Department of Education

HISTORICALLY BLACK COLLEGE AND UNIVERSITY CAPITAL FINANCING PROGRAM ACCOUNT

Fiscal Year 2010 Budget Request

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HISTORICALLY BLACK COLLEGE AND UNIVERSITY
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[Notwithstanding the limitations contained in section 344(a) of the Higher Education Act of 1965 (“HEA”), the aggregate principal amount of outstanding bonds insured under the Historically Black College and University Capital Financing Program is authorized to equal but not exceed $725,000,000, which may be used for loans to public and private historically Black colleges and universities without regard to paragraphs (1) and (2) of section 344(a).] [1]

For the cost of guaranteed loans, [$10,000,000] $20,228,000, as authorized pursuant to [Part] part D of title III of the [HEA] Higher Education Act of 1965 (“HEA”):[2] *Provided*, That such costs, including the cost of modifying such loans, shall be as defined in section 502 of the Congressional Budget Act of 1974: *Provided further*, That these funds are available to subsidize total loan principal, any part of which is to be guaranteed, not to exceed [$100,000,000] $178,221,000.[3] In addition, for administrative expenses to carry out the Historically Black College and University Capital Financing Program entered into pursuant to part D of title III of the HEA, $354,000.[4] (Department of Education Appropriations Act, 2009)

NOTE

Each language provision that is followed by a footnote reference is explained in the Analysis of Language Provisions and Changes document which follows the appropriation language.

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Analysis of Language Provisions and Changes

Language Provision	Explanation
[1] [Notwithstanding the limitations contained in section 344(a) of the Higher Education Act of 1965 ("HEA"), the aggregate principal amount of outstanding bonds insured under the Historically Black College and University Capital Financing Program is authorized to equal but not exceed $725,000,000, which may be used for loans to public and private historically Black colleges and universities without regard to paragraphs (1) and (2) of section 344(a).]	This language increased the total limit on bonds insured under the HBCU Capital Financing Program that was authorized under title III, Part D, of the Higher Education Act of 1965 (HEA), to $725 million, and allowed the program to make loans without regard to the limits on the amount of the program's loan authority devoted to public versus private HBCUs. This language is no longer needed because the limitation on bonds was increased to $1.1 billion and the limits on the authority with respect to public and private HBCUs were increased proportionately when the HEA was reauthorized in P.L. 110-315.
[2] For the cost of guaranteed loans, [$10,000,000] <u>$20,228,000</u>, as authorized pursuant to [Part] <u>part</u> D of title III of the [HEA] <u>Higher Education Act of 1965 ("HEA")</u>:	In accordance with the Federal Credit Reform Act of 1990, the requested language appropriates $20.228 million in subsidy for new loans to be made under the HBCU Capital Financing program. No loans may be insured under the program that would require subsidy above this amount.
[3] *Provided further*, That these funds are available to subsidize total loan principal, any part of which is to be guaranteed, not to exceed [$100,000,000] <u>$178,221,000</u>.	The requested language limits the amount of bonds that may be insured under the HBCU Capital Financing program to $178.221 million in fiscal year 2010.
[4] In addition, for administrative expenses to carry out the Historically Black College and University Capital Financing Program entered into pursuant to part D of title III of the HEA, $354,000.	In accordance with the Federal Credit Reform Act of 1990, this language appropriates funds to administer new loans, service existing loan obligations, and provide technical assistance to prospective and existing program participants.

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Amounts Available for Obligation
($000s)

	2008	2009	2010
Discretionary appropriation:			
Appropriation	$188	$10,354	$20,582
Across-the-board reduction	-3	0	0
Subtotal, discretionary appropriation	185	10,354	20,582
Mandatory appropriation:	18,038	1,541	0
Subtotal, discretionary and mandatory appropriation	18,223	11,895	20,582
Unobligated balance expiring	-30	0	0
Total, direct obligations	18,193	11,895	20,582

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Obligations by Object Classification
($000s)

