



UNITED STATES DEPARTMENT OF EDUCATION  
OFFICE OF INSPECTOR GENERAL



March 2000

Dear Colleague:

This letter transmits the U.S. Department of Education's (ED) Audit Guide, *Audits of Guaranty Agency Servicers Participating in the Federal Family Education Loan (FFEL) Program*.

Section 682.416(e) of Title 34 of the Code of Federal Regulations (CFR) requires annual compliance audits of servicers that contract with eligible guaranty agencies to administer or service any aspect of the Student Financial Assistance programs. However, an exemption applies to this compliance audit requirement if the servicer contracts with only one guaranty agency *and* the audit of that Guaranty agency's FFEL Program includes every aspect of the servicer's administration of the FFEL Program.

Section 668.23(d)(5) of Title 34 of the CFR also requires servicers to annually submit audited financial statements. The financial statements must be prepared on an accrual basis in accordance with generally accepted accounting principles. For servicers that are not nonprofit or governmental organizations, all financial statement and compliance audits conducted to satisfy the annual audit requirements must be performed in accordance with this Guide. Guaranty agency servicers that are nonprofit or governmental organizations are subject to the audit requirements of Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* instead.

Application of this Guide is effective for fiscal years ending June 30, 2000, and thereafter. Earlier application of the Guide is encouraged. This Guide is available on the Internet at this URL: <http://home.gvi.net/~edoig>. Questions pertaining to the Guide should be faxed to the Office of Inspector General at (215) 656-8628. We hope this guide will assist you in fulfilling your responsibilities for completing and submitting the required audit.

Sincerely,

Lorraine Lewis  
Inspector General

# *AUDIT GUIDE*

## *AUDITS OF GUARANTY AGENCY SERVICERS PARTICIPATING IN THE FEDERAL FAMILY EDUCATION LOAN PROGRAM*



*U.S. DEPARTMENT OF EDUCATION  
OFFICE OF INSPECTOR GENERAL*

*March 2000*

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## ***ACRONYMS AND TERMS***

<u>Acronym/Term</u>	<u>Name/Meaning</u>
AICPA	American Institute of Certified Public Accountants
AT	Attestation Standards
AU	Auditing Standards issued by the American Institute of CPAs
CAP	Corrective Action Plan
CFR	Code of Federal Regulations
COSO	Committee of Sponsoring Organizations of the Treadway Commission
DCL	Dear Colleague Letter
ED	U. S. Department of Education
EDOIG	U. S. Department of Education, Office of Inspector General
FFEL	Federal Family Education Loan
FOIA	Freedom of Information Act
GAO	General Accounting Office
GAAS	Generally Accepted Auditing Standards
GAS	Government Auditing Standards
GAAP	Generally Accepted Accounting Principles
HEA	Higher Education Act of 1965, as amended
IPA	Independent Public Accountant
NSLDS	National Student Loan Data System
OIG	Office of Inspector General
OMB	Office of Management and Budget
PDL	Program Determination Letter
RIGA	Regional Inspector General for Audit
SAS	Statement on Auditing Standards
Servicer	Third-Party Servicer
SFA	Student Financial Assistance
SLS	Supplemental Loans for Students
SPA	Supplemental Preclaims Assistance
SSAE	Statement on Standards for Attestation Engagements
SSCR	Student Status Confirmation Report

## SECTION I

### AUDIT PLANNING AND OTHER CONSIDERATIONS

#### BACKGROUND

Guaranty agencies frequently hire servicers to administer Federal Family Education Loan (FFEL) Program functions. The FFEL Program (formerly the Guaranteed Student Loan Program) includes the Federal Stafford Loan Program, both subsidized and unsubsidized, the Federal Supplemental Loans for Students (SLS) Program, the Federal PLUS Program, and the Federal Consolidation Loan Program.

Section 668.23(d)(5) of Title 34 of the Code of Federal Regulations (CFR) requires servicers to annually submit audited financial statements. The financial statements must be prepared on an accrual basis in accordance with generally accepted accounting principles (GAAP). Section 682.416(e) of Title 34 of the CFR also requires annual compliance audits of servicers that contract with eligible guaranty agencies to administer or service any aspect of the FFEL program. The audit must examine the servicer's compliance with the Act and applicable regulations and examine the servicer's financial management of its FFEL program activities. The compliance audit is required unless the servicer contracts with only one guaranty agency, **and** the audit of that guaranty agency's FFEL Program involves every aspect of the servicer's administration of the FFEL Program. To satisfy the compliance audit requirement, this Guide requires an examination-level attestation engagement relating to the servicer management's assertions about certain compliance aspects related to the FFEL program.

The Guide incorporates Statements on Standards for Attestation Engagements (SSAE) #9 issued in April 1999 which amended SSAE's #1, #2 and #3. As a result, this guide provides for the practitioner to obtain management's assertions within a representation letter and to opine on the servicer's compliance with specified requirements, not on management's assertions about compliance. However, SSAE #9 permits opinions on management's assertions on compliance, if such assertions are provided by management in a separate report attached to the auditor's report. Such will be accepted providing the auditor's report meets all requirements in accordance with paragraph 54 of SSAE #3, as amended by SSAE #9. SSAE #3 as amended by SSAE #9 is codified in the Statements on Standards for Attestation Engagements (SSAE) Attestation Standards (AT section 500).

The audits must be performed by a qualified, independent auditor in accordance with the *Government Auditing Standards (GAS)*, issued by the Comptroller General of the United States. Also, the Statements on Standards for Attestation Engagements (SSAEs), as amended by SSAE #9, issued by the American Institute of Certified Public Accountants (AICPA) apply to the compliance attestation engagement.

## **PURPOSE OF GUIDE**

This Guide is to assist IPA's in performing required financial statement and compliance audits of servicers responsible for administering or servicing any aspect of the FFEL Program on behalf of their guaranty agency clients. This Guide will also assist servicer management in preparing written assertions about the entity's compliance with the specified FFEL Program requirements. This Guide is effective for financial and compliance audits (attestation engagements) for fiscal years ending on or after June 30, 2000. Earlier application of the Guide is encouraged.

This Guide is to be used by all servicers (except for servicers exempted as described in the background section). However, servicers that are either a State, local, or nonprofit organization are subject to the audit requirements of Office of Management and Budget (OMB) Circular A-133 in lieu of the requirements set forth in this Guide. *[Note: This Guide must be used if a program specific audit is being performed to satisfy the A-133 audit requirements. Also, organizations that are subject to OMB Circular A-133 requirements but are below the funding threshold for required audits (currently \$300,000 per fiscal year) are exempt from the audit requirements of this Guide. However, these organizations may be asked to submit to ED copies of any financial statement or compliance audits that are otherwise prepared for the organization.]*

### **Audit/Attestation Objectives**

The audit/attestation objectives are to:

1. Determine and report whether:
  - ▶ The servicer's basic financial statements are fairly presented, in all material respects, in accordance with generally accepted accounting principles [GAAP];
  - ▶ The servicer maintained effective internal control and complied with laws, regulations, and the provisions of contracts or grant agreements which could have a direct and material effect on the financial statements; and
  - ▶ The servicer maintained internal control and complied, in all material respects, with specified compliance requirements in Section II of this Guide (ED Forms 1189 and 1130; Federal reinsurance; death, disability and bankruptcy claims; default aversion; collections; Federal share of borrower payments; assignment of defaulted loans to ED; collection charges; enforcement action).
2. Assist the U.S. Department of Education (ED) in meeting its stewardship responsibilities by ED's acting upon noncompliance and internal control weaknesses noted in the independent public accountant's (IPA's) reports. If applicable, the IPA's audit report findings must contain adequate information to give reported matters perspective and to allow ED to take necessary corrective action (See Example F).

### **Layout of the Guide**



This Guide is divided into three sections:

- Section I** Provides general information about engagement planning and other considerations.
- Section II** Identifies the compliance requirements and management's assertions that must be reported on by the IPA.
- Section III** Provides the reporting requirements and illustrative reports.

This Guide is not intended to be a complete manual of procedures, nor is it intended to supplant the IPA's judgment of the work required. Suggested procedures described may not cover all circumstances or conditions encountered at a particular servicer. The IPA should use professional judgment and due care to tailor the procedures so that the financial statement audit and compliance attestation engagement objectives are achieved. However, all applicable management assertions contained in this Guide must be addressed by the IPA. The IPA may wish to contact the Non-Federal Audits Advisory and Assistance Team (See Appendix A) for technical assistance related to performing the engagement required by this guide.

### **ENGAGEMENT PERIOD AND REPORT DUE DATES**

The audit is based on the servicer's fiscal year for:

- ▶ The servicer's basic GAAP financial statements, in accordance with *GAS* and generally accepted auditing standards (GAAS); and
- ▶ Compliance by examining and reporting on the servicer's compliance with specified FFEL laws and regulations, in accordance with SSAEs and *GAS*.

Servicers may engage different IPAs to perform the audit of the financial statements and the compliance attestation engagement. However, the financial statement audit and the compliance audit must be for the same fiscal year and must be submitted by the servicer to ED as one reporting package.

Audits must be submitted to ED within six months of the end of the servicer's fiscal year or, if applicable, in accordance with the deadlines established in the Single Audit Act, and OMB Circular A-133.

A servicer's failure to meet report due dates may result in administrative sanctions described in 34 CFR 668, Subpart G.

### **MANAGEMENT RESPONSIBILITIES**

Among other management responsibilities discussed in this Guide, management is responsible for the following:

- a. Preparing the required financial statements in accordance with GAAP (The financial statements must reflect the servicer's financial position, results of operations, and, where appropriate, cash flows for the fiscal year audited. The financial statements must be for the same organizational unit and fiscal year that is required to meet the audit requirements identified in this section and must include notes that describe the significant accounting policies used in preparing the statements.);
- b. Identifying the applicable laws and regulations and compliance requirements;
- c. Complying with laws, regulations, and provisions of contracts or grant agreements;
- d. Establishing and maintaining effective internal control over compliance related to its administration of the FFEL Program on behalf of its guaranty agency clients;
- e. Evaluating and monitoring compliance and the effectiveness of internal control over compliance;
- f. Ensuring that the required audits are properly performed and submitted when due;
- g. Providing the practitioner with assertion(s) about the servicer's compliance with the specified compliance requirements and the effectiveness of the servicer's internal control structure over compliance <sup>1</sup>;
- h. Providing the practitioner with their written representations about all other matters in SSAE No. 3, as amended by paragraph 67 of SSAE No. 9 ;
- i. Preparing a summary schedule of prior audit findings and a corrective action plan in accordance with this Guide; and
- j. Following up and taking corrective action on audit findings (see Corrective Action Plan below).

## **Corrective Action Plan**

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<sup>1</sup> Management's refusal to provide the practitioner with the required compliance and internal control assertions related to the compliance audit may subject the entity to administrative actions by ED.

To assist ED in resolving instances of reported noncompliance, reportable conditions, and material weaknesses in the internal control identified by the IPA, ED requires a Servicer to develop a corrective action plan (CAP) as part of its audit report package. The CAP is considered an essential part of the audit report package. The CAP must be prepared by the Servicer on the Servicer's letterhead, and include the name, title, and telephone number of the Servicer official responsible for its preparation.

The CAP must describe the corrective action taken or planned in response to findings identified by the IPA. In addition, the Servicer must comment on the status of corrective action taken on prior findings. Additional guidance for the CAP is provided in Example H.

