

Reforming the Governance Structure of the California Student Aid Commission and EdFund

L E G I S L A T I V E A N A L Y S T ' S O F F I C E

Presented To:
Joint Assembly and Senate Education Committee





A History of Governance Problems

Initial Problems:

- ☒ In the 1980s and early 1990s, the California Student Aid Commission (CSAC) struggled to administer the federal student loan programs effectively.
- ☒ In response, the Legislature passed Chapter 961, Statutes of 1996 (AB 3133, Firestone), which authorized CSAC to establish an auxiliary agency. The auxiliary agency was entrusted with administering the federal student loan programs on the state's behalf.
- ☒ In 1997, the commission created EdFund as its auxiliary agency.

Recent Problems:

- ☒ Since its inception, EdFund and CSAC have struggled with a new set of governance problems.
- ☒ These governance problems came to the fore last spring when the commission dismantled the EdFund Board of Directors.

Legislative Response:

- ☒ In response to these more recent governance problems, the Legislature directed our office to submit a report identifying the range of structural options for administering the federal student loan programs. We released this report in January.
- ☒ In our February *Analysis*, we have a follow-up piece that recommends specific changes to the existing CSAC/EdFund governance structure.



Other Operational Problems Might Exist But Still Under Investigation

Another Set of Potential Problems:

- ☒ Last spring, the evident governance problems were compounded by allegations that EdFund might have inappropriate compensation and contracting practices.

Legislative Response:

- ☒ In response to these allegations, the Legislature directed the State Auditor to investigate these practices. The audit report is scheduled for release in April 2006.
- ☒ Given the audit is underway and its findings and recommendations have not yet been shared, we do not address these other operational issues.

Possible Impact of Audit Findings:

- ☒ If the state audit finds that EdFund has operational problems, the Legislature could either respond to those issues separately or in the same legislation addressing governance problems.
- ☒ One of the major benefits of the state audit is likely to be the identification and recommendation of stronger accountability provisions that could be critical under any governance structure.



EdFund Created to Overcome Initial Governance Problems

- ☒ In 1979, CSAC began administering the federal student loan programs.
- ☒ From 1979 to 1996, CSAC served as the single state agency responsible for administering both state grant programs and federal student loan programs.
- ☒ In the early to mid-1990s, concerns with CSAC administration of the federal student loan programs grew.
- ☒ The creation of EdFund essentially was the state's attempt to overcome existing governance problems and improve the efficiency and effectiveness of the state's administration of the federal student loan programs.
- ☒ Statute designated the auxiliary agency as a nonprofit public benefit corporation, and, as such, the agency was exempt from certain state employment and procurement practices.
- ☒ The new governance structure and associated statutory provisions were viewed by lawmakers and legislative staff as critical changes needed to enhance the state's responsiveness to loan market dynamics, colleges, and students.



Governance Problem 1: Tension Among Organizational Leadership

Separate Governing Bodies Have Created Tension Among Organizational Leadership.

- ☒ The commission consists of 15 representatives appointed by the Governor and Legislature that reflect the interests of higher education institutions, students, secondary schools, and the general public.
- ☒ The commission determines the size and composition of the EdFund Board of Directors.
 - As of April 1, 2005, the EdFund board had 14 representatives reflecting the interests of higher education institutions, students, business, law, EdFund employees, the CSAC Executive Director, and EdFund president.
- ☒ EdFund's bylaws permit the commission to remove any individual serving on the EdFund board at any time, with or without cause.
- ☒ When the commission voted to dismantle the EdFund board last spring, the minutes from the commission meeting indicated that the action was motivated by concerns with governance as well as by a desire to ensure that both agencies were working together toward a united set of goals.
- ☒ A disconnect continues to exist between organizational authority and operational responsibility.



Governance Problem 2: Disagreement Over Roles and Responsibility

State Law Does Not Adequately Delineate Which Agency Is Responsible for Which Operational Functions.



In our interviews with the two agencies, several areas of ambiguity and tension were identified, including determining which agency is responsible for:

- Developing EdFund's budget.
- Designating the use of Operating Fund monies.
- Representing EdFund's interests to the state.
- Negotiating EdFund's performance contracts with the federal government.



This tension is vividly illustrated by the inability of the two agencies to agree on any of the various draft proposals regarding their respective roles and responsibilities.



Governance Problem 3: Incompatible Incentive Systems

Incompatible Incentive Systems Have Detracted From a Student Focus

- ☒ Whereas CSAC is structured as a traditional state agency whose employees are subject to civil service laws and regulations, EdFund is structured as a nonprofit corporation whose employees are exempt from these laws and regulations.
- ☒ Whereas CSAC has typical civil service compensation plans based on routine step increases, EdFund uses variable incentive compensation plans that reward employees for providing high-quality service in their respective area.
- ☒ The leadership of both agencies has expressed concern that these incompatible incentive systems have led to certain perceptions of unfairness among staff.
- ☒ The resulting interagency tension also has detracted from a public focus on providing high-quality loan and grant service to students.



Range of Restructuring Options



The Legislative could select one of five basic organizational models for administering state grant and federal student loan programs.

Organizational Options	
Single Agency	
<p>State Agency Model</p> <p>Single state agency administers state grant programs and federal loan programs.</p> <p>Agency subject to state employment and procurement laws and regulations.</p>	<p>Nonprofit Public Benefit Corporation Model</p> <p>Single nonprofit public benefit corporation administers state grant programs and federal loan programs.</p> <p>Agency exempt from state employment and procurement laws and regulations.</p>
<i>Options as Applied to California:</i>	
(1) California Student Aid Commission (CSAC) (or another state agency) administers both grant and loan programs.	(2) EdFund (or another nonprofit public benefit corporation) administers both grant and loan programs.
Two Agencies	
<p>State/Dependent Guarantor Model</p> <p>A state agency administers state grant programs and a separate state-dependent or auxiliary agency administers federal loan programs.</p> <p>State employment and procurement laws apply to state agency but not loan agency.</p>	<p>State/Independent Guarantor Model</p> <p>A state agency administers state grant programs and an independent agency administers federal student loan programs.</p> <p>State employment and procurement laws apply to state agency but not loan agency.</p>
<i>Options as Applied to California:</i>	
<p>(3) Make no changes to existing CSAC/EdFund arrangement.</p> <p>(4) Modify CSAC and EdFund's roles and responsibilities.</p>	(5) Rely on CSAC (or another state agency) to administer state grant programs and an independent agency to administer federal loan programs.



LAO Restructuring Recommendation

- ☒ Given the unique intricacies of student financial aid, we recommend the Legislature authorize a single agency, with a single board and Executive Director, to administer both state grant and federal loan programs.
- ☒ Given the unique aspects of the federal student loan programs, we recommend the agency be structured as a nonprofit public benefit corporation but subject to stronger accountability requirements.
- ☒ This option is most likely to overcome existing governance problems.
 - With a single board and Executive Director, tension is less likely among organizational leadership.
 - With a single agency, confusion about roles and responsibilities is likely to be more easily and quickly resolved.
 - As a nonprofit public benefit corporation:
 - The agency could reward all employees for providing high-quality service to students.
 - The agency would retain flexibility to respond to externally driven changes in loan programs and loan competitors.
- ☒ Greater operational autonomy should be coupled with greater accountability and reporting requirements.
- ☒ The new structure could accommodate broader reform.