WRITTEN STATEMENT FOR
U.S. SECRETARY OF EDUCATION MARGARET SPELLINGS
U.S. HOUSE OF REPRESENTATIVES COMMITTEE ON EDUCATION AND LABOR
THURSDAY, MAY 10, 2007

Introduction

Thank you, Mr. Chairman and Members of the Committee. I appreciate this opportunity to set the record straight on my department's oversight of college student aid and the Reading First program.

We've heard a lot lately about alleged unethical practices in the student loan industry. Students and families expect and deserve honest, ethical behavior from our government, our universities, and our lenders.

Annually, ten million students in our country receive Federal financial aid. My department is the means by which almost half of them are able to afford college. We work with schools and lenders across our country. The vast majority of them are doing the right thing for students.

However, the fact is, federal student aid is crying out for reform. The system is redundant, it's Byzantine, and it has failed to keep up with dramatic changes in higher education. In many ways, it's also a prime target for those looking to game the system.

In the instances when the public's trust is violated, it's our responsibility to act – and that is what we've done.

Federal Student Aid Purposes, Operational Scope and Scale

The Department of Education's grant, loan, and work-study programs represent the largest source of student aid for postsecondary education in the United States. In 2006, these programs provided approximately $77 billion to more than ten million students and their families.

Federal Student Aid is charged with operational responsibility for oversight and administration of all the Department's Federal student financial assistance programs under Title IV of the Higher Education Act of 1965 (HEA) and, as one of the government's few Performance-Based Organizations, upholds high standards of operational efficiency, innovation, and customer care.

The Higher Education Amendments of 1998 established Federal Student Aid, under the direction of the Secretary, as the Federal Government's first Performance-Based Organization, with particular emphasis on modernizing the delivery of the Federal student assistance programs. The authorizing statute provides that the purposes of the Performance-Based Organization are to:

- Increase accountability;
- Improve service to students;
- Integrate information systems;

- Implement a common integrated delivery system;
- Strengthen program integrity; and
- Reduce costs of administering the programs.

The Department's Federal Student Aid office ensures the availability and accessibility of the Free Application for Federal Student Aid (FAFSA) to students and parents and receives and processes FAFSAs for over 14 million aid applicants each year. Over the past several years, Federal Student Aid has dramatically transformed the aid application process from a 100 percent paper process to one that is now 96 percent web-based.

The Department's Federal Student Aid office is one of the largest originator of student loans, annually making nearly three million Direct Loans totaling nearly $13 billion to almost two million student and parent borrowers. In 2006, it originated over 1.2 million Direct Consolidation Loans totaling more than $19 billion. It is responsible for servicing the over $89 billion outstanding loan portfolio of 18 million Direct Loans made to more than seven million borrowers. It is also responsible for collection on over $21 billion of defaulted student loans, including Direct Loans (DL), Family Federal Education Loans (FFEL), and Perkins Loans. It oversees the approximately $450 billion outstanding student loan portfolio, including loans held by lenders, guaranty agencies, and schools. It also ensures the delivery of nearly $13 billion in Federal Pell Grants to over five million undergraduate students each year. The Federal Student Aid systems process millions of financial and other transactions annually and its websites receive billions of hits each year. Its customer care centers annually handle more than 34 million inbound and outbound phone calls. And each year it sends more than 41 million communications to aid applicants and borrowers.

State of Affairs in 2001

Despite the critical role that the Department and Federal Student Aid (FSA) plays in helping millions of students attend college, when this Administration took the helm of the Department in January 2001, we inherited a situation in which both were in a state of complete disarray. The Department and Federal Student Aid had not received clean audit opinions in years and there was not any expectation of receiving them in the near future. Millions of dollars of grant money could not be accounted for. The Inspector General's Office, the General Accounting Office, and outside auditors had identified 661 audit recommendations for improving financial management, internal controls, operational management, program management, and compliance oversight that needed immediate attention. The situation was dire and the evidence of mismanagement egregious.

This Administration immediately committed to cleaning up these programs. Specifically, we committed to:

- Ensuring the removal of Student Financial Assistance Programs from the GAO High Risk List;
- Obtaining clean financial audit opinions;
- Putting in place effective systems of internal controls to protect the Department's assets from waste, fraud, and abuse;

- Making the systems and processes supporting student aid delivery and management more efficient and less costly;
- Continuing efforts to reduce student loan default costs; and
- Making accountability for results the primary operating principle for all Education managers, grantees, and contractors.

These commitments were ambitious and important, and I'm pleased to report we have achieved each and every one of them.

Prior to the establishment of Federal Student Aid as a Performance-Based Organization, the Federal Student Aid programs were plagued with oversight and management challenges, high default rates, and customers who were not happy with the service they received. In 1990, the Government Accountability Office (GAO) found the federal student aid programs at high risk for fraud, waste, abuse, and mismanagement. Financial management and internal controls around the programs were largely non-existent and unqualified audit opinions were not attainable. In 1990, student loan cohort default rates had hit an all-time high of 22.4%. Customer satisfaction was not even measured.

It was indeed shocking the amount of hard work necessary to address the clear oversight and management issues that landed the federal student aid programs on the GAO High Risk list in 1990 and where they remained when this Administration arrived on the scene.

