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DEPARTMENT OF EDUCATION

Status of Efforts to Address Major Management Challenges

Statement of Linda Calbom
Director, Financial Management and Assurance

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Highlights

Highlights of GAO-03-531T, a testimony before the Subcommittee on Select Education, Committee on Education and the Workforce, House of Representatives

Why GAO Did This Study

In its 2003 performance and accountability report on the Department of Education, GAO identified challenges in, among other areas, student financial aid programs and financial management. The information GAO presents in this testimony is intended to assist Congress in assessing Education's progress in addressing and overcoming these challenges.

What GAO Recommends

GAO is not making new recommendations in this testimony, but past reports have made specific recommendations aimed at addressing some of these major management challenges.

www.gao.gov/cgi-bin/getrpt?GAO-03-531T.

To view the full testimony, click on the link above. For more information, contact Linda Calbom at (202) 512-9508 or calboml@gao.gov.

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What GAO Found

Education has taken steps to address its continuing challenges of reducing vulnerabilities in its student aid programs and improving its financial management, such as establishing a senior management team to address management problems, including financial management, throughout the agency. And, while Education has made significant progress, weaknesses remain that will require the continued commitment and vigilance of Education's management to resolve.

- **Reduce vulnerability of student aid programs to fraud, waste, abuse, and mismanagement.** Education has made considerable changes to address the ongoing challenges in administering its student aid programs. However, Education needs to continue to address systems integration issues, reduce fraud and error in student aid application and disbursement processes, collect on student loan defaults, and improve its human capital management.

- **Improve financial management.** Education has implemented many actions to address its financial management weaknesses. Significant progress was made recently when Education received an unqualified—or "clean"—opinion on its financial statements for fiscal year 2002. While this is an important milestone for the department, internal control and systems weaknesses remain that impede Education's ability to produce timely, accurate, and useful financial information for its managers and stakeholders.

History of Financial Management Weaknesses

Fiscal year	Audit opinion[a]	Material internal control weaknesses	Noncompliance with federal systems requirements[b]
1995	Disclaimer	Yes	N/A
1996	Disclaimer	Yes	N/A
1997	Unqualified	Yes	Yes
1998	Disclaimer	Yes	Yes
1999	Qualified	Yes	Yes
2000	Qualified	Yes	Yes
2001	Qualified	Yes	Yes
2002	Unqualified	Yes	Yes

Source: Auditors' reports for fiscal years 1995-2002.

[a]Auditors issue unqualified opinions when the financial statements are presented fairly, in all material respects. Qualified opinions are issued when the financial statements are presented fairly, with exceptions that are specifically disclosed and described. Disclaimers of opinion are rendered when auditors cannot satisfy themselves as to whether the financial statements are presented fairly.
[b]These requirements became effective for fiscal year 1997.

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to discuss the major management challenges faced by the Department of Education, its progress in addressing them, and challenges that remain.

As you know, this January, we issued our Performance and Accountability Series on management challenges and program risks at major agencies, including the Department of Education.[1] The report for Education focused on a number of management challenges and continued the high risk designation for student aid programs. You asked me to focus my testimony on two areas in that report. These are Education's efforts to (1) reduce fraud, waste, abuse, and mismanagement in its student aid programs while continuing to ensure access to postsecondary education and (2) improve its financial management to help build a high performing agency. Education has taken steps to meet these challenges, such as establishing a senior management team to address management problems, including financial management, throughout the agency. And, while Education has made significant progress, including receiving a clean opinion on its fiscal year 2002 financial statements, weaknesses remain that will require the continued commitment and vigilance of Education's management to resolve. I will discuss Education's student aid programs and financial management in turn.

Student Aid Programs

Ensuring access to postsecondary education while reducing vulnerability of aid programs to fraud, waste, abuse, and mismanagement is one of the key management challenges Education faces. Education helps millions of students enroll in higher education programs by providing for more than $50 billion in grants and loans annually. The department is responsible for ensuring that these programs are efficiently managed, establishing procedures to ensure that loans are repaid, and preventing fraud and abuse. Since 1990, we have identified Education's grant and loan programs as high risk for fraud, waste, abuse, and mismanagement.

