CALIFORNIA EDUCATIONAL FACILITIES AUTHORITY
STAFF SUMMARY AND RECOMMENDATION

Cal Loan Student Loan Program
December 7, 2000
Resolution Number: 184

Background

In March 1997, CEFA issued $30.26 million in tax-exempt bonds for the "Cal Loan" program, the first of two student loan programs developed by the Authority. The Cal Loan program was designed to provide a unique and significant contribution to higher education lending in California, and it offers a number of important benefits for students as follows:

- Serves low income students as a "needs based" program, whereby loans are determined on the basis of financial need rather than the credit strength of the borrower. Exhibit A shows that 40% of Cal Loan recipients responding to an information survey had family incomes less than $30,000.

- Fixed interest rate, compared to the Federal Stafford and PLUS Loan programs, and the vast majority of commercially available loans which offer only variable interest rates;

- Low interest rate, compared to commercial lenders. One of only two loan programs in the state using low cost, tax-exempt bond financing. The other program is this Authority's own Cal Edge program; and a

- Minimal 5% loan loss fee compared to commercial lenders, which generally offer a sliding scale fee dependent upon the credit risk of the borrower.

Lending History

Initially, the Cal Loan program was slow to originate loans which was expected due to the fact the program was a start-up with no prior operating or marketing history. In its first two years of existence, Cal Loan generated a total of $7.2 million in loans. More recently, however, program performance has improved dramatically as (i) colleges and students have familiarized themselves with the strong benefits of the program and have increased usage accordingly and (ii) the Program has realized a "multiplier effect" as subsequent loans are made to repeat borrowers.

Over this last year of operations, the program generated a significant $8.5 million in loans, and current program projections foresee the program utilizing the entire $23 million dedicated for loans[1] by August of 2001. Exhibit B provides an analysis of expected program demand through August 2001.

[1] Although the program issued $30,260,000 in bonds, only $23 million was dedicated for student loans. The remaining $7 million was targeted for program reserve funds ($3 million) and to finance bond interest payments ($4 million) over expected student deferment periods.

Board Request

In preparation for issuing bonds next year to continue the Cal Loan program, staff is requesting that the Authority:

1. Approve staff to seek a $40 million bond allocation in January 2001 from the California Debt Limit Allocation Committee (CDLAC). This will finance program operations for an estimated additional three years through 2004.

2. Commit to a loan for the program in an amount not to exceed $700,000 from California Student Loan Authority (CSLA) reserves to finance certain program reserve and cash flow requirements. This proposed loan is consistent with the first issuance of the program that also required a CSLA loan, in the amount of $900,000.

3. Approve staff to work to develop a program enhancement (described below) to further improve program accessibility. This enhancement may require an additional Authority loan of approximately $200,000 to $400,000, with the final enhancement cost to be approved by the Authority at its March 2001 meeting.

Expected Structure of Transaction

The expected financial structure and estimated sources and uses of funds are as follows. This information will be refined further and presented to the Authority at its March 2001 meeting, prior to bond issuance. Other relevant program structure information can be found in Exhibits C and D.

Type of Issue:	Public offering, fixed rate
Credit Enhancement:	MBIA insurance
Credit Rating:	AAA (Standard & Poor's) & Aaa (Moody's) based on insurance
Senior Underwriter:	Prager, McCarthy & Sealy
Bond Counsel:	Orrick, Herrington & Sutcliffe

Estimated Sources of Funds:		Estimated Uses of Funds:	
Bond proceeds	$40,000,000	Amount available for loans	$31,920,000
CSLA loan for enhancements (max amt.)	400,000*	Debt service reserve fund	4,000,000
CSLA loan for reserves/cash flow	700,000	Capitalized interest	4,000,000
		Program enhancements	400,000
		Program reserves and cash flow	700,000
		Bond insurance	80,000
Total Sources	$41,100,000	Total Uses	$41,100,000

*The CEFA loan for enhancements is estimated at $200,000 to $400,000.

CEFA Loan for Reserves and Cash Flow Requirements

Staff is proposing a loan to the program in an amount estimated at $700,000 to assist with additional reserves and liquidity to fund ongoing program operating costs. CEFA's Student Loan Authority (CSLA) fund has an approximate $6 million balance and money from this fund was used for these purposes during the initial start-up of the Cal Loan Program as well as the start-up of the Cal Edge Program.