We recognized the inherent challenges in providing billions of dollars of grants and loans, through thousands of intermediaries to millions of students; however, we chose to aggressively manage the challenge to ensure access to postsecondary education while reducing the vulnerability of student aid programs to fraud, waste, error, and mismanagement. To accomplish this goal, in April 2001, this Administration made obtaining clean audit opinions a top management improvement priority. The Department established a Management Improvement Team composed of eight members of the senior staff of the Education Department who worked exclusively on attacking the problems and developed a comprehensive "Blueprint for Management Excellence". In addition, the President's Management Agenda (PMA), announced in the summer of 2001, included an initiative specifically focused on improving the Department's financial management and removing the federal student aid programs from GAO's high-risk list.

The task at hand was daunting and required the Department and Federal Student Aid to:

- Clearly demonstrate strengthened financial management and internal controls over the federal student aid programs and the Department as a whole;
- Obtain unqualified audit opinions both on Federal Student Aid and the Department's financial statements;
- Demonstrate Federal Student Aid was integrating its delivery systems while providing high-quality services to students, colleges and universities, and financial institutions;
- Provide assurance and direct evidence that the Department has the systems, leadership, and processes in place to continue to maintain the integrity of its financial management, the major hurdle for the federal student aid programs' high-risk designation;

- Maintain a balanced management approach in the federal student aid programs that seeks to minimize non-compliance and default rates while still promoting the widespread use of the programs; and
- Demonstrate the existence of plans, processes, and infrastructure to address risk issues identified as key to the success of the federal student aid programs.

Theresa "Terri" Shaw, appointed as the Chief Operating Officer of Federal Student Aid in September 2002, was charged specifically with the task of ensuring the removal of the federal student aid programs from the GAO High Risk list and achievement of clean financial audit opinions as her top two priorities. Terri came to the Department after twenty-two years of exemplary work in federal student aid delivery, information technology, business process reengineering, contract management, and organizational change management.

Under this Administration, clean financial audit opinions have been achieved for the past five consecutive fiscal years beginning with FY 2002. The only prior clean financial audit opinion in the history of the Department was in 1997. When GAO removed the federal student aid programs from its High Risk list in early 2005, it recognized the significant progress of Federal Student Aid and the Department in resolving financial integrity and management issues and demonstrating strong commitment and senior-level leadership support for addressing issues and risks.

In addition, on March 31, 2005, Federal Student Aid achieved "all green" status on the President's Management Agenda (PMA) scorecard for Elimination of Fraud and Error in the Student Aid Programs and Deficiencies in Financial Management.

Federal Student Aid also focused on student loan default prevention and management through default prevention strategies implemented by participants across the programs. Since FY 2000, the combined FFEL and Direct Loan FY 2000 cohort default rate has been reduced by nearly 14 percent from 5.9 percent to 5.1 percent for FY 2004. Cohort default rates have been reduced from an all-time high of 22.4 percent for FY 1990. It is expected that when the FY 2005 cohort default rates are announced in September 2007 that they will be even lower than the current 5.1 percent.

At the same time, we also moved to make the financial aid application (FAFSA) and the process for filling it out more user-friendly. We went from a process that was 100 percent paper to one that is now 96 percent electronic. In fact, electronic processing has been implemented in all phases of the financial aid process. This is accomplished through a series of secure, user-friendly, and efficient electronic processes that have simplified the financial aid process for students and families. Federal Student Aid's new Public Service Announcement (PSA) "Only a Dream" was ranked in the Top 10% most viewed Nielsen-tracked PSAs in January, Top 5% in February and Top 6% in March resulting in reaching an audience of over 160 million.

The FY 2006 American Customer Satisfaction Index (ACSI) ratings for Federal Student Aid's highest volume products and services- including the electronic FAFSA, Common Origination and Disbursement and Direct Loan Servicing, score in the "Excellent" and "Good" range. Our products and services score higher than the federal government aggregate scores and on par with private sector scores.

Fair and effective oversight and monitoring of the approximately 6,000 institutions of higher education that participate in the programs is one of Federal Student Aid's core responsibilities, as is its oversight of the nearly 3,500 lenders, guaranty agencies, and servicers that participate in the FFEL Program.

Federal Student Aid's oversight activities include real-time quality control. Federal Student Aid has built into its systems and processes edits, triggers, risk assessments, and other features that enable it to monitor and correct errors and to provide early warnings of potential trouble. For example, our monitoring alerted us to: (1) anomalies in access to the National Student Loan Data System (NSLDS); (2) the financial condition of the Oregon Student Aid Commission (OSAC) early enough so that a seamless closure and transition of OSAC's guaranty services could occur; and (3) the increase in special allowance payments made to loan holders on certain FFEL loans made or purchased with tax-exempt funds which led the Administration to include a proposal in the President's FY 2005 Budget that would stop the increase in 9.5% special allowance.

In addition, Federal Student Aid monitors the school and lending community by reviewing required annual compliance audits and financial statements, performing on-site program reviews, and analyzing partner-specific data to detect trends and areas that could be of concern.

Federal Student Aid engages in an ongoing process of actively identifying risks in the programs. Noncompliance with statutes, regulations, and policies by schools, lenders, guaranty agencies, and servicers not only places Title IV funds at risk but also erodes the public trust in the programs. We partnered with the Department's Office of the Inspector General to establish a joint task force to identify real or potential risks for fraud, waste, abuse, and mismanagement in the programs. Federal Student Aid also established an Enterprise Risk Management unit to better coordinate risk monitoring and action plans among our various business units and with other Department of Education offices.

