



Arizona Commission for Postsecondary Education

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October 9, 2007

Debra K. Davenport
Auditor General
2910 North 44th Street, Suite 410
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Dear Ms Davenport:

As the Executive Director of the Arizona Commission for Postsecondary Education (ACPE), I respectfully submit the Commission's response to the Performance Audit and Sunset Review of the Commission submitted on October 1, 2007. The Commission commends the Auditor General's office for the thoughtful and careful examination of the Commission's operations, activities, and initiatives that began with the Executive Director's response to the Sunset Factors in August 29, 2006 and resulted in the revised preliminary report draft to which this response is directed.

Much of the detailed investigation for this audit centered upon the Arizona Family College Savings Program (AFSCP), also known as the Arizona 529 plan. Furthermore, all recommendations in this report are related to the Arizona Family College Savings Program. This Program is administered by the Commission as a part of its core responsibilities of providing student financial assistance programs to postsecondary education students and their families.

The Commissioners commend the Auditor General's Office for making recommendations that will enhance and improve Commission procedures, identifying the significant changes in both the Commission and the AFCSP that have taken place over the past few years, and recognizing the value and expertise provided for the AFCSP administration through the AFSCP Oversight Committee. The structure established in Statute for the Arizona Family College Savings Program provides for a ten-member Oversight Committee of financial experts in fields within and contiguous to the 529 plan industry. The Oversight Committee is charged with the responsibility of recommending to the Commission appropriate program managers, contract terms, and administrative improvements of the Arizona 529 plan. Several of the recommendations within this audit report allow the Oversight Committee to make the final determination of how recommendations should be implemented. Because of this recognition of the expertise of the Oversight Committee, the Commission is in agreement with all ten recommendations posed in the report.

The staff and Commissioner's appreciate the professionalism of your staff during the audit and their willingness to engage in dialogue to ensure accuracy and understanding. The Commission looks forward to continuing this process and implementing the recommendations contained in the report.

Sincerely,

Dr. April L. Osborn
Executive Director

Response of the Arizona Commission for Postsecondary Education

to the

Revised Draft Performance Audit and Sunset Review by
the Office of the Auditor General

October 9, 2007



Submitted by Dr. April L. Osborn
Executive Director

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I. The Agency Mission is Outlined in Statute

ARS 15-1851 through ARS 15-1879 Defines the Program of Work for the Arizona Commission for Postsecondary Education

Because the Auditor General's Report was predominately focused on the role of the Arizona Commission for Postsecondary Education (ACPE) and its administration of the Arizona Family College Savings Program. The response to the Draft Performance Audit and Sunset Review will begin with an overview of the work of the agency as a whole and then address the two findings that were limited to the Arizona Family College Savings Program.

The Arizona Commission for Postsecondary Education has undergone significant changes since its last performance audit in November of 1997. The Commission was originally established within the Arizona Board of Regents (ABOR) and through legislative action taken in 1994 the Commission was permanently separated from ABOR.

This permanent separation was undertaken to allow the Commission to meet federal requirements for the administration of federal programs. Likewise, it provided the ability for the Commission to serve as a neutral, non-regulatory agency which serves all constituencies within the higher education system including community colleges, public universities, private colleges and universities, and vocational programs. The 1994 enabling legislation named a number of responsibilities to be undertaken by the Commission. Many of these ACPE responsibilities have remained constant over the past decade, including:

- administration of the Leveraging Educational Assistance Partnership grant (formerly SSIG),
- administration of the Paul Douglas Teacher Scholarship Program repayments and the ATIP repayment programs,
- provision of a forum for private and public postsecondary education institutions to discuss issues of mutual interest,
- provision of reports and the promotion of collaborative studies on issues of mutual interest for postsecondary education, and
- compilation and dissemination of information to the public regarding postsecondary education opportunities.

Over time the enabling statute for the ACPE was modified in a number of ways. The most notable changes required the ACPE to take on additional responsibilities of:

- administration of the Private Postsecondary Education Student Financial Assistance Program (PFAP) in 1996,
- administration of the Arizona Family College Savings Program (AFCSP) in 1997, including the initiation of the AFCSP Trust in 2005,
- administration of the Postsecondary Education Grant Program in the 2006 legislative session,
- administration of the Early Graduation Scholarship Grant Program in the 2007 session, and
- oversight of the Foster Youth Transition to Postsecondary Education Case Manager Program, also in the 2007 session.

In summary, many of the core areas of responsibility, as outlined in statute, for the Commission have remained constant since 1994. Over the past decade the legislature has required the Commission to assume additional administrative duties in student financial assistance with the addition of PFAP, the Arizona Family College Savings Program, the Postsecondary Education Grant Program, and the Early Graduation Scholarship Grant Program.

