Report on the development of policies and procedures which minimize the use of paper checks when issuing any reimbursements of student loan balances from universities and community colleges. These efforts should include reimbursement through debit cards, direct deposits, or other electronic means.

Chapter 3, 2012 Appropriation Act requires the Department of the Treasury (Treasury) to work with universities and community colleges to reduce the use of paper checks when providing reimbursements for student loan balances as noted below:

> *Item 277 G. "The State Treasurer shall work with universities and community colleges to develop policies and procedures which minimize the use of paper checks when issuing any reimbursements of student loan balances. These efforts should include reimbursement through debit cards, direct deposits, or other electronic means. The Treasurer shall report to the Chairmen of the House Appropriations and Senate Finance Committees on the status of these efforts on or before November 15, 1012."*

The Department of the Treasury formed a workgroup which included college, university and community college representatives and staff from the Department of Accounts and Treasury to develop policies and procedures that would enhance the use of electronic payments. In compliance with this request, the project team developed two documents:

1. Discussion Paper – Student Loan Refunds outlines the background of the student loan reimbursement process, current landscape, cost analysis, options and key considerations, regulatory environment, and conclusive recommendations of the project team.

2. Proposed Policy and Procedure for Converting Student Loan Refunds to Electronic Means outlines the proposed policy and procedures along with legal and regulatory requirements, and compliance and reporting requirements. Also discussed is the possible use of a third party vendor for the administration of such programs by the institutions.

Attachment 1

Student Loan Refunds

Initiative for the Conversion of Paper Disbursements to Electronic Methods

Discussion Paper – Student Loan Refunds

November 15, 2012

Chapter 3, 2012 Appropriation Act, requires the Department of the Treasury (Treasury) to work with state universities and community colleges to develop policies and procedures which minimize the use of paper checks for student loan refunds as noted below.

> *Item 277 G., Chapter 3, 2012 Appropriation Act:*
> *"The State Treasurer shall work with universities and community colleges to develop policies and procedures which minimize the use of paper checks when issuing any reimbursements of student loan balances. These efforts should include reimbursement through debit cards, direct deposits, or other electronic means. The Treasurer shall report to the Chairmen of the House Appropriations and Senate Finance Committees on the status of these efforts on or before November 15, 2012."*

A work group consisting of representatives from Old Dominion University, Virginia Commonwealth University, Virginia State University, the Virginia Community College System, the Department of Accounts, and Treasury was developed to address this directive.

Background

A student refund typically occurs when the student's account shows a credit balance. This credit balance can result from a number of circumstances, including:

- **Financial Aid Refund:** The student's financial aid is greater than the costs assessed by the institution and the remaining balance is generally considered a credit balance. Financial Aid can come in many forms including loans, grants, and scholarships. Financial Aid that is provided by the Federal Government is called Title IV Aid and is subject to strict regulations for handling and delivery. It is important to note that the aid is administered by the institution to the student and that the refund in this case is usually the amount left over after tuition and other expenses have been satisfied. Often this is used by the student for living expenses, housing, etc.

- **Dropped Class Refund:** Students who pay by a check, cash, credit card or other electronic methods and then subsequently drop a class within a prescribed period of time are due a refund for all or part of the cost of that class. This would also create a credit balance and necessitate a refund back to the student. For students paying with a credit card, the refund is generally returned electronically to the credit card used for the original payment.

- **Other:** There are a variety of other scenarios that would result in a credit balance and thus a refund. Examples include parking fees, dining, rooming, etc. In most cases, if a check or electronic payment was used for the original payment, a refund will need to be delivered to the student.

Prior to 2000, most institutions distributed student refunds in one of two ways:

1. Students were required to visit an office on campus, wait in line and physically pick up a student refund check.
2. Student refund checks were mailed to students at an address on file in the campuses Enterprise Resource Planning (ERP) system.

Both methods presented different challenges for students:

- At peak student refund periods (usually the start of each semester), students had to wait in long lines to collect their student refund checks during business hours.
- Students had to wait for checks to arrive in the mail, which could take up to five days.
- Checks were lost in the mail or sent to incorrect or out-of-date addresses. This would cause additional delays for students.
- Students had to research, qualify for, and open an account with a local banking institution so they could easily and conveniently deposit their student refund checks in an FDIC-insured bank account.
- Students who could not qualify for a bank account would incur high check cashing fees to obtain their student refund money.

