CHAPTER 3

Requesting and Managing FSA Funds

Except for funds received as an administrative cost allowance (ACA), FSA program funds received by a school are held in trust by the school for students, the Department, and, in the case of FFEL program funds, for lenders and guaranty agencies. FSA program funds cannot be used as collateral or for any other purpose.

The cash management regulations establish rules and procedures that a school must follow in requesting and managing funds for the Pell Grant, FSEOG, Perkins Loan, FWS, Direct Loan, and FFEL programs. These rules and procedures also apply to third-party servicers.

DRAWING DOWN FSA FUNDS

Current Funding Level & GAPS

The Current Funding Level (CFL) is one of the mechanisms that ensure schools are reporting disbursements on a timely basis. A separate CFL is maintained for each program by award year. A school's program CFL is the amount of cash available for a school to draw down from GAPS or the amount that can be drawn down for a school. Schools operating under advance payment receive an initial CFL against which they can draw funds. Schools operating under reimbursement do not receive an initial CFL.

The Grants Administration and Payments System (GAPS) is a delivery system that supports program award and payment administration. Schools may use GAPS to request payments, adjust drawdowns, and report expenditures. It also provides continuous access to current grant and payment information, such as authorized amounts, cumulative drawdowns, current award balances, and payment histories. GAPS can be accessed through the Internet at the GAPS Web page

http://e-grants.ed.gov./egHome.asp

The GAPS Payee Hotline phone number is 1-888-336-8930.

CHAPTER 4 HIGHLIGHTS

- **Drawing down FSA funds**
  - schools use the Department's GAPS payment system
  - most schools use the Advance Payment or Just-in-Time payment methods
  - some schools with administrative deficiencies are placed on Reimbursement or Cash Monitoring
- **Maintaining & accounting for funds**
  - bank account notification requirements
  - rules for maintaining federal funds in separate or commingled accounts
  - rules for treatment of interest earned on federal funds
- **Excess cash**
  - allowable tolerances
- **Escheating prohibited**

Purpose of cash management regulations

- promote sound cash management of FSA program funds by schools
- minimize the costs to the government of making FSA program funds available to students and schools
- minimize the costs to students who receive FSA loans.

34 CFR Subpart K
Purpose 34 CFR 668.161

The advance payment method

Under the advance payment method, a school may submit a request for Pell Grant, Direct Loan, and campus-based program funds through GAPS at any time — prior to or after disbursing aid to eligible students and parents. If GAPS accepts a school's request for funds, it will make an electronic funds transfer (EFT) of the amount requested to a bank account designated by the school.

A school may not request more funds than it needs immediately for disbursements the school has made or will make to eligible students and parents. Therefore, a school must make the disbursements as soon as administratively feasible, but no later than three business days following the date the school receives those funds.

GAPS does not automatically accept a request for funds from a school under the advance payment method. For example, the Department may reject a request if the amount of the request exceeds the amount of funds the school is authorized to draw down.

Just-in-Time payment method

Under the Just-in-Time pilot project, a school submits a disbursement record (which is both a report of a disbursement and a request for funds) no earlier than seven days before the actual reported date of disbursement. For each disbursement the Department accepts, the appropriate amount of funds is deposited directly into the school's bank account.

Schools participating in the just-in-time pilot are exempt from the following regulatory requirements with respect to Federal Pell Grant funds:

- the 3-day-use rule discussed previously in Chapter 2 of this Volume,
- the recertification of student eligibility at the time of disbursement (a school may rely on its determination at the time it submits the disbursement record for Federal Pell Grant funds),
- the requirement that a school maintain Federal Pell Grant funds in an interest-bearing bank account (See the discussion under *Maintaining and accounting for funds.*), and
- the excess-cash rules (see the discussion under *Excess cash*).

For pilot participants, this regulatory relief does not extend to FSA programs other than the Pell Grant Program.

Reimbursement & cash monitoring payment methods

Under these methods the Department releases funds to the school *after* the school has made the disbursement to the student (or parent borrower). Since relatively few schools are required to use these methods, we'll discuss them separately (see boxed text).

Funding methods

Currently, there are four funding methods through which a school requests funds from the Department, they are

- the advance payment method,
- the just-in-time payment method,
- the reimbursement payment method; and
- the cash monitoring payment method.