II. The Agency Mission is Addressed through a 5-Year Strategic Plan

Staff are Directed by a 5-Year Strategic Plan Developed by Commissioners

The work of the Arizona Commission for Postsecondary Education (ACPE) is guided by a 5-year strategic plan that focuses its staff and resources on the Commission's legislative mandates. The purpose of the plan is to ensure the activity of this small agency and its eight staff members is focused on the appropriate activities and initiatives in order to increase productivity and impact in the areas of its statutory authority. The Commission is comprised of 14 Governor-appointed representatives who are senior management in the various sectors of postsecondary education and two Commissioners named by position: the Executive Directors of the Arizona Board of Regents and the Arizona State Board for Private Postsecondary Education.

The Commissioners identified an agency mission of *expanding access and increasing success in postsecondary education for Arizonans*. Three goals were named to achieve this mission: (1) increase available student financial resources, (2) implement strategies to help students and their families plan, enter, and succeed in postsecondary education, and (3) provide a forum for all sectors of higher education to dialogue, partner, and problem solve issues of mutual interest. At the time of this performance audit, the Commission had just completed its third year of the 5 year plan and review of goals, performance, and outcomes as outlined in the plan.

In response to the Commissioner directed goals, the ACPE staff has identified efficient and effective administration of the financial assistance programs under their management as the primary strategy to achieve Goal 1. The second and third goals are supported through policy analysis and research, as well as by collaborative action led by ACPE task forces and participation in college access initiatives led by foundations, government, or non-profit entities with similar missions.

The strategies of efficient and effective administration and leveraging resources through collaboration and partnerships are born of necessity, as the agency received less than \$240,000 of state general funds for agency operations in 2006-2007. This amount is only 51% of the total operational budget, while program administration fees, donations, and grants fund the balance of the operational budget of the agency.

III. Outcomes of Agency Activities and Initiatives

FY 2006-2007 Outcomes of the Arizona Commission for Postsecondary Education

Objective 1: Effective, efficient administration of student financial assistance programs under the ACPE

- Leveraging Educational Assistance Partnership (LEAP)

\$2.8M was disbursed to more than 4,000 low income students attending 47 postsecondary institutions including community colleges, public universities, and private colleges and universities in FY 2007 through the LEAP program.

- Private Postsecondary Student Financial Assistance Program (PFAP)

\$150,000 was disbursed to 101 students with financial need who graduated from Arizona community colleges and attended private colleges and universities to attain a baccalaureate degree in 2007.

- Postsecondary Education Grant (PEG) Program

PEG program funds were released to the ACPE in November. Staff was hired, the program developed, technology was in place, and in the last three months of FY2007 \$1.8M dollars were disbursed to 1,077 students seeking a baccalaureate degree from Arizona private colleges or universities.

- Repayment Programs

Seventy-six students were in repayment for Paul Douglas and PFAP forgivable loans in FY 2007. Likewise, forty-five students were in process for repayment or have been turned over to the Attorney General's office for collection in that year.

- Early Graduation Scholarship Grant Program

This new program is designed to provide an incentive to motivate high school students to graduate early and transition into a postsecondary educational experience. The EGSG Program is currently under development.

- Arizona Family College Savings Program

More than 45,000 accounts were opened and more than \$422 M was saved by families to pay for college expenses in the Arizona Family College Savings Program since 1999. The number of Arizona accounts increased 21.5% in FY 2007.

- Arizona Family College Savings Program Enhancements Have Been Implemented Program Restructuring A rigorous annual provider review process concluded in the non-renewal of two program providers (Pacific Life and Securities Management & Research).

Professional money management is now provided by three experienced and trusted financial institutions

College Savings Bank (Direct-sold CD)
Fidelity Investments (Direct-sold Mutual Funds)
Waddell & Reed (Adviser-sold multiple funds)

College Savings Plan Network (CSPN) Principles of Disclosure is the standard *The Arizona Family College Savings Program* providers offering materials are required to meet. Review of provider materials and documentation are measured against these voluntary profession-identified standards for clarity and investor disclosure by the Arizona Commission for Postsecondary Education.

A broad range of investment options are available. Fidelity Investments announced several enhancements to the Fidelity Arizona College Savings Plan including a new line of Index Funds portfolios, which are among the lowest cost in the 529 industry. In addition, Waddell & Reed has launched a new class Ivy Funds of shares giving financial advisers access to a wider range of choices more adaptable to individual needs as they work with their clients. College Savings Bank offers a FDIC insured Certificate of Deposit.

