CALIFORNIA EDUCATIONAL FACILITIES AUTHORITY
Cal Loan Collection Proposal

Staff Summary of
Resolution no. 2004-6

August 26, 2004

ISSUE:

As of July 31, 2004, the California Alternative Loan Marketing Association (Callie Mae), the administrator for the Cal Loan Program, has identified 134 borrowers with 211 loans in default, which total approximately $1.7 million that were funded by the 1997A and 2001A Bonds for which CEFA is the guarantor. Callie Mae has developed procedures to collect on the identified defaulted loans and/or ascertain the reason(s) for non-payment so that proper action(s) can be taken.

BACKGROUND:

In August 1997, CEFA issued a $30 million bond for an alternative student loan program administered by the California Alternative Loan Marketing Association (Callie Mae). For this bond issue, the participating institutions are liable for the first 12% of defaulted loans, after which CEFA becomes liable for the next 5% of defaulted loans. In August 2001, a second bond was issued for the program in the amount of $45 million. For this second bond issue, the guarantee positions were reversed by which CEFA is liable for the first 5% of defaulted loans and the participating institutions are liable for the next 12% of defaulted loans.

The terms of the Cal Loan Program 1997A and 2001A Bonds specify the guaranty positions of the participating institutions and CEFA, but there are no provisions or guidance for collection on these defaulted loans in the bond documents. The procedures proposed by Callie Mae are loosely based on the Federal Family Education Loan Program (FFELP) in order to use FFELP forms, rather than creating new ones, etc. The proposal created by Callie Mae is not identical to the FFELP procedures, since it contains items such as interest waivers to compel borrowers to repay.

PROPOSED COLLECTION PROCEDURES:

The proposed collection procedures (see Attachment A) seek flexibility and levels of loan forgiveness by CEFA. Specifically, the proposed collection procedures would require CEFA to:

- Accept FFELP forms for the purposes of deferring or discharging (in the case of permanent or total disability) the Cal Loan

- Allow the removal of “Default” on the borrower’s credit report upon receipt of 12 monthly, on-time payments

- Refer the borrower who is able, but unwilling to establish repayment to a collection agency, an attorney or for wage garnishment to compel repayment.

- Waive interest during certain deferment period as an incentive to the borrower to resume repayment after the deferment.

- Write off debt if borrower dies or becomes permanently/totally disabled.

Approving these actions will result in several costs to CEFA.

Collection Performance - Callie Mae will execute/perform collection duties with its internal staff, rather than employ a third-party collection agency. The charge to CEFA will be $5 per account, per month. In addition, Callie Mae will charge CEFA any out of pocket expenses, e.g. skip search services, filing fees, credit reports, etc. Monthly payments to Callie Mae will be due and payable, as per the standard invoice payment agreement specified in the existing Administration Agreement.

Once the account becomes current, Callie Mae will reinstate the account for monthly servicing at which point Callie Mae will discontinue the $5.00 per account, per month charge.

Based on the identified loans in default, the cost to CEFA would be approximately $13,000 over the next 12 months.

Interest Waiver – Callie Mae has proposed waiving interest during certain qualified periods as an incentive for a borrower to resume payment. For example, if the proposed collection procedures are approved, a student attending a non-Cal Loan participating institution could extend the deferment period for principal and interest payments. Currently, a student attending a non-Cal Loan participating institution is required to pay interest during this time. Two other examples involve a student attending school at least half time and less than twelve hours or a student extending deferment due to a disability. Under the proposed procedures, CEFA would waive interest payments by extending the deferment period while these circumstances are on-going. The Administrator estimates these scenarios apply to 20% of the portfolio.

The cost to CEFA by extending the deferment period in the two examples stated would be a cash flow, not necessarily a real expense. The students would be required to repay both principal and interest, however the payments would be deferred until the specific reason for additional deferment (school attendance or a disability period) is complete.

A true interest waiver under the proposed collection procedures involves military attendance. Callie Mae's proposal suggests waiving interest for students in the military. While repayments would resume after military service, waiving interest completely during service may compel students in this situation with a defaulted loan(s) to repay.

