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Macias, Wendy

From: [redacted]
Sent: Tuesday, June 09, 2009 3:44 PM
To: negreg09
Subject: Recommendations for DOE Policy earings
Attachments: DOE_060909.pdf; 2008 Little Wing Annual Letter EMAIL.pdf; oigcriticismdefaultratesa03c0017.pd.pdf; 120908DefaultRatesCohortYearsAttach2.pdf

Please find attached scanned letter to Wendy Macias and attachments to that letter.

QUILCAP CORP.

[redacted] [redacted]

June 9, 2009

Ms. Wendy Macias
U.S. Department of Education
1990 K Street NW
Room 8017
Washington, DC 20006

Subject: Recommendations for Department of Education Policy Hearings

Dear Ms. Macias,

We applaud the renewed efforts of the Department of Education under the new Administration to protect students and taxpayers through regulatory and administrative improvements to program integrity provisions of the Higher Education Act subject to its jurisdiction. On [redacted] May 29th call with the investment community he asked for input on topics for review by the Department's upcoming public hearings. The purpose of my letter to you today is to respond to that request.

First, allow me to introduce myself. My name is [redacted] I am the [redacted] of [redacted], an investment management firm based in New York City. Attached you will find our most recent annual report.

Quilcap prides itself on detailed fundamental securities analysis. We look for under-valued securities of companies to buy and over-valued securities of companies to sell (including selling short)—buy low, sell high. We are unapologetic capitalists and our mission is to produce high risk-adjusted investment returns for our clients. When they make money, we make money.

We have followed companies in the education and student loan industries for over a decade and have made numerous purchases and sales of their individual securities during that time period. More recently we have become increasingly concerned over the sustainability of certain publicly traded for-profit schools' business models and have been primarily sellers of their securities.

The growth of most of the publicly traded for-profit schools has been exceptionally strong. Enrollments, pricing, margins, and most importantly, profits have risen dramatically. Normally, we would celebrate these trends…and, indeed, many on Wall Street have.

However, after extensive analysis, including review of financial statements and exhaustive interviews with students and prior employees, we are convinced that much of the growth comes from a highly refined manipulation and abuse of Title IV student aid programs. We have found overwhelming evidence that many of these schools' enrollment practices are in violation of applicable regulations and/or contrary to stated federal goals of improving the educational experience for students while maximizing the value to tax-payers.

We see extensive evidence that certain for-profit schools act more as enrollment mills and predatory lending originators, rather than educators. (It is worth noting that the largest for-profit education company, Apollo Group, reported in its 2008 10-K filing that it spent $805.4 million on selling and promotion, as compared to only $272.5 million on faculty compensation.) And while the for-profit schools have profited handsomely, the Department's two constituents, students and tax-payers, are suffering to an increasing degree.

No doubt, there exist individual success stories coming out of for-profit schools. What is unclear to us as investors, as well as to us as concerned citizens, is how does the Department objectively and systematically attribute "success" or "failure" to individual student outcomes and to specific school performance? As Title IV now tops $100 billion each year, what yardstick(s) is the Department using to see to its beneficial delivery?

What hard metrics—graduation rates, job placement data, student loan defaults—will the Department rely on in judging school performance? Graduation is an inconsistent standard and can be artificially altered by the schools themselves to effect outcomes.

Job placement is also an inconsistent standard. Job placement A may not equal job placement B. Only if the education leads to a *better* job than was available before the time and money spent on school, could the result be measured as a "successful" outcome. It is all very well to get a job "placed" at minimum wage, but not if the student has a pile of compounding student debt to pay down on that meager salary.

We think a more objective metric in considering "success" or "failure" is the student loan default rate. If a student defaults on her student loan, then, unequivocally, her life has been impaired by the borrow-to-educate experience. She is now buried under a debt that will compound and hound her future. Clearly, more individuals struggling in debt default is not something our society wants nor should public policy encourage. Thus, measuring student default rates is paramount to assessing an individual school's performance.

By the default rate, we mean the *real* default rate—an ongoing cumulative calculation over the lifetime of the loan—not a default rate proxy limited to a (arbitrary) window of time that excludes many non-performing loans. Historically, the Department has been satisfied with the limited (and more easily manipulated) Cohort Default Rate. This "default rate" involves complex rules calculating defaults over a limited period of time. While the Cohort period is now two years (moving to three), due to the calculation rules, the default window in practice is actually shorter still.

Furthermore, borrowers that are not current on their payments, but have received "deferments" or "forbearances" are not calculated in the numerator of the Cohort figure. Even though an individual may have failed to honor loan repayments, he can avoid for a limited period of time—not coincidentally often within the Cohort window—the designation of "default."