Both Education and Congress have made changes to address management challenges in the student financial aid programs. Congress established Education's Office of Federal Student Aid (FSA) as a performance-based

[1]U.S. General Accounting Office, *Major Management Challenges and Program Risks: Department of Education*, GAO-03-99 (Washington, D.C.: Jan. 2003).

organization in 1998. Its purpose is to increase accountability of officials, provide greater flexibility in management, integrate information systems, reduce costs, and develop and maintain a system that contains complete, accurate and timely data that can ensure program integrity. In 2001, Education established a Management Improvement Team (MIT) of senior managers to formulate strategies to address key management problems throughout the department. According to Education, MIT has developed a system to identify, track, and resolve audit and management issues both agencywide and in the student financial aid programs.

Education has faced challenges in four areas related to its grant and loan programs. These are (1) financial aid system integration issues, (2) fraud and error in student aid application and disbursement processes, (3) defaulted student loans, and (4) human capital management. I would now like to briefly discuss each of these challenges.

Education has spent millions of dollars to integrate and modernize its many financial aid systems in an effort to provide more information and better service to students, parents, institutions, and lenders. Effectively and efficiently investing in information technology requires, among other things, an institutional blueprint that defines in both business and technical terms the organization's current and target operating environments and provides a transition road map. Because Education did not have this blueprint, commonly called an enterprise architecture, we recommended in 1997 that the department develop an architecture and establish standard reporting formats and data definitions.[2] In September 2002, Education's Office of the Inspector General (OIG) reported that the department had made progress in taking specific actions to lay the groundwork for an enterprise architecture. Still, critical elements need to be completed, including integrating separate architectures into a departmentwide architecture and fully implementing common identifiers for students and institutions to use in departmentwide system applications. Education is planning to brief us shortly about the department's enterprise architecture and progress it has made. Also, in April 2002, we recommended that FSA and the department develop and include clear goals, strategies, and measures to better demonstrate its progress in implementing plans for integrating its financial aid systems in FSA's performance plans and subsequent performance reports.[3]

[2]U.S. General Accounting Office, *Student Financial Aid Information: Systems Architecture Needed to Improve Programs' Efficiency*, AIMD-97-122 (Washington, D.C.: July 29, 1997).

[3]U.S. General Accounting Office, *Federal Student Aid: Additional Management Improvements Would Clarify Strategic Direction and Enhance Accountability*, GAO-02-255 (Washington, D.C.: April 30, 2002).

With respect to modernization plans, we reported in November 2001 that FSA selected a viable, industry-accepted means of integrating its existing data on student loans and grants.[4] FSA has made progress in implementing this approach for its Common Origination and Disbursement process, which includes the implementation of a common record that institutions can use to submit student financial aid for Pell Grant and Direct Loan programs. The ultimate success of this process, however, hinges on addressing serious postimplementation operational problems and helping thousands of schools implement the common record. Further, as we reported in December 2002,[5] FSA has not completed a number of elements that are important to managing any information technology investment. These include determining whether expected benefits are being achieved and tracking lessons learned related to schools' implementation of the common record. We have recommended that FSA develop metrics, baseline data, and a tracking process for certain benefits expected from the system, and that they develop and implement a process for capturing and disseminating lessons learned to schools that have not yet implemented the common record. FSA has begun to act on both of these issues.

[4]U.S. General Accounting Office, *Student Financial Aid: Use of Middleware for Systems Integration Holds Promise*, GAO-02-7 (Washington, D.C.: Nov. 30, 2001).

[5]U.S. General Accounting Office, *Federal Student Aid: Progress in Integrating Pell Grant and Direct Loan Systems and Processes, but Critical Work Remains*, GAO-03-241 (Washington, D.C.: Dec. 31, 2002).

