



STATE OF ILLINOIS
**OFFICE OF THE
AUDITOR GENERAL**

William G. Holland, Auditor General

SUMMARY REPORT DIGEST

**ILLINOIS STUDENT ASSISTANCE COMMISSION –
ILLINOIS DESIGNATED ACCOUNT PURCHASE PROGRAM**

FINANCIAL AUDIT

For the Year Ended: June 30, 2010

Release Date: April 7, 2011

Summary of Findings:

Total this audit:	5
Total last audit:	3
Repeated from last audit:	2

INTRODUCTION

This report covers our financial audit of the Illinois Student Assistance Commission (Commission) – Illinois Designated Account Purchase Program (IDAPP) as of June 30, 2010 and for the year then ended.

SYNOPSIS

- IDAPP did not provide auditors with complete and accurate financial statements on a timely basis.
- IDAPP did not properly apply student loan payments to principal and interest.
- IDAPP invested in a money market mutual fund with holdings in securities not permitted by its investment policy.

{Expenditures and Activity Measures are summarized on the reverse page.}

ILLINOIS STUDENT ASSISTANCE COMMISSION
ILLINOIS DESIGNATED ACCOUNT PURCHASE PROGRAM
FINANCIAL AUDIT
For The Year Ended June 30, 2010 (in thousands)

STATEMENT OF NET ASSETS	2010	2009
Unrestricted assets		
Cash and investments.....	\$ 731	\$ 1,131
Capital assets, net.....	25	34
Restricted assets		
Cash and cash equivalents.....	49,108	\$ 61,822
Investments.....	229,436	138,999
Student loans receivable, net.....	1,107,530	1,200,037
Notes receivable, net.....	16,520	43,209
Accrued interest.....	21,563	25,549
Other.....	1,475	5,107
Total.....	<u>\$ 1,426,388</u>	<u>\$ 1,475,888</u>
Liabilities		
Accounts payable and accrued liabilities.....	\$ 1,064	\$ 1,918
Accrued interest payable.....	1,567	1,556
Federal special allowance and interest subsidy.....	2,820	2,677
Revolving credit lines.....	360,175	398,947
Revenue bonds payable.....	1,019,701	1,027,300
Other.....	4,482	3,984
Total.....	<u>\$ 1,389,809</u>	<u>\$ 1,436,382</u>
Net Assets		
Invested in capital assets, net of related debt....	\$ 25	\$ 34
Restricted.....	41,369	46,921
Unrestricted.....	(4,815)	(7,449)
Total.....	<u>\$ 36,579</u>	<u>\$ 39,506</u>

REVENUES, EXPENSE AND CHANGES IN NET ASSETS	2010	2009
Operating revenues		
Interest - student loans.....	\$ 44,340	\$ 49,495
Interest - investments.....	5,237	1,314
Net increase in the fair value of investments....	3,227	-
Fees.....	2,268	-
Total.....	<u>\$ 55,072</u>	<u>\$ 50,809</u>
Operating expenses		
Student loan costs and fees.....	\$ 14,386	\$ 9,101
Interest on revenue bonds.....	12,603	29,903
Salaries and employee benefits.....	6,316	6,101
External loan servicing.....	5,493	3,515
Management and professional services.....	3,435	3,596
Other.....	3,237	5,785
Total.....	<u>\$ 45,470</u>	<u>\$ 58,001</u>
Operating income		
Federal special allowance and excess interest..	(11,779)	(1,891)
Special item.....	-	(2,730)
Transfers to ISAC.....	(750)	-
Change in net assets.....	<u>\$ (2,927)</u>	<u>\$ (11,813)</u>

AGENCY EXECUTIVE DIRECTOR
During Examination Period: Mr. Andrew Davis
Currently: Mr. Andrew Davis

FINDINGS, CONCLUSIONS, AND
RECOMMENDATIONS

**FINANCIAL REPORTING PROCESS NEEDS
IMPROVEMENT**

**Insufficient controls over
financial reporting**

The Illinois Student Assistance Commission (Illinois Designated Account Purchase Program) did not provide the auditors with complete and accurate financial statements on a timely basis. Also, the Illinois Designated Account Purchase Program (IDAPP) does not have sufficient control over financial reporting.

**Management changes occurred
long after the agreed upon
deadline**

During the audit entrance conference on May 11, 2010, a deadline for submission of IDAPP's draft financial statements was determined and agreed to by the auditors and IDAPP management. The deadline for delivery of the complete draft financial statements to the auditors for fiscal year 2010 was October 1, 2010. An initial draft was provided to the auditors on September 30, 2010, which was incomplete and had not been fully reviewed by the Commission and all parties involved with the preparation and approval of the financial statements. Changes and adjustments to the initial draft occurred as late as November 15, 2010, 46 days after the agreed upon deadline, when several reclassifications and other changes were made affecting the financial statements and note disclosures.

Errors and omissions identified

Several errors and omissions were identified and corrected during the audit of the draft financial statements for IDAPP. Some of the more significant items were as follows:

Transfers out of balance

- Transfers in and out were out of balance, requiring an adjusting entry in the amount of \$750,000 to the general ledger.

