Cal Loan Activity Reconciliation and Projections

for

California Educational Facilities Authority (CEFA)

Board Meeting, April 25, 2013

Background -- Cal Loan Program Overview

- $75.3 million in Bonds were sold to fund two Cal Loan programs (1997 and 2001).
    - $30.3 million in Student Loan Revenue Bonds were sold in 1997 and an additional $45 million were sold in 2001.
    - Proceeds from each tranche of Bonds were deposited into separate trustee accounts and each program was administered separately by All Student Loan Resources Corporation (ASLRC).

- $6 million of the $75.3 million in Bonds remained outstanding as of December 31, 2012.
    - All $30.3 million of 1997 Bonds were redeemed by March 2007.
    - A net of approximately $2.7 million of the 2001 Bond proceeds were used to redeem the 1997 Bonds.
    - After the redemption of the 1997 bonds in 2008, the remaining funds from the 1997 bonds were transferred to the 2001 Bond program.
    - As of December 31, 2012, $39 million in 2001 Bonds had been redeemed, leaving $6 million outstanding.

- About $1.6 million in cash was on deposit with the trustee as of December 31, 2012.
    - The Reserve Trust account for the 2001 Bond program has been reduced from $4 million in FY 2003 to $324,000 as of December 31, 2012, per the calculations set forth in the Second Supplemental Indenture.

- CEFA monitors Cal Loan activity through various financial reports.
    - Monthly Trustee Statements (“Trustee Statements”) that show cash receipts and expenditures.
    - ASLRC's Quarterly Reports (“Quarterly Reports”), which shows operating revenues and expenses booked in the general ledger using accrual accounting procedures.
    - CEFA's Annual Audited Consolidated Financial Statements (“Annual Financial Statements”), which includes attachments showing certain Cal Loan operating activity.

Overview of Work Performed, Results, and Recommendations and Considerations

At CEFA's request, Macias, Gini, and O'Connell (Macias) (1) reconciled past operating activity shown in ASLRC's fiscal year-end Quarterly Reports to CEFA's annual audited financial statements and the Trustee Statements in order to highlight any differences, and (2) projected future cash collections and expenses to assess whether cash-on-hand at the end of FY 2012 and cash generated from future operations would provide sufficient funds to redeem the remaining $6 million in outstanding Bonds. This work was not an audit, but rather an accounting reconciliation. Our reconciliation work revealed two areas where the operating activity showed differences, as follows:

1) Student loan interest revenue shown in ASLRC's fourth quarter year-end Quarterly Reports was significantly higher than actual cash collections of interest shown in the Trustee Statements. The large difference is due to ASLRC accruing interest revenue on both performing and non-performing loans.
2) Significant increases in loan loss provisions were occurring after ASLRC submitted its fiscal year-end Quarterly Report to CEFA. While the increases are reflected in CEFA's Audited Financial Statements, the amount of the increase is not readily apparent because loan loss provisions are aggregated with other operating expenses and only the total is reported.

In light of these differences, we recommended that CEFA request additional financial information from ASLRC to enhance the communication and transparency of Cal Loan operating results, as follows:

- In the Quarterly Reports, include a reconciliation of cash receipts and expenditures to accrual basis revenue and expenses, with significant differences highlighted.
- Report increases in loan loss provisions that are not reflected in the Quarterly Reports submitted to CEFA.