Let me speak specifically about the issues that have received recent attention:

National Student Loan Data System (NSLDS):

In 1994, the Department of Education created NSLDS in order to facilitate students' access to financial aid and loan information. Lenders may have access to the National Student Loan Data System (NSLDS) for the purpose of assisting with determining the eligibility of an applicant for federal student aid and the collection of federal student loans and grant overpayments.

NSLDS information may not be used for any other purpose, including the marketing of student loans or other products. In fact, NSLDS does **not** provide access to email addresses, phone numbers, or addresses of borrowers that could be used for marketing purposes. NSLDS information is protected by the Federal Privacy Act, and pursuant to the routine uses published in the NSLDS system of records notice the Department discloses to external authorized entities, information such as borrower social security number, date of birth, and data regarding Title IV aid received, as well as federal loan amounts, outstanding balance, current status of the loan, and grant amounts only for the purposes described above.

NSLDS does not authorize a user to "dig through tons of data", nor does it authorize the analysis of multiple borrower records for identification of hidden patterns or behaviors, nor does it authorize the exploring of transactions, nor does it permit database searches for multiple borrowers. These activities are commonly referred to as "data mining". NSLDS only allows a user to look up a single borrower at a time and only if the user has a relationship with the borrower or the borrower's specific permission to do so, as demonstrated by the borrower's return of a solicitation which contains such an authorization, by other written authorization by the borrower; or verbal permission as noted in call records of the lender. The use of automated tools to speed up the process of looking up borrower records one entry at a time is prohibited. Federal Student Aid deploys a variety of tools and techniques specifically designed to detect the use of such automated tools. These tools and techniques alert us to the possibility that automated tools are being used and automatically suspend the access for the user ID.

A common practice in the consumer credit industry is the purchase of data from credit bureaus and other sources for the specific purpose of making an offer of credit to an individual, such as credit card offers. Consolidation lenders participating in the FFEL program also follow this practice. Once the solicitation offer is made to a borrower and permission by the borrower is granted, the lender is authorized to access NSLDS to obtain information on the underlying loans that the borrower wishes to consolidate. It is the responsibility of the chief officer of each entity to ensure that its authorized users are in compliance with NSLDS access requirements.

There are 60 million student records in NSLDS representing loans that are both active and paid in full. The signature of the chief officer of the organization is also required to certify appropriate use of the system by his or her employees. In addition, the signature of the individual authorized by the chief officer of the organization is required for system access and use. With their signature, users confirm their understanding of the requirements for system use and agree to use the system in accordance with all rules and regulations. There are approximately 29,000 school accounts and 7,500 lender accounts.

The data residing in NSLDS are confidential and are protected by a series of both federally mandated and discretionary security measures, including the Privacy Act of 1974. These measures include access management, network and physical security policies and procedures such as protective surveillance of recurring threats such as virus and mail-ware filters, monitoring of suspicious external traffic, such as attempted denial of service attacks, firewalls, access and usage monitoring and tracking, and routine testing and surveillance using intrusion detection systems. NSLDS must annually pass, at a minimum, a FISMA audit, a financial audit or Security Certification and Accreditation. Most systems are annually tested by more than one of these three procedures and all systems must pass every test within any three-year period.

Federal Student Aid continuously monitors access to NSLDS to prevent unauthorized use and, since 2003, Federal Student Aid has invested over $650,000 in improved system security and monitoring tools and processes to ensure the integrity of student information.

Since 2003, these oversight efforts have resulted in the revocation of over 52,000 user IDs. The majority of these revocations were due to user inactivity; however, 261 user IDs were revoked due to suspicious activity. Of these 261 revoked IDs, 246 user IDs belonged to lenders, loan holders, guaranty agencies and servicers; and 15 user IDs belonged to schools.

As a result of the Department's monitoring of NSLDS usage, we issued a Dear Colleague Letter (DCL) in April 2005. This DCL explicitly reiterated to program participants that failure to comply with NSLDS usage requirements may result in the organization or individual losing access to the system and/or being subject to further sanctions.

Following the release of the DCL, we observed a significant increase in usage by lenders, loan holders, servicers, and guaranty agencies. Based on this increase, the Department had concerns as to the appropriateness of such access and discussed the termination of access by lenders, loan holders, servicers, and guaranty agencies. As a result, the Department decided to temporarily suspend access to NSLDS by all entities except schools and borrowers -- effective April 17, 2007. During this temporary suspension of access, the Department is conducting a comprehensive review of the specific uses of NSLDS to determine if there has been unauthorized access or use. The Department is consulting with the Inspector General to complete this review. As part of my Task Force on Student Loans established on April 24, 2007, we are also reviewing all guidance to determine if enhancements are necessary.

On May 2, 2007, the Department began to notify entities, beginning with guaranty agencies, of the process to restore their access to NSLDS. Access to NSLDS will be restored only after the Department has determined that it is appropriate to do so based on the analysis of access and usage information for each entity. As such, the timing of access restoration will not be the same for all entities.

This analysis is being conducted in a manner that assures the Department that an entity has only accessed and used NSLDS for approved purposes. Additionally, restoration of access will be predicated on the receipt and approval by the Department of: (1) a listing that identifies each of the entity's personnel for whom it wishes to have NSLDS web access and the specific authorized use or uses by that person; and (2) a certification, signed by the entity's Chief Executive Officer (CEO) and its Department of Education Data Point Administrator (DPA), that affirms that the entity and each of its staff for whom it has requested, or will request, NSLDS access is in compliance with all applicable guidance provided by the Department.

