

10.

EDUCATION AND CULTURE - STUDENT ASSISTANCE

BACKGROUND

10.1 The Student Assistance Office of the Department of Education and Culture administers the Canada Student Loan Program (CSLP) on behalf of the Government of Canada and the Nova Scotia Student Loan Program (NSSLP) for the Province. Student loans are advanced and collected by chartered banks, under the provisions of contracts with the Federal and Provincial governments.

10.2 At present, only the Royal Bank of Canada (RBC) issues Nova Scotia student loans under a two-year contract which expires January 1, 1999. Nova Scotia student loans were also issued by the Canadian Imperial Bank of Commerce (CIBC) until June 1997. The CIBC did not renew their contract which expired at that time.

10.3 The NSSLP was established in August 1993 replacing the previous bursary assistance program. This was our second audit of the NSSLP. The results of our last audit of the Program were reported in our 1995 Annual Report.

10.4 For the academic year ended July 31, 1997, the Student Assistance Office approved 18,238 Canada Student Loans and 18,217 Nova Scotia Student Loans with a value of \$70.3 million and \$50.3 million respectively. Exhibit 10.1 on page 118 includes several key statistics for the programs.

10.5 The administration costs of the Student Assistance Office to deliver both the CSLP and the NSSLP consist primarily of salary and data processing expenditures and totalled \$2.8 million for the year ended March 31, 1997. The Province receives a contribution from the Government of Canada for administering the CSLP. During the 1996-97 fiscal year, the Government of Canada contributed \$567,336.

10.6 In addition to administration costs, the Province's costs for the NSSLP consist of:

- interest on Nova Scotia Student Loans while students are studying and for six months after completion of studies (the Federal government pays the interest and other lending costs of the CSLP);
- an Interest Relief Program which provides an additional 30 month interest-free period, at any time during the repayment period, should the borrower be unemployed or underemployed;
- guarantees to the bank of repayment of student loans for those who become bankrupt or deceased at any time prior to the seventh month after the completion of studies;
- costs of the Loan Remission Program whereby a portion of a student's loan will be repaid by the Province, upon successful completion of the year's studies, to the extent that the loan for the year exceeds a predefined maximum debt level; and
- a risk premium of 5% of the amount of loans awarded, payable to the bank by the Province, to compensate the bank for assuming the risk of default by the borrower.

10.7 The costs to the Province of interest payments, loan remission grants, loan guarantees, risk premiums, administration costs and the Interest Relief Program for the fiscal years 1993-94 to 1996-97 are presented in Exhibit 10.2. Exhibit 10.3 shows lending activity for the period from 1993-94 to 1996-97.

10.8 Canada and Nova Scotia Student Loans are provided to eligible students to continue their education at the post-secondary level at designated universities, community colleges and trade schools. The amount of loan available to a student depends on the student's financial need. Financial need is the difference between assessed educational costs and living expenses, and student resources and, if applicable, parental or spousal resources.

10.9 For the 1996-97 academic year, student loans were limited to \$165 per week of study under the CSLP plus \$150 per week under the NSSLP. A student, with no other means of support, registered for a 34-week study period (a typical university academic year) could borrow a maximum of \$10,710 each year under both loan programs. A four-year study program could accumulate debt of \$42,840. The Loan Remission Program, described above, reduces student debt levels. Using the above example, the full-time university student could be eligible for loan remission of \$3,560 each year. Maximum debt at the end of the four-year period could be reduced from \$42,840 to \$28,600. Average loan awards tend to be less than the maximum available. For the 1996-97 academic year, the average approved loan per student (CSL and NSSL combined), net of loan remissions, was \$6,338.

10.10 Nova Scotia Student Loans are available only to full-time students who are residents of the Province of Nova Scotia. There is no age limit and a student may attend an institution anywhere in the world, provided the institution has been designated as eligible by the Student Assistance Office.