Fees have been reduced. Waddell & Reed implemented fee reductions in the beginning of 2006 across all its age-based portfolios and converted all mutual funds Class B and Class C shares to the lower-cost Class A shares at no cost to the investors. Furthermore, Fidelity Investments eliminated its low-balance annual fee and reduced the initial investment minimums as well as the monthly contribution amount minimums for those accounts with automatic investment plans.

Objective 2: To provide information to parents and students to assist in college preparation, planning, transition, and success

- Arizona College and Career Guide

15,000 copies of this publication which provides a comprehensive listing of all Arizona postsecondary institutions, programs offered, and tuition and fees were distributed to high school counselors, high school seniors, vocational rehab program administrators, postsecondary education professionals, and other parties of interest in FY 2007.

13,000 visits were counted on the Arizona College and Career website that same year.

- Countdown to College

800,000 copies of this 12-page insert detailing financial aid processes and opportunities and college-going information for families and students were distributed across the state on Sunday, February 4, 2007 in the *Arizona Republic*. This is a partnership effort with USA Funds.

- Web portal for college-going and financial assistance

41,880 visits were counted for the Commission website. The site includes extensive information regarding student financial aid and instructions for completing the processes and meeting the deadlines for securing student financial aid.

- College Savings Planner

2,000 copies of a 16-page college savings planning document, which describes and compares various savings vehicles families can use to save for college, were distributed to families and 13,140 downloads of the planner from the website took place in FY 2007.

- Rapid Guide to Student Financial Aid

This pocket-sized laminated guide provides to high school juniors Arizona-specific information about federal, state, and local financial aid. This new initiative is being undertaken to assist students as they navigate the complex processes necessary to access the financial aid that is available. The Arizona Commission for Postsecondary Education plans to distribute 15,000 copies of this guide with the help of high school counselors in FY 2007-2008.

Objective 3: Serve as a forum to problem solve and seek opportunities across all sectors of public and private postsecondary education and through policy analysis and research to identify issues of common interest to the postsecondary education leaders.

- College Goal Sunday Program (statewide)

This grant-supported program (1) provides timely information on the financial aid processes and encourages students to access the financial aid that is available to them, and (2) coordinates a statewide event for students and their families where they are assisted by more than 300 college financial aid professionals in completing the Free Application for Federal Student Aid (FAFSA). The FAFSA is the single form required to access nearly 95% of all financial aid. The FAFSA has been found by researchers to be more difficult to complete than the annual IRS income tax form.

More than 2,800 parents and students attended the February 2007 event where more than 310 college financial aid professionals assisted them in completing the FAFSA.

18,974 visits were counted on the College Goal Sunday website where information and line-by-line instructions are available for the public's use in completing the FAFSA on-line.

- Arizona Minority Education Policy Analysis Center (AMEPAC)

This donation supported policy analysis center is housed within and supported by the staff of the ACPE. Published studies include

The Road to Higher Education, 2006;

Investing in Arizona's Future, 2005; and

Minority Student Report 2007: A Snapshot of Arizona's Educational Achievement

- Developing Arizona's Human Capital Conference & Pathways to Higher Education Awards

The 8th conference takes place on November 8 & 9, 2007 with a goal of providing a forum for discussion and planning for the improvement of the Arizona postsecondary education system.

20 applications describing Arizona college access, transition, and success programs were received and 5 award winners were recognized at the 2006 conference as a means to publicize Arizona's best practices and encourage the initiation or the adoption of successful programs.

IV. Agency Response to Performance Audit Findings and Recommendations

Finding 1: Arizona's 529 Program Offers Most Features of a High Quality Program

Recommendation 1:

The Oversight Committee should continue to monitor the performance of all of the mutual fund options to ensure that they meet or exceed their benchmarks, and the Commission should take appropriate action as necessary based on the Oversight Committee's recommendations.

The Arizona Family College Savings Program (AFCSP) Oversight Committee places great importance in its responsibility to monitor the performance of all providers' investment options, both mutual funds and the Certificate of Deposit. As the Auditor General's office reported, this takes place through the quarterly reports from the vendors, an annual written report wherein vendors evaluate their own investments against benchmarks appropriate to their products, and the annual face-to-face interviews with representatives of each of the program manager representatives. Questions are asked and answered regarding performance at the time of the review of the written report, at the face-to-face interviews with providers by the Committee, and follow-up questions are asked when necessary after the interview. If answers are not satisfactory regarding investment performance following the report, interview, and questions, an on-going discussion regarding investment performance is initiated with the AFCSP staff leading the dialogue.

