
Audit of Case Management and Oversight's Audit Tracking and Resolution Process

FINAL AUDIT REPORT



Audit Control Number ED-OIG/A03-90003
September 2000

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



UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF INSPECTOR GENERAL

THE INSPECTOR GENERAL

MEMORANDUM

SEP 29 2000

TO: Greg Woods
Chief Operating Officer
Student Financial Assistance

FROM: Lorraine Lewis

SUBJECT: FINAL AUDIT REPORT
Audit of Case Management and Oversight's Audit Tracking and Resolution
Process
ED Audit Control Number: A03-90003

Attached is our subject final report that covers the results of our review of Case Management and Oversight's Audit Tracking and Resolution Process, at Washington, D.C., during the period October 1, 1997 through September 30, 1998. We received your comments concurring with the findings and recommendations in our draft audit report.

Please provide the Supervisor, Post Audit Group, Office of the Chief Financial Officer and the Office of Inspector General, with quarterly status reports on promised corrective actions until all such actions have been completed or continued follow-up is unnecessary.

In accordance with the Freedom of Information Act (Public Law 90-23), reports issued by the Office of Inspector General are available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act. Copies of this audit report have been provided to the offices shown on the distribution list enclosed in the report.

We appreciate the cooperation given us in the review. Should you have any questions concerning this report, please call Bernard Tadley at 215-656-6900.

Attachment

NOTICE

Statements that management practices need improvements, as well as other conclusions and recommendations in this report represent the opinions of the Office of Inspector General. Determination of corrective action to be taken will be made by the appropriate Department of Education officials.

In accordance with Freedom of Information Act (5 U.S.C. §522), reports issued by the Office of Inspector General are available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act.

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EXECUTIVE SUMMARY

We reviewed Case Management and Oversight's (CMO) processes for ensuring that: 1) all required annual financial statement and compliance audit reports are submitted when due; 2) findings are coded correctly; 3) reports are issued by the Document Receipt and Control Center (DRCC) contractor in a timely manner, and, if necessary, 4) reports are resolved in a timely manner.¹

We determined that CMO does not ensure all required Student Financial Assistance (SFA) compliance audit reports, Single Audit reports, and third-party servicer audit reports are submitted when due. We also found that CMO does not ensure that: 1) all compliance audit report findings are coded correctly; and 2) the contractor for the DRCC issues all compliance audit reports in a timely manner. We concluded that CMO has an effective system in place to ensure the timely submission of financial audits of proprietary institutions, and that CMO generally resolves compliance audit reports in accordance with the Office of Management and Budget (OMB) Circular A-50 requirement for timely resolution.

In order to manage and track the resolution of audit findings, the findings are assigned numeric deficiency codes. We reviewed 50 compliance reports to determine the correctness of the deficiency codes assigned. We found that for 17 of the 50 reports, there was at least one finding for which an improper deficiency code was assigned. Also, for 10 of the 50 reports, there was at least one finding for which a deficiency code was not assigned. Ten of the 50 reports were submitted late, but were not coded accordingly. The effect of improper coding is that matters that should be identified for resolution are not.

The contractor that operates the DRCC did not always meet its contractual responsibility to issue reports within 30 days of their receipt date. Of 3,139 issued reports that we analyzed for timeliness of processing, 1,433 (46 percent) were issued untimely with an average of 79 days. Significant findings (requiring resolution action) were included in 706 of the issued reports, and 321 (45 percent) of these were not issued on a timely basis. The longer the delay in issuing "deficient" compliance audit reports (those with significant findings), the more difficult it is for CMO to resolve these reports in accordance with the OMB requirement of 180 days for timely resolution of audit findings.

There were some data omissions and data errors that we noted in the two computer systems used in the process for receiving, logging, screening, issuing, and resolving audit reports.

¹ Case Management and Oversight is a division within the Student Financial Assistance Schools Channel.

We noted significant improvement in the timeliness of audit resolution by CMO from conditions that we reported in our SFA Action Memorandum No. 97-6, issued in August 1997. Of the 745 reports we were able to review for timely resolution, 290 had been closed, and 253 (87 percent) of these were timely resolved. Of the 455 reports still in process, only 54 (12 percent) had been on hand for more than 180 days. In the SFA Action Memorandum, we reported that 92 percent of reports were not timely resolved for Award Year 1995, and 57 percent were not timely resolved for Award Year 1996.

We recommend the Chief Operating Officer (COO) for Student Financial Assistance:

- improve the oversight of audit report submissions;
- ensure that reports are processed properly;
- achieve timely issuance of reports by the DRCC contractor; and
- take corrective action to ensure that required data elements are completely and correctly recorded in PEPS and Lotus Notes.

SFA concurred with all of our recommendations and noted that it has either already implemented or will be implementing actions to address the issues raised in the audit's findings. We summarized SFA's response after each finding and a copy of the complete response is contained in the Appendix.

AUDIT RESULTS

Case Management and Oversight (CMO) administers a process for receiving, logging, screening, issuing and resolving audit reports required to be submitted by all institutions that participate in the Student Financial Assistance (SFA) programs. To perform these functions, CMO has established a Document Receipt and Control Center (DRCC) operated by a contractor. CMO uses two principal systems for performing these responsibilities: the Postsecondary Education Participant System (PEPS), and Lotus Notes.