The Department has sole discretion in determining the funding method and cash monitoring status under which FSA program funds are provided to a school.

34 CFR 668.162, except as noted

Advance requests for Perkins funds

Before requesting any funds from its Perkins FCC, a school should compare the total of the cash on hand in its Perkins account plus its expected collections, plus any expected interest and reimbursements against its anticipated disbursements.

Three-day rule

The institution must disburse the funds requested as soon as administratively feasible but no later than three business days following the date the institution received those funds.
34 CFR 668.162(b)(3)

Reimbursement funding method

Schools placed on the reimbursement payment method must disburse Pell Grant, Direct Loan, and campus-based program funds to eligible students and parents *before* the schools may request funds from the Department. Generally, the Department places a school on reimbursement if it determines that there is a need to monitor strictly the school's participation in the FSA programs. A school on reimbursement cannot request more cash than it actually disbursed to eligible students and parents. A school on reimbursement must

- identify the students and parents for whom it is seeking reimbursement; and
- submit documentation demonstrating that each student and parent included in the request was eligible to receive and has received the FSA program funds for which reimbursement is requested.

Before approving disbursements for a school on reimbursement, a FSA reimbursement analyst ensures that the school has accurately determined the FSA eligibility of each student, accurately determined the FSA payment to each student and parent included in its request, and submitted the required documentation.

Once a school's Pell disbursements are approved and accepted, the funds flow to GAPS. The FSA reimbursement analyst removes the block on the school's drawing down funds, requests a drawdown for the school, and then reestablishes the block. When Direct Loan disbursements are approved and accepted, direct cash payments are deposited in the school's bank account.

Limitations on the use of FFEL funds for schools on reimbursement

There are limitations on the use of FFEL funds that are comparable to those applicable in the reimbursement method. If a school is placed on reimbursement, or if a school that participates only in the FFEL program has most of the limitations of reimbursement placed on it, the school

- may not disburse FFEL program funds to a borrower until the Department approves a request from the school to disburse funds to that borrower, and
- if prohibited by the Department, may not certify a loan for a borrower until the Department approves a request from the school to make the certification for that borrower (this restriction becomes effective on the date that the Department notifies a school that it must obtain approval from the Department to certify loans).

The school must provide documentation demonstrating that each borrower included in the request is eligible to receive the disbursement or certification. The documentation must be provided to the Department or an entity approved by the Department for that purpose (for example, a certified public accountant, financial aid consultant, or guaranty agency).

Until the Department approves a request, the school may be

- prohibited from endorsing a master check or obtaining a borrower's endorsement of any loan check the school receives from a lender,
- required to maintain loan funds that it receives from a lender via EFT in a separate bank account, and
- prohibited from certifying a borrower's loan application.

Because the school's submission and the Department's review of documentation to support a borrower's eligibility take time, the school may delay returning FFEL Program funds provided by EFT or master check to a lender for a specified period of time.

Note: *This provision is applicable only in the FFEL programs, see* 34 CFR 668.167(c) & (d)

Cash monitoring payment method

The cash monitoring payment method is similar to the reimbursement payment method, but less onerous. Schools placed on Heightened Cash Monitoring (HCM) generally have to meet less demanding criteria before they can receive federal cash. As with the reimbursement payment method, under the cash monitoring payment method a school must make disbursements to eligible students and parents before it may request or receive funds for those disbursements from the Department. However, unlike the reimbursement payment method, where a school must provide detailed documentation for each student to whom it made a disbursement before the Department provides FSA program funds to the school, the Department provides funds to a school in one of two less restrictive ways:

1. At the beginning of an award year, a school on Heightened Cash Monitoring 1 (HCM1) will not have an initial CFL. Its CFL is created as the school reports and ED accepts actual disbursements in the COD system. The Department reimburses the school for those disbursements based on a modified and streamlined review and approval process under which a school may draw down cash through GAPS or have direct cash payments deposited in the school's bank account, based on actual disbursements to students reported to and accepted by the COD system. For example, under HCM1, the Department might simply require the school to identify students and their disbursement amounts and provide FSA program funds to the school based on that information alone.
2. Heightened Cash Monitoring 2 (HCM2) is more similar to the reimbursement payment method than is HCM1. Under HCM2, as under reimbursement, a school must submit some specific documentation before funds will be made available to it. However the Department may require less stringent documentation under HCM2 than under reimbursement.