The Administrator estimates this situation applies to 0.10% of the portfolio, which would result in an approximate annual cost to CEFA of $1,800.

Debt write-off – Based on statistical analysis from Callie Mae's FFELP loan portfolio, 0.10% of borrowers die or become permanently/totally disabled. Using this percentage, debt write-off under these circumstances could cost the Authority approximately $1,700 this year based on the current default data.

In summary, based on the current default data, approximate annual costs to CEFA over the next twelve months will be $17,000. Scheduled student loans repayments will be on-going over the next 17 years. If the collection proposal is approved, the total length of time students will be in repayment will increase. By assuming all loans will be repaid within the next twenty years, a rough estimate of how much collecting on loans in default is $350,000.

STAFF RECOMMENDATION:

Staff recommends the Authority approve the following requirements that will enable Callie Mae to collect on loans in default for both the 1997A and 2001A Cal Loan Bond issues:

1. Accept FFELP forms for the purposes of deferring or discharging (in the case of permanent or total disability) the Cal Loan.
2. Allow the removal of "Default" on the borrower's credit report upon receipt of 12 monthly, on-time payments.
3. Refer the borrower who is able, but unwilling to establish repayment to a collection agency, an attorney or for wage garnishment to compel repayment.
4. Waive interest during certain deferment periods as an incentive to the borrower to resume repayment after the deferment.
5. Write-off debt if borrower dies or becomes permanently/totally disabled.

Attachment A

CAL LOAN PROGRAM
COLLECTION PROCEDURES FOR 1997A and 2001A BOND DEFAULTS
July 2004

Executive Summary

In August 1997, 1997A Bond was issued to raise capital for funding the Cal Loan Program, an alternative/private loan program that is administered by the California Alternative Loan Marketing Association (Callie Mae or CALMA), on behalf of the California Education Facilities Authority (CEFA). Firstmark Services, Inc. (FMS) services the Cal Loan Program. For the 1997A Bond, the participating institutions are liable for the first 12% of the defaulted loans, after which CEFA becomes liable for the next 5% of defaulted loans.

In August 2001, the $5,000,000 of the 1997A Bond was redeemed, and a new bond, $45,000,000 2001A Bond, was issued to raise capital for additional funding the Cal Loan Program. For this new bond issuance the guarantee positions were reversed by which CEFA is liable for the first 5% of defaulted Cal Loans, and the participating institutions are liable for the next 12% of the defaulted Cal Loans.

As of July 31, 2004, there were 211 loans for 134 borrowers that were in default and for which CEFA was the guarantor. 76 loans for 35 borrowers were funded by the 1997A bond, and 135 loans for 99 borrowers were funded by the 2001A bond.

The Administration Agreement between CEFA and CALMA, dated as of March 1, 1997 and as amended and restated as of September 1, 1999 ("the Agreement"), does not stipulate a provision for collecting on the defaulted Cal Loans for which CEFA is the guarantor. Therefore, CALMA has developed the procedures below for submission to CEFA as a proposal to collect on the defaulted Cal Loans that were funded by the 1997A and 2001A Bond, and for which CEFA is responsible.

Objectives

The objectives of the procedures below are to:

1. Identify all of the defaulted Cal Loans that were funded by the 1997A and 2001A bonds, and for which CEFA is responsible. Select a sample of the defaulted loans to determine reasons for default and non-payment. Prioritize collection efforts by the oldest default dates and the highest principal balances.
2. If the borrower is able to establish repayment, compel borrower to do so by offering certain benefits and explaining consequences of default.
3. If the borrower has legitimate and/or compelling reason(s) for non-payment, offer the borrower appropriate options for deferring/forbearing payments.
4. If the borrower's loan(s) are determined to be eligible for write-off, obtain appropriate documentation for recommending to CEFA the discharge of the loan(s).