10.11 Under the terms of the contracts with the chartered banks, interest is paid to the banks by the Province while the student attends school and for six months after the completion of studies at an interest rate equal to the bank's prime rate plus 0.25%. Students are required to commence loan repayment after this date at an interest rate of bank prime plus 2.5% or 5% depending on whether a variable or fixed interest rate is selected by the borrower. The repayment period of a student loan can be as long as eight years depending on the amount of the loan.

10.12 The collection of delinquent accounts is the responsibility of the banks for which the Province pays a one-time fixed fee, or risk premium, of 5% of the loan balance at the time repayment by the student commences.

10.13 There is a high degree of harmonization between the NSSLP and the CSLP. There are common application forms, program guides and needs assessment processes. There are aspects of the NSSLP that are different from the CSLP. For example, the Loan Remission Program is unique to the NSSL, loans to part-time students are available only under the CSLP, and there are separate contracts with lenders. There are ongoing discussions with the Federal government concerning harmonization of student debt management programs and contracts with lenders.

RESULTS IN BRIEF

10.14 The following are the principal observations resulting from our examination.

- Based on our testing of loan advances, loan awards are calculated accurately and are supported by required documentation in the student files. The average processing time for loan applications for the 1996-97 academic year was 21.6 days.

- Based on our testing of billings from the banks, controls appear adequate to ensure billings from the banks for interest, interest relief and risk premiums are accurate and complete. We have recommended strengthening of controls over interest verification and changes to student end-of-study dates.
- Loan transaction data and loan default information from the bank are not adequate. We have recommended that deficiencies be corrected.
- There is no regular reporting of outcomes and performance standards of the Student Assistance Office. Thus accountability reporting to senior management of the Department is not adequate. Key outcome measures for the Office should be reported to the House of Assembly through the Department's annual report.
- There are no formal standards for the designation of educational institutions although draft designation criteria are now being developed. There is presently no requirement for designated educational institutions to report graduation, retention and employment rates to the Student Assistance Office. We have recommended that the Department finalize development of designation and reporting requirements for educational institutions.
- There continues to be no written agreement with the Federal government concerning the recovery of administration costs. The administration costs incurred by the Province in delivering the CSLP exceeded Federal recoveries by \$459,370 for 1995-96.
- The Department has not fully recorded its liability and the corresponding expense for risk premiums on loans issued to March 31, 1997. We believe that Department expenditures and liabilities were understated by \$2.7 million as a result of this omission.
- Under the terms of the financing contract with the banks, the Province assumes long-term financial obligations under the Interest Relief and Loan Remission programs. Contingent liabilities under these programs are not currently disclosed in the Province's financial statements. The loan information required to calculate the Province's financial exposure to loan remission and interest relief claims is not being gathered. There is evidence that the amounts could be significant because one bank reported a 30% default rate for student loans on repayment status. We have recommended that the required loan information be gathered and, if material, contingent liabilities should be disclosed, by way of note, to the Public Accounts of the Province.

AUDIT SCOPE

10.15 The objectives of this assignment were to:

- follow up on the results of the 1995 audit of the Student Assistance Program; and
- examine and test the systems of control over loan awards, interest relief and loan remission claims, and billings from the banks for interest and risk premiums.

10.16 The following general criteria were used in our audit.

- There should be adequate systems of control to ensure loan awards are made only:

- to eligible students;
 - for eligible educational costs;
 - if enrolled in designated educational institutions;
 - for eligible educational programs; and
 - in the proper amount based on an accurate assessment of student financial need.
- There should be adequate systems of control to ensure that billings from the banks for interest, interest relief and risk premiums are accurate and complete.
 - There should be an established process for setting and reporting program objectives, outcomes and performance measures.
 - There should be established criteria for the designation of educational institutions.
 - There should be a written agreement with the Federal government concerning the recovery of administration costs.
 - There should be established policies and procedures for the NSSL Program.
 - Bursary overawards should be properly recorded and appropriate action should be taken to recover overawards.
 - There should be an estimated liability for risk premiums on loans advanced in the accounting records of the Province.
 - There should be adequate disclosure of contingent liabilities for interest relief and loan remission costs related to loans advanced in the accounting records of the Province.