For campuses this process was expensive and labor intensive:

- Collecting student addresses
- Check printing
- Envelope stuffing
- Reconciling bad addresses
- Handling returned checks and escheatment
- Staffing the business office to hand out checks
- Providing customer service
- Complying with the Department of Education’s rules and regulations pertaining to Title IV distribution

Around 2000, some campuses both nationwide and within Virginia began to distribute students refunds by direct depositing the funds into a bank account, much in the same way they were handling payroll. While this represented a quicker, more efficient manner in which to deliver refunds, it did not present solutions for all of the challenges associated with paper check refund distribution and it presented a few new challenges.

- Only a small percentage of students enrolled in the direct deposit program so campuses had to manage two student refund distribution processes: Paper check and direct deposit.
- Campuses had to manage compliance with Department of Education's rules and regulations pertaining to Title IV distribution.
- Not all students could qualify for bank accounts, rendering them ineligible for direct deposit enrollment.
- Campuses still had to provide customer service, but now they were doing so for two different student refund processes.
- Campuses had to reconcile returned money; most likely due to incorrect or changed bank account information.
- Campuses had to educate their students about the direct deposit student refund program, so students would understand the enrollment process.

In July 2008, the Department of Education released new regulations encouraging Electronic Refund Delivery that included:

- Specific guidelines for electronic disbursements
- A rule that enabled institutions to <u>require</u> students to choose an electronic method for delivery of funds
- A clause that mandated a paper check be disbursed if a student took no action in terms of enrolling in a direct deposit program

At the same time, Higher Education was facing a number of significant challenges such as:

- Slashed budgets
- Growing student populations
- Changing student needs and expectations
- Increased security risks
- Reduced staffing
- Compliance
- Calls for sustainability
- Increases in tuition

The convergence of these factors led to a heightened interest in electronic refund disbursement and spurred a move by schools to strongly consider utilizing this method for student refund delivery. As a result, a number of Colleges and Universities launched electronic refund programs using the Automated Clearinghouse (ACH) Direct Deposit service.

Current Landscape

Current profile consists of 16 universities and 23 community colleges. All the universities and community colleges responded to the student refund survey. The attached results (Table A) reflect over 492,000 credit balance refunds were issued totaling over $672 million in FY 2012. Twelve of the universities have made progress to disburse funds electronically to a varying degree of success. For the 16 universities 39% of refunds were issued by direct deposit to the student and/or parent. 61% are still refunded by paper check. Responses have also indicated most institutions issue campus cards, however refunds are not dispensed to the card because a campus card cannot be used unless it is tied to a true bank account or via other special arrangement. The Virginia Community College System currently disburses 100% of refunds via paper checks.

Cost Analysis

Paper check processing continues to be more expensive. Based on the cost analysis completed for the Governor's Operational Review Task Force for Banking Services in November 2010, bank and related cost of sending a payment electronically is 9 cents per transaction compared to 74 cents for a paper check. This cost savings of 65 cents per transaction does not include administrative handling costs colleges and universities may incur. Our analysis reflects only 19% of refunds are being disbursed by direct deposit method. This leaves opportunity for more than 80% of paper checks currently issued as eligible for conversion.

Based on estimated annual costs for paper checks reaching $331,498 and the estimated annual cost for electronic transactions estimated at $40,317, bank and related cost savings could exceed $291,180 per year. (See Table A for details.)

The above is based on the Treasury cost structure which has many advantages over individual institutions costs due to the spreading of fixed costs over a much greater volume. According to the report entitled "Review of State-Wide Disbursement Methods" conducted by the Commonwealth of Virginia Auditor of Public Accounts dated November 1, 2010, banking services cost breakdown for check writing by college and universities have a range from 71 cents to $2.55 per transaction with an overall average cost of $1.75. This presents additional opportunities for savings. However, any third party provider fees would need to be included in a cost/benefit analysis.