We reviewed CMO's processes for ensuring that: 1) all required annual financial statement and compliance audit reports are submitted when due; 2) findings are coded correctly; 3) reports are issued in a timely manner, and, if necessary, 4) reports are resolved in a timely manner. In August 1997, we issued SFA Action Memorandum No. 97-6 reporting problems with the tracking of audit report submissions and timely issuance and resolution of reports. While CMO has taken some actions to correct the problems in the audit tracking and resolution process, there are several areas where processes need to be improved.

Finding No. 1 Oversight of Compliance and Financial Statement Audit Report Submission Requirements Needs Improvement

CMO does not have adequate processes in place to identify and take timely action against institutions that fail to submit annual compliance audit reports and audited financial statements. Consequently, there is no assurance that these institutions: 1) meet annual compliance audit and financial statement report submission requirements; 2) initiate prompt corrective action on audit recommendations; and 3) are financially responsible.

An institution participating in any SFA program is required by the Single Audit Act (for public and private non-profit institutions that expend \$300,000 or more in a year in Federal awards) and by the Higher Education Act (for proprietary institutions) to annually have an independent auditor conduct a compliance audit of its administration of those SFA programs in which it participates, and an audit of its general purpose financial statements. Depending on the type of institution and audit, reports are due six, nine or thirteen months after an institution's fiscal year ends.

As provided by the Higher Education Act (HEA) a third-party servicer that administers any aspect of an institution's participation in SFA programs must have annual compliance and financial statement audits performed by an independent auditor, and must submit these audits annually to the Secretary.

CMO should ensure that all institutions submit their required annual compliance audit reports in a timely manner.

CMO does not have a system in place to ensure that all institutions participating in the SFA programs submit their required annual compliance audit reports in a timely manner. Efforts by CMO to notify institutions that had not submitted compliance audit reports for award year 1996 did not begin until July 1998, over a year after most of the reports were due. In July 1998, CMO identified and mailed delinquency letters to 213 institutions that did not submit 269 required SFA compliance audit reports covering award years 1994 through 1996. Also, in December 1998, CMO identified and mailed delinquency letters to 614 institutions that did not submit 839 required Single Audit compliance reports covering award years 1994 through 1996. At the time of our review, no effort was underway to determine compliance audit reports that were past due for award year 1997, although most Single Audit reports were due by July 31, 1998, and most SFA compliance reports were due by either December 31, 1997, or June 30, 1998.

CMO is not monitoring institutions participating in the SFA programs to ensure they submit required annual compliance reports on a timely basis. Therefore, they cannot assure that prompt corrective actions are taken on audit findings, which in some cases require unallowable expenditures be repaid to the Department.

During our review CMO personnel informed us that a process was in development using PEPS and Lotus Notes software to generate letters requesting institutions' SFA compliance audit reports on a real-time basis.

CMO should ensure that all public and private non-profit institutions submit annual audited financial statements.

CMO does not have a system in place to ensure that public and private non-profit institutions that participate in the SFA programs submit their required annual audited financial statements. CMO provided us with a listing, as of February 25, 1999, which indicated that there were 731 institutions (approximately 19 percent of the total universe of eligible single audit filers) which had not submitted audited financial statements that were due during the period October 1, 1997 through September 30, 1998.

CMO does have a system in place for the real-time identification of annual audited financial statements due from proprietary institutions that participate in the SFA programs. Proprietary institutions are sent a reminder notice to submit their financial statements 60 days prior to the financial statement due date. If proprietary institutions fail to submit audited financial statements, CMO will send them a delinquency letter 30 days after the financial statement due date. In addition, each month institutions that fail to submit their financial statements within ten days of the date of a delinquency letter are referred to CMO's Administrative Action and Appeals Division for

appropriate administrative action. Our review revealed that during the period October 1, 1997 through September 30, 1998, CMO generally complied with these procedures. Since CMO does not identify late or missing annual financial statement audits of public and private non-profit institutions participating in the SFA programs, there is no assurance that the financial statement audits of all these institutions are being performed. As a result, institutions that are not financially responsible may continue to participate in SFA programs and SFA funds may be at risk (e.g., lack of resources to meet program and financial obligations).

CMO should establish an audit resolution system for third party servicer reports.

CMO needs to establish and implement procedures for receiving, logging, screening, issuing and resolving third-party servicer audit reports. CMO has not performed any audit resolution on its inventory of 122 third-party servicer audit reports covering fiscal years 1994 through 1998.

OMB Circular A-50, "Audit Followup," requires Federal departments and agencies to document and have in place a system of audit resolution. CMO is not monitoring third-party servicers' compliance with audit requirements. Consequently, there is no assurance that third-party servicers:

- meet the annual compliance audit and audited financial statement report submission requirements;
- initiate prompt corrective actions on audit findings; and
- are financially responsible.

Recommendations:

We recommend that the COO for SFA:

- 1.1 Establish a system to track the receipt of SFA compliance audit reports and Single Audits on a real-time basis, and initiate appropriate action to ensure these reports are received when due.
- 1.2 Establish a system to track, process, and resolve third-party servicer audit reports, assigning priority to resolving those third-party servicer audit reports with the most serious deficiencies.