		2008	2009	2010
11.10	Full-time permanent	$103	$132	$136
11.31	Full-time temporary	0	0	0
11.52	Awards	1	3	3
12.00	Benefits	26	31	32
	Subtotal, personnel	130	166	171
21.00	Travel	13	32	32
23.10	Rent to GSA	4	5	8
22.31	Communications	2	0	0
25.21	Other services	0	137	129
25.72	Information technology contract ..	1	13	13
26.00	Supplies	5	0	0
32.00	Building Alterations	0	1	1
41.02	Subsidies for credit program	18,038	11,541	20,228
	Total	18,193	11,895	20,582

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Summary of Changes
($000s)

2009..	$10,354
2010..	20,582
Net change..........................	+10,228

	2009 base	Change from base
Increases:		
Built-in:		
Increase in personnel compensation primarily for the enacted 2.9 percent 2009 and proposed 2 percent 2010 pay increases.	$132	+$4
Increase in benefits for the Department’s share of health, retirement, and other benefits.	31	+1
Program:		
Increase in new loan subsidy.	10,000	+10,228
Increase in rent to GSA due to increased costs.	5	+3
Subtotal, increases		+10,236
Decreases:		
Program:		
Decrease in other services due to change in needs.	137	-8
Net change		+10,228

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Authorizing Legislation

($000s)

Activity	2009 Authorized	2009 Estimate	2010 Authorized	2010 Request
Federal administration *(Federal Credit Reform Act of 1990, section 505(e) and Title III, part D, HEA)*	Indefinite	$354	Indefinite	$354
New loan subsidy *(Title III, part D, HEA and Federal Credit Reform Act of 1990, section 505(e))*	Indefinite	10,000	Indefinite	20,228
Total appropriation		10,354		20,582

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Appropriations History
($000s)

	Budget Estimate to Congress	House Allowance	Senate Allowance	Appropriation
2000	$207	$96	$207	$207
2001	208	207	208	208
2002	208	208	208	208
2003	211	208	208	207
2004	210	210	210	209
2005	212	212	212	210
2006	210	210	210	208
2007	190	N/A[1]	N/A[1]	209
Supplemental (P.L. 109-234)	0	0	0	304,560
2008	188	188	188	185
2009	10,354	10,354[2]	10,354[2]	10,354
2010	20,582			

[1] This account operated under a full-year continuing resolution (P.L. 110-5). House and Senate Allowance amounts are shown as N/A (Not Available) because neither body passed a separate appropriations bill.

[2] The levels for the House and Senate reflect action on the regular annual 2009 appropriations bill, which proceeded in the 110th Congress only through the House Subcommittee and the Senate Committee.

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Federal administration

Federal administration
(Federal Credit Reform Act of 1990, section 505(e)
and the Higher Education Act of 1965, title III, part D)

FY 2010 Authorization ($000s)
Federal administration: Indefinite
New loan subsidy costs: Indefinite

Budget Authority ($000s):

	2009	2010	Change
Federal Administration	$354	$354	0
New loan subsidy costs	10,000	20,228	+$10,228
Total	10,354	20,582	+10,228
Full-time equivalent employee	1	1	0

PROGRAM DESCRIPTION

Since fiscal year 1996, the Historically Black Colleges and Universities Capital Financing Program has provided HBCUs with access to capital financing for the repair, renovation, and, in exceptional circumstances, construction or acquisition of educational facilities, instructional equipment, research instrumentation, and physical infrastructure.

HBCUs, which have played a prominent role in our Nation's history, have significant needs for capital improvements. However, in most cases these institutions cannot access traditional funding sources at reasonable interest rates. The HBCU Capital Financing Program provides HBCUs with access to low-cost financing to fund infrastructure improvements. This program has made low interest loans available for capital improvements to some of the Nation's most vulnerable institutions of higher education, which have allowed these institutions to make improvements to their capital stock, especially academic facilities and student living-quarters. Under this program, the Department is authorized to provide financial insurance to guarantee up to $1.1 billion in loans and interest to qualifying HBCUs—$733.3 million for private HBCUs and $366.7 million for public HBCUs.

In order to limit the Federal Government's exposure to incurring losses due to defaults and delinquencies, 5 percent of all loans are deposited in a mandatory, pooled escrow account from which loan payments can be made in the event of defaults or delinquencies. Analysis has shown that the funds held in the escrow account are not sufficient to cover all potential program costs, including delinquencies and defaults. As a result, the Department concluded in 2007 that the program could no longer be operated as a zero subsidy program.