Assumptions

The procedures incorporate the following assumptions:

- CEFA will accept valid FFELP forms for the purposes of deferring the Cal Loan
- CEFA will allow the removal of the "Default" on the borrower's credit report upon receipt of 12 monthly, on-time payments as an incentive for establishing monthly repayment.
- CEFA will refer the borrower who is able, but unwilling to establish repayment to a collection agency, an attorney, or for wage garnishment to compel repayment.
- CEFA will waive interest payments during certain deferment period as an incentive to the borrower to resume repayment after the deferment.
- CEFA will agree to write off debt if borrower dies or becomes permanently/totally disabled (based on receipt of proper/valid documentation.)

CALMA Compensation

The collection procedures below were designed to be performed by CALMA internal staff, rather than employing a third-party collection agency. CALMA will collect and charge CEFA a $5.00 per account, per month charge. In addition, CALMA will charge CEFA any out-of-pocket expenses, e.g., skip search services, filing fees, credit reports, etc. Out-of pocket expenses are anticipated to be nominal, but are not subject to estimation at this time. For example, filing fees are required to make a claim against the estate of a deceased borrower. Monthly payment to CALMA will be due and payable, as per the standard invoice payment agreement on "the Agreement."

Once the account becomes current, FMS will be responsible for monthly servicing of the account, at which point, CALMA will discontinue the $5.00 per account, per month charge.

Estimated Principal and Interest Waivers

<u>Death and Disability Claims</u>

Because there are no provisions for loan write-offs for death and permanent/total disability claims in the Cal Loan Program, there is no data available with this information. However, based on ALL Student Loan Corporation's Federal Family Education Loan Program portfolio, approximately 0.10% of borrowers have claims paid/pending due to death or disability, as of July 31, 2004.

Deferment and Forbearance Interest

Based on the interest accrual analysis of the defaulted Cal Loans that were funded by 1997A and 2001A Bonds, the monthly interest accruing is $10,600 per month. This will increase as additional defaulted loans are added to the pool.

In addition, total outstanding accrued interest as of July 31, 2004 is $123,087.00.

Procedures

The procedures set forth below have been reviewed by CALMA's legal counsel to ensure that they meet all of the regulatory requirements and applicable laws with regard to the collection of debts relating to defaulted student loans.

1. Create a spreadsheet of the defaulted borrowers, with the following data elements:
   - SSN
   - Last Name
   - First Names
   - Loan Date(s)
   - Loan Amount(s)
   - Default Date
   - School Name
   - Address (street, city, state, zip)
   - Phone number
   - Columns for documenting phone attempts (date/time) and mailing of correspondence
   - Columns for documenting results of successful contacts and any required follow-up.

2. Call the borrower within the legally allowed timeframes and not at any unusual or inconvenient time or place. (Call between 9AM to 7PM of the borrower's time zone.)

3. In any subsequent communications with the borrower, state that the communication is from a debt collector attempting to collect on defaulted Cal Loan(s).

4. Within 5 days of the initial communication, send a written notice to the borrower containing the following (unless the following information was contained in an initial written communication):

   - The amount of the debt;
   - The name of the creditor to whom the debt is owed; and
   - A statement providing that:

     (i) unless the borrower disputes the validity of the debt within 30 days after receipt of the notice, the debt will be assumed valid;

     (ii) if the consumer disputes the debt within the 30 day period, the debt collector will obtain and mail to the consumer a copy of a verification of the debt or a copy of a judgment against the consumer;

(iii) upon the consumer's request within the 30-day period, the debt collector will provide the consumer with the name and address of the original creditor, if different from the current creditor.

The written notice must not use any language or symbol on any envelope or in the contents of any communication effected by the mails or telegram that indicates that the debt collector is in the debt collection business.

5. If the borrower states that an attorney represents him, collector will cease all communication with the borrower immediately, other than to request the name and contact information of the attorney.

6. Successful borrower contact and dispositions:

(i) <u>Borrower is willing and able to make payments</u>: Advise borrower to remit the past due amount of $xxx.xx and to make monthly payments to FMS in the amount of $xx.xx thereafter. Upon receipt of past due payments, we will remove the default remarks on his credit report.