SFA's Reply:

SFA concurred with both recommendations. SFA acknowledged that prior to our audit CMO did not have a system in place to track the receipt of SFA compliance audit reports in real-time, but noted that this has changed. CMO also generates a monthly combined notification to remind proprietary schools that their compliance reports and financial statements will be due in 60 days.

With respect to Single Audits, SFA stated that in order to meet its oversight responsibility it will work with the Office of the Chief Financial Officer (OCFO) and the Census Bureau's Federal Audit Clearinghouse to identify and notify Single Audit Act institutions that have failed to submit their Single Audits of their obligations.

SFA also stated that by September 2000 it will initiate a study for the development and implementation of an electronic audit and financial statement process that will enable CMO to track the receipt of all audits, proprietary and Single Audit, in real-time.

Regarding third-party servicer audits, SFA stated that CMO's Data Management and Analysis Division (DMAD) "determined that resolving servicer audits is a redundant process as independent auditors performing institutional audits are required to review servicer audits as part of their overall review of institutional compliance." SFA also stated that it had previously requested the OIG to review the cost benefit of the servicer audit submission requirements.

OIG's Response:

SFA's statements that it has established a system to track the receipt of compliance audit reports on real-time basis, and a process to generate a monthly notifications to remind proprietary schools that their compliance reports and financial statements will be due in 60 days, should improve the audit tracking process. However, SFA's planned actions do not ensure that it will establish a system to track the receipt of Single Audits on a real-time basis. Each fiscal year CMO plans to wait until all Single Audits are past due before attempting to identify institutions that have not submitted reports.

Resolving third-party servicer audits would not be duplicative of ongoing activities. CMO personnel informed us that servicer audit findings included in institutional audit reports are not being resolved. Also, an independent auditor's review of a servicer audit for the limited purposes of completing an institution's compliance audit would not resolve all possible issues that might arise from the audit of the servicer, particularly systemic issues.

We acknowledge that in response to the OIG's 1999 request for workplan suggestions, SFA requested a cost benefit analysis of servicer audits. However, until SFA begins to track and resolve servicer audits, sufficient data is not available to conduct a meaningful analysis.

Finding No. 2 Compliance Audit Reports Were Not Processed In Accordance with CMO's Established Procedures

The DRCC did not always properly code compliance audit report findings. As a result, matters that should have been identified for resolution were not.

CMO's processes for: (1) determining if a compliance report contains findings and or other deficiencies not identified as such by the auditor (i.e., the audit report is submitted late); (2) coding the findings and or deficiencies in order to track their proper resolution; and (3) determining whether the report warrants full resolution by a Case Team, are set forth in its Procedures Memorandum 97-19, "Procedures for Classifying and Issuing 'Deficient' and 'Non-deficient' Audit Reports."

The DRCC is required to classify each finding in an acceptable audit, using 4-digit deficiency codes established by CMO. Each deficiency code has been assigned a designation that denotes whether the finding is considered "significant" or "minor." The DRCC is also charged with entering these codes into PEPS. Reports are classified as either "deficient" (i.e., contain findings requiring resolution action) or "non-deficient" (i.e., do not require resolution action).

Based on the coding of findings, PEPS designates whether the audit report is a "deficient" (Deficiency Indicator 1) or "non-deficient" (Deficiency Indicator 0 or 2) report. Deficiency indicator "0" reports have no findings, while deficiency indicator "2" reports have findings that do not require resolution by a Case Team. Deficiency indicator "1" reports have questioned costs of at least \$10,000 or more; or an error rate of 10% or greater on a significant finding; or a significant finding that automatically requires resolution by a Case Team.

The procedures also state that: "Deficient audits are resolved by the Case Team through the issuance of a Final Audit Determination. Non-deficient audits with findings (Indicator 2) are resolved by incorporating into the issuance letter standard language instructing the school to correct the deficiencies cited, and document the corrective action."

Compliance audit report findings were not assigned appropriate deficiency codes.

CMO provided us with a file, which listed every compliance audit report received during fiscal year 1998. The universe included 4,628 compliance audit reports.

We randomly selected 50 compliance audit reports for review. The 50 compliance audit reports included:

- 10 deficiency indicator 0 reports;
- 10 deficiency indicator 1 reports; and
- 30 deficiency indicator 2 reports.

Ten of the 50 compliance reports processed by the DRCC contained at least one finding for which the DRCC failed to assign a deficiency code. Also, 17 of the 50 reports contained at least one finding in which the code assigned for the finding did not relate to the instance of non-compliance as presented in the audit report.

As a result of the non-coding and mis-coding of findings, 4 reports that were processed as deficiency indicator "2" reports should have been processed as deficiency indicator "1" reports and undergone full resolution by the Case Team through the issuance of a Final Audit Determination letter. We also noted one deficiency indicator "0" report and one deficiency indicator "1" report that should have been processed as deficiency indicator "2" reports.

The coding errors appear to be the result of the DRCC contracted employees' lack of familiarity with SFA programs, and attempts to code findings using a deficiency code listing that does not reflect all the finding possibilities. The non-coding of findings appears to be the result of errors on the part of the DRCC staff.

Delinquent compliance audit reports were not coded for lateness.

