Iowa Superintendent of Banking

Annual Review of the Qualified Student Loan Bond Issuer
Iowa Student Loan Liquidity Corporation (ISLLC)
For the fiscal year July 1, 2018 to June 30, 2019

Introduction

Pursuant to paragraph b, subsection 6, of Iowa Code Section 7C.13, the superintendent of banking is required to annually review the qualified student loan bond issuer's total assets, loan volume, and reserves, and it's procedures to inform students about the advantages of loans available under Title IV of the federal Higher Education Act of 1965, as amended, for which the students may be eligible. The review shall also verify that the qualified student loan bond issuer issued bonds in accordance with Iowa Code Chapter 7C in conformance to the letter requesting approval of the governor as set forth in subsection 5, of Iowa Code Section 7C.13. Examiner Joseph Gordon was appointed by Superintendent Jeff Plagge to conduct the review.

Report of Total Assets, Total Liabilities, Loan Volume, Reserves and Affiliates

ISLLC provided audited financial statements dated June 30, 2019 (FY19) which the independent auditors' report noted presented fairly, in all material respects, the financial position of ISLLC as of that date.

As of June 30, 2019, total assets and total deferred outflows of resources* were $1.33 billion. Total assets consisted primarily of net student loans receivable of $1.13 billion and investments of $112.60 million. Total assets and deferred outflows decreased $214.66 million (13.88%) from June 30, 2018 (FY18). Cash and investments decreased $85.10 million (42.58%) compared to FY18. Cash used for on-going operating expenditures, debt service, and loan funding exceeded student loan payment collections. Total use of cash for debt pay down totaled $247 million and was partially offset by proceeds received through the issuance of new notes payable ($51.7 million). A portion of student loan purchase funding was covered through the use of General Fund cash without utilizing proceeds from new debt issuances. Net student loans receivable decreased $114.89 million (9.21%) compared to FY18. The decrease is primarily due to borrower cash receipts being in excess of loan additions and capitalized borrower interest. ISLLC purchased or originated $111.7 million in student loans during FY19, a decrease from the $153.9 million during the same period in FY18. The in-school loan product was the biggest component of new volume at $64 million. Loan refinance and the purchase of outside student loan portfolios made up the rest of the new volume amount. While both investments and student loans decreased during FY19, accrued interest receivable increased $1.77 million (6.61%) due to increases in variable interest rates that offset the declining asset base.

Government guaranteed loans made up 37.71% of the student loan portfolio with private loans being the remaining 62.29% at the end of FY19 compared to 38.77% government loans and 61.23% private at the end of FY18. Federally insured student loans currently carry a 97% guaranty of the principal and interest on loans disbursed after July 1, 2006, while there is no guaranty for private loans. ISLLC management periodically reviews the student loan portfolio performance and evaluates the probability of losses to determine its allowance for loan loss reserve (ALL). The ALL evaluation on the federally insured loan portfolio is conducted separately from the private loan portfolio. ISLLC considers a private loan to be in a default status when it reaches 120 days delinquent. For defaulted loans, a 100% allowance is applied to the outstanding principal balance for the allowance calculation less a future recovery factor for certain loan types. For all other nondefaulted private loans a net allowance percentage based on historical experience is applied to the outstanding principal balance A private loan is charged-off when the loan reaches 270 days delinquent without any principal or interest payment activity during the previous 12 months. ISLLC established a loan loss reserve of 0.10% on the government portfolio ($0.44 million) and 2.12% on the private portfolio ($15.19 million) in FY19. At the end of FY18 the loan loss reserve for government loans was 0.09% ($0.45 million) and 2.04% ($15.77 million) for private loans.

ISLLC had cash deposits of $2.13 million, which were covered by federal depository insurance or collateralized trust accounts. Investments of $112.60 million included $10.14 million of corporate notes/bonds and $102.46 million of money market mutual funds investing in United States government and agency obligations.

Total liabilities decreased $201.50 million (20.40%) as compared to FY18 with debt activity making up most of the change. Bond and note maturities totaled $247.3 million and were offset by the issuance of notes payable totaling $51.7 million. A portion of the new note issuance ($23.7 million) was used to refund existing debt.

Deferred inflows of resources*, which includes refundable origination fees and deferred gains on refunded debt activities, decreased $16.00 million (34.56%) compared to FY18. The refundable origination fee decrease of $0.2 million is primarily due to normal amortization and changes due to early loan payoff activity. ISLLC does not charge a fee on newly originated loan volume. The decrease of $15.82 million in deferred gain on refunded debt activity includes amortization and is based on changes in applicable outstanding debt.