Access by an individual will be permanently terminated if the NSLDS access requirements are violated. Access by an entity will be permanently terminated if there are three violations of the NSLDS access requirements within a 12-month period by persons associated with that entity. In addition, unauthorized access or use of NSLDS may subject users to criminal or civil penalties, including fines and/or imprisonment.

The Department is also developing a fact sheet -- "Protecting Your Private Information" -- designed to help students and families understand the importance of protecting their private information and granting of permission for others (specifically entities other than schools) to access their NSLDS information.

Alleged Close Relationships with the FFELP Industry:

It has been suggested that the Department administers the FFEL and DL programs with favoritism to the FFEL program due to alleged close relationships to the FFEL industry. This suggestion is totally without merit and has no basis in fact.

A recent example that demonstrates the falsehood of this assertion is the Department's swift response to the Inspector General's September 2006 report that one lender, Nelnet, was improperly billing loans from ineligible sources for 9.5% special allowance payments. Within two weeks, 9.5% payments to Nelnet were frozen and within months, the industry received a Dear Colleague letter (DCL) restating the statutory requirements for eligible sources, and we announced that 9.5% payments would be suspended for the entire industry. The DCL also indicated that henceforth 9.5% payments would only be made for loans proven to be eligible after new, industry-wide audits. The Department then issued the methodology to be used in these audits, which it developed with the Office of the Inspector General.

While the IG's report highlighted another dimension to the problem, our work on the 9.5% payments began well before the report's release. In the summer of 2003, Department staff noted an alarming increase in special allowance payments made to loan holders on certain FFEL loans made or purchased with tax-exempt funds. The Department's staff determined that these claims for the higher payment were being made under a loophole in the rules written during the previous administration that allowed certain loans financed with tax-exempt funds to qualify for a 9.5 percent special allowance subsidy, minus the applicable rate of interest on such loans. This led the Administration to include a proposal in the President's FY 2005 Budget that would stop the increase in 9.5% special allowance payments.

After the Higher Education Act reauthorization was delayed that year, we began working closely with Congress to address the issue. President Bush closed the loophole when, on October 30, 2004, he signed the Taxpayer-Teacher Protection Act of 2004 (TTPA), which enacted a 1-year moratorium, since made permanent, on granting 9.5% special allowance subsidies on a wide variety of loans financed with tax-exempt obligations.

The savings achieved by closing the loophole went to a purpose close to my heart – to increase loan forgiveness programs for borrowers who participate in the Federal student aid programs and serve our country as teachers. Under the law, teachers who are employed full-time for five consecutive years and are highly qualified in secondary-school science or math, or are highly qualified in elementary or secondary school special education, qualify for loan forgiveness of up to $17,500.

As significant as the Taxpayer-Teacher Protection Act was in curbing a significant abuse in the Federal student loan programs and increasing loan forgiveness for teachers, the Higher Education Reconciliation Act of 2005 (HERA) promises to have a longer and likely more significant positive impact on academic preparation and higher education in the U.S. The origins of many of the initiatives contained in the HERA can be traced directly to President Bush's fiscal year 2006 budget, which proposed significant savings in the Federal student loan programs and redirected significant funding to student benefits. These initiatives include curbing excessive special allowance payments and insurance, making the changes to the treatment of loans in the

Taxpayer-Teacher Protection Act permanent, supporting additional need-based grant funding, and raising first- and second-year loan limits.

Congress also chose to authorize the two new Federal grant programs to help low-income students pay for postsecondary education – Academic Competitiveness and National SMART Grants. These new programs – authorized on February 8, 2006, and launched just 143 days later on July 1, 2006 – have already awarded more than $400 million to over 330,000 Pell Grant-eligible students helping to reduce their student loan debt. While these programs are complex and required significant work by the Department and institutions, I believe that they will: first, change the way that our high school students prepare for postsecondary education; and second, encourage more college juniors and seniors to study critical, high-need subjects. For this reason, I'm pleased that Congress made the decisions that they did in enacting the HERA with these two new programs.

President Bush has consistently put the needs of students -- particularly those from low-and middle-income families -- first.

Most recently, the President's fiscal year 2008 budget request, which is pending before Congress, would reduce interest subsidies on student loans by 1/2 percent, saving $12.4 billion over 5 years. He also proposed to reduce insurance on FFEL loans from 97% to 95%, saving an additional $1.6 billion over 5 years. And he proposed to increase the fee lenders pay when making a consolidation loan from 0.5 percent to 1.0 percent reducing Federal costs by $850 million. These savings will be used to pay for increases in the Pell Grant and Academic Competitiveness Grant programs and to raise loan limits for juniors and seniors in college. As I am sure you are aware, we have been criticized by FFEL lenders, some of whom have claimed lower subsidies will force them to reduce borrower benefits or leave the program. However, I believe that we can and must responsibly reduce subsidies in the FFEL program and use those savings to increase grant aid.