Our review disclosed that 10 of the 50 compliance audit reports (6 SFA Audit Reports and 4 Single Audit Reports) were not submitted in a timely manner. SFA Audit Reports are due six months after an institution's fiscal year end. Single Audit Reports are due thirteen months after an institution's fiscal year end for fiscal years beginning on or before June 30, 1998, and nine months after an institution's fiscal year end for fiscal years beginning on or after July 1, 1998.

Although the 10 reports did not meet the applicable timely filing requirements, DRCC staff did not identify these reports as delinquent with a 4-digit deficiency code in PEPS as required by CMO procedures. CMO's Procedures Memorandum 97-18, "Procedures for Receiving and Determining the Acceptability of a Student Financial Assistance Report," instructs the DRCC staff to, based on the audit period end date and current date, determine whether the audit is on time or late. The memorandum also states, "The DRCC staff also identify and classify findings not identified as such by the auditor but observable in the report (e.g. the audit is submitted late)."

We found that 2 of the 10 reports were processed as deficiency indicator "0" reports; however, they should have been processed as deficiency indicator "2" reports since submitting a delinquent audit report is considered a significant finding per CMO Procedures Memorandum 97-19.

Recommendations:

We recommend that the COO for SFA:

- 2.1 Ensure that the deficiency code listing is updated to include all finding possibilities.

2.2 Ensure that the DRCC properly codes each finding as well as findings not identified as such by the auditor but observable in the report (e.g. the audit is submitted late).

SFA's Reply:

SFA concurred with these recommendations.

Finding No. 3 Compliance Audit Reports Were Not Issued Timely by the Contractor

The contractor that operates the DRCC did not always meet its contractual responsibility to issue compliance audit reports within 30 days of their receipt date.

CMO established the DRCC to solicit, receive, track, screen and file compliance audits, financial statement audits, and recertification applications. To perform these functions, CMO obtained the services of a contractor. For SFA audits and Single Audits, the *Statement of Work for the DRCC Contract* states that: "The contractor shall issue all compliance audit reports within 30 days of receipt." For SFA audits, issuance of the compliance audit report includes "screening for completeness and acceptability, coding the findings and questioned costs...." For Single Audits, issuance "includes coding the findings and questioned costs...." The issue date for these reports is the date of the correspondence sent from CMO to the SFA and Single Audit filers acknowledging the receipt of an acceptable audit report.

CMO received 4,628 compliance audit reports during fiscal year 1998. We were unable to analyze whether 1,456 of these reports were issued timely because the DRCC: 1) failed to record the receipt date for 810 of the reports; 2) rejected 634 of the reports due to problems with the report; and 3) recorded improper receipt and or issue dates for 23 reports (11 were also rejected reports). Of the 3,172 reports we were able to analyze, 3,139 were issued and 33 were not as of November 27, 1998. Of the issued reports, 1,433 (46 percent) were not issued within 30 days of their receipt at the DRCC, with an average of 79 days to issue. Further, 32 of the 33 unissued reports had been in receipt at the DRCC for over 30 days as of November 27, 1998.

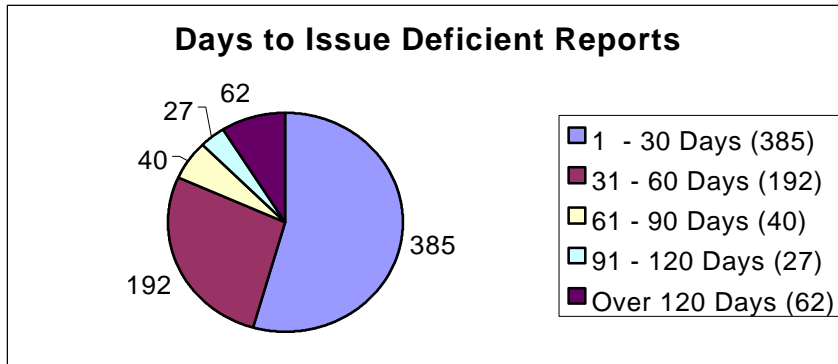
Analysis of Issued SFA Audit Reports

Deficiency Indicator	Number of Reports Analyzed	Number of Reports Issued Within 30 Days	Number of Reports Not Issued Within 30 Days	Average Number of Days for Reports Not Issued Within 30 Days
Code 0 (No Findings)	978	509	469	76
Code 1 (Significant Findings)	613	319	294	77
Code 2 (Minor Findings)	740	320	420	89

Analysis of Issued Single Audit Reports

Deficiency Indicator	Number of Reports Analyzed	Number of Reports Issued Within 30 Days	Number of Reports Not Issued Within 30 Days	Average Number of Days for Reports Not Issued Within 30 Days
Code 0 (No Findings)	542	412	130	66
Code 1 (Significant Findings)	93	66	27	113
Code 2 (Minor Findings)	173	80	93	64

While it is required that all compliance audit reports be issued within 30 days of receipt, it is of critical importance that those reports with significant findings (deficiency indicator code 1) be issued in a timely manner. The longer the delay in issuing “deficient” compliance audit reports the more difficult it is for CMO to resolve these reports within a maximum of six months after their receipt, as required by OMB Circular A-50.



Recommendation:

3.1 We recommend that the COO for SFA ensure that all compliance audit reports be issued within 30 days of receipt.

SFA's Reply:

SFA concurred with this recommendation.