The Department's two constituents, students and tax-payers, are on the hook for the life of these loans. Should not the individual schools be held to that same standard? Otherwise, what is to discourage schools from enrolling sure-to-fail borrowers as long as the inevitable default can be finessed to take place outside of the Cohort period?

In 2003 The Department's OIG filed a report (attached) that warned of the Cohort's weakness. The Department made no material changes to correct the problem. The data of the 2003 report is now almost a decade old and we believe the Cohort's inaccuracy has only increased since then. As many schools have increasingly enrolled more marginal students and have learned how to better push student defaults outside of the narrow Cohort window, the differential between the Cohort and the real default rate has widened to the point where actual outcomes are many times worse than the Cohort proxy. (See attached study by Student Lending Analytics.)

There is a huge, multi-hundred billion dollar default crisis building with student loans. Relying on a misleading Cohort Default Rate impairs transparency and is bad policy. The profiteers would have us believe that the problems are limited to the understated Cohort. Indeed, the press, to date, seems to have swallowed their bait and often does not differentiate between actual default rates and the (manipulated) Cohort.

[redacted] Article attached.)

While this reporter calls alarm to the "soaring" default rate, she unwittingly misses the size of the problem by orders of magnitude. The student loan default crisis we face is not at 6.9%, as the Department's fiscal 2007 Cohort figures would imply, but many, many times worse!

The Department in representing students and the public at large should consider actual default outcomes as they accrue. All non-current loans (deferred or in forbearance) should be included, or, at the very least, counted in a separate publicly disclosed calculation. While shifting to a more meaningful real default rate would require Congressional action for eliminating eligibility for institutions that have gamed the system, nothing in current law should prevent the Department from publishing accurate default information immediately. Accurate information and honest accounting are essential for consumer choice and good public policy. Let's have it.

The Department of Education should collect and publicly disclose actual cumulative default rates and non-performing loan rates for every school that participates in Title IV.

Additional measures to improve the integrity of programs financed with federal dollars and to better protect students include:

- **Regulation of excessive and misleading advertising by schools that rely heavily on federal financing.** There should be limits on the percentage of institutional expenses devoted to advertising, and the Department should require all advertisers to back up their claims with facts.

- **Stronger state oversight as a condition of participation.** The Department should better define state licensure and require a substantive review of participating institutions by an agency of jurisdiction at the state level. It should also mandate ongoing oversight of for-profit institutions by the appropriate state agencies.

- **Better criteria for accrediting bodies.** Accrediting bodies should be recognized as qualified gatekeepers for Title IV only if they have adequate resources to engage in meaningful reviews of entities that they render eligible for hundreds of millions of dollars of federal financing. As it is, small and under-resourced organizations are allowed to evaluate multibillion dollar corporations that they cannot realistically evaluate or confront. The current regulatory environment is, in fact, rigged in favor of lax and lenient accreditation because it does not create consequences for accreditors with a history of poor judgment. It is no wonder that accreditation has gradually turned into a race to the bottom where the less rigorous and less demanding an accreditor, the more it attracts shoddy schools.

- **Better definition of gainful employment in a recognized profession.** Many for-profit schools market vague and nebulous "careers" to unsuspecting victims, who only learn that they must repay the thousands of dollars of student debt with nothing but minimum wage employment upon graduation (or dropping out) from weak programs. Gainful employment should be redefined as actual earnings above and beyond unskilled minimum wage rates, and should be algorithmically tied to debt-levels upon graduation. Only programs that enhance the post-debt-service wages of their graduates should qualify as preparing students for gainful employment. Also, in our review of these programs, we have seen a pattern of embellishments in describing the careers for which students are allegedly trained. Basic keyboarding, for example, is often labeled as information technology and the most elementary security guard programs are marketed as homeland security training. The Department should do a better job of ensuring that the programs advertised are actually tied to recognized—ideally, state licensed—professions.

- **More regulatory focus on distance education.** The Web has become the ideal hunting grounds for victims by predatory schools. With the unwise and ill-thought-through repeal of the 50 percent rule in 2006, any website can now re-brand itself as a "university" and tap into Pell Grants and student loans by charging tuition. Lax and inadequate accreditation and the absence of any state oversight make distance education particularly susceptible to fraud. The total absence of brick-and-mortar presence on the ground makes this type of fraud especially attractive, since the sites' operators may well be located off-shore. The Department should pay particular attention to this area and regulate programs delivered by virtual "universities" appropriately.

We invite any questions you may have and are happy to discuss these topics further.

