8.0 percent to 7.75 percent, in recognition of the difficult economic challenges facing the United States and the world during the next decade. Similarly, it is recommended that the tuition inflation assumption remain unchanged from last year. While the long-term annual tuition inflation assumption remains at 7.0 percent, 2003-2004 *College Illinois!* contract prices are based on an expectation that next year, Illinois public university tuition and fees once again will rise on average by 10.0 percent, due to the continued adverse impact of the state's budget crisis upon Illinois' public universities and community colleges.

- ◆ Stabilization Reserve Requirements. Continuation of the program's stabilization reserve requires additional revenue that will serve two purposes: (1) in the immediate future, stabilization revenue will help to reduce the program's current actuarial deficit and improve the program's funded ratio; and (2) over time, a stabilization reserve will counteract the impact of future unanticipated spikes in college tuition and fees, annual volatility of contract sales, and periods of investment under-performance. For 2003-2004, all recommended contract prices are increased for this purpose by approximately 2.5 percent.

The pricing schedule set forth in Table A and proposed for Commission approval once again reflects conservative assumptions designed, first and foremost, to ensure that the financial commitments made by *College Illinois!* to Illinois families remain secure. Prices have been set at a level that will provide revenue sufficient not only to fund future contract obligations and current administrative costs, but also to gradually reduce the program's current actuarial deficit and ultimately create a stabilization reserve. This stabilization reserve is intended as a hedge against the kind of adverse economic conditions we currently are experiencing: specifically, the adverse impact of periodic spikes in college tuition and fees, annual volatility in the level of contract sales, and extended periods of investment under-performance. Stabilization reserve revenue, like all *College Illinois!* monies, are deposited in the Prepaid Tuition Trust Fund, and can be used at some future date only for payment of contract benefits or for program administrative purposes. By law, such reserve funds cannot be used for any purpose extraneous to the *College Illinois!* program.

Assumptions

For 2003-2004, in contrast to last year, there is no major modification in the College Illinois! program's approach toward pricing. The contract prices recommended in Table A have been developed using the same fundamental assumptions adopted by the Commission last year. The projections of future investment performance and future tuition and fee increases have been reviewed once again this year (in collaboration with both our actuarial and investment advisors: Richard Kaye & Associates in association with PricewaterhouseCoopers, and Marquette Associates, respectively), but have not been altered.

Tuition and Fees. The Commission has assumed that tuition and fees at Illinois public universities and community colleges shall increase at an average annual long-term rate of 7.0 percent, consistent with past experience in Illinois (during the past two decades). Recommended prices for 2003-2004 assume that this long-term trend will continue, with one important modification. It is expected that tuition and fee increases at Illinois public universities will increase on average by 10.0 percent during 2004-2005. The State of Illinois' present budgetary problems that resulted in double-digit tuition increases at many Illinois public universities during the past two years will not likely be resolved fully within the next 12 months. Therefore, it appears reasonable to expect higher than usual tuition and fees increases will be authorized at Illinois public universities for at least one more year. This modification has not been applied toward Illinois community colleges, however. A number of factors, including community colleges' traditional mission to ensure access and affordability, combined with their lesser reliance on state appropriations (because of funding derived from local property tax revenue), makes it less likely that community

colleges' tuition and fee increases will spike. Evidence from this past year confirms this: Illinois community colleges' tuition increased, on average, by only 5.7 percent for 2003-2004.

Investment Performance. Currently, the program's assumption is that over the long-term (i.e., 10 years or more), investment returns would increase by 7.75 percent (a 5.25 percent real return on equities and fixed income investments; 2.5 percent annual inflation). No change is recommended in this long-term investment return assumption. Particularly now, when equity markets appear to have emerged from a three-year down cycle, 7.75 percent appears to be a reasonable long-term investment assumption for the program.

Stabilization Reserve. For 2003-2004, all recommended contract prices increased by approximately 2.5 percent to generate additional revenue that will create, over time, a stabilization reserve. These revenues are necessary to enhance the program's actuarial soundness. In the near-term, these revenues will help to reduce the program's current actuarial deficit. Long-term, the stabilization reserve is designed to act as a financial bulwark against future unanticipated spikes in college tuition and fees, annual volatility of contract sales, and periods of investment under-performance. This is the third year in which this factor has been incorporated into pricing. In each of the past two years, this premium has generated significant revenues that have helped to diminish the program's actuarial deficit and improve the funding ratio during a period when the rate of return on most equity investments has been negative.