CEFA Loan For Program Enhancement

As noted earlier, the Cal Loan program is meeting its objectives of serving low-income students and generating strong demand. However, both staff and the Program Administrator believe that, if we are to continue to expand the program, we must consider potential enhancements to attract a greater number of colleges into the program. To that end, staff has reviewed several program enhancements and concluded that restructuring the program's security requirements is the most cost-effective proposal. This may require an additional Authority loan estimated between $200,000 and $400,000 as described below.

Currently, colleges are required to guaranty 12% of all loans made to their students. In addition to this guaranty, a 5% loan loss fee deducted from each loan provides additional security. The college guaranty is in first loss position. That is, colleges are required to pay up to their required 12% guaranty before the 5% loan loss fee revenue is tapped to cover remaining defaulted loans.

The program has faced marketing difficulties due to colleges' hesitancy to assume the first loss position. Staff is currently working with the program's bond insurer and rating agencies to restructure the guaranties such that the 5% loan loss fee is in the first loss position and the college guaranty is in the second loss position.

While not affecting the overall 17% guaranty in place for the program, the proposed program enhancement does impact program liquidity. Under the current structure the colleges' first loss position of 12% assures that the 5% loan loss fee will remain virtually untouched because overall defaults are expected to be less than 12%. This allows the 5% loan loss fee revenue to also serve as extra program liquidity to cover operating costs, if necessary. By putting the loan loss fee in first loss position, this money will assuredly be used for default purposes, and will deplete the extra liquidity in the program.

To maintain this extra liquidity required by the bond insurer and rating agencies, the Authority may be required to loan between $200,000 and $400,000 to the program. Staff will present the final results of this negotiation and required loan size to the board at its March 2001 meeting.

CSLA Loan - Payback Provisions

Given specific rating and bond insurance stipulations that govern program cash flows, both CSLA loans listed above would be structured such that periodic payments would be contingent on the program achieving threshold levels of excess cash reserves. Therefore, the final loan amounts requested by staff will, among other things, be based on a review of program cash flows indicating that income generated by the program would be sufficient to pay the loans back.

Summary

The Cal Loan Program has provided a significant contribution to higher education student lending in this state. However, without a bond issuance in 2001, the program funds will be depleted. Receiving bonding allocation through CDLAC is a key step in the future of the program.

Approving the above requests will demonstrate to CDLAC the necessary Authority commitment and financial backing required to obtain an allocation to issue bonds. Before reissuing bonds for the program, staff will present specific, detailed program parameters and documents for Board review and consideration at the Authority's March 2001 meeting.

Recommendation

Staff recommends the approval of resolution number 184 for the Cal Loan Program, authorizing the following:

- Approval for staff to seek a $40 million bond allocation in January 2001 from the California Debt Limit Allocation Committee (CDLAC).

- Commitment for an approximate $700,000 loan to the program from California Student Loan Authority (CSLA) reserves to finance certain program reserves and cash flow requirements.

- Approval for staff to develop program enhancements to improve the attractiveness of the program for participating colleges. This enhancement may require an additional Authority loan to the program in an amount estimated between $200,000 and $400,000, with the final enhancement cost to be approved by the Authority at its March 2001 meeting

Exhibit A

California Educational Facilities Authority
Cal Loan Program

Borrower Financial Characteristics

Because the Cal Loan does not look at income level factors to determine eligibility, the income level of participating students is not readily available. In September of this year, however, a survey was mailed to current Cal Loan borrowers, which asked, among other questions, what the student's family's adjusted gross income was when the student applied for the loan. Although the survey only received a 22% response rate, the results obtained show that the program appears to be obtaining its goal of reaching lower income students, as shown in the following table.

