Statement of Lorraine Lewis
Inspector General
U.S. Department of Education

Before the

Task Force on Education
Committee on the Budget
U.S. House of Representatives

On

Financial Management at the Department of Education

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Good morning, Mr. Chairman and members of the Task Force. I appreciate the opportunity to present testimony to you today. I will address our work in identifying waste, fraud and abuse at the Department of Education. Specifically, I will discuss the recent guilty plea of a Bell Atlantic employee working under a service agreement with the Department of Education, Pell grant fraud and improper student loan forgiveness. I will also talk about the need for an environment with strong internal controls, which are necessary to maintain the integrity of our Education programs.

Inventory Control Case

We are conducting an investigation of individuals who, for approximately three years, made equipment purchases with federal funds for non-business related purposes, billed the Department for hours not worked, and received goods for personal use. At present, two individuals have pled guilty to their involvement in the case. The first, Joseph Dennis Morgan, pled guilty to one count of receiving stolen property. Mr. Morgan illegally received approximately $14,000 in electronic equipment since 1998. The second individual, Robert J. Sweeney, pled guilty to one count of conspiracy and one count of theft of government property. Much of the following information was reported by the U.S. Attorney's Office for the District of Columbia, as part of the plea agreement for Mr. Sweeney.

Mr. Sweeney was an employee of Bell Atlantic who had been assigned full-time to the Department to install telephone lines and telephones. Mr. Sweeney and a second Bell Atlantic technician reported to a Telecommunications Specialist in the Department's Office of the Chief Information Officer. Approximately three years ago, the Department's Telecommunications Specialist began asking Mr. Sweeney to order materials under the Bell Atlantic service agreement that were unrelated to official Department business. These items began with additional telephones and answering machines. Mr. Sweeney would deliver the items, which were paid for by the Department, to the Telecommunications Specialist, who would then distribute them to co-workers and family members for personal use.

Over time, the Telecommunications Specialist's requests escalated and began to include more expensive items. For example, a 61-inch television was ordered under the Bell Atlantic service agreement and delivered by Mr. Sweeney and another Department employee to the Telecommunications Specialist's son's house. Additionally, eight Gateway computers ordered from Bell Atlantic were picked up by Mr. Sweeney and delivered to the Telecommunications Specialist's house or to locations that she designated.

Overall, from 1997 through 1999, the Telecommunications Specialist requested numerous items from Bell Atlantic that were unrelated to the service agreement, including computers, printers, computer software, scanners, cordless telephones, a 61-inch television, Palm Pilots, walkie-talkies, compact disc players, and many other items. The total cost of these items to the Department was over $300,000.

Mr. Sweeney also performed numerous personal tasks for the Telecommunications Specialist. In exchange for Mr. Sweeney's assistance with the Telecommunications Specialist's personal requests, Mr. Sweeney was permitted to falsely claim overtime hours. For example, Mr. Sweeney was permitted to turn in time sheets while he was on vacation showing that he had worked his regular schedule as well as overtime hours. It is estimated that, between January 1, 1997 and November 30, 1999, approximately $634,000 in unworked hours was fraudulently charged to the Department by Mr. Sweeney and the other Bell Atlantic technician.

Our contractors, Ernst & Young, identified numerous Department internal control deficiencies in their "Report on Internal Control" for the fiscal year 1999 financial statement audit. A sound internal control environment provides management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition. The lack of a sound internal control environment heightens the risk that the Department will not be able to safeguard its assets and accurately record, process and summarize financial data.

Federal Pell Grant Program Fraud

OIG investigations and audits have disclosed patterns of fraud against the Pell grant program. The most common fraud scheme involved ineligible or non-existent applicants who falsified Free Applications for Federal Student Aid (FAFSAs) and other documents to obtain Pell grants for which they or their institutions were not entitled. For example:

- In October 1999, four New York men were sentenced for their roles in a Pell grant fraud scheme. The defendants were convicted on an indictment charging conspiracy, program fraud, false statements, wire fraud, mail fraud and tax fraud in connection with postsecondary programs that they falsely claimed to be administering. Judge Barbara Jones noted that the serious and sophisticated long-term fraud committed against the Department warranted substantial periods of incarceration and also ordered the men to make restitution of $11 million to the Department. Judge Jones stated that the $11 million loss to the Department's Pell grant program was a very conservative estimate since it related to losses associated with only one of the fraudulent educational programs administered by the defendants. The defendants were also charged with and convicted of defrauding the Small Business Administration and the "Section 8" rental subsidy program of the Department of Housing and Urban Development.