   Under HCM2, once a school's disbursements have been approved, Case Management initiates a drawdown through GAPS on behalf of a school or direct cash payments to the school's bank account based on actual disbursements submitted to and accepted by the COD system.

A school that is placed on HCM is subject to the same disbursement and certification limitations on its participation in the FFEL/Direct program as a school on reimbursement. However, in keeping with the nature of cash monitoring, the Department may modify those provisions. In addition, the Department may tailor the documentation requirements for schools operating under HCM on a case-by-case basis.

MAINTAINING AND ACCOUNTING FOR FUNDS

All schools must maintain a bank account into which the GAPS transfers, or the school deposits, FSA program funds. The account must be federally insured or secured by collateral of value reasonably equivalent to the amount of FSA program funds in the account. A school generally is not required to maintain a separate account for each FSA program unless the Department so specifies. If as a result of a program review or other administrative action the Department imposes this requirement, we will notify the school in writing.

A school is not required to maintain a separate bank account for FFEL program funds that the school receives from a lender by EFT. A school must maintain and account for FFEL program funds in the same manner required for other FSA program funds.

Bank account notification requirements

For each account that contains FSA program funds, a school must identify that FSA program funds are maintained in the account by

- including the phrase *federal funds* in the name of the account, or
- notifying the bank or investment company of the accounts that contain FSA program funds and keeping a copy of this notice in its records *and*, except for public institutions, filing a Uniform Commercial Code Form (UCC-1) statement with the appropriate state or municipal government entity that discloses that an account contains federal funds.

The school must keep a copy of the UCC-1 statement in its records.

Maintaining FSA funds in a separate or commingled account

The Department may require a school to maintain FSA program funds in an account that contains only FSA program funds if the Department determines that the school failed to comply with cash management requirements, recordkeeping and reporting requirements, or other program regulations.

When a school doesn't maintain a separate federal bank account

A school has a fiduciary responsibility to segregate federal funds from all other funds and to ensure that federal funds are used only for the benefit of eligible students. Absent a separate bank account, the school must ensure that its accounting records clearly reflect that it segregates FSA funds. Under no circumstances may the school use federal funds for any other purpose, such as paying operating expenses, collateralizing or otherwise securing a loan, or earning interest or generating revenue in a manner that risks the loss of FSA funds or subjects FSA funds to liens or other attachments (such as would be the case with certain overnight investment arrangements or sweeps). Clearly, carrying out these fiduciary duties limits the ways the

Maintaining & accounting for funds
34 CFR 668.163

Not applicable to some programs
The cash management requirements are not applicable to the state grant and scholarship programs. The Special Leveraging Educational Assistance Partnership (SLEAP), the Leveraging Educational Assistance Partnership Program (LEAP— formerly the State Student Incentive Grant [SSIG] Program), the Robert C. Byrd Honors Scholarship (Byrd) Program, and the Gaining Early Awareness and Readiness for Undergraduate Programs (GEAR UP) are administered under rules established by the states.

Bank notification via UCC-1 form
The requirement that a school file a UCC-1 statement when an account's name does not include the phrase *federal funds* was established to reduce the possibility that a school could misrepresent federal funds as its own funds to obtain a loan or secure credit. Because public institutions generally do not seek to obtain credit in the same manner as private institutions, they are exempt from the requirement.

school can otherwise manage cash in an operating account, when that account contains FSA funds.

Accounting and financial requirements

If a school is not required to and chooses not to maintain a separate account for FSA program funds, its accounting and internal control systems must:

- identify the balance for each FSA program that is included in the school's bank or investment account as readily as if those funds were in a separate account; and
- identify earnings on FSA program funds in the school's bank or investment account.

A school must maintain its financial records in accordance with the recordkeeping requirements of 34 CFR 668.24 as described in *Volume 2 –School Eligibility and Operations).*

Timely return of funds when a school does not maintain a separate federal bank account

The Department considers a school that maintains FSA, HEA program funds and general operating funds in the same bank account (commingles) to satisfy the requirement that it return unearned funds on a timely basis if:

- the school maintains subsidiary ledgers for each type of funds commingled in that account that clearly show how and when those funds were used and reconciled to its general ledger,
- the subsidiary ledger for each FSA program provides a detailed audit trail on a student-by-student basis that reconciles to the amount of FSA program funds received and disbursed by the school, and
- the school updates the relevant subsidiary ledger accounts in its general ledger no later than 30 days after it determines that the student withdrew.