*Audit report packages submitted without an applicable CAP are incomplete and will be returned to the servicer.*

### **IRREGULARITIES OR ILLEGAL ACTS**

This Guide requires practitioners to design and perform procedures to provide reasonable assurance of detecting significant illegal acts and to report directly to the ED Office of Inspector General (EDOIG) any fraudulent act or indication of such acts. In addition, SSAE #3, as amended by SSAE # 9, paragraph 28 says that an examination-level engagement includes “designing the examination to detect both intentional and unintentional noncompliance that is material to management’s assertion.” Accordingly, practitioners should be aware of fraud or high risk areas and recognize basic weaknesses in internal control.

As described in Paragraph 4.16 of GAS, if the practitioner becomes aware of fraud or indications of fraud, the practitioner should exercise due professional care in pursuing indications of possible fraud and illegal acts so as not to interfere with potential future investigations, legal proceedings, or both. Under some circumstances, laws, regulations, or policies may require practitioners to report indications of certain types of fraud or illegal acts to law enforcement or investigatory authorities before extending audit steps and procedures. Practitioners may also be required to withdraw from or defer further work on the audit or a portion of the audit in order not to interfere with an investigation.

Upon discovery of a fraudulent act or indication of such an act related to Title IV Federal programs, regardless of dollar value, this Guide requires the practitioner to immediately contact the ED Office of Inspector General, Investigation Services (EDOIG/IS), by phone or fax at the numbers shown below before extending audit steps and procedures (GAS 4.16). In addition, the practitioner must promptly prepare a separate written report concerning fraudulent acts or indications of such acts and include all information described in Section V on reporting findings. This report should be submitted to the EDOIG/IS, within 30 days after the date of discovery of the act or within the time frame agreed to by the practitioner and the EDOIG/IS. The report should be submitted to EDOIG/IS at the following address:

U.S. Department of Education  
Assistant Inspector General for Investigations  
400 Maryland Avenue, SW

MES, Room 4122  
Washington, DC 20202-1510  
Phone: 202-205-8762  
Fax: 202-205-9449

Failure to notify the ED Office of Inspector General, Investigative Services, of fraud could subject the IPA to sanctions. For supplemental guidance, see Chapters 4 and 5 of *GAS*. In addition, practitioners may wish to consult SAS No. 82, *Consideration of Fraud in a Financial Statement Audit*, and SAS No. 54, *Illegal Acts by Clients* (AICPA, *Professional Standards*, AU Sections 316 and 317, respectively).

### **DUE CARE AND PROFESSIONAL SKEPTICISM**

Paragraph 3.26 of *GAS* states that due professional care should be used in conducting the audit and in preparing related reports. SSAE #3, as amended by SSAE #9, paragraph 35 requires that the practitioner:

“exercise (a) due care in planning, performing, and evaluating the results of his or her examination procedures and (b) the proper degree of professional skepticism to achieve reasonable assurance that material noncompliance will be detected.”

Practitioners are cautioned against ignoring basic weaknesses in internal control, performing audit steps mechanically (auditing form over substance), and accepting explanations for audit exceptions without competent evidence.

### **AUDITOR QUALIFICATIONS**

IPAs must meet the qualification and independence standards specified in *GAS*, including continuing education and peer review requirements. Internal auditors of a servicer are not independent while auditing within it. However, IPAs may consider the work of the internal auditors in performing the financial statement audit and the examination-level compliance attestation engagement. IPAs should apply the concepts and guidance in SAS No. 65, *The Auditor's Consideration of the Internal Audit Function in an Audit of Financial Statements* (AICPA, *Professional Standards*, vol. 1, AU sec. 322) when addressing the competence and objectivity of internal auditors; the nature, timing, and extent of work to be performed; and other related matters.

*Government Auditing Standards* require IPAs and audit firms to comply with applicable provisions of the public accountancy law and rules of the jurisdiction in which they are licensed and where the engagement is being conducted. If the servicer is located in a state outside of the home state of the IPA, and the IPA performs substantial field work in the servicer's state, the IPA should document his/her compliance with the licensing requirements of the public accountancy laws of that state. This Guide does not impose additional licensing requirements beyond those established by the individual State Boards of Accountancy.

### **GENERAL PLANNING CONSIDERATIONS**

## Engagement Letter

An engagement letter between the servicer and the IPA shall be prepared and must include the following:

- ▶ A statement that the engagement (financial statement and compliance attestation) is to be performed in accordance with *Government Auditing Standards*, and for the compliance engagement, the AICPA's Statement on Standards for Attestation Engagements (SSAE) No. 3 as amended by SSAE No. 9;
- ▶ A description of the scope of the engagement and the related reporting that will meet the requirements of this guide;
- ▶ A statement that both parties understand that ED intends to use the IPA's report to help carry out its oversight responsibilities of the Title IV programs; and
- ▶ A provision that the IPA is required to provide ED, the Inspector General and their representatives access to working papers (including making photocopies, as necessary). [IPAs should refer to AU Section 9339, "Interpretations of AU Section 339 'Working Papers,'" of the AICPA Professional Standards for guidance.]

Although not a mandatory requirement, this Guide suggests that practitioners also include a statement in the engagement letter that describes the practitioner's responsibility to communicate and report fraudulent acts or indications of such acts directly to the ED Office of Inspector General.

## Follow-up on Prior Audit Findings

This Guide requires practitioners to:

- ▶ follow-up on reported findings and recommendations from previous audits and reviews to determine whether timely and appropriate corrective action has been taken; and
- ▶ report the status of uncorrected reported findings and recommendations.

The IPA should review prior findings, including findings from the previous IPA audit, and recent ED OIG audits, ED and guaranty agency audits or program reviews, including the resolution of those findings. In many cases the procedures performed in the current audit will provide a basis for the IPA to evaluate prior findings. If prior findings have all been corrected, make a statement to that effect. An illustrative report for providing auditor's comments on resolution matters is shown in Example G of this Guide.

## Working Papers

For both the financial statement audit and the compliance audit, practitioners should follow the guidance in paragraphs 4.34 through 4.38 of *Government Auditing Standards (GAS)*, which address working papers. In addition to retaining a record of the work performed in the form of working

papers, paragraph 4.35 of GAS states further that the practitioner's working papers should "contain sufficient information to enable an experienced auditor having no previous connection with the audit to ascertain from them the evidence that supports the auditor's significant conclusions and judgments". The working papers should contain:

- ▶ the objectives, scope, and methodology, including any sampling criteria used;
- ▶ documentation of the work performed to support significant conclusions and judgments; and
- ▶ evidence of supervisory review.

In addition, for the compliance audit, paragraph 71 of SSAE No. 1, *Attestation Standards* (AICPA, *Professional Standards*, AT sec. 100.78) says that working papers "...ordinarily should indicate that (a) the work was adequately planned and supervised and that (b) evidential matter was obtained to provide a reasonable basis for the conclusion or conclusions expressed in the practitioner's report."

Servicers or practitioners who deem any of the working paper information to be "confidential commercial information" should take appropriate steps to so designate that information. Such designation may protect its confidentiality if, in the future, a request is made for disclosure of this information under the Freedom of Information Act (FOIA). "Confidential commercial information" means records that may contain material protected from release under Exemption 4 of the FOIA (pertaining to trade secrets and commercial or financial information that is privileged or confidential) because disclosure could reasonably be expected to cause substantial competitive harm.

ED OIG has implemented procedures for evaluating audits performed by non-Federal auditors. As part of this evaluation, the IPA must make the supporting audit working papers available to ED OIG upon request in accordance with 34 CFR 668.23(e). To facilitate these requests, the management's reporting package should include an information sheet (Example E) identifying the name, address, and telephone number of the partner on the engagement. Working paper reviews will normally take place at the practitioner's office. If the working papers are requested, the IPA should consider the guidance in AU Section 9339.1, *Providing Access to or Photocopies of Working Papers to a Regulator*.

Whenever an evaluation of a report or working papers discloses inadequacies, the practitioner may be asked to take corrective action. Certain State Boards of Accountancy have requested that the ED OIG send them copies of correspondence detailing deficiencies noted during its reviews. This includes the licensee's home state and the state(s) where the engagement was conducted, if different. This is for information only and is not a referral for disciplinary action at this time. However, if ED OIG determines that the report and working papers contain repetitive substandard performance or significant inadequacies, referral to the AICPA and the cognizant State Board of Accountancy will be considered. In this instance, ED OIG may also initiate action to suspend and debar the practitioner from performing governmental audit work.

### **AUDIT SUBMISSION/REPORTING PACKAGE**

The servicer must transmit two copies of the audit report package and a corrective action plan to:

U.S. Department of Education  
SFA/Financial Analysis and Oversight  
400 Maryland Avenue, S.W.  
ROB-3  
Room 4616, Mail Stop #5138  
Washington, D.C. 20202-5138  
202-401-2280

## Financial Statement Reporting

A servicer's financial statement portion of the audit report package must include the following:

1. A Report on the Audit of the Basic Financial Statements (Example A-1); **AND**
2. A Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards* [No Reportable Instances of Noncompliance and No Material Weaknesses, No Reportable Conditions Identified] (Example A-2); **OR**
3. A Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards* [Reportable Instances of Noncompliance and Reportable Conditions Identified] (Example A-3).

## Compliance Attestation Reporting

The compliance report, or the compliance report section if a single combination financial and compliance audit report package is issued, must start with a page that clearly identifies the servicer's name and address, and period examined. The reporting package must include the following:

1. Report Cover Page (Example B)
2. A Report on Compliance with Specified Requirements Applicable to the FFEL Program (Example C);
3. A Report on Internal Control Over Compliance in accordance with SSAE #3, as amended by SSAE #9, paragraph 44 (No Reportable Conditions) (Example D-1); **OR**  
  
A Report on Internal Control Over Compliance in accordance with SSAE #3, as amended by SSAE #9, paragraph 44 (Reportable Conditions Identified [No Material Weaknesses]) (Example D-2);
4. Information Sheet (Example E);
5. Schedule of Findings and Questioned Costs (Example F);

6. Auditor's comments on resolution matters relating to the FFEL Program (Example G);
7. Corrective Action Plan (Example H); and
8. A separate report on illegal acts that could result in criminal prosecution if one was submitted in accordance with the instructions set forth earlier in this Guide.<sup>2</sup>

## **AUDIT OF FINANCIAL STATEMENTS**

The audit of the servicer's basic GAAP financial statements must be performed in accordance with AS and generally accepted auditing standards (GAAS).

### **Consideration of Internal Control**

Guidance on the IPA's consideration of internal control in the financial statement audit is provided in GAS and SAS No. 78, *Consideration of Internal Control in a Financial Statement Audit*. The IPA's responsibility to communicate reportable conditions and material weaknesses in internal control noted in the financial statement audit are described in SAS No. 60, *Communication of*

*Internal Control Related Matters Noted in an Audit* and GAS and SAS No. 87, *Restricting the Use of an Auditor's Report*.

Management is responsible for establishing and maintaining internal control. Audit standards require practitioners to obtain a sufficient understanding of the servicer's internal control to plan the audit. This includes obtaining an understanding of internal control relevant to the financial statement assertions affected by laws and regulations.

Practitioners should follow the internal control guidance contained in paragraphs 4.22 through 4.33 of GAS concerning the control environment, safeguarding controls, controls over compliance with laws and regulations, and control risk assessments when performing the financial statement audits as these aspects of internal control are important to the judgments practitioners make about audit risk and about evidence needed to support their opinion on the financial statements.

In addition to obtaining an understanding of the servicer's internal control, practitioners engaged to examine a servicer management's financial statements are required to assess control risk. This Guide requires that practitioners assess control risk by financial statement assertion(s) for each financial statement line item.

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<sup>2</sup> The practitioner should discuss with the ED/OIG/IS whether or not the report should be provided to the auditee in order not to interfere with potential future investigations, legal proceedings, or both.