10.17 We interviewed staff of the Student Assistance Office and tested a sample of loan applications and billings from the banks. We also examined relevant reports, student loan files and other documents.

PRINCIPAL FINDINGS

Loan Advances

10.18 We tested 40 loan applications for student eligibility, accuracy of loan calculations, proper supporting documentation in the student file and timeliness of processing.

10.19 *Supporting documentation* - For the most part, required documentation was present in the student file, the documentation supported the calculation of the loan award amount and student files were neat and organized. We did note four instances where certain required documentation was missing with no explanation or reason for the missing documents. We note that there is no checklist of required documents contained in the student file with an explanation required for missing documentation. We have recommended that such a checklist be developed.

10.20 Accuracy of loan awards - We found that loan calculations were generally accurate and cost and student resources were properly supported. We noted one instance where student need was understated by \$2,750 because an incorrect tuition fee and text book allowance were used in the calculation.

10.21 Timeliness of application processing - The Student Assistance Office monitors, and has developed performance standards for, the average processing time of loan applications. For the 1996-97 academic year, the average processing time for loan applications was 21.6 days. This average does not include delays caused by following up missing information from a student's application. The standard for average processing time is 14 to 21 days.

Billings from Banks

10.22 We tested one month's billings from both the CIBC and the RBC for interest charges, risk premiums, loan remissions and interest relief. There were no claims for guarantees during the test period.

10.23 Overall findings - No significant monetary errors were noted during our testing of billings from the banks. The Student Assistance Office relies heavily on an edit report generated by the Student Loan System to identify potential errors in billings from the banks. The control system then depends on the thoroughness of Student Assistance Office staff in investigating the items flagged in the edit report and ensuring that monetary errors identified are corrected by the banks in subsequent months' billings. In general, controls appear to be adequate to ensure the Province only pays bona fide billings.

10.24 Interest verification - The Student Loan System performs a reasonableness test on the interest charged for each loan as part of the edit testing on billings. Specifically, the System estimates interest for each loan for the month based on the month-end loan balance. If the interest billed by the bank for a loan exceeds twice the estimated amount, the System flags the transaction in an edit report. In our opinion, the tolerances accepted as "normal" in this edit procedure are too broad to provide an adequate reasonableness check on interest billings. No other overall reasonableness test for interest charges is performed by Student Assistance Office staff.

10.25 Changes to end-of-study dates - Changes to end-of-study dates are processed directly by the banks with no prior approval by the Student Assistance Office. In addition, the banks or the educational institutions do not always provide copies of the applications for changes to end-of-study dates to the Student Assistance Office. Thus the Student Assistance Office cannot verify that changes to end-of-study dates are legitimate in these cases. Accurate end-of-study dates are important because they determine the period that the Province will have to pay interest after the student leaves school. We have recommended strengthening of controls in this area.

10.26 Transaction and default information reported by banks - Banks are required to supply monthly an electronic tape of transactions for each loan on interest free status to the Student Assistance Office. The Student Assistance Office uses these transactions to monitor increases to loan balances, to verify transfers from one financial institution to another and to verify continuity of the total portfolio balance upon which interest is based. The transaction data supplied by the Royal Bank does not distinguish between loan advances and transfers from other financial institutions because of programming deficiencies. Thus it is impossible for Student Assistance Office staff to adequately monitor loan transactions from this bank.

10.27 The Royal Bank does not supply loan default information to the Student Assistance Office. Risk premiums paid to the bank, currently 5% of loan advances, are based on assumptions about

future repayments by borrowers. Future contracts with banks may include higher or lower risk premiums depending on actual repayment experience under the NSSLP. Monitoring loan default information is critical to negotiating appropriate risk premiums in future contracts.