Solutions in use include:

- School developed and managed direct deposit program for student refunds (paper check distribution handled separately)
- "e-Refund" software to administer a direct deposit program for student refunds (paper check distribution handled separately)

- Partially outsourced student refund distribution with or without Paper Check
- Comprehensive student refund solution with paper check
- 100% paper check student refunds (in person pickup or by mail)

There are a number of vendors that provide outsourced refund solutions. These providers fall into several categories:

- **Software Providers –** These companies generally offer a software solution that enables campuses to run their own direct deposit refund program. Typically this solution is packaged as part of a broader electronic commerce solution. In most cases, these companies store the student banking data securely and deliver the ACH refund to the student's bank account. The school bears the responsibility of recruiting students to the program, managing the banking data, handling any exceptions, mailing paper checks where an electronic option is not chosen and bearing full responsibility for all compliance (Title IV as well as state and federal banking regulations).

- **Banks / Lenders** – These companies will offer more features and will often take on the responsibility of mailing paper checks when the student does not select an electronic refund delivery option. Limited assistance around Title IV Compliance is sometimes a part of the solution as well as some recruitment of students to the program. Generally these companies look to student refund disbursement as an inexpensive opportunity to create brand loyalty with students who will one day require more comprehensive banking services such as savings accounts, credit cards, and loans. While these vendors will often offer electronic refund assistance as part of a broader banking relationship, it is important to note that the Department of Education considers these vendors 3rd Party Servicers for the purposes of this process and as such, they are required to comply with all regulations pertaining to that designation.

- **"Stand-alone" 3rd Party Servicers** – Some companies offer comprehensive electronic refund delivery services not connected with a broader banking relationship. Typically these companies will offer varying levels of assistance with regards to recruiting students to the program, managing the banking data, handling any exceptions, mailing paper checks when an electronic option is not chosen and bearing a degree of responsibility for compliance (Title IV as well as state and federal banking regulations).

It is important to note that the experience level, scope of the offering and commitment to a comprehensive solution vary widely from provider to provider across these categories.

Comparison of Options

The delivery of electronic refunds entails a variety of duties:

- Initial set-up of the program
- Marketing of Program / Recruitment of students
- Collection and storage student banking data
- Delivery of the refund based on student preference
- Handling on any exceptions in a manner compliant with Title IV regulations
- Reporting or reconciliation back to the Student Information System (ERP)
- Student and administrative service

In comparing the various options available and choosing the appropriate solution, it is important to note which of these duties would be performed by the vendor and which would fall back onto the school. Ideally, in most circumstances, all duties would be performed by the vendor in a comprehensive solution.

From the schools' perspective, this provides added service, *greater efficiencies* and *reduced costs* to the school. If the school is required to handle some of these duties, not only will it require additional resources, but, it will often create the need for new internal processes actually *increasing cost* and *reducing efficiency*.

From the students' perspective, a comprehensive solution will present the student with a singular resource for their refund administration which will further *simplify* the process. If all of these duties are not handled by one entity, it can actually create confusion on the part of the students. Practically, when duties are split between the vendor and the school, the student is often unsure of where to turn for a particular question or concern.

Key Considerations

In the development of an electronic refund solution, experience and adherence to regulations have led to several key considerations that are seen as integral to a comprehensive and successful program. These include:

- **Student Choice –** Students want choices. Although the electronic option is faster, more convenient and more secure, experience has shown that some students prefer a paper check. Although the Department of Education guidelines allow for schools to require electronic delivery, they must automatically receive a paper check if they do not enroll in the mandated electronic refund delivery program 21 days after the campus draws down the funds.

- **Compliance –** Whether the program is administered internally or by a 3rd Party Servicer, compliance with all Title IV regulations and ongoing vigilance must be the foundation of any program as Title IV regulations do frequently change. Regulations require joint and severable liability for both the school and the 3rd Party servicer so failure to comply by the vendor does not limit the school's liability with regards to this matter. Specific attention should be paid to the timing around how quickly the refund is delivered, what happens when a student does not select an electronic option (they must be mailed a default paper check) and escheatment of stale dated Title IV checks.

- **Exception Handling –** Comprehensive electronic refund distribution is much more than simply delivering the student refund. Particular attention should be paid to the customer service component of the program. There are numerous exceptions that occur throughout the refund distribution process that must be quickly handled with care for the students involved as well as in compliance with the regulations that govern the distribution of the Title IV funds. Common exceptions include items such as incorrect address or banking information (for ACH), lost or stolen checks, and stale dated Title IV checks. It is highly recommended that the entity responsible for managing the refund process (either the vendor or the school) have an “exception handling” flowchart that outlines all exceptions and the Title IV compliant resolution for each.