Sincerely,

[redacted]

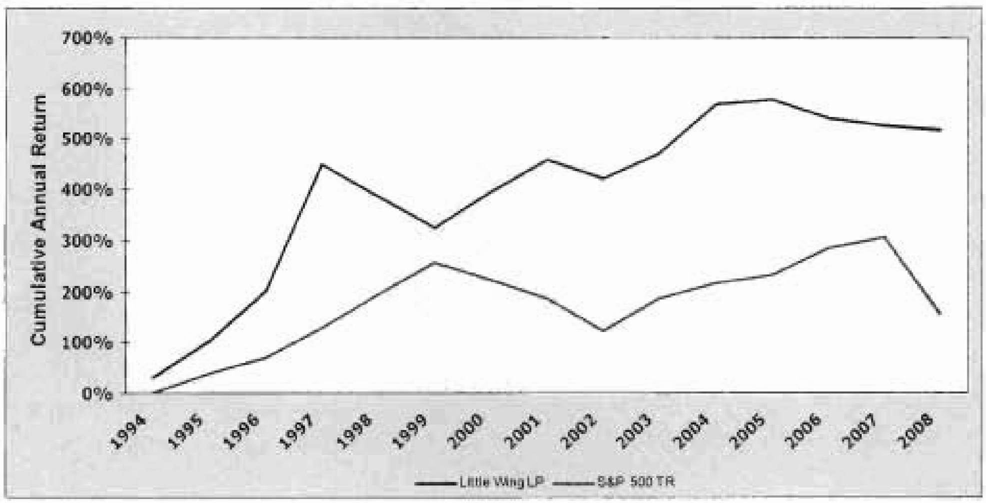
Quilcap Management, LLC.

January 2009

Dear Investing Partner,

Little Wing L.P. lost 1.20% net of fees and expenses for the year 2008. Our long investments lost 30.99% for the year, while our short positions generated profits of 29.80%.

Since the August 1994 inception of Little Wing, the partnership has generated a net return to its investors of 518.12%, or an average compound rate of return of approximately 13.47%. The S&P 500 meanwhile has compounded over that same time period at roughly 6.75% annual rate.



It can be helpful to compare specific investment performance to broad indices, and we have illustrated our returns within the context of the S&P 500. However, we are not overly concerned with relative returns in and of themselves. We are seeking high absolute returns over long periods of time.

Interests of my family and mine represent the largest and longest standing investors in our funds. We manage the assets as if it were our own money, because it is. We do not celebrate successes over weeks or months, but over years and in absolute gains.

Our priorities are to preserve capital—yours and ours—and to compound wealth, in that order. Unlike many of our peers, we believe it is important to hedge when managing a hedge fund. We carry both long and short positions and our aim is to make money regardless of broad market direction. We would gladly give up relative performance in favorable markets, so long as we can perform absolutely well in all environments.

In 2008 our negative 1.20% performance was a modest disappointment. It was an extraordinary year, of course, and most investment funds were down spectacularly. Relatively, our fund's performance was excellent. But, again, we are not relative players.

Most of the draw-down on our long portfolio was driven by the dramatic contraction of equity valuations across the board. Going into 2008, we were concerned about credit expansion and consumer spending and we were fortunately very underweight sectors with these particular sensitivities. (Please read past year-end reports for our historic macro-view.) Our long losses were generally a function of lower equity prices everywhere, rather than particular allocation to underperforming sectors.

Part of the negative performance of our long book was a result of a cathartic, house cleaning by us. Some of our long positions were made up of fixed income securities without an electronic quote. By year-end, we had either sold or marked to zero all of these positions, contributing just over 8% to overall losses in reported performance. It would be inappropriate to characterize these write-downs and liquidations as strictly "one-time" in nature. However, we can characterize these devaluations as extremely conservative, leaving no room for any further performance degradation in these positions going forward.

If there were any themes to the poor performance of certain long investments, it would be more to the size and maturity of the enterprises rather than the sectors in which they belonged. Many of the positions in our long book were small capitalized companies and many of these were companies early in their life cycle. While the opportunity in these investments was high, some of the companies still required further financing to achieve their near-term goals. In the second half of 2008 funding availability came to a screeching halt. Good projects, as well as bad, could not find financing. Many promising infant companies, including some in our portfolio, died as a result.

Fortunately, our portfolio was well hedged in 2008. We managed to escape the year's ravages without much loss because of excellent performance from our short positions. While we came into 2008 with net long exposure of just over 20%, the higher beta (market correlation) of our shorts paid off. We were also well (negatively) exposed to particular macro themes—consumer discretionary, retail, and finance—that gave our short book an added boost. For sure, it was a good year, particularly in the Fall, to be short stocks.

