

Statement Regarding 9.5 Special Allowance Payments

A recent audit has alleged that Kentucky's nonprofit Federal Family Education Loan Program (FFELP) provider received improper special allowance payments from the federal government on 9.5% floor loans.

The fact is that the Kentucky Higher Education Student Loan Corporation (KHESLC) billed and used 9.5% funding under the specific rules and guidance of the U.S. Department of Education (USDE) to provide benefits to Kentucky citizens and fulfill its public purpose of making higher education more accessible to Kentuckians.

When 9.5 special allowance payments became available, an opportunity presented itself to direct much-needed funding to Kentuckians. KHESLC followed the exact guidance and regulations from the USDE. USDE auditors reviewed KHESLC's practices and determined that they were proper. KHESLC followed all the rules that were in place at the time and has done so throughout the history of its 9.5% floor loan billings. In October 2005, a USDE audit not only approved KHESLC's 9.5% billing processes but concluded that KHESLC had, in fact, underbilled for 9.5% eligible loans and allowed KHESLC the opportunity to recover the funds.

In January 2007, USDE changed how it determined eligibility for the 9.5% floor billing and then attempted to retroactively apply the new requirement to previously USDE-approved actions by KHESLC. To change the rules after the fact and then say that KHESLC's actions were "improper" is completely without merit.

Once USDE issued its new requirements regarding 9.5% floor loan eligibility, it announced that lenders would be able to collect future 9.5% loan payments only if they provided an acceptable review from an audit based on the USDE's new interpretation of eligibility. Because KHESLC's portfolio would not meet the new requirements, the cost of the audit outweighed the potential gain, and KHESLC ceased billing the USDE for 9.5% subsidy payments. (Eight of the 15 lenders who submitted the audit did not meet the new requirements.)

These funds (along with our other federal loan-related income) went directly to Kentucky citizens in the form of zero-fee loans and interest and loan forgiveness programs for Kentuckians working in the Commonwealth's critical-shortage professions of teaching, nursing, and public service law—totaling \$166.1 million since FY 2003.

Specifically, KHESLC provided \$59.9 million in interest and loan forgiveness to teachers, \$15.8 million in interest and loan forgiveness to nurses, and \$1.2 million in interest and loan forgiveness to public service attorneys since FY 2003. All Stafford and PLUS borrowers were given zero-fee loans and interest rate reductions totaling \$89.2 million.

As a public nonprofit corporation, KHESLC firmly believes in openness and transparency in government. We have openly discussed 9.5% subsidy payments with federal and state policy makers and

made formal presentations to state legislative committees. KHESLC staff have visited Washington, D.C., to personally meet with USDE and our Congressional Delegation to express our concerns on behalf Kentuckians who would be impacted by elimination of 9.5% subsidy payments to KHESLC as well as cuts to KHESLC's revenue from the College Cost Reduction and Access Act and the credit crisis. Our Board meetings are open to the public.

KHESLC was created by the Kentucky General Assembly in 1978 and is firmly committed to its public purpose of providing capital and lowering the cost of financing higher education for Kentuckians. KHESLC has a history of providing borrower benefits since 1996. In an age of reduced state revenue and financial conservatism, KHESLC takes considerable pride in providing student loan relief to citizens of the Commonwealth, which fully supports its mission to increase Kentuckians access to higher education.