The HBCU Capital Financing Advisory Board, appointed by the Secretary, advises the Secretary and the Designated Bonding Authority (DBA) as to the most effective and efficient means of implementing the program. The DBA, also selected by the Secretary, provides for the operation of the HBCU Capital Financing Program, which includes raising bond capital, making loans to eligible institutions, charging interest, and providing for a schedule of repayments. Direct loans are financed through the Federal Financing Bank and guaranteed loans are financed through the private market, with all loan payments fully insured by the Federal Government.

Federal Administration

Funds for this activity pay the Federal costs for administering the HBCU Capital Financing Program. The administrative costs for this program include the personnel compensation and benefits for 1 full-time equivalent (FTE) employee, overhead, and other administrative services. The FTE reported in this account reflects the Department's estimate of the staff time devoted to administering the program. This estimate does not include FTE associated with the Department's centralized services, which are reflected in the Program Administration account in the Salaries and Expenses Overview. The major non-personnel costs include support for the HBCU Capital Financing Advisory Board and a contract with the DBA to provide technical assistance workshops.

Subsidy Costs

In the first 10 years that the HBCU Capital Financing Program operated, there were no delinquencies or defaults. The rigorous application and credit review process imposed by the Department and the DBA was credited with ensuring that institutions receiving loans under this program had the ability to comply with the terms of their loans. However, in 2004, Barber Scotia College lost its accreditation with the Southern Association of Colleges and Schools. As a result, students enrolled at Barber Scotia College were no longer eligible for Federal student assistance. With approximately 90 percent of the College’s students receiving some form of government assistance, this rendered the College unable to service its debt under the program. Barber Scotia College has one $7 million loan under the program, of which $6,964,340 has been disbursed. When capitalized interest is included, there is a total of $6,573,045 currently outstanding. In addition, there will be a total of $4,234,729 in interest due over the remaining life of the loan. Since March 2005, Barber Scotia College’s principal and interest payments have been made from the pooled escrow account. The DBA, which holds the loans that are guaranteed through this program, initiated foreclosure actions against Barber Scotia College to recover funds owed.

In light of these events, the Department reexamined the appropriateness of the cash-flow assumptions for the program, especially the default assumptions. Previously, the default estimate was calculated based on prevailing market-based rates. The Department re-calculated the default assumptions based on individual assessments of risk and potential recovery for each loan. The credit subsidy for the program, previously estimated at zero, was upwardly re-estimated in fiscal year 2007 to $14.1 million for loans already made. Furthermore, the Department concluded that the funds set aside in the program’s escrow account would not be enough to cover defaults and, as such, the program could no longer be considered a zero subsidy program, according to the terms of the Federal Credit Reform Act of 1990.

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Funding levels for the past 5 fiscal years were:

	($000s)
2005	$210
2006	208
2007	304,769
2008	185
2009	10,354

FY 2010 BUDGET REQUEST

The Administration requests $20.582 million for the Historically Black College and University (HBCU) Capital Financing Program account for fiscal year 2010. The request includes $354,000 for administrative expenses and an additional $20.228 million for loan subsidy costs for new loans under the program.

The $354,000 in administrative expenses will be used to maintain technical assistance services, which were expanded in 2009, to fill a finance skill and expertise gap in the HBCU community and assist HBCUs to enhance their fiscal stability and prepare to access capital markets. For presentation purposes, the full-time equivalent and administrative costs financed by this account are also included under the justification materials in the Salaries and Expenses Overview.

The Administration's request includes $20.228 million for loan subsidy costs. Based on current assumptions of the default risk of the expected loan applicants, the Department anticipates that the available subsidy will be sufficient to guarantee $178.220 million in new loans in fiscal year 2010.

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PROGRAM OUTPUT MEASURES **($000s)**

	2008	**2009**	**2010**
Number of new loans:			
Private HBCUs	0	1	6
Public HBCUs	0	0	1
Total	0	1	7
New loan volume:			
Private HBCUs	0	$61,312	$138,220
Public HBCUs	0	0	40,000
Total	0	61,312	178,220
Total number of loans:			
Private HBCUs	24	25	31
Public HBCUs	7	7	8
Total	31	32	39
Total loan volume:			
Private HBCUs	$530,631	$591,943	$730,163
Public HBCUs	79,197	79,197	119,197
Total	609,828	671,140	849,360

NOTE

All loans made to date are direct loans financed through the Federal Financing Bank.