Other Factors. In addition to assumptions about the level of tuition and fees, investment returns and a stabilization reserve, there are certain other factors that must be considered each year when developing contract prices. Now that the program has been established for five years, there is finally a meaningful amount of experience and data from which to derive reasonable assumptions. Consequently, when developing FY2004 contract prices, it is projected that:

- ◆ between 5,000 and 6,000 contracts will be purchased in FY2004 and each year thereafter -- a conservative level of sales consistent with the program's experience during the past five enrollment periods;
- ◆ contracts will be allocated similarly by type in FY2004 and each year thereafter;
- ◆ through annual pricing decisions, along with improved actual investment performance, the program's actuarial deficit will likely be diminished, then eventually eliminated, and an actuarial reserve may be created and maintained in future years; and
- ◆ the program's administrative costs approved for FY2004 are incorporated into contract pricing.

Recommended Contract Prices

Recommended prices for the 2003-2004 enrollment period were determined first by referencing estimated tuition and fee rates for the 2003-2004 academic year at all Illinois public universities and community colleges and at private Illinois colleges. As always, prior year trends and projected future trends in tuition and fee rates for Illinois higher education also were referenced when crafting this pricing recommendation.

This past year, according to the most recent data submitted to ISAC, tuition and mandatory fees have increased in Illinois by an average of 9.2 percent at public universities, and by an average of 5.7 percent at public community colleges. For the 2003-2004 enrollment period, recommended *College Illinois!* contract prices for public university semesters and community college semesters exceed these

increases, due to the adverse impact of recent investment performance and the premium necessary to create a stabilization reserve for the program.

This *College Illinois!* recommendation for contract prices is not unique and is, in fact, more moderate than price increases being imposed in many other states that operate Section 529 prepaid tuition programs. Like *College Illinois!*, almost every other state-sponsored Section 529 prepaid tuition program has incorporated a premium into their contract prices, due to recent investment performance and the trend toward higher tuition and fees imposed at public universities and other higher education institutions nationwide.

A recent trend analysis confirmed that tuition and mandatory fees at Illinois public universities increased by 7.0 percent annually during the decade 1993-2003. Incorporating community college tuition and fees into the equation, these tuition and fees increased overall by 6.4 percent during that same decade. During the past two years, however, the trend has been higher, partly due to increases imposed at the state's largest public university campuses: University of Illinois at Urbana and at Chicago. For 2003-2004, base tuition and fees increases at these two large University of Illinois campuses were relatively moderate: approximately 5.0 percent at both Urbana and Chicago, but 8 out of the other 10 Illinois public university campuses authorized double-digit base tuition increases for freshman students in response to lower state appropriations received from the state for FY2004.

After analyzing this and other data, *College Illinois!* staff continues to believe that public university tuition and mandatory fees during the next year could once again average nearly 10.0 percent. Once Illinois digs out of its current budgetary crisis, both the hope and the expectation would be that in subsequent years these tuition and fees increases will revert closer to the historical norm and increase by an average annual rate of 7.0 percent.

Similarly, the program's investment advisor, Marquette Associates, has confirmed as reasonable the program's current long-term investment return assumption of 7.75 percent.

College Illinois! contract options proposed for the upcoming enrollment period are generally consistent with those offered during prior enrollment periods. Purchasers can select from one to nine semesters at an Illinois public university, from one to four semesters at an Illinois community college, or the combination plan, which combines four semesters at a community college with four semesters at a public university.

Program staff is, however, recommending that more extensive payment options be offered for the first time this year. As a result of ISAC-initiated legislation that was enacted into law eliminating previous restrictions on 10-year installment plans, additional payment options have been added for newborns through eighth graders. Both 10-year monthly and annual installment options are available for the first time for plans covering less than 8 university semesters. This new pricing initiative is proposed with the goal of increasing plan affordability and encouraging families to begin a prepaid tuition plan, even if on a small scale initially.

Once again, as in prior years, a separate schedule is proposed for preschool students/beneficiaries (through Kindergarten); for elementary and middle school students/beneficiaries (grades 1-8), and for high school students or beneficiaries who have graduated from high school (grades 9-12 and older). These three groupings were selected to simplify the number of plan offerings and for their intuitive appeal (i.e., preschool, grade school and middle school, and high school and older). Pricing distinctions for each age category do not constitute a discount. Instead, lower price contracts are offered for younger beneficiaries because payments received can be invested over a longer period of time, providing a greater opportunity to earn the necessary rate of return on contributions invested.