ISLLC's net position (similar to the net worth of a for-profit company) at the end of FY19 was $515.65 million, a $2.82 million (0.55%) increase from FY18.

Total operating revenues for FY19 were $74.85 million, an increase of $2.33 million (3.22%) from FY18. Investment income remained flat in FY19 compared to FY18. Student loan interest income increased $2.02 million (3.21%) compared to FY18. ISLLC's average owned outstanding student loan portfolio decreased $89.5 million (6.23%) in FY19. This outstanding balance decline and impacts to student loan interest income was offset by better yields (an average increase of 42 bps). Borrower interest allowance adjustments on defaulted private loans reduced student loan interest income by $1.3 million in FY 19 compared to a $3.1 million reduction in FY18.

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Total operating expenses for FY19 were $72.02 million, an increase of $2.44 million (3.51%) over FY18. Total interest expense on bonds and notes payable during FY19 increased $1.31 million (3.60%) from FY18. Average debt outstanding decreased from FY18 to FY19 by $109.1 million (10.69%). This was offset by increased debt yields during FY19 of 57 bps and contributed to increased debt interest expense. Debt-related expenses decreased by $1.5 million in FY19 compared to the FY18 amount. Most of this decrease relates to lower cost of issuance expense incurred during FY19 compared to FY18 due to less new debt issuances. The provision for loan losses, related primarily to private loans, increased $0.5 million in FY19 when compared to FY18.

With a $515.65 million total net position, loan loss reserves of $15.62 million and an investment policy requiring cash deposits to be back by federal depository insurance or collateralized trust accounts, investments only in U.S. government/agency obligations, highly rated corporate notes and commercial paper, it appears ISLLC has adequately protected the organization's assets from potential future losses.

Aspire Resources, Inc. (ARI), a wholly owned for profit subsidiary of ISLLC, was incorporated in 2001 to provide services not related to ISLLC nonprofit purpose. ARI has developed systems and procedures for loan origination and disbursement related process including the functions of electronic data transmissions management, web reporting, loan information deliver, and centralized loan disbursement services. ARI also provides on-going portfolio servicing for student loan portfolios. ARI's board of directors is appointed by the board of ISLLC but operates independently with members who are not members of ISLLC's board. ARI and ISLLC share operating costs with interfund payables/receivables reflecting the net activity associated with the shared services.

ARI is reported as a discretely presented component unit of ISLLC. Total assets for FY19 were $45.81 million, total liabilities $8.95 million and a net position $36.86 million. For FY19 total operating revenues were $19.55 million and total operating expenses $18.61 million, resulting in a net income of $937,389.

In addition to $12.08 million in cash, ARI had $26.39 million invested in United States agency obligations and $634,579 in money market mutual funds investing in United States government and agency obligations.

At the end of FY19, ARI was servicing 336,833 student loans with an outstanding principal balance of $2.45 billion.

* The Governmental Accounting Standards Board (GASB) defines deferred outflows of resources as a consumption of net assets that is applicable to a future reporting period and deferred inflows of resources as an acquisition of net assets that is applicable to a future reporting period. Deferred outflows of resources have a positive effect on net position that is similar to assets, but are not assets, and likewise deferred inflows of resources have a negative effect on net position but are not liabilities. Thus, the GASB requires them to be identified separately from the assets and liabilities.

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Review of Procedures to Inform Students of Advantages of Title IV Loans

ISLLC has established adequate procedures to inform students about the advantages of loans for which the students may be eligible that are available under Title IV of the Federal Higher Education Act.

ISLLC's online application site contains the statement that Iowa Student Loan's Partnership and College Family loans are designed to supplement-not replace- other sources to fill funding gaps for students and parents. Students and parents should work with financial aid professionals at their respective colleges and universities to explore and exhaust all sources of student financial aid before seeking a private loan. To determine eligibility there is a link that directs the applicant to the Federal Student Aid site of the U.S. Department of Education.

Disclosures given at the time a student or parent applies for a private student loan include extensive information about the cost of guaranteed student loans versus private student loans. In addition, the loan programs are described as supplements to, not replacement of, federal, state, or institutional sources of funding for education costs.

Verification of Compliance with Tax-exempt Bond Issuing Requirements

ISLLC did not issue any tax-exempt bonds during the fiscal year under review.

Respectfully submitted,

Joseph T. Gordon

Joseph T. Gordon, Examiner-in-Charge

Jeff Plagge

Jeff Plagge, Iowa Superintendent of Banking

January 8, 2020

Date