- On February 28, 2000, the Director of the Orange, California, branch campus of Travel and Trade Career Institute was sentenced to five months in jail, five months confinement in a community halfway house, $83,000 restitution, $50 special assessment, and three years supervised release. The Director conducted a scheme in which he drew down approximately $83,000 in federal Pell grants on behalf of students that did not exist. He used the money for his own personal gain and miscellaneous school expenses.

- On April 18, 2000, a federal Grand Jury in the Northern District of Illinois returned indictments against three former school officials of the now defunct American Career Training school in Chicago, Illinois. The three individuals were indicted on conspiracy and financial aid fraud for falsifying student eligibility documents that made ineligible students appear to be eligible to receive Pell grant funds during 1993 through 1996. They received in excess of $250,000 in Pell grant funds. The school officials created GED certificates, falsified Ability-to-Benefit test results, created Internal Revenue Service documents and created fraudulent letters from lenders and the U.S. Department of Education's Debt Collection Service.

- On April 26, 2000, the Director of the PSC School for Careers was arrested based upon allegations that she engaged in the submission of false claims for Pell grants and New York State Tuition Assistance Program grants. The criminal complaint alleges that the Director instructed school employees to create fictitious attendance records.

- On May 1, 2000, a former school owner, the school owner's daughter and a former instructor pled guilty to conspiring to steal and misapply more than $1.4 million in federal Pell grant funds. The funds were fraudulently obtained by forging and creating false documents and submitting fraudulent grant applications to the Department of Education for non-existent or non-eligible students. The three defendants used some of the funds for student operations and converted the rest to their own personal use, including the purchase of jewelry, real estate, furniture and an automobile.

- On July 15, 1998, a self-employed financial aid consultant was sentenced on one count of fraud against the Department, was ordered to serve 21 months in federal prison and then placed on two years of supervised release. He was also ordered to pay restitution in the amount of $5,000 plus an assessment of $50. The consultant offered a fee to assist parents and students with their applications for Title IV funds to attend postsecondary institutions. The investigation was initiated based on information from a confidential informant who alleged that the consultant falsified various federal financial aid documents, including tax returns, to assist parents and students in obtaining Title IV funds. A preliminary review of 1,200 seized customer files revealed that the consultant had approximately 700 parent/student files covering a period of five years. His account ledgers for 1995 reflected an income of $51,188 based on 228 separate customer entries. Included in the seized customer files were completed Free Applications for Federal Student Aid, Student Aid Reports, tax forms and fraudulent tax forms prepared in the name of the consultant's clients. A preliminary review of several files revealed that clients' incomes were lowered on numerous FAFSAs and tax forms. These alterations had the effect of increasing the students' chances of receiving federal financial aid. Another finding of the file review revealed that numerous student files reflected that some students were listed as orphans or wards of the court. This caused the students to be considered independent, which substantially increased their chance of receiving financial aid. The consultant usually charged a fee of 10% of a Pell grant, or approximately $230, for his services.

- On November 30, 1999, a student at Mid-State College was sentenced for her role in defrauding the Pell grant and Federal Family Education Loan programs. She was sentenced to six months incarceration to be followed by a 3-year period of supervised probation, ordered to make $6,062 in restitution to the Department and pay a $900 fine. The student made multiple false statements regarding her marital status and her husband's income on her Free Application for Federal Student Aid.

- On March 15, 2000, a student at Pacific Lutheran University was indicted for allegedly falsifying financial aid applications to receive Pell grants. She also allegedly falsified information on Social Security applications to receive Supplemental Security Income (SSI) benefits. Her scheme involved falsifying her marital status as "separated" to avoid having to report her spouse's income on the applications. Our investigation found evidence that she was living with her spouse during the entire period she received SSI benefits and student financial aid benefits. The total amount of fraud was $68,475.

To help combat one of these patterns of Pell grant fraud, the Higher Education Act (HEA) Amendments of 1998 (P.L. 105-244) included a provision authorizing the Department, in cooperation with the Treasury Department, to confirm with the Internal Revenue Service (IRS) key pieces of information on the federal income tax returns of applicants and their parents. Without specific authorization in the Internal Revenue Code, however, the IRS indicates that it must obtain written taxpayer consent before individual income information may be released to the Department. We recommend that the Congress enact any necessary additional legislation to address this matter.

