

EDUCATION ASSISTANCE FOUNDATION

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May 11, 1999

Comment Letter No. 7
File Reference: 1082-194R
Date Received: 5/17/99

Director of Research and Technical Activities
Financial Accounting Standards Board
401 Merrit 7
P.O. Box 5116
Norwalk CT 06856-5116

Subject: Consolidated Financial Statements of Not-for-Profit Corporations

Dear Sir:

This letter is in reference to your proposal to consolidate financial statements for affiliated companies of not-for-profit organizations.

We believe, due to the complexity and uniqueness of our business situations, a consolidation of financial data of any kind would only accomplish a distorted, inaccurate financial reported position of our affiliated companies.

The enclosed summary illustrates our situation.

We would appreciate your review of this summary. Our conclusion is that we should be exempt from any consolidation of financial information, based on our primary position of separate "control" of each affiliated company.

We would like to hear from you how you perceive our analysis. Please feel free to call me (206) 461-5310 or Email me at tonyb@sifaloo.com at any time.

Thank you for your attention in this matter.

Sincerely,



TONY BRIGHT
Vice President of Finance

Enclosure

EDUCATION ASSISTANCE FOUNDATION

Proposal by the F(inancial) A(ccounting) S(tandards) B(oard) to consolidate not-for-profit financial statements for affiliated companies

Analysis

Intention of Proposal

The proposal intends to require not-for-profit companies to consolidate their financial statements into one if affiliates are controlled (1) by a parent.

Effective Date

The proposal, if adopted, would become effective for fiscal years starting after December 15, 1999. FASB encourages earlier implementation. FASB invites comments, which must be submitted to them by May 24, 1999.

Requirements

If adopted, and if applicable, NELA, SLFA, HEFA and SLFA Services' financial statements would have to be consolidated into one financial statement (Balance Sheet, Statement of Revenues and Expenses and Cash Flows) under EAF. Comparative statements for prior periods would have to be prepared.

Organization

Education Assistance Foundation (EAF) was incorporated in the State of Washington in 1986 as a not-for-profit corporation, exempt under IRC Sections 501(c)(3), 509(a)(1) and 170(b)(1)(A)(vi). Its purpose (per IRS Form 1023 and Articles of Incorporation) is to promote and facilitate the attainment of higher education by individuals and to serve as sole voting member for both NELA and SLFA, and to create, own and operate such other companies as it deems necessary to carry out its purpose.

Northwest Education Loan Association (NELA) was incorporated in the State of Washington in 1978 as not-for-profit corporation, exempt under IRC Sections 501(c)(3) and 509(a)(1) and 170(b)(1)(A)(vi). Its purpose (per IRS Form 1023) is to guaranty against default loans made pursuant to the Federal Family Education Loan Program (rev.) (FFELP). In this capacity NELA entered into contractual agreements with the U.S. Department of Education (DoE) (a Federal government agency) to perform, on its behalf, the following functions: To perform the guarantee process of student loans, pay lenders on defaulted accounts (claims) and collect on such defaulted accounts from the borrowers. NELA receives a fee from the DoE, under its contracts, to perform such services. As claims are paid, the DoE for such payments reimburses NELA. As NELA collects from borrowers it retains a 24% share of such collections; the balance is paid to the DoE. NELA, in addition to the contracted services with the DoE it must

provide, also offers other services to lenders and school in the FFELP. Such services include the handling of disbursement of loans to borrowers/schools on behalf of the lenders. NELA guarantees loans mostly to Washington State and Idaho banking institutions. NELA is the designated guarantor (by the DoE) in the States of Washington and Idaho. All administrative functions handled by NELA are contracted to SLFA Services. NELA maintains no employees.

Student Loan Finance Association (SLFA) was incorporated in the State of Washington in 1982 as a not-for-profit corporation, exempt under IRC Sections 501(c)(3) and 509(a)(2). Its purpose (per IRS Form 1023) is to acquire student loan notes which are 100% guaranteed by NELA in order to promote and facilitate current and future access to student loans, all for the benefit of the citizens of the State of Washington and students of institutions of higher education situated in the State of Washington and to carry out the federal policies reflected in the FFELP. To acquire the funds to purchase such loans, SLFA issued tax-exempt bonds to the public. SLFA currently maintains a student loan portfolio with outstanding receivables amounting to approximately \$92 million. All administrative functions handled by SLFA are contracted to SLFA Services. SLFA maintains no employees. External servicers and SLFA Services service SLFA's student loans.

SLFA Services (Services) was incorporated in the State of Washington in 1998 as a not-for-profit corporation, exempt under IRC Sections 501(c)(3) and 509(a)(3). (Note: Application pending with the IRS). Its purpose per IRS Form 1023 is to perform activities that facilitate access to higher education through increased availability of student loans. Its planned activities include: 1) services to affiliates of EAF for centralized administrative, marketing and related services; 2) loan servicing and 3) other services. Staff in Services through contractual agreements handles all administrative functions for EAF affiliates.

Higher Education Finance Association (HEFA) was incorporated in the State of Washington in 1995 as a not-for-profit corporation, exempt under IRC Sections 501(a) and 501(c)(3) to facilitate education loans that bridge the gap between limited federally supported financial aid and the too-expensive commercial credit market.