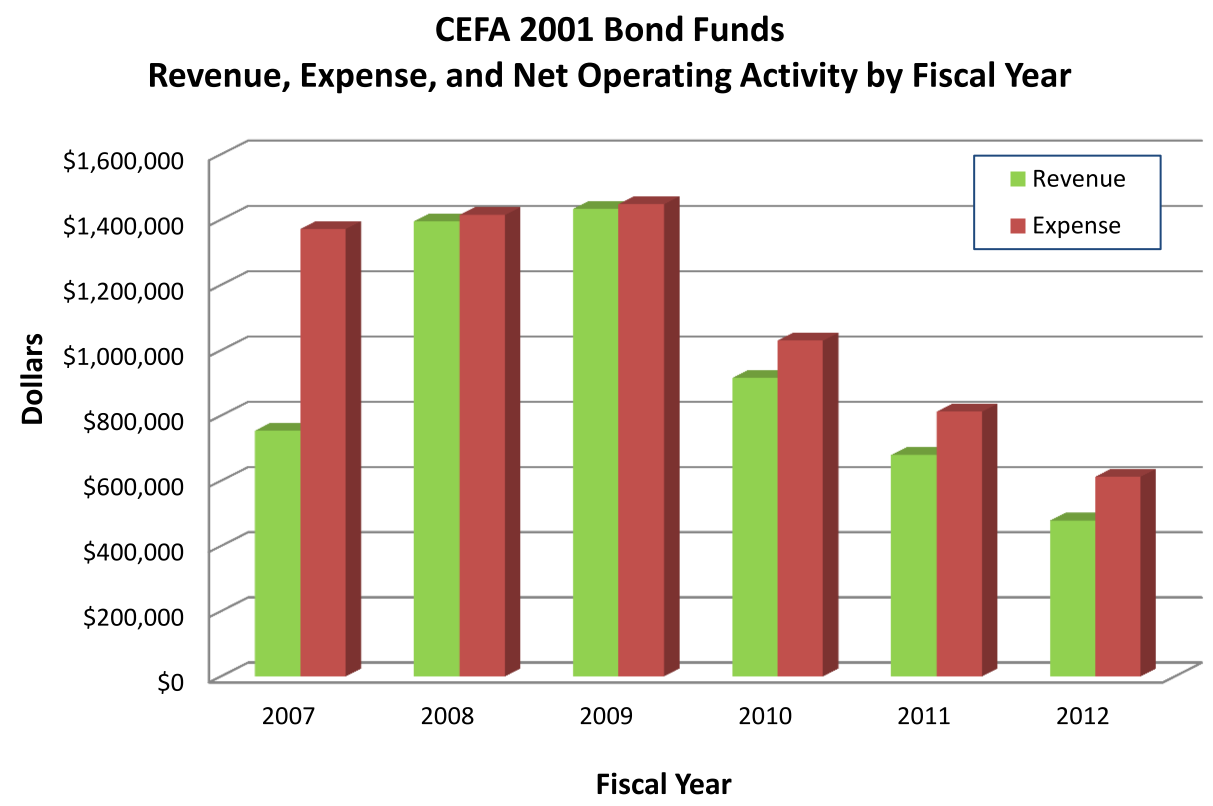
Our projections of future operating activity indicate that a shortfall of up to $4 million may exist after performing loans are paid off in the next 5 years. To minimize the potential shortfalls, we recommended CEFA consider:

- Redeeming bonds early to reduce annual bond interest expenses (bond interest is $54,000 per year per million in bonds outstanding).
- Implementing more aggressive collection strategies for non-performing loans.

Past Cal Loan Operating Activity

- Chart 1 shows that between the fiscal years 2007 and 2012 cash collections of interest on student loans, late payment fees, and interest earned on Trustee investments did not cover operating expenses for Bond interest, third-party administrative fees, and Trustee fees.

Chart 1: Comparison of Cash Revenue to Expenses FY 2007 - 2012 for the 2001 Bond Program