- **Bank Card Option –**The two most popular reasons for low adoption of electronic refund distribution are students 1) lack of awareness of the program and 2) inability to open a checking account. According to a recent FDIC study over 8% of American households are unbanked and 28% are under-banked. This appears to be an even greater challenge among the student demographic. Additionally, Colleges and Universities are seeing a greater number of non-traditional students due to changes in the broader economy and web-based programs. These students often have difficulty accessing traditional banking channels. The result is that these students often resort to utilizing check cashing facilities or other methods to get their refund checks cashed. These options are less secure and often more expensive. With that in mind, an important component of a successful electronic refund program is the inclusion of a pre-paid debit card option. Electronic refund programs that include pre-paid debit cards following specific guidelines for fee assessment and usage could be compliant under current Department of Education regulations. Use of pre-paid cards do, however, present additional challenges for consumers.

    - ✓ Regulations - Pre-paid card market is less regulated than traditional banking
    - ✓ Fees - Pre-paid cards are often subject to fees and practices outside traditional banking
    - ✓ Security - Liability and protection of the user from fraud are limited
    - ✓ Inequality - Students required to use a Pre-paid rather than a traditional checking account can feel unfairly treated
    - ✓ Financial Literacy - The use of a “true” checking option helps to promote Financial Literacy

- **Scope and Scale –** The Department of Education regulations pertaining to Title IV distribution have changed numerous times and will continue to change as new challenges arise. Recently, the Department of Education announced it is convening a Negotiated Rulemaking Committee to focus on preventing financial aid fraud through electronic distribution of student refunds. When choosing a 3rd Party processor, it is highly recommended that special attention be paid - not only to the compliance of the solution in the existing environment – but also to the willingness and ability of the company to modify their solution as the regulations and rules evolve.

Regulatory Environment

The Department of Education regulations are extensive, detailed and ever evolving. As such, compliance with Title IV regulations regarding the delivery of Financial Aid refunds is difficult and an ever moving target. That said, the Department of Education has expressed its approval for electronic delivery and has encouraged Colleges and Universities to explore their options to reduce the number of paper checks issued for student refunds. Some considerations that should be taken into account when developing a program or utilizing one from a 3rd Party Servicer are:

- **Tight Regulation of 3rd Party Servicers –** Currently, 3rd Party Servicers that provide refund disbursement must be audited annually for Title IV compliance and must agree to share liability with the institution.

- **Choice/Access –** Students should have choice when it comes to how they receive their refund and *must not* be required to open a bank account or *have one opened for them* without their consent in order to receive their refund. Nor should they be charged a fee for simply receiving their refund.

- **Fully Compliant Free-standing Solution –** The electronic refund solution should be able to stand on its own, be fully compliant and not rely on other services such as a Campus ID/Debit Card.

- **No Revenue Sharing –** Revenue sharing deals create the appearance that the school is benefiting from their students' banking choices and should be avoided. Furthermore other "sweetheart deals" such as land gifts, loan/investment offers and signing bonuses should also expect to receive heightened scrutiny and thus are not recommended.

- **Additional Product Marketing -** Marketing of additional products to students as part of the refund process should be avoided if possible. Specifically, the marketing of credit products to students as part of a relationship involving student refunds is highly discouraged.

- **Transparency –** Schools should provide access to all elements of their relationship with any 3rd Party Servicer.

- **Storage of Student Banking Data –** While this does not fall under the auspices of the Department of Education, the storage of student banking data by the school for the purposes of delivering an electronic refund raises security concerns and may result in additional costs to the institution to adequately secure the data.

- **Financial Literacy –** Schools should work with the 3rd Party Servicer to enhance Financial Literacy among its students.