Practitioners should report deficiencies in internal control that they consider to be “reportable conditions.” Reportable conditions involve matters relating to significant deficiencies in the design or operation of internal control that could adversely affect the servicer’s ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. A material weakness is a reportable condition in which the design or operation of internal control does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited could occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Management and practitioners should be aware that the reporting criteria and required accompanying report on internal control required for the financial statement audit is not the same as or a substitute for the reporting criteria and accompanying report on internal control for the compliance audit required in this Guide.

### **Materiality**

Paragraph 4.8 of *Government Auditing Standards* states that materiality in a financial statement audit is a matter of professional judgment and is influenced by the practitioner’s perception of the “needs of a reasonable person who will rely on the financial statements.” ED intends to rely on the financial data and reports submitted by servicers to help meet its stewardship responsibilities in overseeing the FFEL Program. Because of this, practitioners are permitted but not required to set lower materiality levels when performing the examination of the servicer’s financial statements.

### **Compliance with Laws and Regulations**

Paragraph 4.15 of *GAS* states that practitioners are required to “obtain an understanding of the possible effects on financial statements of laws and regulations that are generally recognized by auditors to have a direct and material effect on the determination of amounts in the financial statements.”

The requirements identified in Section II of this Guide may not cover all the laws and regulations with which noncompliance could have a direct and material effect on the financial statement amounts. Practitioners, therefore, may have to use the work of legal counsel in determining which laws and regulations, in addition to those noted in this Guide, must be considered for the financial statement audit. The practitioner should define what would be considered material in the request to legal counsel. The determination of which laws and regulations may have a direct and material effect on financial statement amounts should be properly documented in the audit working papers.

### **Management and Legal Counsel Representation Letters**

The IPA is required to obtain management's and legal counsel's written representations as part of the financial statement audit. Management's written representations must also be obtained for matters concerning compliance with FFEL Program laws and regulations that have a direct and material effect on the financial statement amounts. Additional guidance is provided in SAS No. 85, *Management*

*Representations and SAS No. 12, Inquiry of a Client's Lawyer Concerning Litigation, Claims, and Assessments.*

## **COMPLIANCE ATTESTATION ENGAGEMENT**

The compliance attestation engagement must be performed as an examination-level engagement in accordance with SSAEs and GAS. Management's written assertions are the basis for the IPA's testing and therefore are an integral part of the engagement. The servicer management should determine whether the entity performs the functions addressed in Section II and whether it can make all or part of the required management assertions. If a servicer does not perform for any of its guaranty agency clients, the functions addressed by a single assertion, that assertion may be modified but must clearly identify the responsibilities of the servicer so that the servicer management's written assertions address only the functions the servicer performs. Otherwise, management is to provide all written assertions and representations required by the Guide.

SSAE #1, as amended by SSAE #9, paragraph 1 defines an attest engagement as:

“...one in which a practitioner is engaged to issue or does issue a written communication that expresses a conclusion about the reliability of a written assertion that is the responsibility of another party.”

Furthermore, SSAE #9, paragraph 10 states:

“Performing attest services is different from preparing and presenting an assertion. The latter involves collecting, classifying, summarizing, and communicating information; this usually entails reducing a mass of detailed data to a manageable and understandable form. On the other hand, performing attest services involves gathering evidence to support the assertion and objectively assessing the measurements and communications of the asserter. Thus, attest services are analytical, critical, investigative, and concerned with the basis and support for the assertion.”

SSAE No. 3, as amended by SSAE No. 9, paragraph 9c, states, in part, a practitioner may perform an examination engagement if management makes written assertions about the entity's compliance with the specified requirements. Management's written assertions are the basis for the practitioner's testing and, therefore, are an integral part of the engagement. The nature of the written assertions made by the servicer management (and, thus, the scope of the practitioner's engagement) may vary depending on the extent to which the servicer performs certain compliance functions on behalf of their guaranty agency clients. Because servicers are not required to make such specific written assertions to ED, such assertions should be obtained from management in a representation letter to the practitioner.

In addition to the specific assertions identified in the Guide, as applicable, management must also provide in the letter, written representations about the matters in SSAE No. 3, as amended by SSAE No. 9, paragraph 67. If management omits any of the required assertions (except for assertions

relating to functions not performed by the servicer) or representations, the practitioner should consider the guidance in SSAE No. 3, as amended by SSAE No. 9, paragraphs 57 and 68 about restrictions on the scope of the engagement.

### **Contracting With More Than One Guaranty Agency**

Some servicers perform different services for different guaranty agencies. This Guide provides for a servicer with more than one guaranty agency client to submit a single, organization-wide report that covers the compliance functions addressed in Section II for each guaranty agency. Servicers should complete Example E, including the associated matrix, identifying their guaranty agency clients and the compliance functions performed for each.

### **Inherent Risk**

SSAE No. 3, as amended by SSAE No. 9, paragraph 30, requires that, in assessing inherent risk, the practitioner “should consider factors relevant to compliance engagements, such as. . . prior experience with the entity’s compliance [and] the potential impact of noncompliance.” In addition, SSAE No. 3, as amended by SSAE No. 9, paragraph 46, states:

“For engagements involving compliance with regulatory requirements, the practitioner’s procedures should include reviewing reports of significant examinations and related communications between regulatory agencies and the entity and, when appropriate, making inquiries of the regulatory agencies, including inquiries about examinations in progress.”

Accordingly, this Guide requires the practitioner to consider reported noncompliance identified in prior audits, guaranty agency reviews, and ED program reviews related to the FFEL Program. (See also the “Audit *Follow-Up*” in previous section of Guide.)

### **Consideration of Internal Control Over Compliance**

Overall guidance for the consideration of internal control in an examination-level attestation engagement is provided in GAS and in SSAE #3, as amended by SSAE #9, paragraphs 42 through 44. Paragraph 42 states that the IPA should obtain an understanding of relevant portions of internal control over compliance sufficient to plan the examination engagement and to assess control risk for compliance with the specified requirements (that is, compliance requirements specified in Section II and Section IV). **IPAs must document their understanding (may include flowcharts, narrative, or other means) and their assessment of control risk.** Section II of this Guide include footnotes for the suggested audit procedures that have related internal control and risk assessment documentation requirements.

During an examination-level attestation engagement, the IPA may become aware of reportable conditions or material weaknesses in the servicer’s internal control over compliance. A reportable condition is a significant deficiency in the design or operation of internal control over compliance that could adversely affect the servicer’s ability to comply with the specified requirements. A material

weakness is a reportable condition in which the design or operation of internal control does not reduce to a relatively low level the risk that noncompliance with one or more of the specified requirements could occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. The IPA's responsibility to communicate these deficiencies in an examination of management's assertion is similar to the IPA's responsibility described in SAS No. 60 (AU sec. 325). However, this Guide requires all communications of reportable conditions and material weaknesses in internal control over compliance to be in writing and requires the IPA to include a copy of such report(s) in the IPA's reporting package (See Example D). **The IPAs considerations on materiality should be properly documented in the audit working papers.**

### **Materiality**

SSAE #3, as amended by SSAE #9, paragraphs 33 and 52 provides guidance on the IPA's consideration of materiality as it relates to each separate management assertion about compliance. Materiality for purposes of compliance assertions differs from materiality for financial reporting purposes. Accordingly, materiality relates to each separate management assertion about compliance. The IPA should consider the materiality of management's assertions in relation to each of the individual services performed. The IPA should issue a qualified or adverse opinion when reporting instances of noncompliance that are material in relation to each of the specific compliance requirements

This Guide also requires all servicer noncompliance to be reported (except for certain instances of immaterial noncompliance) in the auditor's "Schedule of Findings and Questioned Costs" (see "Reporting Noncompliance" later in this section).

### **Obtaining Sufficient Evidence and Sampling**

The examination procedures suggested in this Guide are not all of those that the practitioner may determine are necessary to provide reasonable assurance of detecting material noncompliance, nor are they intended to supplant the practitioner's judgment of the work required. Suggested procedures described may not cover all circumstances or conditions encountered. Further, the Guide does not suggest procedures for performing the financial statement audit or an examination of a servicer management's assertion about the servicer's internal control over compliance with the specified requirements. For the financial statement audit, practitioners should refer to guidance about "Evidential Matter" in SAS No. 31 (SAS No. 80, *Amendment to SAS No. 31, Evidential Matter*, for engagements beginning on or after January 1, 1997). For the compliance audit, practitioners should refer to guidance about "Obtaining Sufficient Evidence" in SSAE No. 3, as amended by SSAE No. 9, paragraphs 45 and 47.

Although this Guide requires no specific or minimum sample size or sampling methodology for the compliance audit, it does require that samples be selected in such a way to be representative of the population and period under audit, the guaranty agency clients serviced, and the functions performed by the servicer for those guaranty agency clients that are contained in the compliance requirement. Practitioners should consider the guidance in the AICPA's *Professional Standards*, vol. 1, AU sec.

350, *Audit Sampling*. **This Guide requires practitioners to document the sampling methodology used in their working papers.**

When selecting a representative sample of borrowers from the National Student Loan Data System (NSLDS), the practitioner should pull the sample from the guaranty agency's most recent NSLDS extract that was sent to ED. The practitioner is not required to contact ED's NSLDS contractor to obtain a representative sample from its database.

### **Reporting Noncompliance**

This guide requires that all instances of noncompliance identified by the servicer's management in its assertions or by the IPA during his/her engagement must be reported as a finding in the Schedule of Findings and Questioned Costs. This applies even in those cases where corrective action was taken by the servicer after the examination period. The only exceptions are those instances of noncompliance that were detected by the auditee's internal control and for which complete corrective action has been satisfactorily accomplished.

Managements's assertions and the IPA's reports issued pursuant to this guide are a primary tool used by program managers in meeting their stewardship responsibilities in overseeing the FFEL program. The areas of noncompliance noted in management's assertions and/or the IPA's reports must be acted upon by ED program managers. To be of value, these reports must contain adequate information to give reported matters perspective and to allow the managers to take necessary corrective action. As such, for each instance of noncompliance reported, the following information must be presented in the Schedule, if applicable:

- ▶ Identifying information for the guaranty agencies that comprise the population from which the sample was selected;
- ▶ Sampling methodology;
- ▶ Number of units and dollar value of the population;
- ▶ Number of units and dollar value of the selected sample;
- ▶ Number of units and dollar value of the instances of noncompliance; and
- ▶ Population of applicable transactions administered by the servicer for each guaranty agency in the population.

## **FUTURE REVISIONS**

Revisions to certain auditing standards are contemplated. As they become effective, the IPA must modify audit performance to meet the revised audit standards.

ED periodically revises the FFEL Program compliance requirements, and the OIG plans to issue revisions to this Guide to reflect changes. The IPA is responsible for assuring that he/she is using the most current version of this Guide. Upon beginning the audit engagement, the IPA should review the ED OIG Non-Federal Audit Team internet website at <http://www.ed.gov/offices/OIG/nonfed/sfa.htm>, to determine the most current version of this guide which should be used.

Any suggestions for improvement to this Guide are welcome and should be sent to:

U.S. Department of Education  
Office of Inspector General  
Director, Non-Federal Audits  
Wanamaker Building  
100 Penn Square East, Suite 502  
Philadelphia, PA 19107

Fax: (215) 656-8628



**UNITED STATES DEPARTMENT OF EDUCATION**  
**SECTION II**



**OFFICE OF INSPECTOR GENERAL**  
**REQUIRED MANAGEMENT ASSERTIONS, COMPLIANCE**  
**REQUIREMENTS, AND SUGGESTED PROCEDURES**

**INTRODUCTION**

March 2000

This section:  
Dear Colleague:

1. Sets forth the compliance requirements that are the subject of management's written assertions. This letter transmits the U.S. Department of Education's (ED) Audit Guide, *Audits of Guaranty Agency Servicers Participating in the Federal Family Education Loan (FFEL) Program*.