10.28 We have recommended that deficiencies in the reporting of transaction data for loans and loan default information be corrected as soon as possible.

Recording Expenses for Risk Premiums, Loan Remissions and Interest Relief

10.29 *Risk premiums* - Risk premiums are payable to the banks at the time a student commences repayment of a loan. However the obligation to pay risk premiums is incurred when the loan is advanced. In our opinion, the Department should record a liability and expense for risk premiums as loans are advanced. In this way the expense for risk premiums would be recognized in the year the related loan was advanced.

10.30 For the 1997 fiscal year, the Department recorded an accrued liability of \$936,158 representing estimated risk premiums on loan advances made during the 1996-97 fiscal year. However the Department did not record a liability for unpaid risk premiums on loan advances made prior to 1996-97. We estimate that Department liabilities and expenses for the 1996-97 fiscal year are understated by \$2.7 million as a result of this omission.

10.31 *Loan remission claims* - There is also no disclosure in the financial statements of the Province of the exposure to additional expense for loan remissions and interest relief claims. Loan remissions and interest relief expenses are recorded in the year claims are approved.

10.32 The Department's financial exposure to loan remission claims depends on whether individual loans exceed the maximum debt levels established for the program and whether the student successfully completed studies. This can be estimated from prior years' experience. During the period April to October 1997, the Student Assistance Office approved \$2.0 million in loan remissions related to loan advances made during 1996-97. This contingent liability was not disclosed in the March 31, 1997 Public Accounts of the Province.

10.33 *Interest relief claims* - The Department's financial exposure to interest relief claims depends on the value of the loan portfolio on repayment status, students' employment prospects, the average interest rate for loans in the portfolio and the average number of months that loans remain on interest relief.

10.34 Since 1993-94 there has been a conversion of \$58.3 million of loans to repayment status. The Student Assistance Office could not tell us the actual value of the loan portfolio on repayment status at March 31, 1997 because this information is not reported by the banks. Student Assistance Office staff project an additional \$111.5 million in conversions to repayment status by the 1999-2000 fiscal year. Therefore the portfolio of loans with the ability to attract interest relief claims could be as high as \$169.8 million by the year 1999-2000. Default information reported by the CIBC in September 1997 reveals a 30% default rate for loans on repayment status. Loans in default are defined as loans that are more than two monthly payments in arrears.

10.35 It is difficult to estimate the exposure of the Province to interest relief claims based on the above information. There is a lack of information from the banks on the number and value of loans on repayment status, the average interest rate and the repayment term of these loans, the number and value of loans granted interest relief and the average number of months that loans tend to remain on interest relief. We have recommended that information be gathered to enable estimates of the Province's exposure to interest relief claims. If material, this contingent liability should be disclosed in the Public Accounts of the Province.

Follow-up to 1995 Audit

10.36 *Outcome measures and performance standards* - Program objectives, target outcomes and performance standards are not developed annually by the Student Assistance Office. We have recommended that program objectives and outcome measurement criteria be developed and that the achievement of program objectives, outcomes and performance standards be documented and reported annually to senior management of the Department. Key outcome measures should be reported to the House of Assembly through the Department's annual report.

10.37 *Regulations and policies and procedures manuals*- Regulations still have not been approved under the Student Aid Act, even though the Program has been in operation since August 1993. Management informed us that regulations are in the final stages of revision but have not been finalized. We have recommended that regulations be finalized and submitted to Executive Council for approval as soon as possible.

10.38 The Department developed a draft policies and procedures manual for the NSSLP in November 1997. We have recommended that the draft policies and procedures manual for the NSSLP be finalized as soon as possible.

10.39 *Position descriptions* - We reported in our 1995 Report that position descriptions for most key positions within the Student Assistance Office were significantly out of date. This continues to be the case. A significant organizational change during 1996-97 is the primary reason why position descriptions have not been updated.