At 2008 year-end the portfolio had 84.42% invested short and 80.55% invested long, giving it net -3.87% exposure. With the short positions more highly market sensitive than the longs, the total portfolio had the feel of a net 38.82% short exposure when adjusted for beta.

Sector exposure ended 2008 as follows:

Industry Sector	Long Exposure	Short Exposure	Net Exposure	Beta Long Exposure	Beta Short Exposure	Beta Net Exposure
Basic Materials	13.82%	0.00%	13.82%	4.72%	0.00%	4.72%
Conglomerates	1.14%	0.00%	1.14%	0.00%	0.00%	0.00%
Consumer Goods	5.80%	-5.91%	-0.11%	2.88%	-8.27%	-5.39%
Education	0.00%	-6.74%	-6.74%	0.00%	-8.50%	-8.50%
Energy	13.80%	-5.12%	8.69%	20.28%	-11.35%	8.93%
Etails	3.41%	-5.96%	-2.55%	2.67%	-9.15%	-6.48%
Finance	7.48%	-12.15%	-4.67%	4.49%	-9.43%	-4.94%
Healthcare - Biotech	8.48%	-0.93%	7.56%	5.68%	-0.73%	4.95%
Healthcare- Services	6.85%	-6.21%	0.64%	4.18%	-5.15%	-0.96%
Industrials	0.10%	0.00%	0.10%	0.10%	0.00%	0.10%
Internet	4.13%	0.00%	4.13%	3.62%	0.00%	3.62%
Media/ Entertainment	0.02%	-0.64%	-0.62%	0.00%	-2.03%	-2.03%
Real Estate/ Housing	0.00%	-12.24%	-12.24%	0.00%	-12.53%	-12.53%
Resorts	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Restaurant	0.00%	-5.99%	-5.99%	0.00%	-9.21%	-9.21%
Retail	4.24%	-13.67%	-9.43%	5.49%	-16.73%	-11.24%
Services	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Technology	8.67%	0.00%	8.67%	8.06%	0.00%	8.06%
Telecommunications	0.67%	-0.67%	0.00%	0.82%	-0.82%	0.00%
Transportation	1.93%	-8.19%	-6.26%	-0.20%	-7.72%	-7.92%
Total	**80.55%**	**-84.42%**	**-3.87%**	**62.79%**	**-101.61%**	**-38.82%**

The trouble with socialism is that you eventually run out of other people's money. –Margaret Thatcher

The economy and financial markets start 2009 with a viscous hangover. At the root of this distress is too much serial government intervention. But intervention, we think, is a misnomer and gives the wrong connotation. When one pictures an intervention, one may think of a setting where concerned parties step in and virtually force an alcoholic or drug addict to go clean and check into rehab. Interventions and going clean are no fun for anyone, but they are usually the only way to save an addict in denial. It's not called "warm and cozy turkey." It's cold turkey; it's unpleasant, but necessary.

Our government, led by the Federal Reserve, has done anything but "intervene" for the last two decades. Quite the opposite, our government has been the chief enabler in our economy's easy credit and deficit dependency. We have become hooked on monetary and fiscal stimuli. And like a resourceful pusher, our government is now back again with the pure stuff just as the withdrawal gets rough.

The Federal Reserve and central banks throughout the globe made credit too easy for too long. With artificially low interest rates western societies, the U.S. in particular, binge consumed and speculated. The Now Generation embraced the *carpe diem* policies of its leaders and spent their way to a "prosperity" never before seen. GDP, profit margins, and asset values reached at all time highs.

Speculating in real-estate and securities markets was Millennium Man's retirement plan. Saving at punitive interest rates was considered plain stupid. Why save with less than a 2% passbook savings account when you could consistently get double digit returns (and higher with leverage) on a speculation house or brokerage account? Sure, there were periodic short-term sell-offs, but "the Maestro", [redacted], was always quick to put a floor in lower prices. All you had to do was "buy the dips"—sustained bear markets impossible with such ready government "interventions."