Education has also faced challenges in ensuring that information reported on student aid applications is correct and that adequate internal controls are in place to prevent improper payments of grants and loans. The department has taken steps, in two pilot programs with the Internal Revenue Service (IRS), to match income reported on student aid applications with federal tax returns.[6] To continue this income match and implement it on a broader scale, legislation to allow the IRS to release the information is necessary. Education has worked with the Department of the Treasury and the Office of Management and Budget to ask that the Congress enact such legislation. The department also verifies income information by asking 30 percent of applicants to provide copies of their tax returns to their student financial aid offices. In addition to strengthening its controls over student aid applications, we found that Education also needed to address institutions that were disbursing grants to ineligible students.[7] The department has taken steps to analyze student data to identify high concentrations of students over 65 and eligible noncitizens at individual institutions to determine whether problems exist that warrant further review. These actions are encouraging, and if properly implemented, should improve controls over these payments.

[6] U.S. General Accounting Office, *Major Management Challenges and Program Risks: Department of* Education, GAO-01-245 (Washington, D.C.: Jan. 2001).

[7] U.S. General Accounting Office, *Education Financial Management: Weak Internal Controls Led to Instances of Fraud and Other Improper Payments*, GAO-02-406 (Washington, D.C.: Mar. 28, 2002).

A continuing challenge for Education and FSA is preventing and collecting defaulted student loans. While the national student loan default rate has decreased from 11.6 percent in fiscal year 1993 to 5.9 percent in fiscal year 2000, the cumulative amount of defaulted student loans has increased by almost $10 billion over the same period. Education and FSA have implemented several default management strategies, such as establishing electronic debiting as a repayment option, and working with some guaranty agencies to set up alternatives to service and process claims for defaulted loans. Our analysis of FSA's internal documents indicated that for fiscal years 2000 through 2002, FSA met or exceeded many of the goals related to these strategies. However, neither Congress nor the public can determine whether FSA's default management goals have been met because Education did not prepare performance reports that conform to the requirements in the Higher Education Act. FSA's report to Congress on its performance in fiscal years 2000 and 2001 was not timely nor did it indicate whether or not FSA met established performance goals. We have recommended that Education and FSA prepare and issue reports to Congress on FSA's performance that are timely and clearly identify whether performance goals were met.[8]

Like other federal agencies, Education must address serious human capital issues, such as succession planning, because about one-third of Education's workforce is eligible to retire. In June 2001, we recommended that the department develop human capital goals and measures for its performance plans.[9] In April 2002, we recommended that the department and FSA coordinate closely to develop and implement a comprehensive human capital strategy.[10] Education added a specific objective to its strategic plan, and in 2002, issued a comprehensive 5-year human capital plan that incorporates FSA. This plan outlines steps and time frames for improving human capital management and specifies four critical areas where improvements should be made: (1) top leadership commitment, (2) performance management, (3) workforce skills enhancement, and

[8]U.S. General Accounting Office, *Federal Student Aid: Timely Performance Plans and Reports Would Help Guide and Assess Achievement of Default Management Goals*, GAO-03-348 (Washington, D.C.: Feb. 14, 2003).

[9]U.S. General Accounting Office, *Department of Education: Status of Achieving Key Outcomes and Addressing Major Management Challenges*, GAO-01-827 (Washington, D.C.: June 29, 2001).

[10]GAO-02-255, 26.

(4) leadership and succession planning. It will be important that Education focus continually on implementation of the plan to achieve results.

Now, Mr. Chairman, I would like to discuss Education's financial management challenges and the progress they have made in addressing them.

Financial Management

Weaknesses in Education's financial management and information systems have limited its ability to achieve one of its key goals—improving financial management to help build a high-performing agency. Significant progress towards this goal was made recently when Education received an unqualified—or "clean"—opinion on its financial statements. Prior to this, with the exception of 1997, Education had not received a clean opinion since its first agencywide audit in 1995. While this is an important milestone for the department, significant management weaknesses remain that must be addressed for Education to meet its goal in this area.