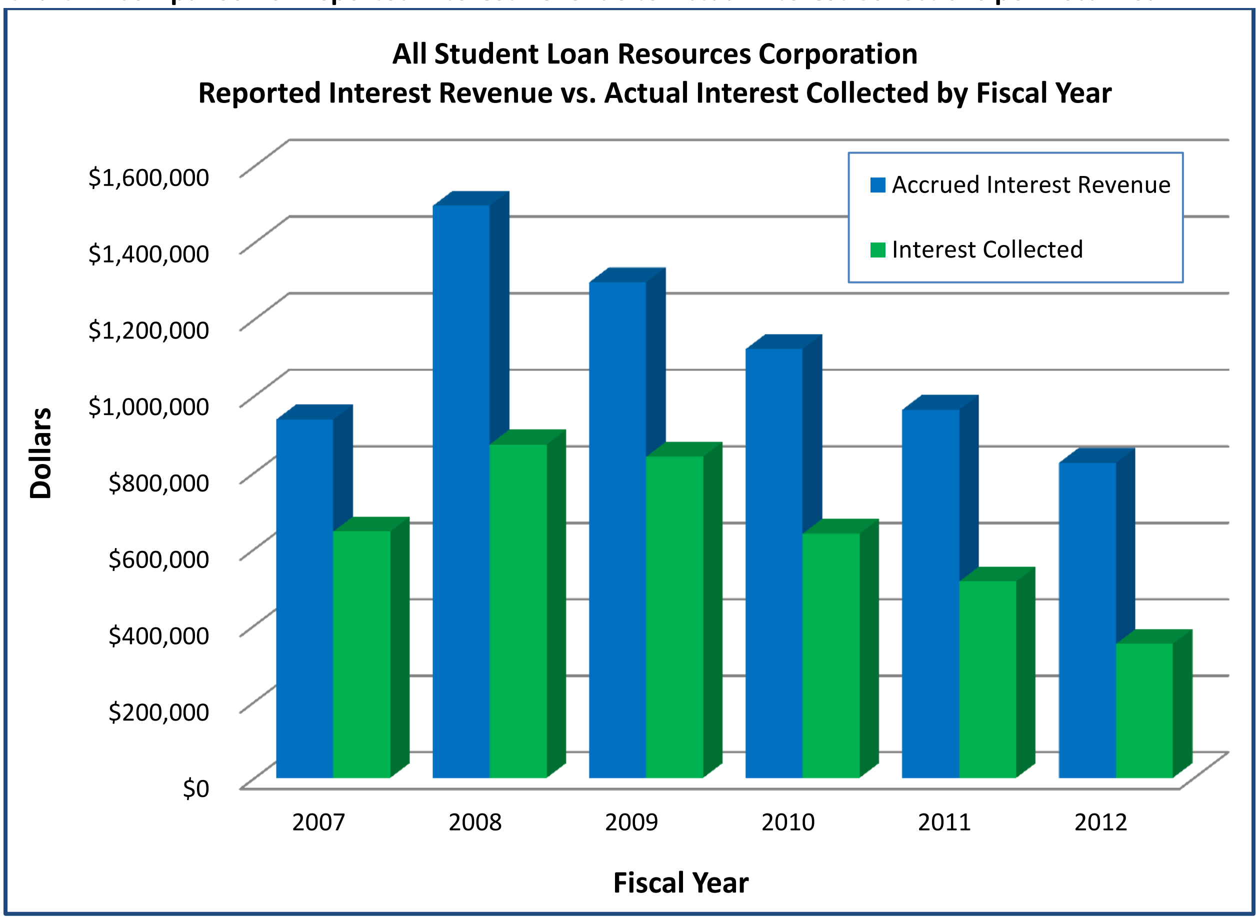


Based on Trustee Statements

Fiscal Year	2007	2008	2009	2010	2011	2012
Revenue	$754,144	$1,395,448	$1,432,963	$915,181	$679,349	$478,343
Expense	$1,371,880	$1,414,419	$1,447,758	$1,029,951	$812,094	$612,846
Net Operating Activity	($617,736)	($18,971)	($14,795)	($114,770)	($132,745)	($134,503)

- Chart 2 illustrates the difference between accrued interest revenue and actual interest collected each fiscal year, as reflected in the Quarterly Reports and Trustee Statements, respectively. The difference between interest revenue accrued and that actually collected is accounted for as a loan loss provision expense each year. ASLRC management informed Macias that approximately $1,075,000 of the $1,295,863 in operating expenses reported in CEFA's FY 2012 Annual Financial Statements were due to loan losses of interest and principal.

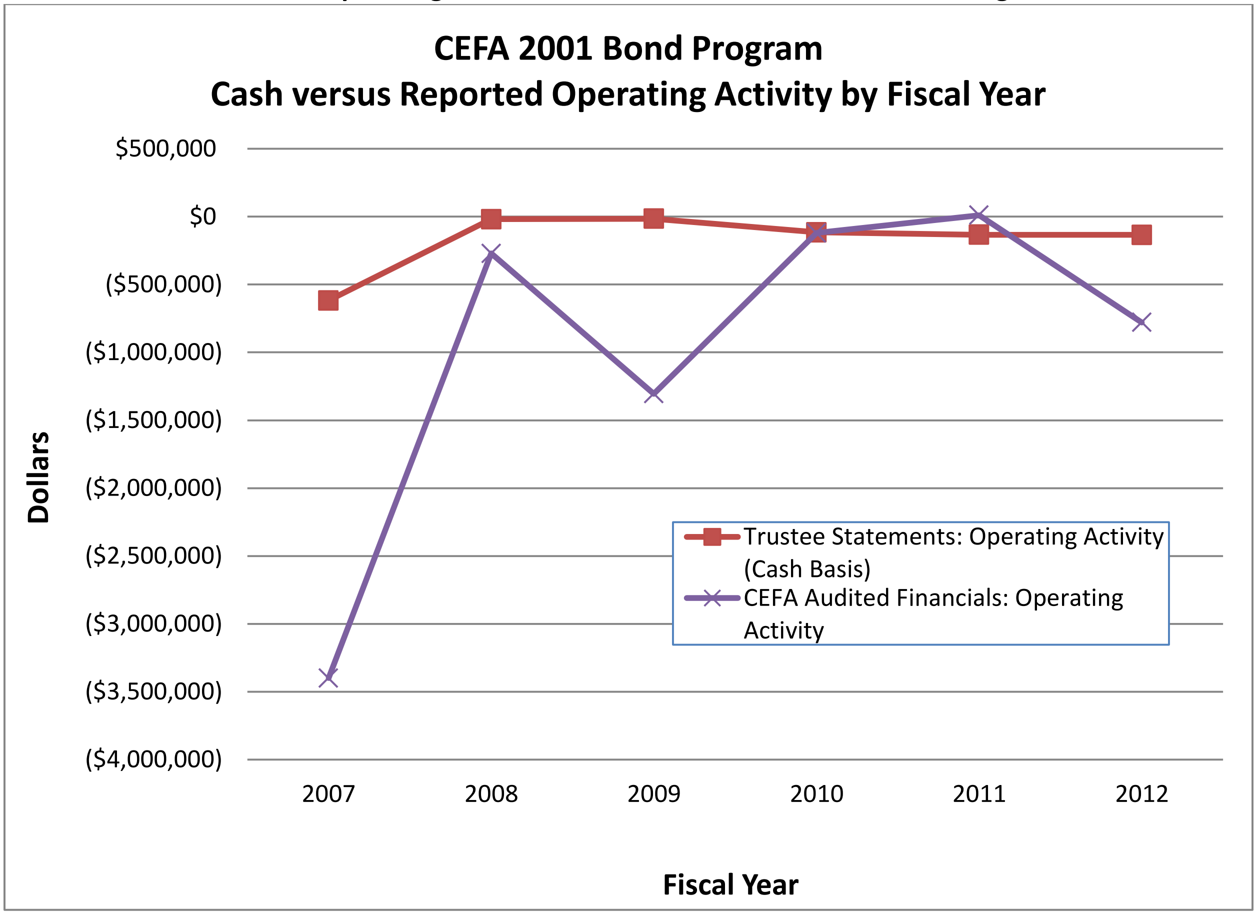
Chart 2: Comparison of Reported Interest Revenue to Actual Interest Collections per Fiscal Year