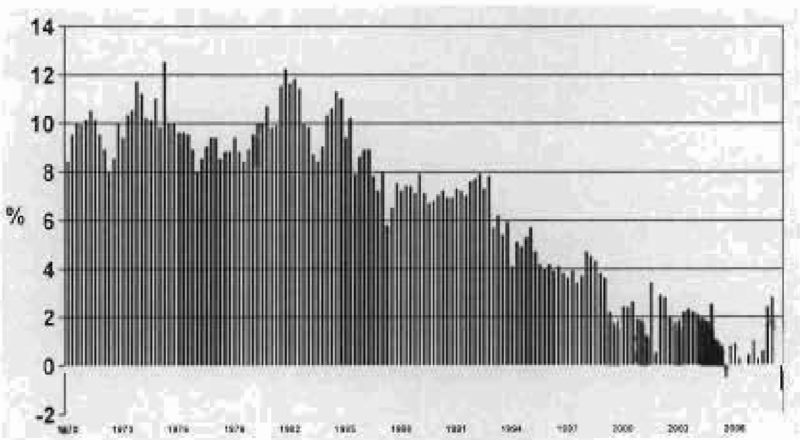
Not only are bear markets inevitable, they are necessary. Natural selection requires periodic droughts to cull the herd and to maintain its health. While painful, contractions are an essential purge for an economy. It is usually in the busts that wasteful business plans are snuffed, accounting scams exposed, and financial pyramids toppled. Periodic bear markets, allowed their natural price discovery, expose [redacted] schemes well before they reach $50 billion. But long ago our central planners abandoned free-market principles and yet again pulled out all stops in Operation Enduring Bubble's goal to keep the borrowing, spending, and speculating binge going.

On January 16th, Senator [redacted] wrote FDIC Chairperson, [redacted], a letter urging her office to extend loan guarantees to motorcycle loans. New heavy bike registrations almost tripled in the decade following 1997 from 206,100 to 578,800, yet apparently even with over 6 million registered motorcycles on the road, Americans have not borrowed and spent enough on new bikes. We wonder what criteria the junior senator from Pennsylvania and his colleagues use when pushing for more government guarantees. If tax-payers need to sponsor more motorcycles, then surely we do not have enough jet-skis, vacation condos, and cosmetic surgeries. Is that the problem? Do we not already own enough stuff?

Wasn't it the excessive borrowing, spending, and speculating that got us into this mess in the first place? Why then should our leaders encourage more borrowing and spending as part of the solution? Albert Einstein said, "Insanity is doing the same thing over and over and expecting a different result." Do we expect a different result this time? Or does the end result not really matter, so long as we get a stimulus fix now? Perhaps the Now Generation is simply so irresponsible and selfish, that it will refuse to live within its means…ever.

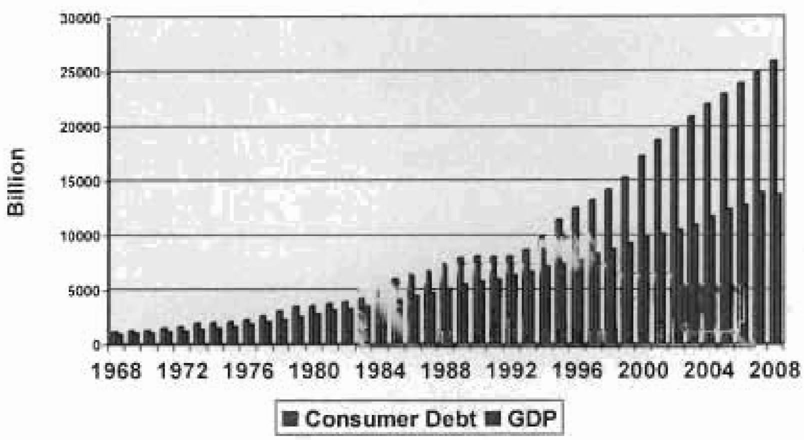
Apparently, this is the master plan: 1) Inhibit natural price discovery of assets by manipulating prices higher with government purchasing programs and incentives. 2) With artificially low interest rates discourage saving and encourage more borrowing and purchasing what we cannot afford. 3) Accelerate fiscal deficits, leaving a massive National Debt and a bankrupt entitlement system for our children. In short, the master plan urges us to ignore the economic lessons recently learned and to party on with even greater vigor than before!