Finding No. 4 Missing Data and Data Errors in Computer Based Systems

CMO's two principal systems for receiving, logging, screening, issuing and resolving audit reports are PEPS and Lotus Notes. During our review, we noted missing data and data errors in these computer based systems.

Compliance audit reports placed on hold appeared as rejected reports in PEPS.

From our review of a sample of 50 compliance audit reports, we identified that for 10 of these reports, rejection dates were recorded in the PEPS system. For nine of these reports, we were unable to locate copies of the rejection correspondence in CMO's compliance audit report folders. CMO personnel explained that these nine reports were never actually rejected; rather, they were entered into the Audit Report screen in PEPS as "on-hold." CMO staff stated that: 1) due to a deficiency in the PEPS system, rejection dates and correspondence are created when an on-hold date is entered in the PEPS Audit Report screen; and 2) these reports had been issued before CMO became aware of this problem. At the time of our review, in order to prevent rejection dates and correspondence from being created by PEPS for on-hold reports, CMO staff had to perform a manual override that required entering the PEPS Correspondence screen and changing the correspondence type code.

Institutions' fiscal year end dates were not recorded in CMO's Lotus Notes database.

CMO provided us with a listing of 312 Single Audit institutions and 52 SFA institutions for which it does not have fiscal year end dates recorded in its Lotus Notes database. The Lotus Notes database is used to track SFA institutions' annual financial statement audit report submissions on a real-time basis.

At the time of our review, CMO was unable to track the receipt of financial statement audit reports from the 364 institutions on a real-time basis.

Recommendations:

We recommend that the COO for SFA:

- 4.1 Initiate appropriate action to ensure that when an on-hold date is entered into the PEPS Audit Report screen, the system automatically generates the appropriate dates and correspondence.
- 4.2 Determine the fiscal year end dates for each of the 364 institutions missing that data and input those dates into the Lotus Notes database.

SFA's Reply:

SFA concurred with these recommendations.

OTHER MATTERS

Audit Reports Are Being Resolved More Timely

When a compliance audit report identifies findings that need to be resolved, CMO follows up with the institutions to work out a course of corrective action. OMB Circular A-50 requires that these findings be resolved within six months of report receipt.

We noted significant improvement in the timeliness of audit resolution by CMO. Previously, we reported, in SFA Action Memorandum No. 97-6, that CMO seldom resolved compliance audit reports within 180 days of receipt as required by OMB Circular A-50. Our review of 290 "deficient" reports closed during fiscal year 1998 revealed that 253 (87 percent) of these were resolved in a timely manner. Further, of 455 "deficient" reports still in process as of November 27, 1998, only 54 (12 percent) had been on hand for more than 180 days.

The "DRCC Referral to the Administrative Action and Appeals Division (AAAD)" report was not supported by source records.

We randomly selected 20 institutions from the January 1999 Report "DRCC Referral to AAAD" to determine if the data recorded on the Referral Report was supported by source records. The Referral Report data reviewed included the status of 80 financial statement reports (four financial statement reports, covering fiscal years 1995 through 1998, for each of the 20 institutions selected). CMO was unable to locate its financial statement folders for 2 of the 20 institutions originally chosen for review and 2 replacement selections were made. Of the 80 financial statement reports included in our review, 57 were coded as either Complete or Incomplete, and 23 were coded as Not Received on the Referral Report. Of the 57 reports coded as either Complete or Incomplete we were unable to verify whether 6 were coded properly, as we could not locate them in the institutional financial statement report folders provided by CMO.

BACKGROUND

The Higher Education Act Amendments of 1998 established a performance based organization (PBO) for managing the operational functions of the Title IV Student Financial Assistance programs. The Office of Student Financial Assistance was designated as the PBO. This office was reorganized in the fall of 1999 and renamed Student Financial Assistance (SFA). Within SFA, the operational procedures of the Institutional Participation and Oversight Service (IPOS) did not change, however, it was renamed Case Management and Oversight (CMO), a division within the SFA Schools Channel.

At the time of our review, CMO was one of six services within SFA that was responsible for administering the Title IV SFA programs. CMO is responsible for determining whether institutions meet statutory eligibility and certification requirements for participation in these programs. CMO also develops and implements: 1) policies and procedures for monitoring institutions participating in the SFA programs to ensure compliance with Federal legislation, regulations and policies; 2) alternative oversight programs such as the Quality Assurance Program; 3) activities related to resolving issues that arise when schools close, declare bankruptcy, or are otherwise in financial or administrative jeopardy; and 4) activities of the Secretary's default reduction initiative.

A CMO report titled "Universe of Eligible and Certified Postsecondary Institutions" stated that as of September 30, 1998 there was a universe of 5,832 institutions eligible and certified to participate in the SFA programs. Institutions participating in the SFA programs are required by the Single Audit Act (for public and private non-profit institutions that expend \$300,000 or more in a year in Federal awards) and by the Higher Education Act (for proprietary institutions) to have annual compliance and financial audits performed by independent public accountants or state auditors. Also, as provided by the Higher Education Act, a third-party servicer that administers any aspect of an institution's participation in SFA programs must have annual compliance and financial audits performed by an independent auditor. CMO is responsible for receiving, tracking, screening, issuing and resolving these reports. To perform these functions, CMO established a Document Receipt and Control Center (DRCC) operated by a contractor.