Conclusion

For any Electronic Student Refund solution, it is recommended that all student refunds are included to promote consistency of process for both students and administration. Colleges and Universities should be encouraged to convert the reimbursement of student loan refunds from paper checks to electronic methods as a more effective and cost saving payment measure. The most cost effective means is via the Automated Clearinghouse Association (ACH) Direct Deposit process. A secondary method would be the use of a pre-paid debit card program. Third party service providers can offer a comprehensive approach, administer these systems uniformly and assume responsibilities traditionally handled by the institutions for communication, implementation and compliance with rules. Outsourcing to vendors would also eliminate the risk and need of in-house warehousing of confidential bank account information and the burden of conducting marketing campaigns to promote student participation, resulting in a much more effective program.

Table A: College Refund Data and Analysis

College Refund Methods and Volumes	Annual Volume Credit Refunds	Annual Volume Dollars	% of Total Refunds by Direct Deposit	% of Total Refunds by Check	Estimated Check Transactions per Year	Estimated Costs for Paper Check per Transaction (74 cents)	Estimated Cost for Electronic per Transaction (09 cents)	Estimated Annual Savings
Virginia Commonwealth	38,375	$116,994,348	55%	45%	17,269	$12,779	$1,554	$11,225
Virginia State University	13,105	$18,264,216	0%	100%	13,105	$9,698	$1,179	$8,518
Longwood	5,631	$7,154,971	46%	54%	3,041	$2,250	$274	$1,976
Virginia Military Institute	1,392	$2,013,549	23%	77%	1,072	$793	$96	$697
James Madison University	19,400	$37,351,593	36%	64%	12,416	$9,188	$1,117	$8,070
Christopher Newport College	5,317	$7,505,889	18%	82%	4,360	$3,226	$392	$2,834
Old Dominion University	36,210	$40,000,000	34%	66%	23,899	$17,685	$2,151	$15,534
William and Mary	7,271	$17,600,000	0%	100%	7,271	$5,381	$654	$4,726
George Mason University	29,018	$74,800,000	23%	77%	22,344	$16,534	$2,011	$14,524
University Mary Washington	5,288	$4,855,183	23%	77%	4,072	$3,013	$366	$2,647
Norfolk State University	15,000	$17,850,000	70%	30%	4,500	$3,330	$405	$2,925
Virginia Tech	35,365	$66,260,199	63%	37%	13,085	$9,683	$1,178	$8,505
Radford University	14,334	$27,173,756	37%	63%	9,030	$6,683	$813	$5,870
University of Virginia	35,012	$87,143,000	36%	64%	22,408	$16,582	$2,017	$14,565
University of Virginia-Wise	945	$7,000,000	0%	100%	945	$699	$85	$614
Richard Bland College	1,675	$2,549,407	0%	100%	1,675	$1,240	$151	$1,089
College Sub Totals	263,338	$534,516,111	39%	61%	160,491	$118,763	$14,444	$104,319
VCCS -23 schools	287,479	$262,978,173	0%	100%	287,479	$212,734	$25,873	$186,861
Grand Totals	550,817	$797,494,284	19%	81%	447,970	$331,498	$40,317	$291,180

Attachment 2

Proposed Policy and Procedures

For Converting Student Loan Refunds To Electronic Means

Proposed Policy and Procedures

For Converting Student Loan Refunds To Electronic Means

(Pursuant to Item 277 G of Chapter 3, 2012 Appropriation Act)

Overview

This policy provides guidelines and references to assist state colleges, universities, and community colleges in developing procedures to minimize the use of paper checks for student loan reimbursements in favor of electronic payment methods when cost effective and consistent with current Federal Student Aid (FSA) programs.

Policy

State colleges, universities, and community colleges are strongly encouraged to disburse student loan refunds via an electronic method. Acceptable methods include direct deposit (use of the Federal Reserve sponsored Automated Clearing House Association or ACH), and pre-paid debit card programs. Institutions must adhere to all Department of Education regulations for the handling and delivery of Title IV funds. Rules and regulations apply to all types of FSA. These include Pell grants, TEACH, and Iraq and Afghanistan Service Grants, Federal Supplemental Educational Grants, Perkins Loans, and Direct Loans as well as PLUS loans to parents. This policy is directed towards the disbursement of FSA refunds, but may also be applicable to other student refund types, including dropped class refunds, parking fees, dining fees or housing fees.

Institutions are directed to the document entitled “Student Loan Refunds; Initiative for the Conversion of Paper Checks to Electronic Methods” dated November 15, 2012 which is located on the Treasury website.