Personal Savings
as a percent of
Disposable Personal Income



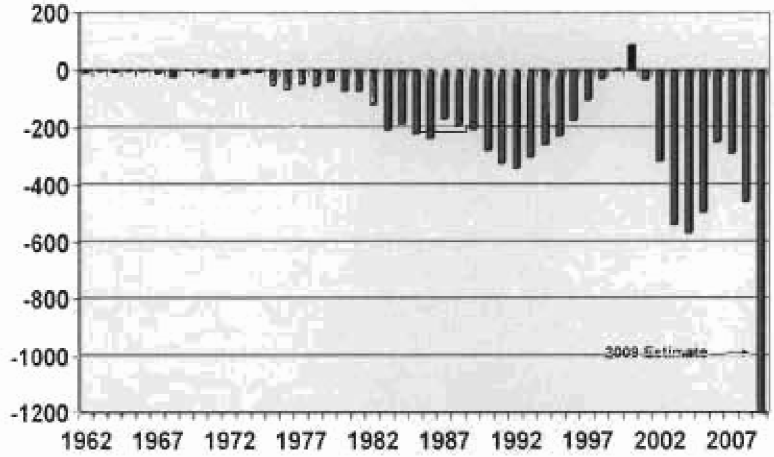
Source: Bureau of Economic Analysis

Consumer Debt to GDP



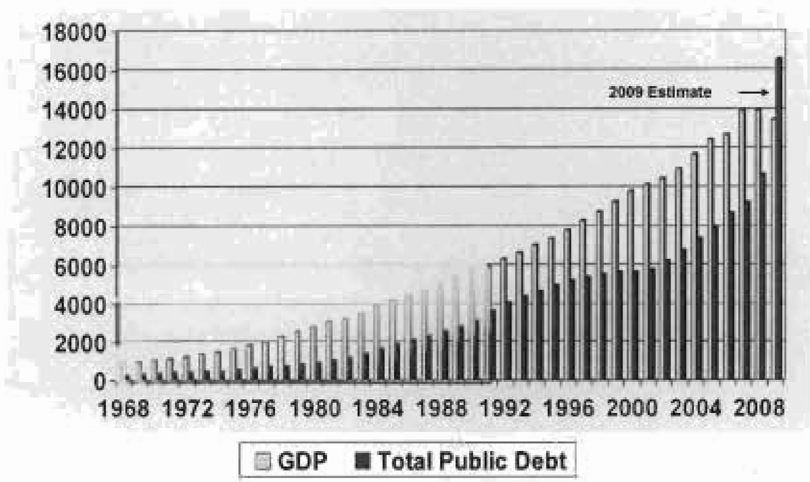
Source: Bureau of the Public Debt

Federal Surplus & Deficit



Source: Congressional Budget Office

GDP Vs Total Public Debt



Source: Bureau of Public Debt & Congressional Budget Office

We have tried spending money. We are spending more than we have ever spent before and it does not work. . . . After eight years of this Administration we have just as much unemployment as when we started. . . . And an enormous debt to boot! –Henry Morgenthau, Jr., Treasury Secretary FDR Administration

Our opinion (disgust) of government policy is of little relevance. Anticipating its impact on economic trends and security prices is what is important. Part of our job is to accurately identify government policies and business trends and make risk adjusted investments on which to profit from them.

We are not sure whether the current policies of socializing bad assets (TARP) and mortgaging our children's future (unprecedented expansion of Federal debt) will deliver the "desired" results of a short-term economic and market rebound. If it does "work," we think at best it will be a quick fix, leaving the core structural imbalances (spending/savings/debt) unaddressed and merely postponing and exacerbating inevitable future corrections.

What we are most certain of is future inflation. There is nothing more inflationary than the whiff of deflation and the current panic to expand the Federal Deficit and the Federal Reserve balance sheet will virtually guarantee a debasement of currency purchasing power.

In his 2002 speech to the National Economic Club then Federal Reserve Governor, Ben Bernake, gave us insights into his monetary policy orientation:

> *Like gold, US dollars have value only to the extent that they are strictly limited in supply. But the US government has a technology, called a printing press (or, today, its electronic equivalent), that allows it to produce as many US dollars as it wishes at essentially no cost. By increasing the number of US dollars in circulation, or even credibly threatening to do so, the US government can also reduce the value of a dollar in terms of goods and services. We conclude that, under a paper-money system, a determined government can always generate higher spending and hence positive inflation... If we do not fall into deflation, however, we can take comfort that the logic of the printing press example must assert itself, and sufficient injections of money will ultimately always reverse a deflation.*

The U.S. is fortunate in its position of currently controlling the world's reserve currency. Like Britain in the beginning of the last century, we have borrowed at unsustainable levels, but did so in our own tender. The staggering amounts we owe, we owe in dollars. Thus, the US government will not default on its dollar denominated debt. It can always print more and simply pay it back debased of its purchasing power. Whether/when the dollar will go the way of the British Pound and lose its global preeminence, we will leave to future speculation. But we have no doubt that a dollar will purchase you far less in goods and services in the next decade than it has in this one.

With the ghosts of Christmases future likely appearing in the form of inflation, we think some of the least appealing investments are U.S. Treasury Bonds. The 10-year Bond is currently yielding less than 2.4%, hardly enticing when you associate your Federal Reserve Chairman with a running printing press.

We are, therefore, short US treasury bonds—both 7-10-year and 20-plus year. Again, the cost of carry (net yield) on these bond short positions is small and the dollars we spend to cover the positions in the future will be far less valuable than the dollars raised on making the bond (short) sales today. With a similar view we continue to hold long positions in gold and gold mining shares.