2. Briefly describes the related regulatory requirements. *[Note: Except for the management assertions, IPAs should consider the term "agency" or "guaranty agency" referred to in this section as applying to a servicer acting on behalf of the guaranty agency];* and service any aspect of the Student Financial Assistance programs. However, an exemption applies to this compliance audit requirement if the servicer contracts with only one guaranty agency and

3. Provides guidance on the general approach the practitioner should consider in designing and the audit of that Guaranty agency's FFEL Program includes every aspect of the servicer's carrying out procedures in his or her examination of management's written assertions. administration of the FFEL Program.

As discussed in Section I, the suggested procedures in this Guide are not intended to be a complete manual of procedures, may not cover all circumstances or conditions encountered, and do not financial statements. The financial statements must be prepared on an accrual basis in accordance supplant the practitioner's judgment of the work required. with generally accepted accounting principles. For servicers that are not nonprofit or

governmental organizations, all financial statement and compliance audits conducted to satisfy SSAE No. 3, as amended by paragraph 37 of SSAE No. 9, states that a practitioner should "obtain an understanding of the specified compliance requirements" considering relevant laws, regulations, and contracts. Accordingly, among other sources, the practitioner should have ready access to: Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and*

*Non-Profit Organizations* instead.

Application of this Guide is effective for fiscal years ending June 30, 2000, and thereafter. Earlier application of the Guide is encouraged. This Guide is available on the Internet at this URL:

<http://home.gvi.net/~edoig>. Questions pertaining to the Guide should be faxed to the Office of Guaranty Agency Monthly Claims and Collections Reports (ED Form 1189); Inspector General at (215) 656-8628. We hope this guide will assist you in fulfilling your responsibilities for completing and submitting the required audit.

- ▶ Higher Education Act of 1965, as amended;
- ▶ Student Status Confirmation Reports/Notification of Change Information
- ▶ Summary and detailed loan records and supporting loan records;
- ▶ Guaranty agency contracts with servicers;
- ▶ Dear Colleague Letter 96-L-186/96-G-287 - Subject - Clarification and interpretative guidance on certain provisions in the FFEL Program regulations published on December 18, 1992.

Sincerely,

Lorraine Lewis  
Inspector General

*[Note: To help ensure consistent implementation of the regulations, ED issued a series of follow-up letters to clarify the answers contained in the DCL. Three of the letters were dated March 14, 1996, April 24, 1996, and May 31, 1996];* and

- ▶ Dear Colleague Letter 98-G-314 - Subject - Revised Guaranty Agency Quarterly/Annual Report (ED Form 1130), Revised Instructions, Revised Due Dates and Extension of the Guaranty Agency Monthly Claims and Collections Report (ED Form 1189).



## 1. ED FORMS 1189 and 1130

### Management Assertion

**The loan information (loan types, interest rate, beginning and ending principal loan balances, and loan status (past due, in grace, in deferment)) reported on ED Form 1189 and ED Form 1130 prepared by [name of Servicer] and submitted to ED on behalf of our guaranty agency clients agrees with system information and supporting documentation.**

### Compliance Requirements

The guaranty agency shall maintain current complete records for each loan that it holds. The records shall be maintained in a system that allows ready identification of each loan's current status, updated at least every 10 business days. The ED Form 1189 is the cornerstone of the monthly cycle used by ED to carry out financial activities between each guaranty agency and ED. ED uses the information from the ED Form 1189 as well as relevant data from the Guaranty Agency Quarterly/Annual Report (ED Form 1130) to determine and process payments from and to the guaranty agency.

A guaranty agency uses the ED Form 1189 to request payments of reinsurance for FFEL Program claims paid to lenders and to request certain payments. An agency also uses the form to report amounts due ED for collections on defaulted loans on which reinsurance has been paid and for refunding amounts previously paid for reinsurance claims.

The ED Form 1189 requires summary information only concerning a guaranty agency's claims, collections, and related activity over a monthly period. The guaranty agency shall maintain detailed records to support each entry on the ED Form 1189 and be able to reconstruct the entries back to individual loan, borrower or lender levels, or to specific guaranty agency level transactions. This includes keeping accurate records of reinsurance payments and collections on defaulted loans at the loan and borrower level.

The ED Form 1130 Guaranty Agency Quarterly/Annual Report shall be submitted by each participating guaranty agency on both a quarterly and an annual basis. The information in the ED Form 1130 is used by the Department of Education to determine whether guaranty agencies are properly administering the FFEL Program, the amount to pay each guaranty agency for transition support, including administrative cost allowance and reinsurance claims. The Secretary uses the quarterly report for the previous September 30 to calculate the amount of loans in repayment at the end of the preceding fiscal year. In determining which amounts to test, particular attention should be given to the September 30 amounts for current year defaults, current year collections, loans receivable and the sources and uses of funds for the reserve account (or equivalent line item(s) pertaining to the Federal/Operating Funds for the September 30 report).

In addition to the ED Forms 1189 and 1130, guaranty agencies are required to submit loan level detail information to the National Student Loan Data System (NSLDS). Key data elements on the NSLDS extract include: social security number, last name, original school code, academic level, current school code, enrollment status code, enrollment status date, originating lender code, loan guarantee date, amount of guarantee, current holder lender code, date entered repayment, loan status code, loan

status date, amount of claim paid to lender, and for loans with a defaulted status- outstanding principal, interest and fee amounts.

### **Suggested Procedures**

- a. Select an ED Form 1189 and an ED Form 1130 (which covers the period September 30) prepared by the servicer and submitted to ED on behalf of its guaranty agency clients and trace loan information reported to the servicers summary system records or ledgers.
- b. Reconcile amounts reported on ED Form 1130 for Federal receivables and reserves to the servicer's accounting system.
- c. Reconcile key information reported on ED Forms 1189 and 1130 with the NSLDS Extract submitted by the guaranty agency. *[Note: Some differences between the ED Form 1130 quarterly report and the NSLDS extracts may exist due to timing factors]*

## 2. FEDERAL REINSURANCE

### Management Assertion

**The loan information reported in Parts A, B, and C of the ED Form 1130 used to calculate loans in repayment and submitted by [name of Servicer] on behalf of our guaranty agency clients during the quarter ended September 30, agrees with summary records (identify the summary records, such as the general or subsidiary ledgers).**

### Compliance Requirements

The Secretary reimburses guaranty agencies for losses on default claim payments made to lenders. Reimbursements are made for different percentages of guaranty agency losses based on the percentage of reinsurance claims paid related to the loans in repayment (reported by the Guaranty Agency) at the end of the preceding fiscal year. To be reimbursed, guaranty agencies shall submit a quarterly 1130 Report to the Secretary. The information in this report is used to determine whether guaranty agencies are properly administering the FFEL Program and to identify the amount to pay each guaranty agency, as well as any amount that shall be returned to ED. The Secretary uses the report for the previous quarter ending September 30 containing complete and accurate data in order to calculate the amount of loans in repayment at the end of the preceding fiscal year. The Secretary does not pay a reinsurance claim to the guaranty agency after the date the quarterly report is due until the guaranty agency submits a complete and accurate report (34 CFR 682.404).

Section 682.404(b)(3) of Title 34 of the Code of Federal Regulations states that the total of reinsurance claims paid by the Secretary to a guaranty agency during any fiscal year does not include amounts paid on claims by the guaranty agency:

- ▶ On loans considered in default under 34 CFR 682.412(e);
- ▶ Under a policy established by the agency that is consistent with 34 CFR 682.509(a)(1); or that were filed by lenders at the direction of the Secretary;
- ▶ On loans made under a guaranty agency's approved lender-of-last-resort program.

Per 34 CFR 682.404(b)(4), the “amount of loans in repayment” means:

The sum of:

- ▶ The original principal amount of all loans guaranteed by the agency; and
- ▶ The original principal amount of any loans on which the guarantee was transferred to the agency from another agency;

Minus the original principal amount of all loans on which:

- ▶ The loan guarantee was canceled;

- ▶ The loan guarantee was transferred to another agency;
- ▶ The borrower has not yet reached the repayment period;
- ▶ Payment in full has been made by the borrower;
- ▶ The borrower was in deferment status at the time repayment was scheduled to begin and remains in deferment status;
- ▶ Reinsurance coverage has been lost and cannot be regained; and
- ▶ The agency paid claims, excluding the amount of those claims:
  - ▶ Paid under Sec. 682.412(e);
  - ▶ Paid under a policy established by the agency that is consistent with 34 CFR 682.509(a)(1);  
or
  - ▶ Paid at the direction of the Secretary.

### **Suggested Procedures**

- a. Compare the amounts of loans in repayment in the guaranty agency system at September 30 to the amount of loans in repayment derived from the September 30th ED Form 1130 report. Determine the propriety of any difference.
- b. Select from the guaranty agency's system a representative sample of loans in "in-school", "repayment status" and in "repayment status for over 10 years." Verify the loan amount and loan status by contacting the current holder of the loan or schools to confirm the authenticity and status of the loans.

### **Management Assertion**

**During the year ended [mo/dy/yr], [name of Servicer] received reinsurance for only those loans that met the requirements for reinsurance.**

## **Compliance Requirements**

A guaranty agency is entitled to reinsurance payments on a loan only if the requirements cited in 34 CFR 682.406 are met. A guaranty agency shall maintain current, complete, and accurate records for each loan that it holds and other records as described in 34 CFR 682.414.

Some of the primary compliance requirements that must be met for a guaranty agency to be entitled to receive reinsurance payments include:

- ▶ The lender provided an accurate collection history and an accurate payment history to the guaranty agency with the default claim filed on the loan showing that the lender exercised due diligence in collecting the loan through collection efforts meeting the requirements of 34 CFR Sec. 682.411, including collection efforts against each endorser [34 CFR 682.406 (a) (3)];
- ▶ The loan was in default before the agency paid a default claim filed thereon [34 CFR 682.406 (a) (4)];
- ▶ The lender filed a default claim thereon with the guaranty agency within 90 days of default [34 CFR 682.406 (a) (5)];
- ▶ The lender resubmitted a properly documented default claim to the guaranty agency not later than 60 days from the date the agency had returned that claim due solely to inadequate documentation, except that interest accruing beyond the 30th day after the date the guaranty agency returned the claim is not reinsured unless the lender files a claim for loss on the loan with the guarantor together with all required documentation, prior to the 30th day [34 CFR 682.406 (a) (6)];
- ▶ The lender satisfied all conditions of guarantee coverage set by the agency, unless the agency reinstated guarantee coverage on the loan following the lender's failure to satisfy such a condition pursuant to written policies and procedures established by the agency [34 CFR 682.406 (a) (7)];
- ▶ The agency paid or returned to the lender for additional documentation a default claim thereon filed by the lender within 90 days of the date the lender filed the claim or, if applicable, the additional documentation, except that interest accruing beyond the 60th day after the date the lender originally filed the claim is not reinsured [34 CFR 682.406 (a) (8)];
- ▶ The agency submitted a request for the payment on a form required by the Secretary no later than 45 days following payment of a default claim to the lender [34 CFR 682.406 (a) (9)];
- ▶ The loan was legally enforceable by the lender when the agency paid a claim on the loan to the lender [34 CFR 682.406 (a) (10)];
- ▶ The agency exercised due diligence in collection of the loan in accordance with 34 CFR Sec. 682.410(b)(6) or (7) [34 CFR 682.406 (a) (11)];
- ▶ The agency and lender complied with all other Federal requirements with respect to the loan including the payment of origination fees and compliance with all preclaims assistance requirements in 34 CFR Sec. 682.404(a)(2)(ii) [34 CFR 682.406 (a) (12)];
- ▶ The agency assigns the loan to the Secretary, if so directed, in accordance with the requirements of 34 CFR Sec. 682.409 [34 CFR 682.406 (a) (13)]; and

- ▶ The guaranty agency certifies to the Secretary that diligent attempts have been made by the lender and the guaranty agency under 34 CFR Sec. 682.411(g) to locate the borrower through the use of reasonable skip-tracing techniques [34 CFR 682.406 (a) (14)].