Fiscal Year	2007	2008	2009	2010	2011	2012
Accrued Interest Revenue	$938,142	$1,495,790	$1,296,199	$1,121,740	$963,307	$824,771
Interest Collected	$645,079	$872,873	$840,818	$639,456	$514,088	$350,815

- Chart 3 shows operating activity reported in CEFA's Annual Financial Statements and actual cash activity from the Trustee Statements. The difference between cash operating activity and the activity reported in CEFA's Annual Financial Statements is due to reporting of the loan loss provisions.

Chart 3: Comparison of Operating Activity in reported CEFA's Annual Financial Statements to the Trustee Statements' Cash Operating Results FY 2007 - 2012 for the 2001 Bond Program



	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
■ Trustee Statements: Operating Activity, Cash	($617,736)	($18,971)	($14,795)	($114,770)	($132,745)	($134,503)
× CEFA Financials: Operating Activity	($3,399,513)	($271,395)	($1,305,292)	($119,429)	$11,383	($778,841)

Projected Future Cal Loan Operating Activity

- Based on historical trends, Macias projected cash collections and expenses into the future to assess whether cash-on-hand as of June 30, 2012 and cash generated from future operations would provide sufficient funds to redeem the remaining $6 million in Bonds that were outstanding as of December 31, 2012.

    - Performing loans
        - Performing loans of $2.3 million as of June 30, 2012
        - Most of the performing loans will be closed out over the next 5 years, as shown in table 1 below.
        - Collecting on only performing loans over the next 5 years is likely to result in up to $4 million in bonds remaining outstanding
        - Macias' analysis of actual activity in the first half of FY 2012-13, indicates that collections have exceeded projections by a little over $100,000.

Table 1: Projected Cal Loan Activity

	FY 2013	2014	2015	2016	2017	Total
Beginning Bank Balance	$1,969,391	$884,400	$30,650	$103,050	$100,250	$1,969,391
Projected Income from Interest and Late Fees	$175,000	$86,250	$53,400	$30,700	$10,200	$355,550
Administration Expenses	($120,000)	($110,000)	($100,000)	($90,000)	($80,000)	($500,000)
Bond Interest	($340,000)	($270,000)	($216,000)	($216,000)	($216,000)	($1,258,000)
Operating Income (Loss)	($285,000)	($293,750)	($262,600)	($275,300)	($285,800)	($1,402,450)
Loan Principal Payments	$900,000	$540,000	$335,000	$272,500	$272,500	$2,320,000
Bond Redemptions	($1,700,000)	($1,100,000)	$0	$0	$0	($2,800,000)
Ending Bank Balance	$884,391	$30,650	$103,050	$100,250	$86,950	$86,941
Bonds Outstanding at Year End	$5,100,000	$4,000,000	$4,000,000	$4,000,000	$4,000,000	
Performing Loans Outstanding at Year End	$1,420,000	$880,000	$545,000	$272,500	$0	

- Non-performing loans
  - Non-performing loans totaled $7.3 million as of June 30, 2012 with an additional $3 million in uncollected interest on these loans at that date.
  - Cost/benefit of increased collection efforts are unknown.
  - Collection efforts will need to net approximately 40% of the non-performing loan principal and interest outstanding as of June 30, 2012 to generate sufficient funds to redeem all outstanding bonds