More specifically, the return of an unearned funds transaction should be recorded as a debit to a FSA program fund subsidiary ledger account and a credit to the school's operating fund subsidiary ledger account. The date of the return is the date this transaction is posted to the school's general ledger.

Interest-bearing or investment account

Direct Loan, Pell Grant, FSEOG, and FWS program funds must be maintained in an interest-bearing account or an investment account unless

- the school drew down less than $3 million of these funds in the prior award year and anticipates that it will not draw down more than $3 million in the current award year,

- the school can demonstrate that it would not earn over $250 in interest on the funds it will draw down during the award year, or
- the school requests these funds under the just-in-time Accounting and financial requirements.

An investment account must consist predominantly of low-risk income-producing securities. If a school chooses to maintain federal funds in an investment account, the school must maintain sufficient liquidity in that account to make required disbursements to students.

Any interest earned on Direct Loan, Pell Grant, FSEOG, and FWS program funds maintained in an interest-bearing account or an investment account that exceeds $250 per award year must be remitted to the Department by June 30 of that award year (see sidebar). A school may keep up to $250 per year of the interest or investment revenue earned (other than that earned on Perkins Loan funds) to pay for the administrative expense of maintaining the account.

A school must retain any interest earned on Perkins Loan funds as part of the Perkins Loan Fund. If a school maintains an account where Perkins funds are commingled with other FSA program funds, the interest earned on the Perkins funds must be identified, and those funds must be retained for use in the school's Perkins program.

Perkins Loan funds

A school that participates in the Perkins Loan Program must always maintain an interest-bearing account or an investment account for Perkins Loan funds. An investment account must consist predominantly of low-risk, income producing securities such as obligations issued or guaranteed by the U.S. Government. The school must maintain sufficient liquidity in its Perkins fund to make all required distributions.

If a school is also required to maintain an interest-bearing account or investment account for other federal funds, the school may use one account for Perkins Loan funds and all other federal funds. However, if the school chooses to maintain one account, it must determine the exact amount of any interest earned on the Perkins Loan funds and retain those funds for use in the Perkins program. The interest earned on the school's Perkins funds is not included in the $250 maximum award year interest the school is permitted to retain.

A school may deduct from the interest earned any bank or service charges incurred as a result of maintaining the fund assets in an interest-bearing account, and deposit only the net earnings.

Remitting Interest

The fastest, most efficient way to remit interest is through the GAPS web site at

http://e-grants.ed.gov/gapsweb/

A school with a user ID and password can go to the main menu and select **"Refunds"** then **"Interest**,"They will be taken to the screens through which they can send ED interest.

Schools can also return excess interest income to ED by check. The check should be sent to:

U.S. Department of Education
P.O. Box 952023
St. Louis, MO 63195-2023

The school should note on the check the school's DUNS number and Document Award Number, and it should also indicate that the remittance is for interest earned.

Excess cash
34 CFR 668.166

Period of peak enrollment
§668.166(b)(2) defines a *period of peak enrollment* as a period when at least 25% of the school's students start classes during a given 30-day period. A school identifies these periods of peak enrollment in advance, based on data from the prior award year:

$$\frac{\textit{Number of students who started classes in the comparable 30-day period in the prior award year}}{\textit{Total number of students who started classes during the entire prior award year}}$$

If a collection agency or third-party servicer receives funds directly from Perkins borrowers, it must immediately deposit those funds in an *institutional trust account.* The agency or servicer may open and maintain the account, but the funds in it belong to the institution. If the funds will be held for more than 45 days, the account must be interest bearing.

EXCESS CASH

As mentioned in the discussion of the advanced payment method, a school must disburse funds no later than three business days following the date the school receives them. *Excess cash* is any amount of program funds, other than funds received under the just-in-time payment method (see the discussion under the *Just-in-time payment method* earlier in this chapter), that a school does not disburse to students by the end of the third business day. Excess cash must be returned to the Department immediately.