Characteristics of EAF and its affiliates

Although all affiliates have a relationship in the business with one another, each affiliate's business purposes are different from the other. EAF and all its affiliates are not-for-profit corporations registered in the State of Washington and exempt under IRC 501(c)(3).

EAF is the holding company of various affiliates (see above). Its only administrative functions include the maintenance of the Pension Plan on behalf of all affiliates, the maintenance of a Deferred Compensation Plan (for some executives employed in SLFA Services) and acts as the Common Paymaster on behalf of all affiliates.

SLFA, as a secondary market corporation, purchases and sells student loans on the secondary market from/to lenders. It also services such loans (through a third party provider). SLFA has no employees. Staff support is provided through a contractual arrangement with and through SLFA Services. SLFA has no other business relationship with HEFA or NELA. NELA, however, guarantees the majority of student loans SLFA maintains in its portfolio. SLFA's assets are restricted for the exclusive use to purchase student loans.

NELA is the guarantor of FFELP loans and acts as a sub-contractor with the Federal government (DoE). In its capacity and through contractual agreements, NELA must perform certain duties to be eligible for government support (reimbursements and assistance 'grants') for such services. NELA has no need of any of EAF's affiliates to conduct its business functions. However, as of FY 99, NELA entered into a contract with SLFA Services. Under that contract, SLFA Services provides all support functions, as far as the work force is concerned, to handle NELA's business functions. NELA has no relationship to SLFA or HEFA other than it is affiliated with these two companies through the control (parent) of EAF. NELA has no employees. All staff support is provided by SLFA Services.

NELA is very highly regulated through the Higher Education Act of 1965, as amended). In its capacity as guarantor, NELA maintains two types of funds in its books: a) Federal Reserve fund (entirely restricted to specific functions, such as paying claims, etc.) and b) Operating fund (used for operational and administrative functions). **It must be noted that all assets in the Federal Reserve fund are considered Federal property and are forbidden to be combined with any other assets (funds). The Federal government at their discretion may recall such funds.**

SLFA Services provides services (staff support) to all EAF affiliates to handle their daily business functions. Such arrangements are agreed to through contracts between SLFA Services and each affiliate, but not with EAF. No support is provided to EAF from SLFA Services. SLFA Services also services student loans to any lender, including SLFA.

HEFA at the current time is not an active corporation. Its charter provides for the guarantee and disbursement process of non-FFELP (privately funded) student loans. HEFA has no relationship with another EAF affiliate other than obtaining staff support to handle its administrative and business functions. HEFA has no employees.

Each affiliate's **Board of Trustees** acts independently from one another. However, some Board of Trustee members of one affiliate are members of the Board of Trustees of other affiliates.

Comments

Following are some major reasons why no consolidation of financial data should take place for any of EAF's affiliates:

- 1) NELA is unique amongst all affiliates with its tight restrictions placed upon it by the Federal Government (DoE). A combination of its assets with any other affiliate would give the reader misleading information would its financial data be included in an EAF consolidated financial statement.

- 2) Each affiliate has its distinct and unique business function and a combination of financial data of EAF affiliates, even with lengthy footnotes, would provide unreliable and wrong information.
- 3) Each board of trustees acts independently from one another and is not, in any way, influenced by the board of trustees of other affiliates. As such EAF's board of trustees has no ability to direct the policies and management of its affiliates and has no decision-making ability over any affiliate.
- 4) Service and management agreements between affiliates clearly identify services that the other affiliates provide.
- 5) SLFA Services, as the support company to all affiliates, charges affiliates agreed-upon management and service fee for services provided.
- 6) The parent (EAF) has no financial interest in any affiliate.
- 7) No affiliate of EAF has any financial interest in another affiliate.
- 8) No affiliate pays any fee of any kind to EAF.

Recommendation

We recommend that such structures and organizations as described above be excluded from the subject Proposal. Each affiliate's financial statement would indicate its affiliation with EAF and its affiliates and disclose appropriate information as required under FASB Statement No. 57.

Definitions: (1)

- Control:
- a) If EAF has a majority voting interest in any affiliate.
 - b) If EAF has a large minority voting interest in the election of an affiliate's governing body and no other party has a significant voting interest.
 - c) If EAF has a unilateral ability to (1) obtain a majority voting interest in the election of an affiliate's governing body or (2) obtains a right to appoint a majority of the affiliate's governing body.
 - d) EAF (as the controlling entity) has the ability to **direct** the policies and management of subsidiaries (affiliates).
 - e) Affiliates pay a fee to EAF.
 - f) EAF has decision-making ability over any affiliate. (Ex: EAF can influence an affiliate to transfer assets to another affiliate to increase the benefits or limit its losses in that affiliate).

Reference Material used for this research: FASB Financial Accounting Series Publication 194-B, Exposure Draft (revised): Proposed Statement of Financial Accounting Standards – Consolidated Financial Statements. Modified to accommodate EAF's situation. FASB Statement of Position 94-3 (Reporting of Related Entities by Not-for-Profit Organizations), FASB Statement of Financial Accounting Standards No. 94 and FASB Statement of Financial Accounting Standards No. 117.