In the interim, the Department just completed the first of two planned test-match studies with the IRS. The Department will use the statistical information from the test match to identify the types of students who are most likely to under-report their income. The Department also intends to use the IRS information to better evaluate the extent of income under-reporting and to support its desire to conduct a full-scale data match with the IRS.

<u>Improper Student Loan Forgiveness</u>

OIG audit and investigative work has also identified concerns with the discharge of loans due to disability or death. Since October 1999, OIG investigative work on fraudulent disability discharges resulted in more than $1,000,000 in loans being reinstated by the holders of the loans, which is either the Department or a guaranty agency. For example:

- On January 13, 2000, an individual was sentenced to six months home detention, five years probation and was ordered to pay $37,743 in restitution. The individual had submitted a fraudulent disability form to the Department of Education stating that he suffered from chronic paranoid schizophrenia and that he had a poor prognosis to be gainfully employed. As a result, he was relieved of his obligation to repay five student loans.

- On May 8, 2000, a doctor pled guilty to charges of student loan fraud and health care fraud. The next day, his brother, who is also a doctor, pled guilty to charges of misprision of the felonies of student loan fraud and health care fraud. Both doctors agreed to make restitution for the total amount obtained through their fraud schemes. The doctors mailed fraudulent total and permanent disability claims to several federal student loan guaranty agencies and lenders to have their medical student loan obligations discharged. One doctor had two student loans discharged, totaling $32,548, including $4,366 refunded directly to him. The other doctor had two student loans discharged totaling $11,992, including $4,098 refunded directly to him. A third loan discharge for the second doctor in the amount of approximately $15,000 was prevented as a result of this investigation. Our investigation revealed that the first brother submitted false disability claims stating that he and his brother were house confined and/or wheelchair-bound. However, OIG agents observed the brothers riding bicycles and swimming at a beach. Our investigation also revealed that the disability claims were certified by a non-existent physician and were often accompanied by letters from a non-existent attorney.

In our June 1999 audit entitled *Improving the Process for Forgiving Student Loans*, which was requested by the Department, we recommended that several steps be taken to enhance the current discharge determination procedures. These include revising the disability form to include, at a minimum, the doctor's professional license number and office telephone number, and requiring certified copies of death certificates. The Department modified its disability form to incorporate our recommendations and OMB approved the form. Also, the Department now requires that a death discharge be based only on an original or certified copy of the death certificate.

Our office continues to pursue this matter. In order to identify fraudulent death discharges, we conducted a data match with the Social Security Administration's Death Index to identify persons who received loan discharges based upon death, but who do not appear in the Social Security Death Index. Working with a sample of these data and with information filed by those who obtained substantial discharges from Sallie Mae and a number of guaranty agencies, our investigators are pursuing leads generated by the match. In the area of disability discharge fraud, we are working with the guaranty agencies to identify potential fraud cases and following up on leads developed from the data.

Internal Controls

A key factor in improving accountability and minimizing operational problems within the Department is the implementation of appropriate internal controls. Recently, the General Accounting Office (GAO) updated its standards for internal control in government. The standards provide a framework for establishing and maintaining internal control and for identifying and addressing management challenges and areas susceptible to fraud, waste and abuse. The GAO standards address the areas of control environment, risk assessment, control activities, communication and monitoring.

Currently, we are reviewing existing internal controls over the procurement of goods and services. Our review is based on the GAO standards. We are conducting interviews with procurement personnel and senior managers in each principal office within the Department and performing transaction testing to verify the Department's internal control procedures. To date, we have found internal control deficiencies in the Department's use of the government purchase card and third party checks. At the completion of our review, we will have delivered an individual report to each principal office and a report containing summary recommendations to the Department.

Conclusion

Ultimately, the design and implementation of any internal control must be based on an analysis of costs and benefits. Even well designed and implemented internal controls cannot provide absolute assurance against fraud, waste and abuse. There always will be factors such as human mistakes and acts of collusion that will be outside the control or influence of management. That is why we need to remain vigilant and maintain a credible deterrence through, among other things, a regular program of management reviews, an active hotline function, and vigorous audit and investigative operations.

This concludes my prepared testimony. I am happy to answer any questions you or other members of the Task Force may have on these issues.