The Secretary requires a guaranty agency to repay reinsurance payments received on a loan if the lender or the agency fails to meet these requirements.

### **Suggested Procedures**

Select a sample of defaulted loans from the ED Form 1189 reports and determine that the conditions of reinsurance are met and documented for all loans.

### **3. DEATH, DISABILITY, CLOSED SCHOOL, FALSE CERTIFICATION AND BANKRUPTCY CLAIMS**

#### **Management Assertion**

**During the year ended [mo/dy/yr], [name of Servicer] a) paid death, disability, closed school, false certification, and bankruptcy claims to lenders within 45 days after receiving appropriate documentation; and b) did not request payment from ED prior to the lenders claim being paid. In bankruptcy proceedings [name of Servicer] took specific actions in accordance with 34 CFR 682.402(i).**

#### **Compliance Requirements**

If an individual borrower or the student for which a parent borrower received a PLUS loan dies, the obligation of the borrower and any endorser to make any further payments on the loan is canceled, in accordance with 34 CFR 682.402(b). If the lender determines that an individual borrower is totally and permanently disabled, the obligation of any further payments on the loan is canceled in accordance with 34 CFR 682.402(c).

If a borrower (or the student for whom a parent received a PLUS loan) could not complete the program of study for which the loan was intended because the school at which the borrower (or student) was enrolled, closed, or the borrower (or student) withdrew from the school not more than 90 days prior to the date the school closed, ED reimburses the holder of a loan received by a borrower on or after January 1, 1986, and discharges the borrower's obligation with respect to the loan in accordance with the provisions of 34 CFR 682.402(d). This 90-day period may be extended if the Secretary determines that exceptional circumstances related to a school's closing would justify an extension.

If the eligibility of a borrower to receive a loan (or the student for whom a parent received a PLUS loan) was falsely certified by an eligible school, ED reimburses the holder of a loan received by a borrower on or after January 1, 1986, and discharges a current or former borrower's obligation with respect to the loan in accordance with the provisions of 34 CFR 682.402(e). For purposes of a false certification discharge, the term "borrower" includes all endorsers on a loan.

If a borrower files a petition of relief under the Bankruptcy Code, ED reimburses the holder of the loan for unpaid principal and interest on the loan, in accordance with 34 CFR 682.402(f).

A lender shall provide the guaranty agency with proper documentation when filing a death, disability, closed school, false certification, or bankruptcy claim as follows:

- ▶ The original promissory note, or, if the lender no longer has the original promissory note, a copy of the note certified by the lender as a true and accurate copy;
- ▶ The loan application.
- ▶ In the case of a death claim, documents that formed the basis for the determination of death;
- ▶ In the case of a disability claim, a copy of the certification of disability described in paragraph 34 CFR 682.402(c)(2);

- ▶ In the case of a closed school claim, the documentation described in 34 CFR 682.402(d)(3) or any other documentation as ED may require;
- ▶ In the case of a false certification claim, the documentation described in 34 CFR 682.402(e)(3);
- ▶ In the case of a bankruptcy claim, evidence that a bankruptcy petition has been filed, all pertinent documents sent to or received from the bankruptcy court by the lender, and an assignment to the guaranty agency of any proof of claim filed by the lender regarding the loan and a statement of any facts of which the lender is aware that may form the basis for an objection or exception to the discharge of the borrower's loan obligation in bankruptcy and all documents supporting those facts.

[34 CFR 682.402(g)]

The guaranty agency shall review a death, disability, or bankruptcy claim promptly and shall pay the lender on an approved claim the amount of loss in accordance with paragraph 34 CFR 682.402(f), not later than 45 days after the claim was filed by the lender [34CFR 682.402 (h) (1)]. In the case of a closed school claim or a false certification claim, the guaranty agency shall document its determination that the borrower is eligible for discharge under 34 CFR 682.402 paragraphs (d) or (e) and pay the borrower or the holder the amount determined under 34 CFR 682.402(h)(2).

Guaranty agencies are required to take specific actions in bankruptcy proceedings in accordance with 34 CFR 682.402(i). Different actions are required depending on whether the bankruptcy claim is: (a) An undue hardship claim, (b) Plan proposed under bankruptcy Chapters 11, 12 and 13, and (c) Plan proposed under bankruptcy Chapters 11, 12 and 13 for loans in repayment less than seven years.

In accordance with 34 CFR 682.402(k)(2), the guaranty agency shall not request payment from ED until the lender's claim has been paid.

### **Suggested Procedures**

Select a representative sample of death, disability, and bankruptcy claims from the guaranty agency's ED Form 1189 reports and perform the following:

- a. Review claims for the existence of proper documentation and determine whether the claims were eligible for payment and paid timely.
- b. Determine whether the lender's claim was paid prior to the servicer requesting payment from ED.
- c. For any bankruptcy claims, determine whether the servicer took appropriate actions.

## **4. DEFAULT AVERSION**

### **Management Assertion**

**For the year ended [mo/dy/yr], [name of Servicer] performed default aversion activities in accordance with ED requirements. [Name of Servicer] did not collect on the same loans for**



**which they performed default aversion activities within 3 years of the dates default claims were paid.**

### **Compliance Requirements**

[For guidance relating to Default Aversion, consult the “Guaranty Agency Partner” Letter, dated November 15, 1999, Subject: Sections 422A, 422B, 428(c)(6), and 428(l) of the Higher Education Act.]

Upon receipt of a complete request from the lender received not earlier than the 60<sup>th</sup> day and no later than the 120<sup>th</sup> day of delinquency, a guaranty agency shall engage in default aversion activities designed to prevent the default by a borrower. [Default aversion activities are activities of a guaranty agency that are designed to prevent a default by a borrower who is at least 60 days delinquent and that are directly related to providing collection assistance to the lender.]

If a guaranty agency contracts with another party to perform default aversion assistance and collect defaulted loans, the party that provides default aversion assistance on a loan may not collect on that loan within 3 years of the date the default claim is paid.

### **Suggested Procedures**

- a. For a sample of loans, review documentation supporting that the servicer performed the necessary default aversion activities.
- b. Verify that if a contractor is used to perform default aversion assistance, the same contractor does not perform default collection activity on the same loans within the 3-year period.

## 5. COLLECTIONS

### **Management Assertion**

**During the year ended [mo/dy/yr], [name of Servicer] complied with the terms of the contracts with our guaranty agencies and performed prescribed collection procedures within required time frames.**

### **Compliance Requirements**

A guaranty agency shall engage in at least the collection activities described in subsections A through C below on a loan on which it pays a default claim filed by a lender, and shall attempt an annual Internal Revenue Service (IRS) offset on each eligible loan, except that the agency may engage in the “Alternative Collection Procedures” described in this section in lieu of the activities described in subsections A and B below [34 CFR 682.410(b)(6)(i)].

The agency may institute a civil suit against the borrower earlier than the first day of the period described in subsection C below. Upon instituting the suit, the agency is not required thereafter to follow the procedures in subsection A, or the Alternative Collection Procedures of this section. [34 CFR 682.410(b)(6)(ii)(B)].

Upon receipt of a payment from a borrower during a period described in subsections A or B of this section, or, in the case of a borrower whom the agency locates through the use of skip-tracing (see C.7 below), the agency is not required to follow the specific collection efforts described in subsections A through C of this section if the written notice described in 34 CFR 682.410(b)(5)(ii) has been sent. However, the agency shall diligently attempt to collect the loan for 60-days following receipt of the payment or receipt of confirmation of the borrower's address, as applicable. If the agency receives no payments during the 60-day period, the agency shall resume its use of the collection efforts described in subsections B through C.5 below, treating the first day after the end of the 60-day period as the first day of the period described in subsection B below. [34 CFR 682.410(b)(6)(ii)(C)].

### **Lapse Days**

The periods of time set forth in this section refer to the number of days that elapse from the date the servicer pays a default claim on a loan or on multiple loans for a borrower. These periods of time do not include any periods during which the agency is engaged in activities related to administrative wage garnishment, or is receiving a payment through garnishment at least once every 60 days during the period specified in 34 CFR 682.410(b)(5)(iv)(B), or during which the agency is engaged in an administrative review of the borrower's indebtedness on the loan pursuant to a request by the borrower as set forth in 34 CFR 682.410(b)(5)(iv). References to the borrower in this section and in the Alternative Collection Procedures subsection include all endorsers on a loan [34 CFR 682.410(b)(6)(ii)(A)].

## Gap in Collection Activity

At no point during the periods described in parts A and B (or D through F if Alternative Collection Procedures are used) of this section may the agency permit the occurrence of a gap in collection activity of more than 60 days 34 CFR 682.410(b)(6)(v)].

The term “gap in collection activity” means, with respect to a loan, any period:

- ▶ Beginning on the date that is the day after:
  - ▶ The date the agency paid a default claim to the lender thereon;
  - ▶ The day on which the agency receives the correct address for a borrower who has made no payment in the preceding 60 days; or
  - ▶ The day on which the agency completes a collection activity as defined in 34 CFR 682.411(k)(1) through (3); and
- ▶ Ending on the date of the earliest of:
  - ▶ The day on which the agency receives the first subsequent payment;
  - ▶ The day on which the agency begins the first subsequent collection activity as defined in 34 CFR 682.411(k)(1) through (3) (with references to the “lender” understood to mean “the agency”); or
  - ▶ The last day of the period described in subsection B below.

[34 CFR 682.410(b)(6)(vi)].

## Regular Collection Procedures

### A. 1 to 45 Lapse Days

The agency during this period shall:

1. Diligently attempt to contact the borrower by telephone to demand repayment of the loan.
2. Send to the borrower a written notice meeting the requirements of 34 CFR 684.410(b)(5)(vi).
3. Send to the borrower a written notice stating that the agency either will initiate procedures to garnish the borrower's wages, or institute a civil suit to compel repayment of the amount that the borrower owes plus related collection costs [34 CFR 682.410(b)(6)(iii)].

**B. 46 to 180 Lapse Days**

The agency during this period shall:

1. Engage in at least two diligent attempts to contact the borrower by telephone to demand repayment of the loan; and
2. Send at least three written notices to the borrower forcefully demanding that the borrower immediately commence repayment of the loan, and informing the borrower that the default has been reported to all national credit bureaus (if that is the case) and that the borrower's credit rating may thereby have been damaged. The final notice also shall indicate that it is the final notice the borrower will receive before the agency will take more forceful action, including the initiation of procedures to garnish the borrower's wages, or to offset the borrower's state and federal income tax refunds, or instituting a civil suit to compel repayment of the amount that the borrower owes plus related collection costs.