10.40 *Performance appraisals* - We reported in our 1995 Report that no written annual performance appraisals had been prepared for staff of the Student Assistance Office. Management informed us that performance appraisals have since been prepared for two staff. However, an annual performance appraisal process has not been established and performance appraisals for the remaining 18 staff have not been completed.

10.41 *Designation of educational institutions* - The designation of educational institutions for the NSSLP and CSLP is a Provincial responsibility. The designation process is carried out by the Director of Student Assistance and approved by the Minister. There are no formal written standards for designating an educational institution. At present, an educational institution applying for designation must be registered in accordance with the regulatory requirements of the jurisdiction involved. Institutions are not required to re-certify after a period of time. There are no provisions for revoking the designation of an educational institution.

10.42 There is also no requirement for designated educational institutions to report graduation rates, retention rates or employment rates upon graduation. These factors are important to ensure the wise investment of public monies in the student loan program.

10.43 Management informed us that draft designation criteria were developed in April 1997. Management plans to discuss the criteria with stakeholders and finalize designation criteria in the near future.

10.44 *Administration cost recoveries from the Federal government* - There continues to be no written agreement with the Federal government concerning the recovery of administration costs incurred by the Province in delivering the Canada Student Loan Program. We have recommended that the Department negotiate a written recovery agreement.

10.45 The Federal government determines recoveries to be paid to the provinces. The amount of payment is based on a national budget allocation divided between the provinces on the basis of eligibility certificates issued by each province.

10.46 In June 1997, the Department received \$542,336 in administration recoveries for the academic year ended July 31, 1996. Administration costs of the Student Assistance Office were \$2.0 million for the fiscal year ended March 31, 1996. Department staff informed us that 50% (\$1.0 million for 1996) of administration costs of the Office are attributable to the delivery of the CSLP.

10.47 Federal recoveries are not sufficient to recover the administration costs incurred by the Province in administering the Canada Student Loan Program. In 1995-96 there was a shortfall of \$459,370 for the year. This situation has existed for a number of years.

10.48 *Bursary overawards* - In 1991 the Student Assistance Office commenced a verification procedure requiring students to submit income tax return information which was compared to the information filed with the Canada Student Loan and bursary application. Significant bursary overawards were identified through this procedure.

10.49 In 1995 we reported significant deficiencies in the accounting, control and collection of overawards. In addition, bursary overawards had not been recorded as a receivable on the accounting records of the Province, nor had an appropriate allowance for doubtful accounts been established. The write-off of uncollectible bursary overawards had not been approved by Executive Council as required by Section 23(1) of the Provincial Finance Act.

10.50 Management informs us that collection of bursary overawards is now being administered by the Department of Business and Consumer Services. A receivable and an allowance for doubtful accounts, of \$1,274,369 and \$829,300 respectively, were recorded on the accounting records of the Province at March 31, 1996.

CONCLUDING REMARKS

10.51 The principal focus of our audit this year was to assess the adequacy of controls over loan awards, interest relief and loan remission claims, and billings from the banks for interest and risk premiums. We found controls to be generally adequate in the areas examined.

10.52 We remain concerned about potential cost escalation of this program and the lack of information to enable the Department to forecast future costs. We also believe there is a need to improve accounting for program costs and the disclosure of financial commitments for the program in the Public Accounts of the Province.

10.53 The Province's exposure to the risk of cost escalation is primarily in the areas of risk premiums and interest relief claims. These areas are affected by student debt levels, employment prospects and income levels after graduation.

10.54 Risk premiums are presently fixed, by contract which expires January 1, 1999, at 5% of loans advanced. Future risk premium rates will depend on the projected cost of loan defaults at the time a new contract is negotiated. It is therefore important that accurate and complete loan default information be gathered by the Department.

10.55 Interest relief is available to students, for up to 30 months, at any time during the repayment period of the loan. To forecast future interest relief costs accurately, it is important that the Department obtain accurate data on the balance of the loan portfolio in repayment status, the number of loans that tend to be granted interest relief and the number of months that students tend to remain on interest relief.