Further, it has been suggested that the Department's employment of skilled staff with industry experience equates to "close ties" to the industry and, therefore, does not allow for unbiased and impartial oversight and instead emphasizes partnership over enforcement. I should note for the record that the previous administration's July 1, 1999 report, "Reinventing Service", from the Customer Service Task Force, specifically stated that Federal Student Aid (then named Office of Student financial Assistance-OSFA)…" should be working in close partnership with financial institutions." Additionally, the previous administration began the practice of recruiting skilled staff with industry experience. Greg Woods, Federal Student Aid's first Chief Operating Officer, created a specific organizational unit, the Financial Partners Channel, to work in close partnership with lenders, guaranty agencies, and third-party services participating in the FFELP. He also began the practice of hiring managers with industry experience. The first General Manager of the FSA Financial Partners Channel was J. Barry Morrow, who was previously an executive with Sallie Mae. Succeeding Mr. Morrow was John Reeves, who was previously the President of Educaid, at the time the sixth largest student loan lender and the fourth largest holder of student loans, and prior to that an executive with The Money Store.

The previous administration understood, and we agree, that the experience and insights that private-sector leaders and managers bring to the important task of making the financial aid system work better for students, schools, and lenders is invaluable.

Since it was first established as a Performance Based Organization in 1998, Federal Student Aid has assembled a senior leadership team possessing over 300 years of experience in the private sector, the higher education community, and government. This team's leadership and expertise ensures Federal Student Aid achieves its strategic objectives, including annually delivering critical financial aid to millions of students and families and managing the inherent risks in the programs.

Since it is responsible for the administration of both the FFEL and DL programs, Federal Student Aid administers these programs in an evenhanded manner. The two programs share the same goals, the same eligibility requirements, and many of the same benefits. We firmly believe that the existence of the two programs has led to increased competition, improved customer service, and lowered costs for students and taxpayers alike. It should be noted that, since 2002, significant operational and management improvements have been implemented to enhance administration and financial and operational management of the DL program. These improvements are focused on better serving the 1,087 DL schools and the nearly 7 million DL borrowers, as well ensuring the sound fiscal management of the more than $93 billion outstanding portfolio. Prior to 2001, billions of dollars disbursed annually under the DL program were not: (1) fully reconciled to the Department's financial records; (2) verified as actually being delivered to students within the required timeframes; and (3) delivered to the DL servicer for on-going servicing within the required timeframes. Today, all disbursements are: (1) 100 percent reconciled from the date of disbursement through loan payoff; (2) verified as being delivered to the students or returned to the Department with 30 days as required; and (3) immediately delivered to the DL servicer for on-going servicing.

Inducements:

New York Attorney General Andrew Cuomo's testimony before this Committee at its recent Hearing on "Examining Unethical Practices in the Student Loan Industry" was ill informed on the Department's actions and on federal law. Any suggestion by a state attorney general that a violation of a state's law on deceptive trade practices and/or a state's fraud law would equate with an automatic violation of Title IV of the Higher Education Act (HEA) is misleading.

As Attorney General Cuomo should know, the Department has no authority to apply the HEA anti-inducement provisions to consumer credit loans that are governed by other federal regulators, including the Comptroller of the Currency, the Federal Reserve, the Office of Thrift Supervision, the Federal Deposit Insurance Corporation, and the Federal Credit Union Administration. The legal, regulatory, and supervisory framework for consumer protection specifically includes the following statutes, which collectively address the lending process, irrespective of the loan product, in terms of equal access, origination, disclosure, and privacy:

- Truth-in-Lending Act
- Fair Credit and Charge Card Disclosure Act

- Fair Credit Reporting Act
- Equal Credit Opportunity Act
- Fair Debt Collection Practices Act
- Home Equity Loan Consumer Protection Act
- Home Ownership and Equity Protection Act
- Fair Housing Act
- Real Estate Settlement Procedures Act
- Fair Credit Billing Act
- Expedited Funds Availability Act
- Truth-in-Savings Act
- Electronic Funds Transfer Act
- Consumer Leasing Act
- Gramm-Leach-Bliley Act
- Patriot Act
- Sarbanes-Oxley Act

The Department is investigating, under its authority, whether, in fact, there have been violations of the anti-inducement provisions of the HEA. Federal Student Aid already has teams performing on-site reviews of the 44 schools and 26 lender/eligible lender trustee relationship for which unethical practices have been alleged to date to determine if there have, in fact, been violations of the anti-inducement provisions of the HEA.

In addition to these efforts to address inducements, we have taken a number of steps to tighten our oversight responsibilities of federal student financial aid programs under existing regulations and within the authority the Department has been given through the congressionally-mandated process for issuing new regulations. These steps include, but are not limited to: (1) improved reporting requirements for guaranty agencies and lenders; (2) improved reporting and monitoring of the required reserve ratios that must be maintained by guaranty agencies; (3) the development of a methodology for establishing a FFELP improper payment error rate; (4) the creation of consolidated risk management scorecards for both lenders and servicers to better target oversight monitoring; and (5) the standardization of the Program Review process. In fact, many of these steps led to the removal of the federal student aid programs from the GAO High Risk List in January 2005.

As noted in my letter to Senator Edward Kennedy on April 17, 2007, the Department issued a Dear Colleague letter on March 30, 2007 reaffirming that student and parent borrowers under the FFEL program may select the lenders of their choice. Additionally, during its annual Title IV compliance training conferences in October and November of 2006, Federal Student Aid specifically addressed the importance of compliance with the anti-inducement provisions in the HEA.

While I appreciate the fact that yesterday, the House of Representatives took an important first step in this process, I determined last year that absent Congressional reauthorization of the HEA, it was my duty to address, among other issues, preferred lender lists and prohibited inducements in the FFEL program through the rulemaking process that you set up by law. Indeed, in January 2007, the Department offered draft regulatory language to strengthen existing regulations on preferred lender list practices and on inducements. Despite the Department's urging that the proposed language be adopted, the negotiated rulemaking committee did not reach consensus at their fourth and final session on Friday, April 20.