AUDIT SCOPE AND METHODOLOGY

The objectives of our audit were to determine whether CMO has established and implemented procedures which provide reasonable assurance that: 1) all required annual financial statement and compliance audit reports are submitted when due, 2) findings are coded correctly, 3) reports are issued and, if necessary, 4) resolved in a timely manner.

To accomplish our objectives we analyzed the file, provided by CMO, which contained the universe of 4,628 compliance audit reports received during fiscal year

1998. We reviewed 50 randomly selected compliance audit report files. In addition, we reviewed CMO's Postsecondary Education Participant System (PEPS) information for the selected 50 institutions. We analyzed the listing provided by CMO of all Single Audit and SFA financial statement reports that were due, but not received, during fiscal year 1998. We examined the financial statement report folders for 20 institutions that we randomly selected from the universe of 607 institutions included on the January 1999 *DRCC Referral to the AAAD Report*. In addition, we reviewed CMO's Lotus Notes information for the selected 20 institutions. We reviewed CMO's procedures for tracking, processing, and resolving compliance audit and financial statement reports. We also interviewed CMO personnel to obtain an understanding of these procedures. We reviewed the Report on Internal Controls for Student Financial Assistance Programs from the U.S. Department of Education's 1997 Financial Statement Report. We also reviewed the 1998 Federal Managers' Financial Integrity Act Report.

We relied in part on computer-processed data contained in CMO's Lotus Notes database and PEPS. We performed limited tests of the output of computer processes to verify reliability. Based on the results of the tests described, we concluded that the computerized data was sufficiently reliable to formulate conclusions associated with the objectives described above.

We conducted our on-site fieldwork at CMO's headquarters in Washington, DC. Our fieldwork was conducted from November 17, 1998 through August 6, 1999. Subsequent to the completion of our fieldwork, additional analyses were performed from October 1999 through December 1999. Our audit was performed in accordance with government auditing standards appropriate to the scope of the audit described above.

STATEMENT ON MANAGEMENT CONTROLS

As part of our audit, we made an assessment of CMO's management controls, policies, procedures, and practices applicable to the scope of the audit. Our assessment was performed to determine the level of control risk for determining the nature, extent, and timing of our substantive tests to accomplish the audit objective.

For the purpose of this report, we assessed and classified the significant controls into the following categories:

- Procedures for Receiving Required Annual Compliance Audit and Financial Statement Reports
- Procedures for Classifying and Issuing Compliance Audit Reports

Because of inherent limitations, a study and evaluation made for the limited purpose described above would not necessarily disclose all material weaknesses in the control structure. However our assessment disclosed management control weaknesses. These weaknesses are fully described in the Audit Results section of this report.

APPENDIX –AUDITEE’S COMMENTS



UNITED STATES DEPARTMENT OF EDUCATION
THE OFFICE OF STUDENT FINANCIAL ASSISTANCE
WASHINGTON, D.C. 20202-5132

AUG 11 2000

CHIEF OPERATING OFFICER

Mr. Bernard Tadley
Regional Inspector General for Audit
Office of Inspector General
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Philadelphia, PA 19107

Dear Mr. Tadley:

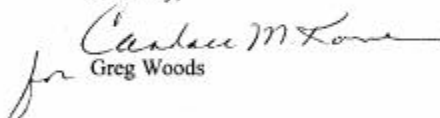
Thank you for the opportunity to review and comment on the draft audit report entitled "*Audit of Case Management and Oversight's Audit Tracking and Resolution Process*," Control Number ED-OIG/A03-90003, June 2000. In general, we concur with all the recommendations in the draft report.

We consider the audit tracking and resolution process to be a critical tool in our overall oversight of student financial assistance funds. Therefore, we are pleased that your draft report notes that we have made significant improvements in the timeliness of audit resolution and we are confident that we will continue to improve our performance in all areas of the audit process.

We will continue to work closely with all our partners, such as the Department's Office of the Chief Financial Officer and the Census Bureau's Federal Audit Clearinghouse, to ensure that all audits are properly accounted for, tracked, and resolved. We will also update our internal guidance and provide our staff with more training. We know that we can improve our efforts in the audit process and we welcome this opportunity to work with you to ensure that this critical oversight tool functions as effectively as possible. In particular, we look forward to continuing to work with you to develop and implement an electronic process for audit and financial statement submissions.

Again, we appreciate the opportunity to review and comment on the draft report. We will take appropriate steps to address the issues identified in the report. The enclosure provides the Department's response to each recommendation.

Sincerely,


for Greg Woods

Enclosure

cc: Lorraine Lewis
Carol Lynch
Patrick Howard
Kay Jacks
Jim Lynch

We help put America through school.

Response to OIG Draft Audit Report, "Audit of Case Management and Oversight's Audit Tracking and Resolution Process," Control Number ED-OIG/A03-90003, June 2000.

Finding 1

Oversight of Compliance and Financial Statement Audit Report Submission Requirements Needs Improvement.

Recommendation 1.1: *Establish a system to track the receipt of SFA compliance audit reports and Single Audits on a real-time basis.*

Response: We concur with this recommendation. Student Financial Assistance (SFA) is dedicated to ensuring that all postsecondary institutions submit their compliance audits and financial statements as required.