Accrued benefits not recorded

- Severance accruals in the amount of \$137,000 relating to benefits for terminated employees were not recorded in the draft financial statements.

**Write off of uncollectible note not
made timely**

- An adjustment to write off uncollectible notes receivable in the amount of \$683,000 was not made timely.

Pledged revenues not disclosed

- Pledged revenue disclosures were not reported for the 2009 series debt issuances in the draft financial statements.

According to IDAPP management, changes subsequent to the initial delivery of the draft financial statements were the result of the ongoing review of the financials by the Commission and the Illinois Office of the Comptroller. (Finding 2, pages 30-31) **This finding was first reported in 2008.**

Comprehensive look at financial reporting process needed

We recommend the Commission improve controls over financial reporting to ensure accurate presentation and disclosure of IDAPP's annual financial statements. The Commission should take a comprehensive look at the entire financial reporting process and make changes needed to timely release financial reports to users and to auditors.

Auditors' recommendation accepted

IDAPP officials accepted our recommendation and stated it's reviewing all of its policies and procedures regarding the close process and the preparation of the financial statements. (For the previous IDAPP response, see Digest footnote #1)

STUDENT LOAN PAYMENTS NOT PROCESSED CORRECTLY

Student loan payments not properly applied

IDAPP did not properly apply student loan payments to principal and interest.

Errors in the application of payments between principal and interest

IDAPP utilizes several external service organizations to manage and monitor its student loan portfolio. During our testing of student loan payments, we noted that for four out of twelve (33%) payments sampled for one of the service organizations, there were errors in the application of the payments between principal and interest.

Retrospective calculation performed on each loan

IDAPP management acknowledged it was aware of a system problem relating to the processing of payments at this service provider. Subsequent to IDAPP's fiscal year ended June 30, 2010, the service provider performed a retrospective calculation for each loan possibly affected by this situation. In addition, IDAPP has hired an independent third party entity to review this retrospective calculation for propriety. Based on the review performed by the service provider, misapplied payments as of June 30, 2010 totaled approximately \$291,000, resulting in an understatement of IDAPP's student loan receivable balance by the same amount. This amount was deemed immaterial and was not recorded at year end.

Independent third party hired to review recalculations

Error due to computer program

According to IDAPP management, this situation occurred due to the way the computer program used by the service organization handled forbearances, deferments and the related capitalized interest.

The service provider in question manages approximately \$312 million of IDAPP's student loan portfolio as of June 30, 2010. This represents 28% of the student loan receivable balance of \$1,107 million at fiscal year end 2010. Misapplication of student loan payments between interest and principal could result in IDAPP's student loan receivable and operating revenue being misstated. Additionally, misapplication of payments could lead to certain borrowers "paying off their loan" when a balance actually remains, or over-paying the remaining loan

Errors could accumulate to more significant amount

balance. Although individual payments misapplied during the year ended June 30, 2010 appear to be insignificant, these amounts can accumulate throughout the years to a more significant amount. (Finding 3, pages 32-33)

Close monitoring of each service organization recommended

We recommended IDAPP management closely monitor each service organization used to manage its student loan portfolio. Reviews of the service organization's processes and controls should be performed on a periodic basis.

Auditors' recommendation accepted

IDAPP officials accepted the auditors' recommendation and indicated it has a process to review the reports on controls of all the outside service providers and follows up on any findings that are deemed material weaknesses.

NONCOMPLIANCE WITH INVESTMENT POLICY

Investment not permitted by IDAPP policy

IDAPP invested in a money market mutual fund with holdings in securities not permitted by its investment policy.

\$13.4 million invested in corporate debt securities

As of June 30, 2010, the Illinois Designated Account Purchase Program (IDAPP) had invested \$13.4 million in a Fund, which invests in corporate debt securities that were not guaranteed by the full faith and credit of the United States of America as required by the investment policy. This investment was approximately 5% of IDAPP's total investment balance as of the fiscal year end 2010. (Finding 4, pages 34-35)

Policy required investments in US backed securities

We recommended IDAPP improve controls over investments to ensure that it is in compliance with its investment policies. Further IDAPP should reinvest the money invested in the money market fund in violation of its investment policy to an allowable investment vehicle.

Auditors' recommendation accepted

IDAPP officials accepted our recommendation and indicated the non-compliant investment was sold and the funds moved into a compliant investment on December 16, 2010.

AUDITORS' OPINION

Our auditors stated the financial statements of the IDAPP are fairly presented in all material respects.



WILLIAM G. HOLLAND
Auditor General

WGH:JAF:pp

SPECIAL ASSISTANT AUDITORS

Our special assistant auditors for this audit were McGladrey & Pullen LLP.

DIGEST FOOTNOTE

#1 – Financial Reporting Process Needs Improvement

We accept the recommendation. IDAPP is reviewing all of its policies and procedures regarding the close process and the preparation of the financial statements. Quality control checks will be put in place to ensure the submission of accurate financial statements.