As you know, on April 24, 2007, I announced the formation of a Task Force on Student Loans to build on the negotiated rulemaking committee's work around key lender issues such as preferred lender lists, prohibited inducements, and NSLDS. This internal task force includes representatives from the Department's Office of Postsecondary Education, Federal Student Aid, and Office of the General Counsel. Representatives in the Office of Inspector General participate in an advisory role.

My Task Force just recommended new plans to strengthen the Department's original position and make it clear that:

- Unethical practices should cease and desist;
- All conduct related to student lending should be centered around borrower interests; and
- Trust and integrity must be maintained in our student aid system.

I appreciate the hard work of the Task Force and their thoughtful recommendations to protect borrowers. They have made insightful suggestions that would curb lender inducements to schools and introduce greater transparency to the practice of selecting preferred lenders. I will carefully consider these recommendations as I draft a Notice of Proposed Rulemaking (NPRM). I plan to publish an NPRM that addresses these issues in the Federal Register in the next several weeks.

Given the limited statutory authority and high threshold that the Department is required to meet in order to bring enforcement action to a school, lender, guaranty agency, or other third party, the Task Force identified areas that we will need to work with you, Chairman Miller, Congressman McKeon and others in order to strengthen the enforcement ability of the Department. I look forward to working with you on these recommendations that put an end to unethical practices, put students' needs first and maintain trust and integrity throughout the system.

On May 1, 2007, Dallas Martin, President of the National Association of Student Financial Aid Administrators (NASFAA), testified during the Subcommittee on Higher Education, Lifelong Learning, and Competitiveness hearing, "Paying for a College Education: Barriers and Solutions for Students and Families". I strongly disagree with Mr. Martin's testimony when he claims that the Department's supposed failure to identify and penalize schools for their inadequate administration of student's financial aid needs has forced schools to seek assistance from lenders, guaranty agencies, and others to print student financial aid consumer information, to perform student loan exit and entrance counseling, to establish call centers, and to provide additional staffing during peak periods in the financial aid office. In fact, for the past five fiscal years, the Department has issued schools 124 citations and assessments totaling nearly $4.4 million for lack of administrative capability--it is one of the top 10 findings in our school program reviews.

Deceptive Marketing Practices:

On May 2, 2007, this Committee asked the Federal Trade Commission (FTC) to investigate the unfair and deceptive practices that lenders use to market their products and services to students. The Committee made this request of the FTC after it had reviewed examples of lenders' unfair and deceptive marketing letters that use what appear to be official government logos and threatening language. The Department shares the Committee's concern and, in fact, over the past few years, Department staff has been communicating with the FTC staff to share information regarding potentially deceptive marketing materials from a variety of lenders. The Department joins you in calling on the FTC to examine these practices.

Reading First

Five years ago, we worked across party lines and made a commitment to have every child on grade level or above by 2014. Today, No Child Left Behind is working—shining a spotlight on student achievement and building an appetite for further change.

An integral part of this law, the Reading First program is the largest, most effective reading initiative in our nation's history. The latest data show that Reading First is producing sizable gains in fluency and comprehension for nearly two million first, second, and third graders. My Inspector General highlighted where its early implementation was flawed, and I took immediate action to correct those problems.

Let me begin by repeating what I have said since the Department of Education's Inspector General first announced the results of his Reading First investigation. We agree with the majority of the OIG's findings and have accepted all of its recommendations to prevent any future reoccurrence of administrative failures.

Flaws in the early implementation of the program must not sidetrack the good work of a critically important and successful education initiative. We have considerable evidence, including three years of continually improving assessment results, that Reading First is working as intended by Congress by building on the federally funded research base. It is expanding the use of research-based reading instruction in the early grades and significantly improving the reading skills of students in some of our historically low-achieving schools.

In short, Reading First and the students who benefit from it deserve your strong support as Congress moves forward in developing the fiscal year 2008 appropriations act and the reauthorization of No Child Left Behind.

Goals of Reading First

The goal of Reading First was to translate scientific insights into practical tools to be used in classrooms. The Federal research investment supported more than 20 years of research that followed over 44,000 children from age 5 into adulthood. Researchers at the National Institute of Child Health and Development and the Institute of Education Sciences tracked children who could read well, and they tracked others who couldn't read at all. The National Reading Panel looked at this and thousands of other high-quality scientific studies to determine what the research tells us about how children learn to read. When their work was over, our nation had gained evidence-based insights into how children read, why some of them have more trouble reading than others, and what we can do to get all children reading well.

The knowledge gained through the research was embodied in the Reading First Program designed to improve the quality of reading instruction so that all children read at grade level by the end of the third grade. The program pursues this goal through three strategies: (1) providing substantial resources at both the State and local levels for implementation of effective reading instruction in schools; (2) using reading programs and materials that are research-based, combined with high-quality professional development, to ensure that all teachers, including special education teachers, have the necessary skills to teach these researched-based reading programs effectively; and (3) using assessments to help classroom teachers screen for, identify, and overcome barriers to students' ability to read at grade level by the end of third grade.

On the issue of research-based instruction, the statute specifies that instructional methods and materials, as well as related professional development, must incorporate the five essential elements of effective primary-grade reading instruction: (1) phonemic awareness; (2) decoding; (3) vocabulary development; (4) reading fluency, including oral reading skills; and (5) reading comprehension strategies.