Beginning with the department's first agencywide audit in 1995, Education's auditors have repeatedly identified significant financial management weaknesses. These weaknesses included Education's inability to provide the auditors with sufficient evidence to satisfy themselves about the accuracy or completeness of certain amounts included in the financial statements, including billions of dollars of adjustments to amounts reported in previous years' financial statements. According to Education's auditor, these adjustments were to correct "unnatural account balances" or otherwise adjust balances to the amount management's analysis supported. The auditor reported that in many cases, the cause of the incorrect balances could not be definitively determined, and the adjusting entry prepared by management was a reasoned judgment of how to correct its accounts. Education's auditors have also consistently reported major internal control weaknesses related to financial management systems and financial reporting. These weaknesses included (1) the absence of a fully integrated financial management system, (2) deficiencies in financial management practices that require extensive analysis of accounts to resolve errors through manual adjustments, (3) the lack of a rigorous review of interim financial data for timely identification and correction of errors, (4) the inability to accumulate, analyze, and present reliable financial information in the form of financial statements, (5) the dependence on a variety of stopgap measures to prepare financial statements, (6) the insufficiency of compensating controls, such as top-level reviews to address and to seek to compensate for systemic control weaknesses, and (7) the lack of a review to identify and quantify improper payments. Education's auditors also reported that internal controls needed strengthening in numerous areas relating to Education's investment of millions of dollars in property and equipment.

Education has taken actions over the last several years to improve its financial management and to address the weaknesses identified. For example, during 2001, Education's MIT developed specific actions to address issues raised in previous financial statement audits. According to a MIT report on its accomplishments, Education began performing certain critical reconciliations on a monthly basis and began preparing interim financial statements, which helped identify areas needing further study. Education also improved its internal controls over property and equipment, and its auditor did not report this area as a weakness in fiscal year 2002. In addition, according to Education's auditor, during fiscal year 2002, the department implemented a new general ledger software package and FSA implemented a new financial management system to support their management information reporting needs. The auditor also reported that the department implemented several processes during fiscal year 2002 to improve its financial management, including

- convening the Accounting Integrity Board, the Audit Steering Committee, and the Accounting Assurance Group to plan, implement and manage quality accounting change control;

- establishing the Financial Statement Committee and continuing the Financial Statement Preparation Team and other special task force teams all of which are designed to improve the financial statement processes; and

- developing and implementing reconciliation work plans, policies and procedures, specialized teams and regular management reviews of the final work products as well as management review for process improvement.

While Education has made progress in addressing many of its weaknesses, in fiscal year 2002, the auditors again reported that significant financial management issues continued to impair the department's ability to accumulate, analyze, and present reliable financial information. These problems, in part, resulted from inadequate internal controls over Education's financial management systems and financial reporting process.

The auditor also reported that weaknesses in the department's ability to report accurate financial information on a timely basis were due to deficiencies in certain of the department's financial management practices, including inadequate reconciliations and account analysis early in fiscal year 2002. The auditor added that issues associated with the transition to a new financial management system in fiscal year 2002 also contributed to the department's difficulties in these areas. While the auditor reported that it noted improvements in the latter part of the fiscal year, it reported that it continues to believe that the department needs to place additional focus on reconciliation procedures, account analysis, and financial reporting. Until these issues are fully resolved, Education's ability to produce timely, accurate, and useful financial information for its managers and stakeholders will be greatly impeded. In addition, beginning with fiscal year 2004, Education and other major government agencies will be required to produce audited financial statements within 45 days after the end of the fiscal year compared to 120 days for fiscal years 2002 and 2003. Education will need to continue to focus strongly on resolution of its financial management deficiencies in order to be in a position to meet these new reporting deadlines.

As we testified before this Subcommittee in April 2002, we identified other internal control weaknesses that make Education vulnerable to improper payments and lost assets.[11] In our testimony and related report,[12] we stated that for May 1998 through September 2000, weak internal controls over the (1) grants and loan disbursement process failed to detect certain improper payments, (2) third party draft processes increased Education's vulnerability to improper payments, and (3) government purchase cards resulted in some fraudulent, improper, and questionable purchases. We also reported that Education lacked adequate internal controls over computers acquired with purchase cards and third party drafts. Among other things, we found that computer purchases valued at almost $400,000 were not recorded in Education's property records, and $200,000 of that computer equipment could not be located.