[34 CFR 682.410(b)(6)(iv)]

**C. After 181 Days**

1. Except as provided in paragraph C.2. below, during this period but no sooner than 30 days after sending the notice (required in 34 CFR 682.410(b)(5)(vi)), the agency shall initiate proceedings to offset the borrower's State and Federal income tax refunds and other payments made by the Federal government to a borrower, and shall initiate administrative wage garnishment proceedings against the borrower by the 225th day. If the agency determines that the borrower has insufficient income to satisfy the debt through wage garnishment, but has assets from which the debt can be satisfied, the agency shall assign the loan to ED. The agency must not file suit to collect a loan from a borrower unless directed to do so by ED [34 CFR 682.410(b)(6)(vii)(A)].

If, after initiating wage garnishment procedures, the agency terminates those procedures for a particular borrower, the agency shall, within 30 days, commence collection efforts at least as forceful as those described previously in subsections A and B, and in this subsection. The agency's collection efforts shall begin with the same collection activities as those that immediately preceded the initiation of garnishment procedures, or, if no collection activities were performed, the agency shall begin with the activities described previously in subsection A, except that the agency may engage in the collection procedures described under the "Alternative Collection Procedures" later in this section, in lieu of the activities described in subsections A and B [34 CFR 682.410(b)(6)(i)].

2. The agency need not initiate administrative wage garnishment if the agency determines and documents in the borrower's file that the borrower does not have sufficient income to satisfy the debt or a substantial portion thereof [34 CFR 682.410(b)(6)(vii)(B)].
3. If as a result of a determination made per C.2 above, the agency does not initiate administrative wage garnishment against the borrower for repayment of the loan and the loan has not been assigned to the Department for a civil suit to be filed, the agency shall conduct diligent semi-annual inquiries to determine if the borrower has since acquired the means to satisfy the

debt or a substantial portion thereof through administrative wage garnishment [34 CFR 682.410(b)(6)(viii)(A)]. *[Note: The agency may discontinue conducting the semi-annual inquiries concerning a borrower's means only in accordance with criteria and procedures approved by the Secretary. (34 CFR 682.410(b)(6)(x))].*

4. If the agency determines that the borrower has acquired the means (See C.3 above) to satisfy at least a substantial portion of the debt and then, if subsequent collection efforts are not successful, the agency, no later than 60 days after the determination, [must] institute administrative wage garnishment against the borrower for repayment of the loan. [34 CFR 682.410(b)(6)(viii)(B)].
5. The agency shall attempt diligently to enforce an administrative wage garnishment order or a judgment obtained against a borrower on a loan and shall ensure that the administrative wage garnishment order or judgment is renewed as permitted by applicable law. If, despite diligent attempts, the agency cannot recover the full amount of the debt because the borrower lacks sufficient assets or income attachable under applicable law to fully satisfy the administrative wage garnishment order or the judgment, the agency must conduct diligent semi-annual inquiries to determine if the borrower has since acquired sufficient attachable assets or income to satisfy an administrative wage garnishment order or a judgment CFR 682.410(b)(6)(ix)(A)]. *[NOTE: The agency may discontinue conducting the semi-annual inquiries concerning a borrower's means only in accordance with criteria and procedures approved by the Secretary, 34 CFR 682.410(b)(6)(x)];*

If the agency determines that the borrower has acquired sufficient income or attachable assets to satisfy the remainder of the debt, the agency, not later than 60 days thereafter, shall notify the borrower in writing of its intention to initiate administrative wage garnishment or resume enforcement efforts unless the borrower makes payment in full of all outstanding amounts. [34 CFR 682.410(b)(6)(ix)(B)];

If the borrower does not make payment in full within 30 days of the date the agency sends the notice, the agency, within 30 days thereafter, shall proceed to enforce the administrative wage garnishment or remainder of the judgment [34 CFR 682.410(b)(6)(ix)(C)].

6. Not later than 10 days after its receipt of information indicating that it does not know the current address of a borrower on a loan on which the agency has neither declined to initiate administrative wage garnishment nor discontinued semi-annual inquiries (See C.2. above), or the 60th day after its payment of a default claim on the loan, whichever is later, the agency shall attempt diligently to locate the borrower through the use of all available skip-tracing techniques, including, but not limited to, any skip-tracing assistance available from the IRS, credit bureaus, and state motor vehicle departments. A guaranty agency shall use any information provided by a school about a borrower's location in conducting skip-tracing activities. [34 CFR 682.410(b)(6)(xii)].

### **Suggested Procedures**

- a. Test a representative sample of defaulted loan accounts and determine whether the procedures described above were followed.

- b. If the servicer used a collection contractor, ascertain whether the contract specified the required collection procedures to be followed for defaulted loans.
- c. Ascertain whether the servicer followed criteria and procedures approved by the Secretary when discontinuing collection activities on a loan.

### **Alternative Collection Procedures (If applicable)**

A Guaranty Agency may engage in collection activities below in lieu of the activities described in parts A and B of the previous subsection. The “Lapse Days” as described earlier, apply to the periods of time set forth for the Alternative Collection Procedures.

Upon receipt of a payment from a borrower, the agency is not required to follow the specific collection efforts described below, but must diligently attempt to collect the loan for 60 days following receipt of the payment. If the agency receives no payments during the 60-day period, the agency must resume its use of the collection efforts described in this subsection, treating the first day after the end of the 60-day period as the first day of the period described in subsection E below.

#### **D. 1 to 30 Lapse Days**

The agency during this period must send to the borrower a written notice that meets the requirements of 34 CFR 682.410(b)(5)(vi). [34 CFR 682.410 (b)(7)(iii)]

#### **E. 31 to 180 Days**

During this period the agency shall:

1. Attempt diligently to collect the loan using such collection tools and activities as it deems appropriate, provided, however, that the agency must make at least one diligent effort to contact the borrower by telephone, and
2. Send at least two forceful collection letters to the borrower.
3. By the end of this period, the agency must refer the loan to a collection contractor who must:
  - a. Be compensated for its services on all FFEL loans referred by the agency solely on a contingency fee basis;
  - b. Be one of at least two collection contractors simultaneously providing collection services to the agency on FFEL loans under a competitive system that the agency has established and that includes the periodic assessment by the agency of the performance of the competing contractors and periodic adjustments in the volume of loans referred by the agency to each competing contractor based on those assessments; and
  - c. Not receive referral of more than 70 percent of the agency's referred loans in any calendar year. [34 CFR 682.410(b)(7)(vi)]

**Suggested Procedures for Alternative Collection Procedures (If applicable)**

- a. Review a representative sample of defaulted loan accounts and determine whether the agency performed the activities described above.
- b. Review Servicer contracts and records to determine that the servicer; (1) did not refer more than 70 percent of its referred loans to a single collection contractor, and (2) compensated the contractors only on a contingency fee basis.
- c. Ascertain that the servicer periodically assessed the performance of the competing contractors, and if necessary, made adjustments in the volume of loans referred to each competing contractor.

## 6. FEDERAL SHARE OF BORROWER PAYMENTS

### Management Assertion

**For the year ended [mo/dy/yr], [name of Servicer] properly computed and remitted borrower payments to the Department in a timely manner.**

### Compliance Requirements

If the guaranty agency receives a payment on a loan after default but before reinsurance has been received, 100 percent of the payment is paid to ED.

If the borrower makes payments on a loan after the Secretary has paid a reinsurance claim on that loan, the Servicer must pay the Secretary an equitable share of those payments. The Secretary's equitable share is the portion of payments that remains after deducting:

- ▶ The complement of the reinsurance percentage in effect when reinsurance was paid on the loan (See 2. Federal Reinsurance Rate above for the applicable reinsurance rate. The complement of the reinsurance percentage equals 100 minus the Federal Reinsurance rate), and
- ▶ 27 percent of borrower payments received before October 1, 1998 and 24 percent of borrower payments received after October 1, 1998 [34 CFR 682.405(g)(2), as amended by 20 USC 1078(c)(6)].

Loans that have been rehabilitated or paid by FFEL program consolidation loans are not covered by this requirement because these transactions do not include "payments made by the borrower." For these loans, under separate authority, agencies are allowed to retain collection costs added to the borrower's balance, not to exceed 18.5 percent of the payoff [34 CFR 682.405(b)(1)(iv) and 34 CFR 682.401(b)(27)].

Unless the Secretary approves otherwise, the guaranty Servicer must submit the Secretary's equitable share of borrower payments within 45 days of the receipt of the payments by the agency or its servicer (whichever is earlier) [34 CFR 682.404 (g)(3)]. *[NOTE: For payments received prior to February 1, 1993, the agency must submit payments within 60 days of receipt. See also Dear Colleague Letter 95-G-286.]*

### Suggested Procedures

Test a representative sample of borrower payments on defaulted loans to determine if ED received its equitable share in a timely manner.



## **7. ASSIGNMENT OF DEFAULTED LOANS TO ED**

### **Management Assertion**

**As of April 15, 19xx, [name of Servicer] assigned all loans that met applicable criteria to the Secretary.**

### **Compliance Requirements**

Unless the Secretary notifies an agency in writing that other loans must be assigned to the Secretary, an agency must assign any loan that meets all of the following criteria as of April 15 of each year:

- ▶ The unpaid principal balance is at least \$100;
- ▶ The loan, and any other loans held by the agency for that borrower, have been held by the agency for at least 4 years (5 years for fiscal years beginning 7/1/97);
- ▶ A payment has not been received on the loan in the last year; and
- ▶ A judgment has not been entered on the loan against the borrower.

The Secretary may also direct a guaranty agency to assign to ED certain categories of defaulted loans held by the agency [34 CFR 682.409]

### **Suggested Procedures**

Review an aging of the guaranty agency's loans to determine whether it is holding loans that should be assigned to ED, in accordance with the above criteria or a directed or approved assignment schedule.

## **8. COLLECTION CHARGES**

### **Management Assertion**

**For the year ended [mo/dy/yr], [name of Servicer] on behalf of our guaranty agency clients, charged borrowers appropriate collection costs on loans for which a default has been paid.**

### **Compliance Requirements**

The guaranty agency shall charge a defaulted borrower an amount equal to reasonable costs incurred by the agency in collecting a loan on which the agency has paid a default. The amount charged the borrower should equal the lesser of the amount that would be charged under the formula in 34 CFR 30.60 or, the amount that would be charged if the loan was held by ED. Costs may include, but are not limited to, attorney's fees, collection agency charges, and court costs [34 CFR 682.410(b)(2)]. In addition, a guaranty agency may add collection costs and late fees on defaulted FFEL loans being consolidated in an amount not to exceed 18.5 percent of the outstanding principal and interest [34 CFR 682.401(b)(27)].

### **Suggested Procedures**

Test a representative sample of defaulted loan accounts to determine whether the servicer charged for reasonable costs of collection. Determine whether the method used to calculate the amount was appropriate.

## 9. ENFORCEMENT ACTION

### Management Assertion

**For the year ended [mo/dy/yr], [name of Servicer] took measures to ensure enforcement of all Federal, state and guaranty agency requirements, including performing program reviews of such lenders and schools that met the criteria specified in 34 CFR 682.410(c)(1). [Name of Servicer] took appropriate and prompt corrective action on all findings identified in such program reviews in accordance with 34 CFR 682.410(c).**

### Compliance Requirements

The guaranty agency must take measures to ensure enforcement of all Federal, state and guaranty agency requirements and at a minimum, conduct biennial on-site program reviews of such lenders and schools that meet criteria specified in 34 CFR 682.410(c)(1). The agency is required to use statistically valid techniques to calculate liabilities owed the Secretary that the review indicates may exist, demand prompt payment from the responsible party and refer to the Secretary any case in which the payment of funds is not made within 60 days.