The need for implementation of effective strategies and methods of teaching reading is unquestioned. Though we have been pleased to report improvements in reading achievement in the early grades over the past several years, and believe that No Child Left Behind is contributing to that improvement, overall achievement levels remain alarmingly low.

Less than one-third of all 4th-graders scored at the Proficient level or above in reading on the 2005 National Assessment of Educational Progress (NAEP), and results for students in the high-poverty schools that are the focus of the Reading First program were even more discouraging. Just 16 percent of 4th-graders eligible for free or reduced-price lunch scored at the Proficient level or above on the 2005 reading assessment, and more than half (54 percent) scored below the Basic level. The 2005 NAEP reading results also highlighted the continuing achievement gaps among student groups, with the percentages of African-American students (13 percent) and Hispanic students (16 percent) scoring at the Proficient level or above falling far below that of white students (41 percent).

To help close these gaps, the Reading First State Grants program has made awards to all 50 States, and States have made subgrants to approximately 1,550 local school districts that serve an estimated 5,200 participating schools. The statute requires a comprehensive national evaluation of the Reading First program, and the Department produced the first report of that evaluation last summer. The most recent Reading First student achievement data, released in April 2007, indicate that students in Reading First schools have experienced strong gains in reading proficiency. The July 2006 *Reading First Implementation Evaluation: Interim Report* also found that districts are implementing the major elements of the program, and that Reading First schools are more likely to be implementing the program features called for in the Reading First law than are non-Reading First Title I schools.

Early Results of Reading First

While we do not yet have comprehensive impact data for Reading First, we do have considerable early evidence that the program is working as intended. This evidence comes from the most recent Annual Performance Report data: the *Interim Report* of the Department's ongoing implementation evaluation; the September 2006 report, *Keeping Watch on Reading First*, produced by the Center on Education Policy (CEP); and a March 2007 report from the Government Accountability Office (GAO).

New achievement data reported by the States in the Reading First Annual Performance Report show that Reading First students from nearly every grade and subgroup (Hispanic, African-American, students with disabilities, English language learners, and economically disadvantaged) made impressive gains in reading proficiency in 2005 and then again in 2006.

In Reading First schools, the percentage of 1st graders meeting or exceeding proficiency on Reading First fluency outcome measures increased by 14 percentage points (43% to 57%) from 2004 to 2006.

In Reading First schools, the percentage of 3rd graders meeting or exceeding proficiency on Reading First fluency outcome measures increased by 7 percentage points (36% to 43%) from 2004 to 2006.

On average, the 26 States with 2004 baseline data increased the percentage of students meeting or exceeding proficiency on fluency outcome measures by 16% for 1st graders, 14% for 2nd graders, and 15% for 3rd graders.

On average, the 26 States with baseline data increased the percentage of students meeting or exceeding proficiency on comprehension outcome measures by 15% for 1st graders, 6% for 2nd graders, and 12% for 3rd graders.

The Reading First Implementation Evaluation: Interim Report highlighted the following key findings regarding the early implementation of the Reading First State Grants program:

- Reading First schools are implementing the major statutory requirements, including the use of scientifically based reading instruction, increased reading time, interventions for struggling readers, reading assessments, and increased professional development.
- Though non-Reading First Title I schools also emphasized reading instruction, Reading First strategies (that is, strategies that reflect the research on what works in teaching children to read) were used more extensively in Reading First schools than in Title I schools.
- Reading First teachers were significantly more likely than their counterparts in non-Reading First Title I schools to place struggling students in intervention programs.
- Reading First schools were more likely than non-Reading First Title I schools to have a reading coach, and Reading First coaches were more likely to provide teachers with various supports than were coaches in non-Reading First Title I schools.

- Reading First staff received significantly more professional development than did non-Reading First Title I staff.

The changes in Reading First schools suggested by these findings contributed to the Effective rating achieved by Reading First State Grants in the 2006 Program Assessment Rating Tool (PART) process. The PART found that the Reading First program benefited from a strong program design and local management practices that appeared to help bring about improvements in student reading achievement. In particular, based on achievement data submitted by participating States, the PART found gains on all program performance measures for the 2004-2005 school year.

Between 2003-2004 and 2004-2005, the percentage of students who met or exceeded proficiency in reading on Reading First outcome measures of fluency increased:

- from 43% to 50% for first-grade students;
- from 36% to 39% for third-grade students;
- from 33% to 39% for economically disadvantaged second-grade students;
- from 27% to 32% for limited English proficient second-grade students;
- from 34% to 37% for African-American second-grade students;
- from 30% to 39% for Hispanic second-grade students; and
- from 17% to 23% for second-grade students with disabilities.

The number of States reporting an increase in the percentage of students who met or exceeded proficiency in reading on Reading First outcome measures of reading comprehension increased:

- from 2 to 14 for first grade-students (20 States had two years of data);
- from 7 to 19 for third-grade students (23 States);
- from 4 to 14 for economically disadvantaged second-grade students (20 States);
- from 5 to 6 for limited English proficient second-grade students (18 States);
- from 5 to 16 for African-American second-grade students (19 States);
- from 5 to 9 for Hispanic second-grade students (19 States); and
- from 2 to 12 for second-grade students with disabilities (19 States).

These achievement gains are all the more remarkable because the schools served by Reading First are among the lowest-performing schools in the country. The early results highlighted by the PART review suggest that comprehensive implementation of research-based reading instruction can bring about rapid improvement even in some of our worst schools.