Sometimes a school cannot disburse funds in the required 3 days because of circumstances outside the school's control. For example, a school may not have been able to disburse funds because of a change in a student's enrollment status, a student's failure to attend classes as scheduled, or a change in a student's award as a result of verification. In view of these circumstances, a school may maintain an excess cash balance for up to 7 additional days.

Allowable excess cash tolerances

During a period of *peak enrollment*, a school can maintain an excess cash balance that is less than 3% of the school's total prior-year drawdowns. The school is required to eliminate the excess cash balance within the next seven days by disbursing program funds to students for at least the amount of that excess cash balance.

For any period other than a period of peak enrollment, the school can maintain the excess cash balance if the excess cash balance is less than 1% of the school's prior-year drawdowns. In this case also, the school is required to eliminate the excess cash balance within the next seven days by disbursing program funds to students for at least the amount of that balance.

Consider a school that did not participate in the Direct Loan Program during the prior year. Such a school does not have prior-year drawdown data. To arrive at an amount to use for prior-year drawdowns, the school should use the total amount of loans guaranteed under the FFEL Program for students attending the school during the prior year.

The Department reviews schools to determine where excess cash balances have been improperly maintained. Upon a finding that a school has maintained an excess cash balance in excess of allowable tolerances, a school is required to reimburse the Department for the costs that the government incurred in making those excess funds available to the school.

Where excess cash balances are disproportionately large or where they represent a continuing problem with the school's ability to responsibly administer the FSA programs, the Department may initiate a proceeding to fine, limit, suspend, or terminate the school's participation in one or more of the FSA programs. For more on fines and other actions against schools, see *Volume 2 – School Eligibility and Operations*.

Generally, a check is *issued* when the school releases, distributes, or makes available the check by mailing the check to the student or parent, or by notifying the student or parent expeditiously that the check is available for immediate pickup. However, upon finding that a school has maintained excess cash balances, the Department considers the school to have issued a check on the date that check cleared the school's bank account, unless the school demonstrates to the satisfaction of the Department that it issued the check to the student shortly after the school wrote that check

PROHIBITION ON ESCHEATING OF FSA FUNDS

Because program funds are awarded to a student to pay current year charges, notwithstanding any authorization obtained by a school from a student or parent, the school must pay any

- remaining balance from loan funds by the end of the loan period, and
- other remaining program funds by the end of the last payment period in the award year for which they were awarded.

A school that has failed to disburse the funds by those dates is in violation of the Department's cash management regulations. If a school pays credit balances by check, and if a school cannot locate a student to whom an FSA credit balance must be paid (i.e., the school has exhausted all possible avenues to find the student), the school must exercise its fiduciary responsibility to the student and the Title IV programs, and return the credit balance to the programs.

A school has a fiduciary responsibility to

- safeguard FSA funds,
- ensure FSA funds are used only for the purposes intended,
- act on the student's behalf to repay a student's FSA education loan debt when the school is unable to pay a credit balance directly to the student, and
- return to the Department any FSA funds that cannot be used as intended.

***NEW* Example of a policy to prevent escheating**

Typically, each state establishes the useful life of a check or bank draft used to disburse FSA program funds. After this established date, the check cannot be negotiated and the proceeds of an uncashed check normally escheat to an unintended third-party (the state or the institution).

In state A, a bank check has a useful life of 180 days. In order to prevent FSA funds from escheating to a third-party, the Business Office at School A, at the end of each month, identifies all outstanding uncashed checks containing FSA funds. Prior to the 180th day, the Business Office voids the uncashed checks and restores the funds back to the applicable FSA program.

A school must have in place a procedure to ensure that funds do not go to an unintended third-party. Moreover, a school must have a process through which it identifies a credit balance that remains on a student's account or is undelivered to the student (or parent, if applicable) and returns those funds to the FSA programs on behalf of the student. The search for the student should end and the refund/return to the Department should be completed prior to the date the funds would otherwise escheat, but no later than a few days after a check to the student would cease to be negotiable (usually 180 days).

Under this process, *FSA funds would never escheat to a state, or revert to the school, or any other third party*. A failure to have such a process in place would call into question a school's administrative capability, its fiscal responsibility, and its system of internal controls required under the Department's regulations. credit balances to escheat.