Not all of our positions, short or long, are "macro plays." Most of our work is company specific and the securities we own are a function of "bottoms up" analysis. Valuation has always been our touchstone. For more than a decade our valuation disciplines essentially priced us out of most of the high flying, larger capitalized market. For long candidates we were relegated primarily to the underbrush and squirrelly nooks of the micro-cap universe.

Now, in the midst of a financial crisis, so much has changed. We can look at a much broader pallet of companies as valuations have compressed everywhere. For the first time in many years you would probably recognize a number of the long holdings in the fund. For example, we have recently established small positions in Intel and Ebay. Both businesses, we think, will be negatively affected by the cyclical downturn, but both companies have good long-term prospects, strong balance sheets, excellent market positions...and most importantly, now come at attractive valuations.

Micro-cap investments often are more binary in their performance—either home runs or strike outs. We like micro-cap investing, as there are usually greater inefficiencies in securities pricing and therefore better risk/reward relationships. However, balancing a long portfolio partially with larger, more established enterprises can offer greater stability if done at reasonable valuations. Ideally, we can have both types of investments—some more aggressive and lumpy, some more steady. We are happy that the recent market revaluation has allowed us to reintroduce some small ball into our overall game strategy.

On the short side of our portfolio some of the low hanging fruit has already been picked. At this point, for example, we do not think that there is much risk adjusted opportunity left in shorting banks. Likewise, the big down moves in U.S. autos and home builders is mostly behind us. However, we still see some opportunity in remaining short many consumer names.

Harley-Davidson (HOG), a perennial favorite of ours, continues to offer rewards on the short-side. While the stock is already well down from our latest entry point and even below our original expected exit (buy to cover) level, the intrinsic value of the business has deteriorated even more than we originally thought and still offers more short potential at current stock prices.

You'll recall that our primary concerns with Harley, other than its high valuation, were its liberal use of consumer financing and its aggressive channel stuffing through its dealerships. On the positive side, it had excellent brand loyalty and a debt-free balance sheet. Alas, HOG executives (who have since resigned) chose to assume large debt burdens in order to provide funding for motorcycle loans as securitization markets evaporated. Harley's balance sheet, pristine a few short quarters ago, consists now of more debt than stated equity and is getting worse as operations drain cash. Not only does HOG's stock have more to go on the downside, but it represents an allegory to so many of its peers and to the US as a whole. Artificially enhancing sales and earnings in the short-term, management mortgaged the future…and the future has arrived.

There are also many sectors heralded as "recession proof" that we think offer short selling opportunities. For example, the for-profit education space has many issues trading near highs as portfolio managers have crowded into positions where they think growth can persist despite a worsening economy. The logic here is that as people lose jobs, they often return to school thereby *increasing* the demand for education.

The flaw, we believe, in this analysis is that it misses the huge role easy credit recently played in the education space. No industry was guiltier of pushing unaffordable loans on its customers than that of the for-profit schools. Many of these schools abused government programs and misled their students into the value prospect of their course offerings. As a result, we have a generation of students, many who dropped out of the course programs before completion, without jobs, and saddled with debts they cannot pay back.

There is a seductive argument for making education more accessible to all. Improved training has a direct correlation to higher productivity and income. Indeed, we all know the adage, "give a man a fish and you feed him for a day; teach a man to fish and you feed him for life." With this in mind, there has been the political support for greater government funding in education. Post-secondary school enrollments have grown substantially in recent periods as a result of larger Title IV and other government programs. Now most students rely on some form of government assistance (grants and loan guarantees), amounting to over $90 billion in 2008 alone.

Where there is a big government program, there will be profiteers with clever schemes to bilk it. Education, and its growing for-profit segment particularly, is no exception. Rather than being in the business of teaching, *per se*, many for-profit schools discovered that the business of *enrolling* was easier and more lucrative. They learned to game the student loan programs and grew their enrollment rosters with unqualified students. Most of these students had little chance of benefiting from the experience and failed to complete their course curriculum. These aggressive schools were not so much teaching a man to fish, but signing him up for an expensive (and unhelpful) fishing course...ultimately impoverishing the man with debt and the tax-payer with the bill.

With over 40% drop-out rates and scores of student lawsuits, most for-profit school customers are clearly dissatisfied with the "shopping experience." An enterprise that consistently disadvantages its clients, and then relies on the financing and continued indifference of regulators in the face of blatant program abuses, is very risky, if not ultimately doomed. We are sellers of the highly valued for-profit education stocks.

Overall, we like where our portfolio is right now. We have ample ideas for both the long and short side of our book. Our positions are more liquid and balanced than they have been for many years. We feel vindicated for our historic macro-view and believe we are well positioned to harvest superior returns as it continues to unfold. We have solid partners, you, who have remained steady in your trust and patience.