PROGRAM PERFORMANCE INFORMATION

Performance Measures

This section presents selected program performance information, including, for example, GPRA goals, objectives, measures, and performance targets and data, and an assessment of the progress made toward achieving program results. Achievement of program results is based on the cumulative effect of the resources provided in previous years and those requested in fiscal year 2010 and future years, and the resources and efforts invested by those served by this program.

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Goal: To improve loan recipients' overall financial stability and enhance their ability to attract, retain and educate students

Objective: *Total revenues and investment return will increase for loan recipients.*

Measure: Maintain a high percentage of borrowers who increase revenues and investment return annually.		
Year	**Target**	**Actual**
2005		67
2006		69
2007		
2008		
2009	70	
2010	70	

Assessment of progress: This performance measure is the percentage of HBCUs that experienced an increase in revenue over the prior year. The percentage of HBCUs that experienced an increase in revenue is one gauge of improved institutional financial stability and capability to fulfill their educational mission. Loans that fund capital and infrastructure improvements are key assets for providing quality postsecondary education. Some HBCUs have significant cash flow problems, which capital improvements from this program are expected to help ameliorate. Revenue is a strong indicator of an institution's success at maintaining or increasing enrollment, expanding fundraising activities, and ultimately the institution's financial stability. The ability to maintain or increase revenue suggests that an institution will be able to service its debts and maintain its operations. This measure helps to assess the financial solvency of borrowers, which is a gauge of default potential. This measure is calculated as the number of HBCUs in the program that have experienced an increase in revenue over the prior fiscal year divided by the total number of HBCUs in the program multiplied by 100. The data source for total revenues is the National Center for Educational Statistics' Integrated Postsecondary Education Data System.

Objective: *The delinquency rate of loan recipients will improve.*

Measure: The delinquency rate of loan recipients		
Year	**Target**	**Actual**
2007		13
2008		
2009		
2010	14	

Assessment of progress: The delinquency rate—the percentage of loan payments received between 11-59 days after the due date—indicates the financial stability of borrowers. The ability to make timely payments reduces the likelihood of default. It also indicates successful monitoring, technical assistance, and enforcement by the Department and the DBA in administering the program. The program allows borrowers a 10-day grace period within which their payments are considered on-time. After that they are considered delinquent. This annual measure will be calculated by counting the total number of payments received by the DBA between 11-59 days after the due date during a fiscal year and dividing by the total number of payments due during the fiscal year. Those institutions with multiple loan disbursals will be counted multiple times each month.

Goal: To improve the capacity of program borrowers to improve student success and provide high-quality educational opportunities for their students.

Objective: *Maintain or increase the persistence rate of first-year students at borrower institutions.*

Measure: The percentage of first-time, full-time, degree-seeking, undergraduate students who were in their first year of postsecondary enrollment in the previous year and are enrolled in the current year at the same loan recipient institution.

Year	Target	Actual
2005		68
2006		67
2007		61
2008		63
2009	64	
2010	65	

Assessment of progress: New and improved physical facilities can help an institution of higher education increase student persistence. Many of the loans have provided support for student housing and many of the borrowers have explicitly cited lack of adequate student housing and facilities as a reason for high attrition rates on their campuses in their loan applications. This measure relies on data taken from the Integrated Postsecondary Education Data System database maintained by the National Center for Education Statistics.

Efficiency Measures

The Department has developed an efficiency measure for this program that will track the estimated Federal cost per dollar made in loan guarantee (or the subsidy rate). The Department is currently working to establish baselines and targets for this measure.

Other Performance Information

In 2006, the U.S. Government Accountability Office (GAO) conducted an examination of the HBCU Capital Financing Program. The objectives of the study were to review: (1) HBCU capital project needs and program utilization, (2) program advantages compared to other sources of funds and schools' views on loan terms, (3) the Department's program management, and (4) new loan provisions enacted in June 2006 to assist in hurricane recovery efforts. GAO noted in the report that HBCUs have extensive and diverse capital project needs and that the HBCU Capital Financing Program provides them with access to low-cost capital financing and flexibilities not available elsewhere. The report also noted that the Department had taken steps to improve the program that included increasing flexibility by providing schools with both fixed and variable interest rate options, allowing for larger loans, affording schools with more opportunities to negotiate loan terms, and increasing marketing efforts for the program. The report also noted specific weaknesses in the Department's management of the program.