It is this rigorous and extensive annual performance review process that resulted in the non-renewal of the contracts of two of five providers in 2006. The process continues to be refined and adapted as necessary and investment performance is a critical factor in the annual review. The finding of the Auditor General is agreed to and the audit recommendation will continue to be implemented.

Recommendation 2:

The Commission should determine what customer service and customer satisfaction information it needs, and require that providers or commission staff collect this information and provide it to the Oversight Committee.

The Arizona Family College Savings Program Oversight Committee has been focused on customer satisfaction of account holders for some time. At the July 26, 2007 Oversight Committee meeting, Committee members again iterated the opinion that the best measures of customer satisfaction lie within the numbers of newly opened accounts, the numbers of accounts closed and rolled over, and growth of the assets in college savings accounts in each of the plans. This data has been a part of the review of the Arizona 529 plan by the Oversight Committee since its inception.

When the Arizona Family College Savings Program Annual Provider Review Process was established there was much discussion around the issue and the challenge of a common

customer satisfaction measurement standard for the three widely varied financial products offered. The AFCSP includes program managers who provide a CD investment option, direct sold mutual fund offerings with application on the internet and guidance provided over the phone, and an advisor sold mutual funds option where advisors provide face-to-face financial advice to clients.

On July 26, 2007 the Committee added to the required Annual Provider Performance Review Report the submission of all customer service data collected by each program manager. The revised process was accepted by the Arizona Family College Savings Program Trustees at the August 15, 2007 Arizona Commission for Postsecondary Education meeting. Therefore, the February 2008 annual provider review report will require each of the three AFCSP program managers to submit all data currently collected regarding customer satisfaction, the benchmarks used for evaluation, and the measurement of results against each of these benchmarks.

The finding of the Auditor General is agreed to and the audit recommendation is being implemented.

Recommendation 3:

The Oversight Committee should determine the best way to use customer service and customer satisfaction information in evaluating the providers.

As stated in the response to Recommendation 2, the Oversight Committee will evaluate the data, benchmarks, and success measures offered by providers regarding their customer satisfaction data and benchmarks in their annual report in early 2008. The Committee will determine following the 2008 provider review process if any further information is needed, and if changes are necessary for the next provider review process to achieve the goal of adequately measuring customer satisfaction among these the three disparate vendors.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Recommendation 4:

Based on the Oversight Committee's determination, the Commission should add customer service benchmarks to its provider contracts to ensure that the standard of customer service evaluation is clear to the 529 program providers.

The advice of the Arizona Family College Savings Program Oversight Committee as outlined in the response to Recommendation 3 will be sought to determine the best way to hold providers accountable for customer service. Again, the diversity of products and the mode of delivery of the products (direct sold and advisor sold, on-line and via a call center) will require careful consideration and review by the Oversight Committee and the ACPE staff to determine if benchmarks are appropriate for each vendor. Likewise, the advice of the Attorney General's office will be sought to determine if such benchmarks are appropriate to include in the negotiated contracts with current and future program managers. With the additional data collected, the Oversight Committee will make a determination regarding customer satisfaction benchmarks.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Finding 2: Provider Monitoring Has Improved, but Should be Further Enhanced

Recommendation 1:

To enable the Oversight Committee to provide more complete and effective oversight of the Arizona 529 program providers, the Committee should:

- a. Standardize its review methodology including documenting its consideration of the eight factors required by A.R.S. {15-1874(C)}; and**
- b. Add Provider partnership to the areas it formally reviews, and establish criteria by which to assess partnership.**

The Arizona Family College Savings Program Oversight Committee has developed and implemented a comprehensive Annual Provider Review Process that has served as a model for other states. This process is derived from the statutory requirements for evaluation included in ARS 15-1874 as cited in Recommendation 1. The Commission Executive Director presented the Arizona Annual (529) Provider Review Process at the July 14-17 *The Roadmap to Operational Excellence* conference held by College Savings Plan Network in New York, NY.

The presentation invitation resulted from recognition within the industry that Arizona has developed a successful method of evaluating varied financial products and diverse financial institutions. The Arizona review process is of interest nationally because in the very young 529 plan industry very few states began their programs with more than one vendor. Today, as many states are moving toward two-provider or multi-provider platforms, Arizona is considered a leader and therefore there is interest in Arizona's evaluation process. Most importantly, this evaluation process successfully guided the Commission's decision to terminate two program managers as they were deemed to be no longer meeting the needs of the State nor the families saving for college in the Arizona 529 Plan.