Student's family's adjusted gross income	Participation in Program
Less than $20,000	25.36%
$20-29,999	13.99%
$30-39,999	12.54%
$40-49,999	9.62%
$50-59,999	9.04%
$60,000+	27.11%

Exhibit B

California Educational Facilities Authority
Cal Loan Program

Projected Annual Lending

Month	Nov-00	Dec-00	Jan-01	Feb-01	Mar-01	Apr-01	May-01	Jun-01	Jul-01	Aug-01
Monthly Loan Activity:										
Projected Disbursements	$ 422,500	$ 1,690,000	$ 845,000	$ 422,500	$ 422,500	$ 422,500	$ 845,000	$ 422,500	$ 422,500	$ 1,267,500
Utilization of Available Funds:										
Total Loan Disbursements, Begin	$ 16,229,777	$ 16,652,277	$ 18,342,277	$ 19,187,277	$ 19,609,777	$ 20,032,277	$ 20,454,777	$ 21,299,777	$ 21,722,277	$ 22,144,777
Actual Disbursements for Month	422,500	1,690,000	845,000	422,500	422,500	422,500	845,000	422,500	422,500	1,267,500
Total Loan Disbursements, End	$ 16,652,277	$ 18,342,277	$ 19,187,277	$ 19,609,777	$ 20,032,277	$ 20,454,777	$ 21,299,777	$ 21,722,277	$ 22,144,777	$ 23,412,277
Original Loan Funds Available	$ 23,171,225	$ 23,171,225	$ 23,171,225	$ 23,171,225	$ 23,171,225	$ 23,171,225	$ 23,171,225	$ 23,171,225	$ 23,171,225	$ 23,171,225
Total Disbursments to Date	(16,652,277)	(18,342,277)	(19,187,277)	(19,609,777)	(20,032,277)	(20,454,777)	(21,299,777)	(21,722,277)	(22,144,777)	(23,412,277)
Unutilized Loan Funds	$ 6,518,948	$ 4,828,948	$ 3,983,948	$ 3,561,448	$ 3,138,948	$ 2,716,448	$ 1,871,448	$ 1,448,948	$ 1,026,448	$ (241,052)

* Projected Activity shows that if actual disbursements are 69% over projected disbursements (the average actual has exceeded projected disbursements by 69% over the past fifteen months), the loan program will exhaust all bond funds by August, 2001.

Exhibit C

California Educational Facilities Authority
Cal Loan Program

Cal Loan Program Structure:

Student Loans: Federal law requires that loans made under the program can only be made to borrowers that have exhausted all available federal and school based aid. All loans bear a fixed interest rate and have a 5% origination fee, with proceeds of the fee used as program reserves. Students may defer their loan payments during the in-school period of their loans. The student is also eligible for other forbearance periods when out of school. There is no application fee.

College Guaranties: Unlike "Credit based" loans which are based on ability to pay, "need based" loans are inherently of lesser credit quality. Therefore, the outside guaranties to support this type of program are greater and require credit support of participating colleges or universities to keep the program affordable.

The program is structured such that colleges rated "A" or better are required to provide a contingent guaranty of loans made to their students. Colleges rated less than "A" are required to directly post cash for their guaranty requirements. The level of guaranty is generally 12% of a college's loan portfolio, but that may increase dependent upon the default history of a participating college's students.

Participating Colleges: The four colleges currently participating in the Cal Loan program are: Mt. St. Mary's, Pepperdine University, University of San Diego and University of San Francisco. Over the last year, the program has experienced significant growth as the schools have increased their usage of the program. Annually, the participating colleges have used funds in excess of the original projected forecasts. As a result, funds will be depleted by August 2001 as shown in Exhibit B.

Program Contractors: The program requires the use of a "Loan Originator" to make loans and a "Loan Servicer" to manage repayments. It also requires the use of a Bank Trustee to manage bond indenture requirements and payments to the bondholders. The program utilizes an investment contract for the significant cash deposits of the program. Given the complexity of managing and monitoring student loan programs, the Authority has hired an outside administrator. The Program Administrator reports directly to the Authority and provides ongoing monitoring of all participants involved in managing the program (i.e. the Loan Originator and Servicer, Bank Trustee and participating colleges). The Administrator also monitors the financial performance of the program and assists in marketing the program, and providing borrower assistance. The California Alternative Loan Marketing Association (Callie Mae), a California non-profit corporation based in Los Angeles, has been designated as the administrator for this program. Access To Loans For Learning Student Loan Group (ALLSLG), a sister California non-profit corporation of Callie Mae's, provides direct program management through a management contract with Callie Mae.

At this point, a change in contractors and financing team is not anticipated, although we are preparing an RFP to evaluate other potential bank trustees. Exhibit D provides an organization chart that describes roles of the various participants in the program.