For example, according to the proposed pricing schedule (Table A):

- one year (two semesters) at an Illinois community college can be purchased for \$2,071 or for \$45 per month over five years for a child in kindergarten or younger;
- one year (two semesters) at a public university for the same child could be purchased for \$6,856 or \$141 per month over five years;
- a four-year (eight-semester) contract for a grade school/middle school student can be purchased for \$28,484.
- This same contract also could be purchased for \$577 per month over five years or \$346 per month over ten years; and a combination contract can be purchased for this same student for \$18,253 or \$371 per month over five years or \$223 per month over ten years.

Purchasers can also choose to pay by annual installments or to make down payments of \$2,000, \$5,000 or \$10,000, when choosing a monthly installment plan in order to lower their monthly payment amounts over either 5 years or 10 years.

The proposed lump sum contract prices for 2003-2004 when compared with last year's lump sum contract prices represent an average increase of 12.0 percent for public university, 8.0 percent for community college contracts, and an average increase of approximately 11.0 percent for the combination plan contracts. Prices for all installment contracts increase by similar percentages as the program's lump sum contracts.

SCHEDULE OF FEES FOR *COLLEGE ILLINOIS!*

Table B presents the proposed fee schedule for the *College Illinois!* 2003-2004 enrollment period. For the first time since the program's inception five years ago, an increase in certain fees is requested. Specifically, the recommendation includes an increase in the non-refundable application fee from \$75 to \$85 (for the first contract) and from \$40 to \$50 (for every contract thereafter, by the same purchaser). An increase also is requested from \$15 to \$20 for the monthly late payment fee and non-sufficient funds (NSF) fee.

This increase in application, late and NSF fees is recommended to compensate for the impact of price inflation during the past five years the program has been in operation. Price inflation has remained low (2.0% to 2.5% per year) during this period, so annual fee increases have not been needed or requested, but at this time an adjustment is warranted to compensate for the cumulative impact of low inflation over the five-year period. Notably, late fees and NSF fees imposed by most financial institutions and credit card companies currently equal or exceed the \$20 amount recommended.

As in past years, the fees in Table B are divided into several groupings: Administrative; Service and Cancellation fees. Administrative fee revenues are used to cover general administrative costs of the program, whereas service fee revenues pay the cost of providing a particular service or to reimburse the Illinois Prepaid Tuition Trust Fund for lost investment opportunity. Cancellation fees are assessed only when an account is cancelled.

The application fee is a one-time non-refundable fee paid by the purchaser at the time of application. This fee is used to defray the costs associated with setting up a new account, including loading information into the program database, generating program documentation and printing of coupon books for purchasers who choose to pay by installments. The discounted application fee is applicable to the second and all subsequent contracts purchased by the same individual. The administrative load that is

built into contract pricing and the application fee (both listed in the administrative category) are assessed every contract purchaser.

In contrast, service fees are charged only when special handling of an account is required and records administration costs and/or administrative costs for the program are incurred. Service fees include charges for late payments, returned payments, account changes requested by the purchaser, as well as the transfer of benefits to private or out-of-state schools.

Cancellation fees are charged only for purchasers who decide to cancel their *College Illinois!* contract. Cancellation fees represent an early withdrawal penalty upon the purchaser, consistent with the intent of the federal law (Internal Revenue Code, Section 529) that authorizes state qualified prepaid tuition programs such as *College Illinois!*.

CONCLUSION

The 2003-2004 *College Illinois!* enrollment period during which these prices are in effect will be from October 29, 2003, through March 31, 2004. The 2003-2004 *College Illinois!* proposed prices represent increases from the previous year that average 12.0 percent for public university contracts and 8.0 percent for community college contracts. The combination plan contract price increases average approximately 11.0 percent

For the first time since the program's inception five years ago, an increase in certain fees is requested. Specifically, the recommendation includes an increase in the non-refundable application fee from \$75 to \$85 (for the first contract) and from \$40 to \$50 (for every contract thereafter, by the same purchaser). An increase also is requested from \$15 to \$20 for the monthly late payment fee and non-sufficient funds (NSF) fee. These increases in application, late and NSF fees are recommended to compensate for the impact of inflation during the past five years the program has been in operation.