The PART data were echoed by the CEP report, *Keeping Watch on Reading First,* which found that the program was "having a significant impact" on reading instruction in participating districts and schools. In particular, more than 90 percent of the 1,700 districts surveyed by CEP reported that the Reading First instructional program and assessment system were "important" or "very important" causes of gains in student achievement in reading.

Another critical benefit of Reading First cited by the CEP report was the use of Reading First as a school improvement strategy under No Child Left Behind. In part, this reflects the statutory requirement that States use Reading First funds to make available professional development in reading instruction to all schools, and not just those participating in Reading First. About 80 percent of States reported that offering professional development through Reading First was a key strategy for schools identified for improvement under NCLB, and a similar percentage of States said that providing curriculum and assessment materials through Reading First was a key improvement strategy. More importantly, about three-fifths of States reported that these Reading First-based strategies were "moderately or very effective in raising student achievement."

A March 2007 report from the Government Accountability Office (GAO) also indicated that States have reported that there have been a number of changes, as well as improvements, in reading instruction since the implementation of Reading First. According to the report, 69% of all States reported great or very great improvement in reading instruction since inception of Reading First.

Management Issues

My message today is that the senior leadership of the Department of Education shares the widespread public concern about these issues, and has moved decisively and rapidly to respond to the issues raised by the Inspector General. Most significantly, in last year's annual performance and accountability report to Congress and the public, I declared a material weakness for program management at the Department based in large part on the issues raised about the management of the Reading First program. The material weakness does not diminish the significant progress we have made as a Department in improving the management of our programs, but rather reminds us that our work to ensure that our programs are managed to the highest standards is not yet complete. In addition, I have instructed my senior staff to implement each of the recommendations from the Inspector General's report. More specifically, the Department has already completed more than a 20 action steps in response to those recommendations. These have included:

- Appointing Dr. Joseph Conaty, a well-respected career executive with nearly 20 years of experience at the Department of Education, to manage the program;
- Establishing an intra-Departmental group that meets regularly to help guide the implementation of the program. The group is made up of various officials within the Department, including representatives from the Office of Elementary and Secondary Education, the Office of the General Counsel, and the Office of the Chief Financial Officer;
- Expanding Reading First staff to reduce reliance on outside contractors;
- Providing guidance on ensuring fairness and objectivity in the peer review process in all formula grant programs. This guidance was specific to issues involving conflict of interest;
- Providing additional guidance to contractors and subcontractors to enhance the objectivity and effectiveness of their services, including clarifying conflict-of-interest prohibitions pertaining to the use of peer review panels and private contractors;

- Reviewing all Reading First applications to ensure compliance with funding criteria. This review determined that the majority of State applications had the appropriate documentation. The Department is continuing to work with the additional States to resolve any remaining issues; and
- Conducting outreach to States on potential concerns about Reading First issues. To date, the Department has received 25 letters from States. 16 of those letters said only positive things about the Reading First program. An additional 13 States responded that they either had no concerns or did not intend to write a letter. We remain committed to working with all States to address any concerns they may have about the program.

In addition, the new Reading First program director, together with representatives from the Office of Inspector General and the Office of the General Counsel, delivered a presentation at the end of January to the National Association of State Title I Directors on the "lessons learned" from the IG's findings, including on the implementation of new internal controls designed to ensure the integrity of the grant application process. This presentation also described steps that the Department is taking to ensure that our officials, consistent with the Department of Education Organization Act, do not take actions that could be interpreted as directing or controlling State and local curriculum decisions.

I have also developed a charter for the peer review panel in Reading First that would further strengthen the program's implementation in line with the Federal Advisory Committee Act. This panel would help the Department review issues that arise with State applications for Reading First and evaluate the third-year progress reports from the States. A notice of intent to establish this panel in accordance with the Federal Advisory Committee Act was published in the Federal Register on March 1, 2007.

We believe that these comprehensive actions will help restore public confidence in the Department's ability to fairly and impartially administer the Reading First State Grants program, and allow us to build on the progress that States, school districts, and schools have made under this program in improving reading instruction in the early grades.

I urge the Members of this Committee to look at the entire record, and not just the recent headlines, as you evaluate the progress of Reading First and consider changes during the upcoming budget and reauthorization debates. If you do, I think you will agree that Reading First, with its emphasis on research-based instruction in the critical early years, is one of our best tools to ensure that all students receive a high-quality education, and it that merits your strong support.

I would also like to take this opportunity to thank Congressman McKeon and Congressman Castle for introducing H.R. 1939, the Reading First Improvement Act. This legislation goes a long way toward addressing many of the concerns about the early implementation of Reading First. I look forward to continuing to work with Mr. McKeon, Mr. Castle, and other members of the Committee to strengthen Reading First.

Conclusion

Where the law needs changing, let's do it. And where families need our help, let's provide it. Together, we can enact policies that better prepare more students for college… and help make sure they can afford it once they get there!

But together, we can and must do more. From K-12 to higher education, you and I now have an opportunity to enact meaningful new policies that make a real difference for students and families--just as we did 5 years ago.

There's no time to wait. Nearly two-thirds of all high-growth, high-wage jobs created in the next decade will require a college degree—a degree that only one third of Americans have. I stand ready to work with you to make a real difference in the lives of the people we're all here to serve.

Thank you. I would be happy to answer your questions.