GAO's recommendations are presented below, followed by a description of the Department's actions to address them.

- *The Department should regularly convene and consult with the HBCU Capital Financing Program's Advisory Board. Additionally, the Department and the Advisory Board should consider the feasibility of alternatives to the escrow arrangement. If the Department determines that statutory changes are needed to implement more effective alternatives, it should seek such changes from Congress.* The HBCU Capital Financing Program's Advisory Board now meets twice each year.

- *The Department should enhance communication with HBCU Capital Financing Program participants by (1) developing guidance for HBCUs, based on other schools' experiences with the program, on steps that applicants can take to expedite loan processing and receipt of loan proceeds, and (2) regularly informing program applicants of the status of their loan applications and Department decisions.* The Department has taken a number of steps to improve communication with HBCU program participants and address this GAO recommendation. The Department studied the experiences of past borrowers and used the resultant data to develop guidance that will allow applicants to expedite loan processing. Further, the Department developed a customer satisfaction survey that is sent to borrowers after they have closed on a loan. This survey asks borrowers to rate the level of service at every stage of the process and asks borrowers to recommend improvements to the loan process. Using the results of this study and borrower feedback, the Department has developed a Question and Answer section on its website that includes an overview of the loan process, a list of the information commonly needed to process a loan, and information about what a school can do to expedite the loan application and closing processes.

- *The Department should change its requirement that borrowers make monthly payments to a semiannual payment requirement.* While the Department understands institutions' preference for semi-annual rather than monthly payments, the potential for default, as well as each institution's potential exposure from the default of another program participant, leads the Department to believe that it would be imprudent to implement a less frequent payment schedule.

- *The Department should ensure that the program subsidy cost estimation process include as a cash flow to the government the surcharge assessed by the Federal Financing Bank (FFB) and paid by HBCU borrowers and pay such amount to the program's financing account. Additionally, the Department should audit the surcharge funds held by the DBA.* In response to this recommendation, the Department audited the funds held by the trustee on behalf of the program generated by this FFB surcharge. The Department worked with the DBA to develop a protocol for regular transfers of these fees into the program's financing account. The Department worked with the Office of Management and Budget (OMB) to incorporate the fee into the Department's cash flow

Federal administration

model. The Department also retained an independent firm to audit the DBA during fiscal year 2007 to assess the handling of loan funds and associated fees. The independent audit concluded that the DBA did not have a process that tracked the FFB fee for the loans that have been made through the HBCU Capital Financing Program. The Department now receives monthly statements that provide loan detail for each borrower, including the borrower's FFB fees and escrow balances.

- *The Department should increase monitoring of the DBA to ensure compliance with contractual requirements and ensure properly marketing the program.* In response to this recommendation, the Department retained an independent firm to audit the DBA during fiscal year 2007 to assess the handling of loan funds and associated fees. This audit assessed the DBA's record-keeping function and determined documents the DBA needs to obtain to complete its files. To assist the DBA, the Department developed a checklist indicating required and optional documents to include in a complete file. The Department uses this list to monitor record-keeping. After each closing, the Department ensures that the borrower's loan transcript file is complete by cross-checking the pre-closing document list with the actual closing document list and actual documents presented at closing.

Program Improvement Efforts

The Department has identified several weaknesses in the program, including problems with its escrow account, contractor fee structure, and loan package inflexibility. To address these weaknesses, the Department is working to strengthen contractor accountability, thereby promoting a high level of performance throughout the entire life of the program. The Department is currently in the process recompeting the contract for the Designated Bonding Authority (DBA). Upon completion of the review process, the Department will negotiate a new Agreement to Insure with the selected DBA. The Department will work to ensure that the new agreement addresses any problems with the contractor fee structure and package inflexibility, and contains provisions requiring monthly reporting on all account activity, including the program's escrow account.