Table A
College Illinois!
Pricing Schedule for 2003 - 2004 Enrollment Period

Type of Plan	Infant - Kindergarten					First - Eighth Grade					Ninth Grade and Older				
	Lump Sum	5 year monthly	5 year annual	10 year monthly	10 year annual	Lump Sum	5 year monthly	5 year annual	10 year monthly	10 year annual	Lump Sum	5 year monthly	5 year annual	10 year monthly	10 year annual
Public Univ - 9 semesters	\$29,785	\$603	\$6,910	\$362	\$4,113	\$31,976	\$647	\$7,418	\$388	\$4,415	\$33,983	*	*	*	*
Public Univ - 8 semesters	\$26,543	\$538	\$6,158	\$323	\$3,666	\$28,484	\$577	\$6,609	\$346	\$3,933	\$30,262	*	*	*	*
Public Univ - 7 semesters	\$23,261	\$472	\$5,397	\$283	\$3,213	\$24,987	\$506	\$5,798	\$304	\$3,451	\$26,541	*	*	*	*
Public Univ - 6 semesters	\$20,026	\$406	\$4,647	\$244	\$2,766	\$21,470	\$435	\$4,982	\$262	\$2,966	\$22,792	*	*	*	*
Public Univ - 5 semesters	\$16,753	\$340	\$3,888	\$205	\$2,315	\$17,949	\$365	\$4,165	\$219	\$2,480	\$19,044	*	*	*	*
Public Univ - 4 semesters	\$13,464	\$274	\$3,125	\$165	\$1,861	\$14,408	\$293	\$3,344	\$177	\$1,991	\$15,269	*	*	*	*
Public Univ - 3 semesters	\$10,167	\$208	\$2,361	\$126	\$1,406	\$10,863	\$222	\$2,522	\$134	\$1,502	\$11,496	*	*	*	*
Public Univ - 2 semesters	\$6,856	\$141	\$1,593	\$86	\$949	\$7,295	\$150	\$1,695	\$91	\$1,010	\$7,693	*	*	*	*
Public Univ - 1 semester	\$3,481	\$73	\$810	\$45	\$483	\$3,725	\$78	\$867	\$48	\$517	\$3,893	*	*	*	*
Comm Coll - 4 semesters	\$3,928	\$82	\$914	*	*	\$4,160	\$87	\$968	*	*	\$4,345	*	*	*	*
Comm Coll - 3 semesters	\$3,008	\$64	\$701	*	*	\$3,169	\$67	\$738	*	*	\$3,294	*	*	*	*
Comm Coll - 2 semesters	\$2,071	\$45	\$483	*	*	\$2,156	\$46	\$503	*	*	\$2,215	*	*	*	*
Comm Coll - 1 semester	\$1,086	\$25	\$255	*	*	\$1,153	\$26	\$270	*	*	\$1,206	*	*	*	*
Combination - 8 semesters (4 CC and 4 Public Univ)	\$17,007	\$346	\$3,947	\$208	\$2,350	\$18,253	\$371	\$4,236	\$223	\$2,522	\$19,376	*	*	*	*

* payment plan is not available

Table B
College Illinois!
Fee Schedule for 2003 - 2004 Enrollment Period

Type of Fee	Description	Amount
ADMINISTRATIVE FEES		
Application	application processing for new account	\$85
Application - additional contracts *	processing of second and subsequent applications (same purchaser)	\$50
Payment processing **	charge assessed for monthly and annual payment plans	\$3 per payment (included in contract prices)
Administrative load	ensure adequacy of annual program administration	included in contract prices
SERVICE FEES		
Late payment - monthly payment plan	payment received after payment grace period	\$20
Late payment - lump sum, annual or down payment	payment received after payment grace period	1% of outstanding balance
Non-sufficient funds/returned payment	payments returned by financial institution	\$20
Change payment schedule	change in payment schedule	\$15
Change of purchaser	change of purchaser of plan	\$15
Change of beneficiary	change of beneficiary of plan	\$15
Change type of plan	changing from one plan type to another	\$15
Document replacement	new coupon book, welcome package, etc.	\$15
Benefits transfer to private or out-of-state school	processing private or out-of-state school invoice	\$15 per institution attended
CANCELLATION FEES		
Cancellation - voluntary ***	purchaser elects to cancel account	The lesser of \$100 or 50% of amount paid
Cancellation - involuntary	plan is canceled due to delinquency, incorrect information, etc.	The lesser of \$100 or 50% of amount paid
Cancellation - fraud	plan is canceled due to deliberate misrepresentation	The lesser of \$500 or 100% of amount paid
Account maintenance - lump sum payment	charge assessed for cancellation of lump sum plans	35 cents per month

* Application fee is \$85 for first contract purchased and \$50 for each contract thereafter purchased by the same individual.

** Payment processing fees are not refunded when a prepaid tuition contract is canceled.

*** For reasons other than death, disability or scholarship.