While most of our peers are in shell shock, we are excited and feel that our fund is in the right place at the right time to play offense. We are in an enviable position to seize on opportunities and build wealth for us all. Our confidence is high.

We wish you health and prosperity in the New Year.

Sincerely,

[redacted]

Audit to Determine if Cohort Default Rates Provide Sufficient Information on Defaults in the Title IV Loan Programs

FINAL AUDIT REPORT

ED-OIG/A03-C0017
DECEMBER 2003

Our mission is to promote the efficiency, effectiveness, and integrity of the Department's programs and operations.

U.S. Department of Education
Office of Inspector General
Philadelphia, Pennsylvania

Default Rates

Cohort Default Rate

Calculated based on BORROWERS and the two year window after entering repayment.

Institutional Category	Cohort Yr 2002 Cohort Default Rate (CDR)%	Cohort Yr 2003 Cohort Default Rate (CDR)%	Cohort Yr 2004 Cohort Default Rate (CDR)%	Cohort Yr 2005 Cohort Default Rate (CDR)%	Cohort Yr 2006 Cohort Default Rate (CDR)%
Public					
Less than 2 Yrs	6.7%	5.8%	5.7%	5.2%	6.4%
2-3 Yrs	8.5%	7.6%	8.1%	7.9%	8.4%
4 yrs +	4.0%	3.3%	3.5%	3.0%	3.4%
Private					
Less than 2 Yrs	9.7%	7.9%	9.0%	9.0%	10.0%
2-3 Yrs	6.1%	6.3%	7.4%	6.7%	6.1%
4 yrs +	3.1%	2.6%	2.8%	2.3%	2.4%
Proprietary					
Less than 2 Yrs	10.1%	7.9%	8.9%	8.9%	10.9%
2-3 Yrs	9.2%	8.0%	9.9%	9.3%	11.1%
4 yrs +	7.3%	6.4%	7.3%	7.2%	8.4%
Foreign Schools(1)	2.0%	1.8%	1.5%	1.0%	1.2%
Over All	5.2%	4.5%	5.1%	4.6%	5.2%

(1) FFELP only

Budget Lifetime Default Rate

Calculated based on DOLLARS for a projected cohort life of 20 yrs. Cohort is based on origination date.
As reflected in the latest estimates as of 7/1/08 (Combined Subsidized and Unsubsidized)

Institutional Category	Cohort Yr 2002 Budget Lifetime Default Rate %	Cohort Yr 2003 Budget Lifetime Default Rate %	Cohort Yr 2004 Budget Lifetime Default Rate %	Cohort Yr 2005 Budget Lifetime Default Rate %	Cohort Yr 2006 Budget Lifetime Default Rate %
2 Yr Non Profit	25.2%	25.8%	26.5%	26.8%	26.7%
2 Yr Proprietary	38.6%	39.9%	38.6%	38.0%	40.8%
4 Yr Freshmen & Sophomores	17.3%	18.0%	17.6%	17.0%	16.2%
4 Yr Juniors & Seniors	8.0%	8.2%	8.5%	9.2%	9.4%
Graduate Students	3.5%	3.6%	4.0%	4.7%	4.9%
Over All	10.8%	11.2%	11.4%	11.7%	11.9%

Cumulative Lifetime Default Rate

Calculated from the time the LOAN enters repayment and a default occurs from repayment inception through 9/30/08.

Institutional Category	Cohort Yr 2002 Cumulative Lifetime Default Rate %	Cohort Yr 2003 Cumulative Lifetime Default Rate %	Cohort Yr 2004 Cumulative Lifetime Default Rate %	Cohort Yr 2005 Cumulative Lifetime Default Rate %	Cohort Yr 2006 Cumulative Lifetime Default Rate %
2 Yr Private	21.8%	21.2%	19.7%	15.2%	11.4%
2 Yr Public	21.1%	19.7%	18.3%	15.5%	11.9%
4 Yr Private	6.9%	6.2%	5.4%	3.9%	3.0%
4 Yr Public	8.5%	7.5%	6.7%	5.2%	4.3%
Proprietary	25.2%	24.0%	22.6%	18.8%	14.0%
Foreign Schools(1)	4.7%	3.5%	2.6%	1.5%	1.5%
Over All	11.5%	10.8%	10.2%	8.2%	6.5%

(1) FFELP only

PLEASE NOTE THESE RATES CAN NOT BE COMPARED SINCE THEY ARE BASED ON DIFFERENT ATTRIBUTES: BORROWERS, DOLLARS, LOANS AND INSTITUTIONAL CATEGORIES.