The guaranty agency is required to demand prompt repayment by the responsible parties to lenders, borrowers, the agency, or the Secretary, as appropriate, of all funds found in those reviews to be owed by the participants with regard to loans guaranteed by the agency, whether or not the agency holds the loans, and monitoring the implementation by participants of corrective actions, including these repayments, required by the agency as a result of those reviews [34 CFR 682.410(c)(2)].

A guaranty agency shall refer to the Secretary for further enforcement action any case in which repayment of funds to the Secretary is not made in full within 60 days of the date of the agency's written demand to the school, lender, or other party for payment, together with all supporting documentation, any correspondence, and any other documentation submitted by that party regarding the repayment [34 CFR 682.410(c)(3)].

A guaranty agency is also required to adopt procedures for identifying fraudulent loan applications and undertaking or arranging for the prompt and thorough investigation of criminal or other programmatic misconduct by its program participants. It is responsible also for promptly reporting all of the allegations and indications having a substantial basis in fact and the scope, progress and results of the agency's investigations to ED [34 CFR 682.410(c)(4-7)].

### Suggested Procedures

- a. Review the servicer's procedures for ensuring enforcement of all Federal, state and guaranty agency requirements, including selecting lenders and schools for review to determine if they meet the regulatory criteria.

- b. Review program review methodology to determine that it is up-to-date and includes, when problems are found, a statistically valid method for determining liabilities due the Secretary.
- c. Review program review reports to determine if amounts due to lenders, borrowers, the agency, or the Secretary, were identified. If so, determine whether appropriate demands for payment and follow-up were conducted.
- d. Determine whether the guaranty agency made referrals to the Secretary for further enforcement action in those instances where repayments were not made within 60 days of written demand.
- e. Through inquiry and review, determine whether the servicer adopted procedures for identifying fraudulent loan applications and for reporting all allegations of misconduct having a substantial basis to ED. Review servicer records on the follow-up of misconduct to determine whether ED was notified when appropriate.

## SECTION III

### ILLUSTRATIVE REPORTS AND APPENDICES

#### Financial Statements:

- Example A-1 Report on the Audit of the Basic Financial Statements
- Example A-2 Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards* (No Reportable Instances of Noncompliance and No Material Weaknesses [No Reportable Conditions Identified]) **OR**
- Example A-3 Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards* (Reportable Instances of Noncompliance and Reportable Conditions Identified)

#### Compliance Attestation:

- Example B Report Package Cover Page
- Example C Report on Compliance with Specified Requirements Applicable to the FFEL Program
- Example D-1 Report on Internal Control Over Compliance (No Reportable Conditions) **OR**
- Example D-2 Report on Internal Control Over Compliance (Reportable Conditions Identified [No Material Weaknesses])
- Example E Information Sheet
- Example F Schedule of Findings and Questioned Costs
- Example G Auditor's Comments on Resolution Matters Relating to the FFEL Program
- Example H Corrective Action Plan

#### Appendices:

- Appendix A U.S. Department of Education Offices
- Appendix B Definitions

**REPORT ON THE AUDIT OF THE BASIC  
FINANCIAL STATEMENTS**

We have audited the balance sheet of *[Name of Servicer]* as of *[Date]* and the related statements of income, retained earnings, and cash flows for the year then ended. These financial statements are the responsibility of the *[Name of Servicer]* management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly in all material respects, the financial position of *[Name of Servicer]* as of *[mo/dy/yr]* and the results of its operations and its cash flows for the year then ended, in conformity with generally accepted accounting principles.<sup>1</sup>

In accordance with *Government Auditing Standards*, we have also issued our report dated *[mo/dy/yr]* on our consideration of the *[Name of Servicer]* internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants.

*[Signature]*

*[Date]*

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<sup>1</sup> The opinion paragraph should be modified as necessary under the circumstances, e.g., if qualified opinion, adverse opinion, or disclaimer of opinion is to be issued.

**Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards* (No Reportable Instances of Noncompliance and No Material Weaknesses [No Reportable Conditions Identified])<sup>1</sup>**

[Addressee]

We have audited the financial statements of [name of Servicer] as of and for the year ended June 30, 19XX, and have issued our report thereon dated [mo/dy/yr].<sup>2</sup> We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*,<sup>3</sup> issued by the Comptroller General of the United States.

**Compliance**

As part of obtaining reasonable assurance about whether [name of Servicer] financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.<sup>4</sup>

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered [Name of Servicer] internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on internal control over financial reporting. Our consideration of internal control over financial reporting would not necessarily disclose all matters in internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more internal control component does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned

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<sup>1</sup>The auditor should use the portions of examples A-2 and A-3 that apply to a specific situation. For example, if the auditor will be giving an unqualified opinion on compliance but has identified reportable conditions on internal control, the compliance section of this report would be used along with internal control section of example A-3. Alternatively, if the auditor will be giving a qualified opinion on compliance but has not identified reportable conditions, the internal control section of this report would be used along with the compliance section of example A-3.

<sup>2</sup>Describe any departure from the standard report (for example, a qualified opinion, a modification as to consistency because of a change in accounting principle, or a reference to the report of other auditors).

<sup>3</sup>The standards applicable to financial audits include the general, fieldwork, and reporting standards described in chapters 3, 4, and 5 of *Government Auditing Standards*.

<sup>4</sup>See paragraphs 5.18 and 5.19 of *Government Auditing Standards* for the criteria for reporting.

functions. We noted no matters involving internal control over financial reporting and its operation that we consider to be material weaknesses.<sup>5</sup>

This report is intended solely for the information and use of the audit committee, management, and the U. S. Department of Education and is not intended to be and should not be used by anyone other than these specified parties.

[*Signature*]

[*Date*]

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<sup>5</sup> If the auditor has issued a separate letter to management to communicate other matters involving the design and operation of internal control over financial reporting, this paragraph should be modified to include a statement such as the following: “However, we noted other matters involving internal control over [list compliance area], which we have reported to management of [Servicer] in a separate letter dated August 15, 19xx.” This reference is not intended to preclude the auditor from including other matters in the separate letter to management. Furthermore, the reference to management is intended to be consistent with paragraph 5.28 of *Government Auditing Standards*, which indicates that communications to “top” management should be referred to.



**Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards* (Reportable Instances of Noncompliance and Reportable Conditions Identified)<sup>1</sup>**

[Addressee]

We have audited the financial statements of [name of Servicer] as of and for the year ended June 30, 19xx, and have issued our report thereon dated [mo/dy/yr].<sup>2</sup> We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*,<sup>3</sup> issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether [name of Servicer] financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards*<sup>4</sup> and which are described in the accompanying schedule of findings and questioned costs as items [list the reference numbers of the related findings, for example, 99-2 and 99-5].

Internal Control Over Financial Reporting

In planning and performing our audit, we considered [Name of Servicer] internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on internal control over financial reporting. However, we noted certain matters involving internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control over financial reporting that, in our judgment, could adversely affect [Name of Servicer] ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items [list the reference numbers of the related findings, for example, 99-1, 99-4, and 99-8].

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<sup>1</sup>The auditor should use the portions of Examples A-2 and A-3 that apply to a specific situation. For example, if the auditor will be giving an unqualified opinion on compliance but has identified reportable conditions on internal control, the compliance section of Example A-2 would be used along with internal control section of this report. Alternatively, if the auditor will be giving a qualified opinion on compliance but has not identified reportable conditions, the internal control section of Example A-2 would be used along with the compliance section of this report.

<sup>2</sup>Describe any departure from the standard report (for example, a qualified opinion, a modification as to consistency because of a change in accounting principle, or a reference to the report of other auditors).

<sup>3</sup>The standards applicable to financial audits include the general, fieldwork, and reporting standards described in chapters 3, 4, and 5 of *Government Auditing Standards*.

<sup>4</sup>See paragraphs 5.18 and 5.19 of *Government Auditing Standards* for the criteria for reporting.

A material weakness is a condition in which the design or operation of one or more internal control component does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of internal control over financial reporting would not necessarily disclose all matters in internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that none of the reportable conditions described above is a material weakness.<sup>5 6</sup>

This report is intended solely for the information and use of the audit committee, management, and the U. S. Department of Education and is not intended to be and should not be used by anyone other than these specified parties.

[*Signature*]

[*Date*]

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<sup>5</sup> If conditions believed to be material weaknesses are disclosed, the report should identify the material weaknesses that have come to the auditor's attention. The last sentence of this paragraph should be replaced with language such as the following: However, of the reportable conditions described above, we consider items [*list the reference numbers of the related findings, for example, 97-1 and 97-8*] to be material weaknesses.

<sup>6</sup> If the auditor has issued a separate letter to management to communicate other matters involving the design and operation of internal control over financial reporting, this paragraph should be modified to include a statement such as the following:  
We also noted other matters involving internal control over financial reporting, which we have reported to management of [name of Servicer] in a separate letter dated August 15, 19xx. This reference is not intended to preclude the auditor from including other matters in the separate letter to management. Furthermore, the reference to management is intended to be consistent with paragraph 5.28 of *Government Auditing Standards* which indicates that communications to top management should be referred to.

**REPORT PACKAGE COVER PAGE**

NAME OF SERVICER

CITY, STATE

COMPLIANCE ATTESTATION EXAMINATION  
OF THE TITLE IV STUDENT FINANCIAL ASSISTANCE PROGRAMS

FOR THE FISCAL YEAR ENDING [MONTH DAY, YEAR]

XYZ & Co.  
Certified Public Accountants

**REPORT ON COMPLIANCE WITH SPECIFIED  
REQUIREMENTS APPLICABLE TO THE FFEL PROGRAM**

**INDEPENDENT ACCOUNTANT'S REPORT**

We have examined management's assertions, that [*Name of Servicer*] complied with the specified compliance requirements regarding: ED Forms 1189 and 1130; Federal Reinsurance; Death, Disability, and Bankruptcy Claims; Default Aversion; Collections; Federal Share of Borrower Payments; Assignment of Defaulted Loans to ED; Collection Charges; and Enforcement Action listed in Section II of the U.S. Department of Education's Audit Guide, *Compliance Audits of Guaranty Agency Servicers Participating In The Federal Family Education Loan Program* (1999 version), during the year ended [*mo/dy/yr*]<sup>1</sup>. Management is responsible for compliance with those requirements. Our responsibility is to express an opinion on the Guaranty Agency Servicer's compliance based on our examination.

Our examination was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States; attestation standards established by the American Institute of Certified Public Accountants; and the Audit Guide, *Compliance Audits of Guaranty Agency Servicers Participating In The Federal Family Education Loan Program*. Accordingly, we examined on a test basis, evidence about the servicer's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion. Our examination does not provide a legal determination on the servicer's compliance with specified requirements.

In our opinion, [*Name of Servicer*] complied, in all material respects, with the aforementioned requirements for the year ended [*mo/dy/yr*].<sup>2</sup>

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1 The IPA should list the assertions applicable to the guaranty agency servicer. Likewise, assertions not applicable should be deleted.

2 The IPA should modify the standard report if any of the following conditions exists:

- ▶ There is a material noncompliance with specified requirements (SSAE #3 as amended by paragraphs 58 through 65 of SSAE #9);
- ▶ There is a matter involving a material uncertainty (SSAE #3 as amended by paragraph 66 of SSAE #9);
- ▶ There is a restriction on the scope of the engagement (paragraphs 55-58 of SSAE #2, as amended by SSAE #9);
- ▶ The IPA decides to refer to the report (excluding servicer audit report) of another IPA as the basis, in part, for the IPA's report (paragraph 59 and 60 of SSAE #2, as amended by SSAE #9); or
- ▶ If management discloses the noncompliance and appropriately modifies its assertion or disagrees with the IPA over the existence of material noncompliance and does not include in its assertion a description of such noncompliance, the IPA should refer to the guidance in SSAE # 3, as amended by paragraphs 58 - 64 of SSAE #9.