However, we feel it is important for the audit report to note that, while SFA's Case Management and Oversight (CMO) has oversight responsibility for the audit process, CMO directly receives only compliance attestation reports and financial statements from proprietary institutions required to submit audits under the Higher Education Act. Public and non-profit institutions subject to the Single Audit Act submit their A-133 compliance audits and financial statements directly to the Census Bureau's Federal Audit Clearinghouse (Clearinghouse). Within the Department, the Office of the Chief Financial Officer (OCFO), not SFA, is responsible for tracking A-133 audits, and performs this function through the Department's inter-agency agreement with the Census Bureau. In addition, the Clearinghouse is responsible for mailing notices to Single Audit Act institutions that their A-133 audits are late.

Nonetheless, in order to meet our oversight responsibility, we are determined to continue working closely with both the OCFO and the Clearinghouse to identify Single Audit Act institutions that have failed to submit their A-133 audits and to ensure that they are notified of their obligations. By August 31, 2000, CMO will provide the OCFO and the Clearinghouse with a list of institutions that have not submitted their 1997 and 1998 A-133 audits and financial statements. By November 2000, CMO will provide the OCFO and the Clearinghouse with a list of institutions that have not submitted their 1999 information. After receiving each of these lists, the Clearinghouse will mail letters to those institutions notifying them that their audits and financial statements have not been received. Once these mailings are complete, CMO will be current in its missing audit notifications for Single Audit Act institutions. Our plan is to provide the OCFO and the Clearinghouse with a list of institutions that have failed to submit their A-133 audits every November for a notification mailing to be performed by the Clearinghouse.

We acknowledge that, prior to this audit, CMO was tracking only the receipt of financial statements for proprietary institutions. This has changed. CMO now tracks, in real-time, both compliance attestation reports and financial statements for proprietary institutions. Since March 2000, CMO generates a monthly combined notification to remind proprietary institutions that their compliance reports and financial statements will be due in 60 days. This monthly process also includes notification to those delinquent institutions that have failed to submit their compliance audits and/or financial statements that they are late and gives them ten days to

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submit the required documents. If an institution fails to submit its audit and/or financial statement within ten days, it is reported on the Cumulative Delinquent Institutions Report for appropriate action by CMO's case teams. If necessary, the case teams refer institutions to CMO's Administrative Actions and Appeals Division (AAAD) for administrative action.

Finally, by September 2000, SFA will initiate a study for the development and implementation of an electronic audit and financial statement process that will enable CMO to effectively track the receipt of all audits, proprietary and Single Audit, in real-time.

Recommendation 1.2: *Establish a system to track, process, and resolve third-party servicer audit reports, assigning priority to resolving those third-party servicer audit reports with the most serious deficiencies.*

Response: We concur with this recommendation, but have reservations. While we understand that, under current requirements, third-party servicer (servicer) audits should be tracked and resolved, we believe the costs outweigh the benefits.

CMO's Data Management and Analysis Division (DMAD) will begin to track and process servicer audits. However, in a September 7, 1999, memorandum from SFA's Chief Operating Officer to the Department's Inspector General, SFA requested that the Office of Inspector General (OIG) review the cost benefit of the servicer audit submission requirements. In addition, DMAD performed a cursory review of some servicer audits and determined that the majority of the audits either had no findings or had insignificant findings.

DMAD also determined that resolving servicer audits is a redundant process as independent auditors performing institutional audits are required to review servicer audits as part of their overall review of institutional compliance. The OIG's SFA Audit Guide (January 2000, p. I-5) clearly states that IPAs (Independent Public Accountants) "should obtain the most recent servicer audit and any other reports regarding servicer compliance. If the audit contains findings of noncompliance, the IPA should assess the effect of that noncompliance on the nature, timing or extent of substantive tests at the institution. If significant noncompliance is disclosed in the servicer's audit, the IPA must assess the effect of that noncompliance on the institution and include that information in the audit report." In addition, the Government Auditing Standards (Revised May 1999), 6.14 and 6.15, also require auditors to determine if other auditors have previously audited the institution and, if they intend to rely on the information in those audits, to determine the significance of the other auditor's work.

CMO plans to request that the third-party servicer compliance audit requirements in § 668.23 of the Student Assistance General Provisions and the statutes be reexamined. In the interim, we plan to work with the OIG to strengthen and reinforce the institutional audit requirement in the SFA Audit Guide that auditors must review servicer audits for an institution when conducting the institution's annual compliance audit.

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Finding 2

Compliance Audit Reports Were Not Processed In Accordance with CMO's Established Procedures.

Recommendation 2.1: *Ensure that the deficiency code listing is updated to include all finding possibilities.*

Response: We concur with this recommendation. CMO formed a team to determine if deficiency codes need to be added, updated or removed. We expect the team to complete its review by September 30, 2000.

Recommendation 2.2: *Ensure that the DRCC properly codes each finding as well as findings not identified as such by the auditor but observable in the report (e.g., the audit is submitted late).*

Response: We concur with this recommendation. CMO's DMAD will determine whether an automated process is needed in the Postsecondary Education Participant System (PEPS) to code audits for being submitted late. In addition, because there have been numerous changes to the audit process, CMO will update its internal guidance and provide additional training to both regional and headquarters CMO staff as well as contractor staff from DMAD's Document Receipt and Control Center (DRCC). We expect training to be completed by January 31, 2001. This training will ensure the proper coding of findings.