(ii) <u>Borrower is willing but unable to bring his account current</u>: Advise borrower to establish repayment by remitting $xx.xx monthly. Upon receipt of 12 monthly on-time payments, we will remove the default remarks on his credit report.

(iii) <u>Borrower is Permanently and Totally Disabled (Never Employable)</u>: Advise the borrower that if we receive confirmation of his or her permanent and total disability, the loans may be eligible for discharge.

- If borrower has submitted a Permanent & Total Disability form for his FFELP loan(s), request a copy of this document for us to review for possible write-off.
- If borrower has a " loan discharge" letter due to permanent and total disability from the guarantor or the U. S. Department of Education, request a copy of this document.
- If no FFELP, send borrower the FFELP Permanent & Total Disability form for his physician's (must be M.D. or D.O.) certification.

Subject to CEFA Board approval, CEFA would allow discharge of loan based on valid FFELP disability form.

(iv) <u>Borrower is Temporarily and Totally Disabled (Currently Not Employed):</u> Advice the borrower that if we receive confirmation of his or her temporary and total disability, the loans may be eligible for disability deferment. Further advise the borrower that interest will continue to accrue and will capitalize once the deferment expires.

Subject to CEFA Board approval, as an incentive for borrower to resume repayment after disability deferment, CEFA would be willing to waive interest during disability deferment.

- If borrower has submitted a Temporary & Total Disability Deferment form for his FFELP loan(s), request a copy of this document for us to review for possible deferment of Cal Loan for the disability period that is certified on the form.

- If borrower has a current Temporary & Total Disability Deferment approval letter from his lender(s), request a copy of this document.

- If no FFELP, request documentation from Department of Human Services of his State of residence of his or her temporary and total disability.

- If no FFELP and so such documentation from Department of Human Services, send borrower the FFELP Temporary & Total Disability Deferment form for his physician's (M.D. or D.O.) certification.

(v) Borrower is In-school: Advise the borrower that if we receive confirmation of Full Time enrollment status at an eligible FFELP school, the loans may be eligible for In-School deferment. Further advise the borrower that interest will continue to accrue and will capitalize once the deferment expires.

Subject to CEFA Board approval, as an incentive for borrower to resume repayment, CEFA would be willing to waive payment of interest during In-School deferment at attendance at a non-Cal Loan participating institution.

Also, subject to CEFA Board approval, CEFA would allow borrower to be eligible for In-School deferment if the borrower's enrollment is at least Half Time, less than 12 hours.

(vi) Borrower is in Active Bankruptcy: Immediately apologize for the intrusion and explain that we were unaware of the active bankruptcy proceedings.

- Ask if an attorney represents the borrower. If so, request the name and contact information of the attorney.
- If not represented by an attorney, request a copy of his First Meeting of Creditors document or request the bankruptcy court's information (circuit #/address/phone #).

7. Unsuccessful borrower contact and dispositions: Collector may communicate with a third party for the purpose of determining the location of the borrower. Collector must:

- Identify him or herself (but not his employer, unless expressly requested);
- State that he or she is confirming location information concerning the consumer;
- Not state that such consumer owes any debt;

Third party contact may disclose the following information regarding the borrower:

(i) Borrower is Dead: Request a copy of the death certificate or contact who may provide such certificate. Update with appropriate comments on spreadsheet.

(ii) Borrower is in Active Military Deployment Overseas: Request copy of military deployment orders. Update with appropriate comments on spreadsheet.

Subject to CEFA Board approval, as an incentive for borrower to resume repayment after military service, CEFA would be willing to waive interest accrual completely or payment of interest during military service.

(iii) Borrower is Out of the Country: Inquire as to when borrower is expected to return to the U.S. Update with appropriate comments on spreadsheet.

(iv) Borrower Does not Reside at this Address: Request current address/contact information. Update with appropriate comments on spreadsheet.

(v) Borrower is Unknown at this Address: Update with appropriate comments on spreadsheet. Refer to FMS for skip tracing.