This report is intended solely for the information and use of the audit committee, management, and the U.S. Department of Education and is not intended to be and should not be used by anyone other than these specified parties.

*[Signature]*

*[Date]*

**REPORT ON INTERNAL CONTROL  
OVER COMPLIANCE  
[NO REPORTABLE CONDITIONS]**

In planning and performing our audit of the [*Name of Servicer*] compliance for the year ended [*mo/dy/yr*], we considered its internal control over specified compliance requirements pertaining to the Federal Family Education Loan Program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and not to provide assurance about the effectiveness of [*Name of Servicer's*] internal control. Our consideration of the internal control would not necessarily disclose all matters in the internal control that might be material weaknesses under standards established by the American Institute of Certified Public Accountants.

A material weakness is a condition in which the design or operation of one or more of internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants that would be material in relation to the Federal Family Education program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. However, we noted no matters involving the internal control and its operation that we consider to be material weaknesses as defined above.

This report is intended solely for the information and use of an audit committee, management, and the U. S. Department of Education and is not intended to be and should not be used by anyone other than these specified parties.

*[Signature]*

*[Date]*

**EXAMPLE D-2**

**REPORT ON INTERNAL CONTROL OVER COMPLIANCE  
(REPORTABLE CONDITIONS IDENTIFIED [NO MATERIAL WEAKNESSES])**

In planning and performing our audit of the [*Name of Servicer*] compliance for the year ended [*mo/dy/yr*], we considered its internal control over compliance with the Federal Family Education Loan program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and not to provide assurance on internal control. However, we noted certain matters involving internal control over compliance and its operation that we consider to be reportable conditions.

Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect the [*Servicer's*] ability to administer the Federal student financial aid programs in accordance with the applicable requirements of laws, regulations, contracts and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items [*identify the finding numbers which are reportable conditions*]. Our consideration of internal control over compliance would not necessarily disclose all matters in internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses.

A material weakness is a condition in which the design or operation of one or more of internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants that would be material in relation to the Federal student financial aid programs being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. However, we believe that none of the reportable conditions described above is a material weakness.<sup>1</sup>

This report is intended solely for the information and use of an audit committee, management, and the U. S. Department of Education and is not intended to be and should not be used by anyone other than these specified parties.

[*Signature*]

[*Date*]

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<sup>1</sup> If the reportable conditions listed in the above paragraph are considered to be material weaknesses, change the last sentence in this paragraph to read: However, of the reportable conditions described above, we consider items [*identify the finding numbers which are materiel weaknesses*] to be material weaknesses.

**INFORMATION SHEET**  
**(Prepared by Guaranty Agency Servicer Management)**

*(Note: This Information Sheet is prepared by the servicer management, for the information of ED.)*

**AUDIT FIRM**

**GUARANTY AGENCY SERVICER**

ENTITY I.D. NO.: \_\_\_\_\_

PARTNER'S NAME: \_\_\_\_\_

PERIOD AUDITED: \_\_\_\_\_

CPA FIRM'S NAME: \_\_\_\_\_

ENTITY'S NAME: \_\_\_\_\_

ADDRESS: \_\_\_\_\_

ADDRESS: \_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

TELEPHONE NO.: \_\_\_\_\_

TELEPHONE NO.: \_\_\_\_\_

FAX. NO.: \_\_\_\_\_

FAX. NO.: \_\_\_\_\_



**EXAMPLE E**

*Please complete the following matrix by identifying the guaranty agencies (by providing their ID numbers) and the FFEL Program compliance functions performed by the servicer during the period covered by the attestation engagement (by placing 'X's' in the appropriate columns for each guaranty agency client the compliance function is performed).*

<b>Guaranty Agency ID</b>	<b>ED Forms 1189 &amp; 1130</b>	<b>Reinsurance</b>	<b>Death, Disability, Bankruptcy</b>	<b>Preclaims, Supplemental Preclaims</b>	<b>Collections</b>	<b>Fed. Share of Borrower Payments</b>	<b>Assignment of Defaulted Loans</b>	<b>Collection Charges</b>	<b>Enforcement Actions</b>

**LISTING OF GUARANTY AGENCY CLIENTS**

	<b><u>ID NUMBER</u></b>	<b><u>NAME OF GUARANTEE AGENCY</u></b>	<b><u>CITY</u></b>	<b><u>STATE</u></b>
(Example)	123456	XYZ STATE GUARANTY AGENCY	ANWHERE	XX

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS**  
**(Must be Attached to Auditor's Report on Compliance)**

*If this schedule is not prepared in accordance with all elements described below, the compliance report package will be rejected and the servicer may be subject to administrative sanctions pursuant to 34 CFR 668 Subpart G.*

This schedule should include the following:

1. The number of loans and dollar value for:
  - ▶ population;
  - ▶ selected sample;
  - ▶ instances of noncompliance (where applicable);
2. IPA's definition of material noncompliance.
3. Well-developed audit findings. A properly developed audit finding generally contains the following attributes:
  - ▶ statement of condition;
  - ▶ criteria;
  - ▶ effect;
  - ▶ cause; and
  - ▶ recommendation.

The IPA should fully develop each of these attributes for each finding to provide sufficient information to ED officials to permit timely and proper corrective action. As part of a finding the IPA is required to make a recommendation for corrective action to the servicer. If corrective action is not necessary, the IPA must state the reason. The servicer must develop a SEPARATE corrective action plan (see Example H) based on the IPA's findings and recommendations and must include this plan when submitting the report package.

**EXAMPLE G**

**AUDITOR'S COMMENTS ON RESOLUTION MATTERS  
RELATING TO THE FFEL PROGRAM**

The IPA should review prior findings, including findings from the previous IPA audit, and recent ED OIG audits and ED and guaranty agency program reviews, including the resolution of those findings. For each finding for which corrective action has not been completed, provide the finding number, a summary of the finding (including recommendation of corrective action, if applicable), and the status of corrective action.

[*Name of Servicer*] has not taken corrective action on findings in prior report, ACN # xx-xxxxx titled [*Title of report*] as identified below.

Finding No. 1

Recommendation

Status

**CORRECTIVE ACTION PLAN**  
(Must be on Servicer’s Letterhead)

Audit Firm \_\_\_\_\_ Audit Period \_\_\_\_\_

**A. Comments on Findings and Recommendations:**

The servicer must provide a statement of concurrence or nonconcurrence with the findings and recommendations. If the servicer does not agree with a finding, it must provide specific information to support its position. If the information is voluminous, an appendix may be attached to the submission.

If the servicer determines that the questioned costs are unallowable or that the charges cannot be supported, the servicer should provide a statement to that effect in the corrective action plan.

If the servicer believes a questioned cost, or a portion of that cost, is allowable, the servicer must identify the allowable portion by program.<sup>1</sup>

**B. Actions Taken or Planned:**

The servicer must detail actions taken or planned to correct deficiencies identified in the report. For planned actions, servicers must provide projected dates for completion of major tasks. If the servicer believes a corrective action is not required, a statement describing the reasons must be included.

**C. Status of Corrective Actions on Prior Findings:**

For all prior audits and examinations, e.g. IPA audits, ED OIG audits, ED program reviews, the servicer must comment on all prior findings whether or not corrective action has been completed.<sup>2</sup>

The servicer must provide a report on the status of corrective actions taken on prior findings that remain open. An update must be included on dates for completion of major tasks and responsible officials for any actions not completed.

\_\_\_\_\_  
(Signature)

Servicer Official’s Name:

Title:

Telephone #:

**APPENDIX A**

<sup>1</sup>The servicer is required to have the IPA provide a statement that the necessary documents were located/obtained and/or that the actions were taken either with the corrective action plan (CAP) or during the audit resolution process.

<sup>2</sup>ED may have issued a FAD for a prior audit/examination. A FAD describes any corrective actions the servicer is required to take within 45 days of receipt (unless otherwise stated) of the FAD.

**U.S. DEPARTMENT OF EDUCATION OFFICES**

**For questions on the application of this guide:**

U.S. Department of Education  
Office of Inspector General  
Non-Federal Audits Advisory  
and Assistance Team  
10220 N.W. Executive Hills Blvd. - 2<sup>nd</sup> Floor  
Kansas City, MO 64153  
Phone: 816-880-4024  
FAX: 816-891-0815

**For comments on this guide:**

U.S. Department of Education  
Office of Inspector General  
Director, Non-Federal Audits  
Wanamaker Building  
100 Penn Square East, Suite 502  
Philadelphia, PA 19107  
Phone: 215-656-6900  
FAX: 215-656-8628

**Audit report package should be mailed to:**

U.S. Department of Education  
SFA / Financial Analysis and Oversight  
400 Maryland Avenue, S.W.  
ROB-3  
Room 4616, Mail Stop #5138  
Washington, D.C. 20202-5138

To contact call: 202-401-2280

**For reporting of fraudulent acts or indications of such acts:**

U.S. Department of Education  
Assistant Inspector General for  
Investigations  
400 Maryland Avenue, SW  
MES, Room 4122  
Washington, DC 20202-1510  
Phone: 202-205-8762  
Fax: 202-205-9449

## **DEFINITIONS**

### **SERVICER**

The term "third-party servicer" is defined in 34 CFR 682.200 subpart B - General Provisions as follows:

*Third-party servicer.* Any State or private, profit or nonprofit organization or any individual that enters into a contract with a lender or guaranty agency to administer, through either manual or automated processing, any aspect of the lender's or guaranty agency's FFEL Program required by any statutory provision of or applicable to Title IV of the HEA, any regulatory provision prescribed under that statutory authority, or any applicable special arrangement, agreement, or limitation entered into under the authority of statutes applicable to Title IV of the HEA that governs the FFEL Program, including any applicable function described in the definition of third-party servicer in 34 CFR part 668; originating, guaranteeing, monitoring, processing, servicing, or collecting loans; claims submission; or billing for interest benefits and special allowance.

### **NONSUBSIDIZED STAFFORD LOAN**

A Stafford loan made prior to October 1, 1992 that does not qualify for interest benefits under 34 CFR 682.301(b) or special allowance payments under 34 CFR 682.302.

### **UNSUBSIDIZED STAFFORD LOAN**

A loan made after October 1, 1992 authorized under section 428H of the HEA for borrowers who do not qualify for interest benefits under 34 CFR 682.301(b).

### **INTERNAL CONTROL**

Internal control means a process, effected by an entity's management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- e. Effectiveness and efficiency of operations;
- b. Reliability of financial reporting; and
- c. Compliance with applicable laws and regulations.

**INTERNAL CONTROL OVER THE FFEL PROGRAM**

Internal control pertaining to the compliance requirements for the FFEL program (internal control over the FFEL program) means a process--effected by an entity's management and other personnel--designed to provide reasonable assurance regarding the achievement of the following objectives:

- a. Transactions are properly recorded and accounted for to:
  - (i) Permit the preparation of reliable financial statements and reports;
  - (ii) Maintain accountability over assets; and
  - (iii) Demonstrate compliance with laws, regulations, and other compliance requirements;
- b. Transactions are executed in compliance with laws, regulations, and the provisions of contracts or grant agreements related to the FFEL Program; and
- c. Funds, property, and other assets are safeguarded against loss from unauthorized use or disposition.

**QUESTIONED COST**

Questioned cost means a cost that is questioned by the practitioner because of an audit finding:

- a. Which resulted from a possible violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the use of Federal funds, including funds used to match Federal funds;
- b. Where the costs, at the time of the audit, are not supported by adequate documentation; or
- c. Where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.