Exhibit 10.1

**SUMMARY OF KEY STATISTICS
ACADEMIC YEAR ENDED JULY 1997**

	NSSLP	CSLP
Maximum Student Loan (34 week program)	\$ 5,100	\$ 5,610
Average Student Loan	\$ 2,760	\$ 3,856
Number of Loans Approved	18,217	18,238
Value of Loans Approved	\$ 50,277,115	\$ 70,318,788
Portfolio Balance - Interest Free Status March 31, 1997	\$ 89,332,534	N/A

Exhibit 10.2

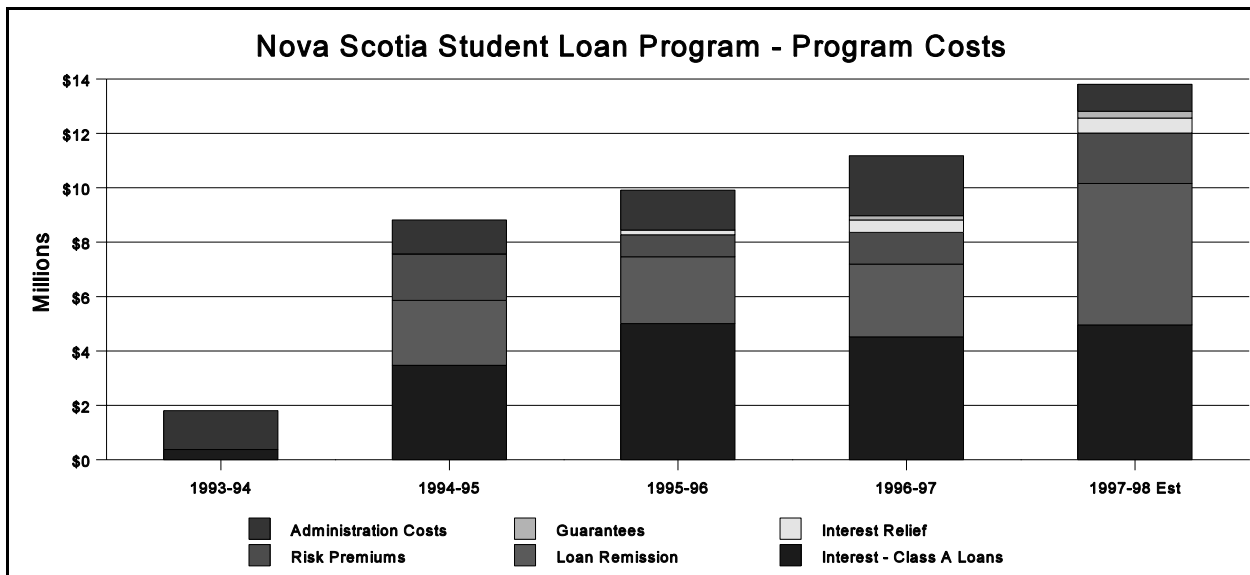
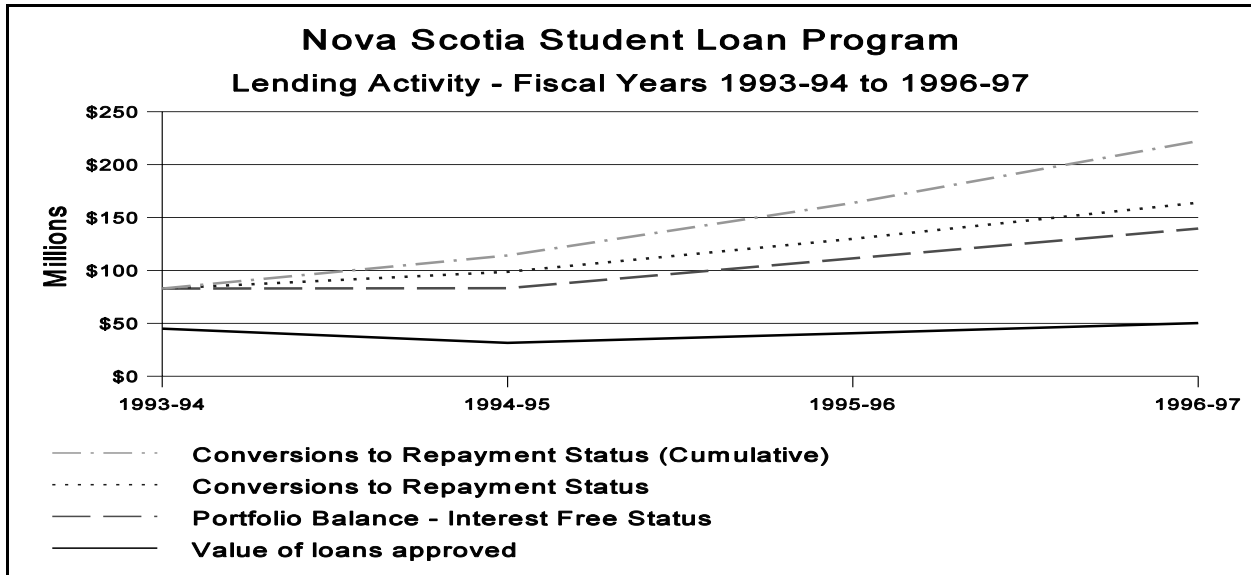