[11]U.S. General Accounting Office, *Education Financial Management: Weak Internal Controls Led to Instances of Fraud and Other Improper Payments*, GAO-02-513T (Washington, D.C.: April 10, 2002).

[12]GAO-02-406.

In response to our work, Education made several changes to its policies and procedures to improve internal controls and program integrity. These changes were a step in the right direction; but in many cases, our follow-up work indicated that they had not been effectively implemented. In March 2002, we reported that vulnerabilities remained in all areas we reviewed, except for third party drafts, which were discontinued altogether.[13] For example, we reported that Education developed a new approval process for its purchase card program; however, our testing of 3 months of purchase card statements under the new process found that over 20 percent lacked proper support for the items purchased. In October 2002, Education told us that new policies and procedures were implemented and aimed at reducing the department's vulnerability to future improper use of purchase cards. These new policies and procedures relate to reviewing and approving purchase card transactions and providing related training. Further, the department told us that misuse of purchase and travel cards is now specifically included in the department's Table of Penalties with the desired effect of reducing misuse and abuse of government issued credit cards. Education also told us that it recognizes that reviewing and improving internal controls is an ongoing task and that it intends to remain vigilant in this area. These are positive steps that should help reduce the instances of improper purchases.

Finally, Education will need to continue its actions in addressing weaknesses in its financial management information systems. The Federal Financial Management Improvement Act (FFMIA) of 1996 requires agencies to institute financial management systems that substantially comply with federal financial management systems requirements, applicable accounting standards, and the federal government's *Standard General Ledger*. Every year since FFMIA was enacted, Education's auditors have reported that Education's systems did not substantially comply with the act's requirements. In previous years, the auditors reported that without a fully integrated financial management system, deficiencies in the general ledger system, deficiencies in the manual adjustment process, and the need to strengthen other financial management controls such as reconciliation processes, collectively impair Education's ability to accumulate, analyze, and present reliable financial information. In addition, according to Education's auditor, although the department implemented a new financial management system during fiscal year 2002, issues associated with the transition to the new system

[13] GAO-02-406, 30.

contributed to difficulties in providing reliable, timely information for managing current operations and timely reporting of financial information to central agencies; therefore, Education still did not substantially comply with FFMIA's requirements.

Education also needs to address identified computer security weaknesses in its financial management and other information systems. In September 2001, we reported that Education had made progress in correcting certain information system control weaknesses.[14] At the same time, we identified weaknesses in Education's systems that place critical financial and sensitive grant information at risk of unauthorized access and disclosure, and key operations at risk of disruption. We recommended that Education correct certain information system control weaknesses and fully implement a comprehensive departmentwide computer security management program. In response, Education stated that it had developed a corrective action plan and is taking steps to further strengthen and develop a more comprehensive information security program. In addition, Education's auditor reported that for fiscal year 2002, the department made progress in strengthening controls over its information technology processes, but needs to continue efforts to develop, implement, and maintain an agencywide risk-based information security plan, programs, and practices to provide security throughout the life cycle of all systems.

In closing, Chairman, I want to reiterate that Education is taking actions and making substantial progress in addressing major challenges related to its student aid programs and financial management. At the same time, some very difficult issues remain that must be resolved before Education is able to produce relevant, reliable, and timely information to efficiently and effectively manage the department and provide full accountability to its stakeholders.

Mr. Chairman, this concludes my statement. I would be happy to answer any questions you or other members of the Subcommittee may have.

[14] U.S. General Accounting Office, *Education Information Security: Improvements Made, but Control Weaknesses Remain*, GAO-01-1067 (Washington, D.C.: Sept. 12, 2001).

Contact and Acknowledgments

For information about this statement, please contact Linda Calbom, Director, Financial Management and Assurance, at (202) 512-9508, or Robert Owens, Assistant Director, at (202) 512-8579. You may also reach them by E-mail at calboml@gao.gov or owensr@gao.gov. Individuals who made key contributions to this testimony include Lisa Crye and Diane Morris. Numerous other individuals made contributions to the work supporting this testimony.