Procedures

Legal and Regulatory Requirements

Institutions are to ensure all students receiving financial aid are adhering to college withdrawal procedures for the return of Title IV funds. Colleges, university and community colleges are referred to the Department of Education Federal Student Aid Handbook, Volume 4 for the adherence to the following requirements:

Credit balances may be paid by check or electronic funds transfer (EFT) to a recipient designated bank account:

- Schools may establish a policy requiring its students to provide bank account information as long as the policy does not delay the disbursement of FSA funds

- Students not selecting a refund option or failing to comply with policy, by default will be mailed a paper check
- Credit balances must be disbursed within the regulatory time frame
- Delivery of FSA funds must be cost free to the student
- Students should have the ability to obtain refund checks in person from the Financial Aid department during regular business hours
- Uncashed and stale dated FSA checks must be voided after 180 days and the funds returned to the Department of Education

FSA credit balances may be placed on a stored value or prepaid debit card:

- Value of the card must be convertible to cash
- Student should not incur fees to receive the card nor for withdrawals from issuing bank ATMs
- ATM access must be on campus or in close proximity to the campus
- Must be FDIC insured
- Card should not be converted to a credit account
- Must meet all regulatory time frames
- Funds must never escheat or revert to any other third party other than the Department of Education

Use of third party vendor

Institutions may want to consider contracting and outsourcing to a third party provider to administer their electronic refund and card program. Institutions may also want to consider structuring a third party contract in which other institutions can participate with the objective of lowering the overall cost for the participants. A third party vendor can offer a consolidated approach to refund management. They can also assist with other student disbursements to streamline the overall disbursement program. Qualified vendors would have expertise and knowledge with financial aid disbursements, Title IV compliance requirements and customizable communication plans. A third party vendor is able to obtain student authorization to perform electronic funds transfers, open a bank account on behalf of the students and manage the issuance and services in a concise approach that an in-house program may not be able to achieve.

Third party service providers can offer a comprehensive approach, administer these systems uniformly and assume responsibilities traditionally handled by the institutions for communication, implementation and compliance with rules. Outsourcing to vendors would also eliminate the risk and need of in-house warehousing of confidential bank account information and the burden of conducting marketing campaigns to promote student participation resulting in a much more effective program.

Student Choice and Communication

Student choice should be a fundamental element of the program. Choices should include ACH direct deposit, debit card if available, or a paper check. Students should be encouraged, not mandated, to elect an electronic payment option.

Effective program marketing to reach the student population is key to a successful program. As with any marketing program it should be comprehensive, multi-channel, and ongoing.

Compliance

Institutions should require in-house programs to have structured and ongoing audit processes to ensure Title IV compliance. All third party services must meet established annual audit requirements for compliance with all Title IV guidelines. Non-compliance may result in serious implications and institutions will be held jointly and severally liable for violations committed by their third party servicer.

Institutions or third party servicers should have a Title IV compliant handling process for all eventualities such as "bounced" ACH's, special requests for "on-demand refunds", stop payments, lost or returned checks and stale date checks.

Debt Set Off

The higher education institutions will need to meet the Comptrollers Debt Set-off (CDS) requirements. All refunds are not eligible to by-pass CDS. Certain federal and Title IV payments are exempt from CDS but there are other payments that are not. The Institutions will need to develop a process to determine if there are any eligible payments that need to be run through CDS and then exclude those payments from the file to the 3rd party vendor or for internally processed refunds and execute those payments through normal processes.

Reporting Requirement

The Department of the Treasury (Treasury) and the institutions will work together in efforts to reduce the volume of paper check disbursements for student refunds. Institutions are requested to report to Treasury by the Fiscal Year end 2014 on their progress.

Applicability

This policy applies to all Virginia state colleges, universities and community colleges that use in-house or third party service providers.

Contacts

Manager, Cash and Banking (Treasury)

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Email: Bankingservices@trs.virginia.gov

References

CAPP Topic 20210 Bank and Cash Management Services

CAPP Topic 20300 Cash Disbursement Accounting

Department of Education Handbook

Student Loan Refunds; Initiative for the Conversion of Paper Checks to Electronic Methods