Finding 3

Compliance Audit Reports Were Not Issued Timely by the Contractor.

Recommendation: *Ensure that all compliance audit reports are issued within 30 days of receipt.*

Response: We concur with this recommendation. SFA's goal is to issue all audit reports within 30 days of receipt. The DRCC has made significant strides over the last three years to ensure that all audits are issued within 30 days.

In order to achieve the goal of issuing audits within 30 days, the DRCC first had to clear up significant backlogs as a result of obtaining missing audits. During the early summer of 1998, DMAD performed a massive mailing to all proprietary institutions that had not submitted their 1994, 1995 and 1996 compliance audits. This mailing, combined with a massive effort by the Clearinghouse in 1998 to reduce its backlog of A-133 audits, resulted in a significant increase in the number of audit receipts in 1998. Although the DRCC concentrated its efforts on eliminating this high volume of 1998 receipts, its efforts were hampered by problems encountered as a result of major enhancements to the PEPS Audit Module. As a result, the 1998 backlog was not eliminated until Spring 1999. Since then, the DRCC has concentrated on issuing audit reports to the Case Teams within 30 days of receipt.

The result has been that the percentage of audits issued in less than 30 days has significantly increased. In FY 1998, only 36% of proprietary audits and only 40% of A-133 audits were

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issued in less than 30 days. In FY 2000, current through July 12, the percentage of audits issued in less than 30 days has increased to 75% for proprietary audits and to 99% for A-133 audits.

Finding 4

Missing Data and Data Errors in Computer Based Systems.

Recommendation 4.1: *Initiate appropriate action to ensure that when an on-hold date is entered into the PEPS Audit Report screen the system automatically generates the appropriate dates and correspondence.*

Response: Appropriate action was not only initiated, but completed during the time the OIG was conducting its fieldwork and analysis. It was a problem DMAD knew about and explained to the auditors. At the beginning of the audit, DMAD notified the OIG about the bug in PEPS that would make audits placed “on hold” to appear as being “rejected.” Further, the OIG was notified that the problem was being fixed. The problem was fixed by August 1999 and all data in PEPS was corrected. DMAD notified the Philadelphia OIG office of this via e-mail on October 5 and on November 3, 1999. Therefore, we believe this recommendation should not be included in the audit report.

Recommendation 4.2: *Determine the fiscal year end dates for each of the 364 institutions missing that data and input those dates into the Lotus Notes database.*

Response: We concur with this recommendation. The fiscal year end (FYE) dates for 359 of the 364 institutions are now in Lotus Notes. The remaining five are public or non-profit institutions for which the DRCC has not yet received A-133 audits. As mentioned in the response to recommendation 1.1 above, CMO will provide the OCFO and the Clearinghouse with a list of institutions that have not submitted 1997 and 1998 A-133 audits and financial statements. These five institutions will be included in the list and will be notified by the Clearinghouse that their A-133 audits have not been submitted. The FYE date for these five institutions will be updated in Lotus Notes as soon as the DRCC receives the missing audits.

Other Matters

Audit Reports are Being Resolved More Timely.

Response: We are pleased the draft audit report notes that CMO has made significant strides in resolving audit reports. It is our goal to resolve all audits within six months and we are confident that we will continue to improve our performance.

The DRCC did not ensure all single audit report receipt dates were recorded in PEPS.

Response: We are pleased that the draft audit report notes that CMO has adequately addressed this issue and that no further action is necessary. However, we feel that this finding should not be in the draft report because, as with recommendation 4.1 above, this was a problem DMAD identified and corrected while the OIG was completing audit work. The OIG was notified by DMAD that an enhancement to add a field to record the Clearinghouse receipt date for A-133

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audits had been requested for the PEPS Audit Module. Further, the OIG was notified during the exit conference on June 4, 1999 that the enhancement was in place and that the data had been fixed. DMAD further notified the Philadelphia OIG office of this resolution via telephone on June 5, 1999, and via e-mail on October 5 and on November 3, 1999.

The “Document Receipt and Control Center (DRCC) Referral to the Administrative Action and Appeals Division (AAAD)” report was not supported by source records.

Response: We concur that at the time the OIG performed its audit the DRCC referral to AAAD report was not supported by source records. In January 1999, DMAD met with CMO managers to streamline the DRCC delinquent financial statement and/or compliance audit referral process to AAAD. A more streamlined and efficient referral process was implemented in March 2000 to eliminate unnecessary work for AAAD. The DRCC, on a monthly basis, now prepares for the case teams a Cumulative Delinquent Institutions Report that identifies schools that have failed to submit compliance audits or financial statements. The case teams use this report to determine what action to take, including referring institutions to AAAD for administrative action.

In addition, the DRCC ensures that receipt dates are entered for all documents and reports. Since the time of the audit fieldwork, CMO has implemented a controlled file room that enables us to maintain and retrieve source records. We are in the process of securing enhanced software that will track to the "document level" rather than to just the "file level". This will assist us in locating individual documents, such as financial statements or compliance audits, more quickly and accurately.

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