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Return Receipt Requested
Audit Control No. ED-OIG/A05-B0033

Mr. Carl Dalstrom
President
United Student Aid Funds, Inc
P.O. Box 6028
Indianapolis, Indiana 46206-6028

Dear Mr. Dalstrom:

This letter is in response to the United Student Aid Funds, Inc.'s (USA Funds) appeal of final program determination Finding 2 made by the U.S. Department of Education (Department) concerning an audit conducted by the Office of Inspector General (OIG) for the period October 1, 1998 through September 30, 2000. In addition, the Department has reviewed the detail information (as requested) provided by USA Funds in response to final program determinations Findings 1.2 and 1.3.

With respect to USA Funds' appeal of Finding 2, USA Funds claims that the outside entity that performs default aversion activities, Student Assistance Corporation, which is a wholly owned subsidiary of SLM Corporation (SLM), does not also (1) hold or service affected loans, or (2) perform collection activities on the loans in the event of default within 3 years of the claim payment date. Rather, other wholly owned, separate subsidiaries of SLM perform those activities.

The Department has reconsidered its earlier position and has determined that the arrangements of USA Funds with the different, wholly owned subsidiaries of SLM do not violate 34 C.F.R. § 682.404(k)(4). This is so because Student Assistance Corporation, which performs default aversion activities, is a separate corporate entity from the Student Loan Marketing Association, which holds loans for which Student Assistance Corporation performs default aversion activities; Sallie Mae, Inc., which provides pre-default loan servicing and post-default portfolio management on loans for which Student Assistance Corporation performs default aversion activities; and General Revenue Corporation and Pioneer Credit Recovery, Inc., both of which provide post-default collection on loans for which Student Assistance Corporation performs default aversion activities. USA Funds represented to the Department that these are separate subsidiaries of SLM, and it is apparent from SLM's website that SLM regards these subsidiaries as separate corporate entities. Indeed, USA Funds represented to the Department that employees of Student Assistance Corporation are not employees of any other SLM subsidiary. In addition, the Department finds that all of the subsidiaries in question

possess separate existences for tax purposes in that they have separate Federal Tax ID numbers, which the Department finds indicative of the presence of separate entities. See BLACK'S LAW DICTIONARY 532 (6th ed. 1990).

Furthermore, although it is not relevant to the Department's determination of whether Student Assistance Corporation is a separate entity from the other SLM subsidiaries, the Department is heartened that, according to USA Funds' representations to the Department, SLM and Student Assistance Corporation use incentives to ensure that default aversion is properly performed. For example, the incentive compensation for the SLM executive to whom Student Assistance Corporation, General Revenue Corporation, and Pioneer Credit Recovery, Inc. report is crafted to encourage and reward aggressive default aversion activities, and Student Assistance Corporation receives a greater share of the default aversion fee as default rates decline. Similarly, the Department is heartened that, again according to USA Funds' representations to the Department, Student Assistance Corporation's employee incentive plans are distinct from the standard plans for employees of the other SLM subsidiaries and include incentives to keep default rates as low as possible.

For these reasons, no further action is required for Finding 2, and it is considered closed.

The detail information provided for Findings 1.2 and 1.3 adequately addresses the issues raised in the OIG audit report concerning the proper handling of collections during October 1995 to October 1998 and that the use of monies, which would have benefited the Operating Fund, was for student financial aid related activities. Specifically, USA Funds provided the following procedures:

- For Finding 1.2, payments received from defaulted borrowers in the USA Funds internal collections department were deposited directly into the USA Funds Federal Reserves. Payments on defaulted loans from external collection vendors and lenders were remitted to USA Group Guarantee Services, Inc., an affiliated not-for profit company. USA Group Guarantee Services posted the payment on defaulted loans to the borrower's account upon receipt from the external collection vendor. At USA Group Guarantee Services, the funds were deposited into a checking account and if any interest was earned on the account, that interest was used to cover the administrative costs of providing the operational guarantee services of USA Group Guarantee Services for USA Funds. USA Group Guarantee Services provided services to USA Funds at cost. Following standard accounting procedures, and FFELP industry billing and collection practices, payments owed to and from USA Funds were settled on a monthly basis. In one to two days prior to the end of each month, an estimate of the net collections was remitted to USA Funds and deposited into USA Funds' Federal Reserves. USA Funds then had the cash in order to remit the Secretary's Equitable Share to the Department the first of the next month on the Form 1189 – Monthly Claims and Collections Report.
- For Finding 1.3, USA Funds has stated that Sallie Mae has not retained any Operating Fund assets of USA Funds. Moreover, no funds need to be returned to

the Operating Fund. Therefore, no further action is required for Findings 1.2 and 1.3 and these findings are considered closed.

Thank you for your cooperation throughout the audit review process. If you have any questions, please contact Katrina Turner at 202-377-3311.

Sincerely,



Matteo Fontana
Deputy General Manager, Financial Partners Services, FSA
U.S. Department of Education

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