The AFCSP Annual Provider Review Process is modified annually as necessary to meet the changing state and 529 plan environments. The Annual Provider Review Process for 2008 was approved by the Arizona Commission for Postsecondary Education in August. It includes a partnership component as suggested in the Performance Audit Report. The Oversight Committee will refine the methods for the evaluation of this parameter throughout the coming years as they gather more data on this aspect of the relationship with financial institutions.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Recommendation 2:

The Oversight Committee should also:

- a. Explore the feasibility of establishing qualitative or quantitative standards for assessing providers according to the statutory criteria, and**

b. Incorporate those standards, as appropriate, into its methodology for reviewing providers.

The AFCSP Oversight Committee intends to continue to improve the Annual Provider Review Process as it is used over repeated years. This will involve continuing to implement modifications that will enhance the process for the benefit of the state and families who invest in the Program. The intent is that it will become a more standardized process and that performance measures can be identified that can be used across products and years. However, the Oversight Committee understands the evaluation process will need to remain fluid as changes in products, providers, and the 529 plan environment will continue to occur rapidly in this very new industry. The evaluation to date has relied on both a qualitative and quantitative approach; however, the Committee will seek to move toward a more refined analysis for evaluation as it deems appropriate.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Recommendation 3:

When its 529 provider contracts can be renegotiated, the Commission should strengthen the language in the contract to require:

- a. If the Commission does not adopt a policy disallowing the sale of mutual fund shares carrying sales charges that must be paid when account shares are sold, in the event of a provider's termination or non renewal, the provider must transfer the accounts to a new provider in a way that does not impose additional costs on the accountholders.**
- b. All providers to submit audited financial statements to the Oversight Committee.**
- c. Providers to undergo a review of their information technology security, take appropriate action if the reviews identify any weaknesses, and report the outcome to the Oversight Committee.**
- d. Providers to take appropriate action if the reviews show IT security weaknesses, and report these results to the Oversight Committee.**

It is the assumption of the Commission that sales charges named in Recommendation 2.a. are Contingent Deferred Sales Charges (CDSC) or back-end fees which are a part of certain investment products. As is indicated in the recommendation, the AFSCP Oversight Committee has considered this issue of these fees and has determined to exclude any products in their recommendation to the Commissioners that charge CDSC fees from future Arizona Family College Savings Program offerings.

Submission of audited financial statements to the Oversight Committee is currently a requirement of the Annual Provider Review report. It is also a requirement of two of three provider contracts. As suggested in the recommendation, a summary of the information

technology security reviews for each provider will be added to the report required of each provider in the Annual Review Process to take place in a few months. The Commission is in agreement that any identified weaknesses will be required to be addressed by the provider.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Recommendation 4:

When renegotiating its 529 provider contracts, the Commission should consider adding a requirement that providers that have undergone an internal control review submit the results to the Oversight Committee.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Recommendation 5:

The Commission should ensure that it includes an asset-based fee provision in its contracts with Fidelity and College Savings Bank, when the contracts can be renegotiated.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Recommendation 6:

The Commission should ensure that:

- a. Rules governing asset-based fees are adopted to allow the Commission to use these monies, and;**
- b. These rules only allow the monies to be used for expenses related to the 529 program.**

Revised rules with language providing the aforementioned fees be used only for the expenses related to the administration of the Arizona Family College Savings Program have been submitted to the Attorney General's Office. The proposed revised rules state that the Commission may use the collected fees to pay for expenses related to the administration of the Arizona Family College Savings Program including but not limited to operating expenses, legal service expenses, and marketing expenses. The rule making process will be concluded at the earliest possible time.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

VI. Conclusion

The Arizona Commission for Postsecondary Education commends the Auditor General's Office for the careful examination of the Commission's operations, activities, and initiatives undertaken on behalf of the State. The Commission will take seriously the recommendations for improvement outlined in the report and is grateful for the fair and objective review provided of the work of the Commission.

Likewise, the Commissioners were pleased that the review of the overall work of the agency found that the Commission has operated in the public interest by providing programs that help provide financial assistance for students, engages in outreach programs that provide information about postsecondary education, and produces studies relating to minority education in Arizona.

The report also named the Commission website as a valuable source of information for the public about postsecondary education. And finally, the audit recognized the Commission for serving as the single state forum where all sectors of public and private education come together to discuss issues of mutual interest.

Likewise, the auditors looked extensively into the administration of the Arizona Family College Savings Program and found the Commission effective in its administration of the 529 plan. Furthermore, the audit report noted recent Commission actions resulting in reduced fees and an extensive annual provider review process.

The goal of the Commission is to continually work toward its mission and objectives of *expanding access and increasing success in postsecondary education for Arizonans*. This examination of Commission operations, activities and initiatives serves as a valuable resource for achieving these goals.