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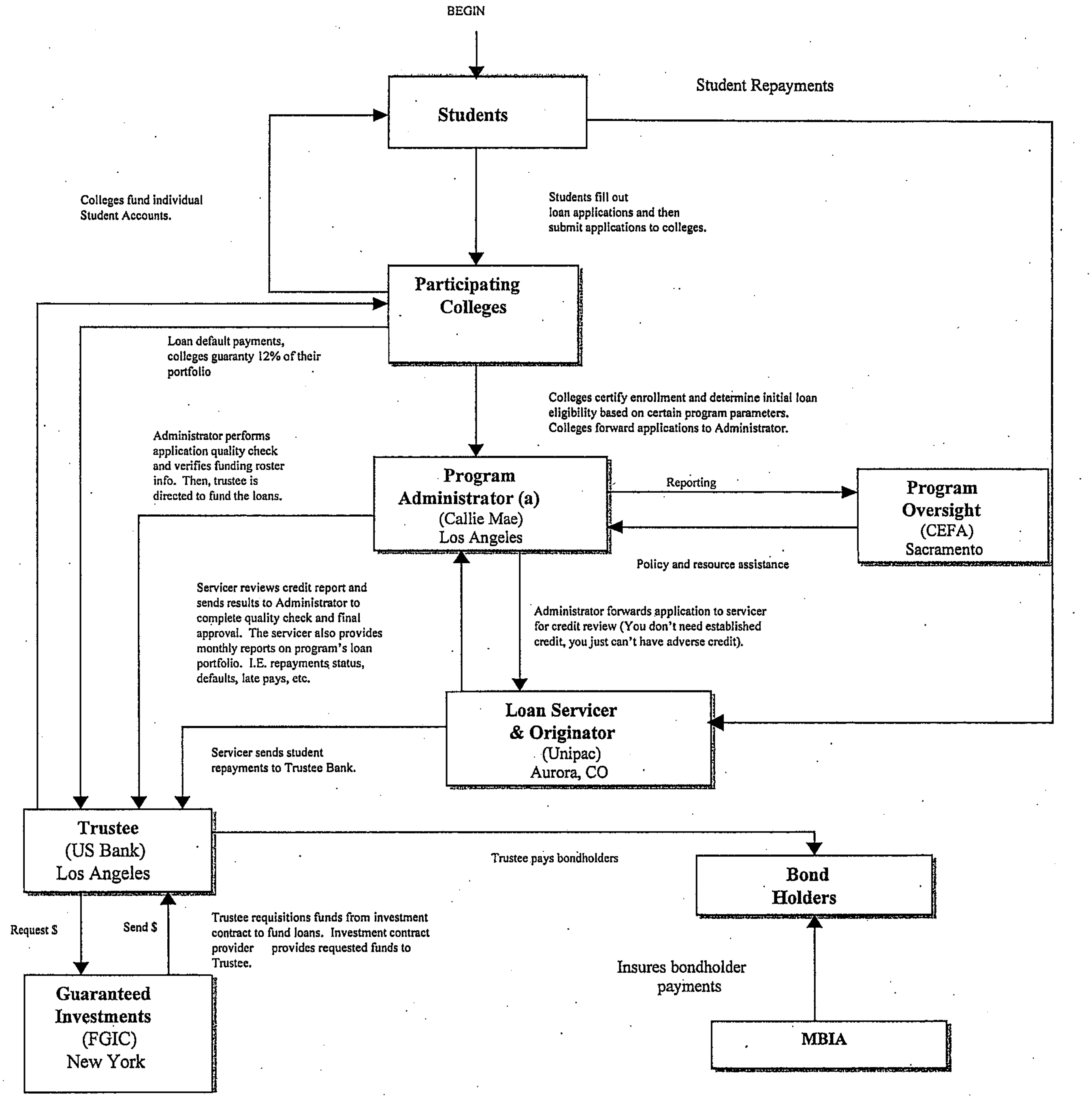
Exhibit D

California Educational Facilities Authority
Cal Loan Program

Organization Chart



(a) Callie Mae, as CEFA's Program Administrator is responsible for program oversight of all counterparties, including College relations. It reconciles Trustee statements with Servicer reports, and it oversees program audit functions including independent audits of the Servicer/Originator's management of the program. Callie Mae also provides monthly and quarterly financial/operational reports.