Exhibit 10.3



DEPARTMENT OF EDUCATION AND CULTURE'S RESPONSE

The Department is pleased with the findings of the recent audit of the Student Assistance Division, which determined that loan amounts had been calculated correctly and that control measures for the Nova Scotia Student Loan program were adequate. Departmental staff are currently working with the Royal Bank to improve reporting procedures and significant progress has been made to date.

The Report also identified a number of areas for improvement including outcome measures and performance standards, position descriptions, a designation of educational institutions policy and administrative cost recovery from the Federal Government. The following actions will be taken:

- A) *Outcome measures and performance standards - Prior to the beginning of each processing year, the Student Assistance Division Management Team develops a Work Plan which establishes the desired results for processing turnaround time, computer enhancements, training, and staffing. The plan is adhered to and forms the basis for the operating standards in each academic year. Weekly Management Team meetings are held to monitor results and make any required adjustments. The Division will formalize appropriate measures and standards by the 3rd Quarter 1998.*
- B) *Regulations - The Regulations under the Student Aid Act are in the final drafting stage by the Department of Justice and will be submitted to the Executive Council for approval during the first Quarter 1998.*
- C) *Policy and Procedures Manual - This Manual will be forwarded to Senior Management for approval during the 1st Quarter 1998.*
- D) *Position Descriptions - The Student Assistance Office has undergone re-engineering and organizational changes over the past four years and as a result, most of the job descriptions do not accurately reflect the tasks being performed by staff. In 1996-97, the introduction of imaging and workflow technology resulted in further changes to staff responsibilities and division organization. Preliminary work has begun to revise all the staff's job descriptions and will be completed by the third quarter 1998.*
- E) *Performance Appraisals - An ongoing performance appraisal process has been established within the Department. The Student Assistance Division will be part of the Department's implementation process.*
- F) *Designation of Educational Institutions - A draft designation policy has been developed. Consultations will be held among the stakeholders during the 1st Quarter 1998 prior to the new policy being implemented.*
- G) *Administrative Cost Recovery from the Federal Government - A formal agreement on sharing administrative costs will be part of our harmonization process. Discussions will begin again in January 1998, with a tentative target date of August 1, 1998 for the signing of this agreement.*
- H) *Bursary Overawards - The Department is pleased with the progress made to date by the Department of Business and Consumer Services in the collection of these overawards.*