Management's Discussion and Analysis

OUR MISSION AND HISTORY

Mission. The U.S. Department of Education's (the Department's) mission is *to promote student achievement and preparation for global competitiveness by fostering educational excellence and ensuring equal access*.

History. The federal government recognized that furthering education is a national priority in 1867, creating a federal education agency to collect and report statistical data. The Department, established as a cabinet-level agency in 1979, celebrated its 30th anniversary during FY 2009. Today the federal role has grown to include federal support for education, including student financial aid, supporting education research and providing information on what works to teachers, education policymakers and parents. For a chronology of education legislation, go to: http://nces.ed.gov/pubs2009/2009020_4.pdf.

The Department is committed to ensuring students develop the skills they need to succeed in school, college and the workforce, while recognizing the primary role of states and school districts in providing a high-quality education, employing highly qualified teachers and administrators and establishing challenging content and achievement standards. The Department is also setting high expectations for its own employees and working to improve management practices, ensure fiscal integrity and develop a culture of high performance.

WHO WE SERVE: OUR PUBLIC BENEFIT

Every American has a stake in the nation's educational success. The Department's Web site and print resources focus on our primary customers—

Students—See more on Departmental services to students at http://www.ed.gov/students/landing.jhtml.

Teachers—See more details on Departmental services for teachers at http://www.ed.gov/teachers/landing.jhtml.

Parents—See more details on Departmental services for parents at http://www.ed.gov/parents/landing.jhtml.

State and Local Educational Agencies—For a list of state agencies, see http://www.ed.gov/about/contacts/state/index.html?src=gu.

Administrators—Principals, superintendents and other administrators are at the center of school reform and accountability efforts. See more details at http://www.ed.gov/admins/landing.jhtml.

Postsecondary Students and Institutions—The Department provides assistance through programs such as the Federal Pell Grant Program, the Federal Family Education Loan (FFEL) Program, the William D. Ford Federal Direct Loan Program, the Federal Perkins Loan Program and the Federal Work-Study Program, authorized under Title IV of the *Higher Education Act of 1965,* as amended (*HEA*). See more details on student financial aid at http://www.ed.gov/finaid/landing.jhtml?src=rt.

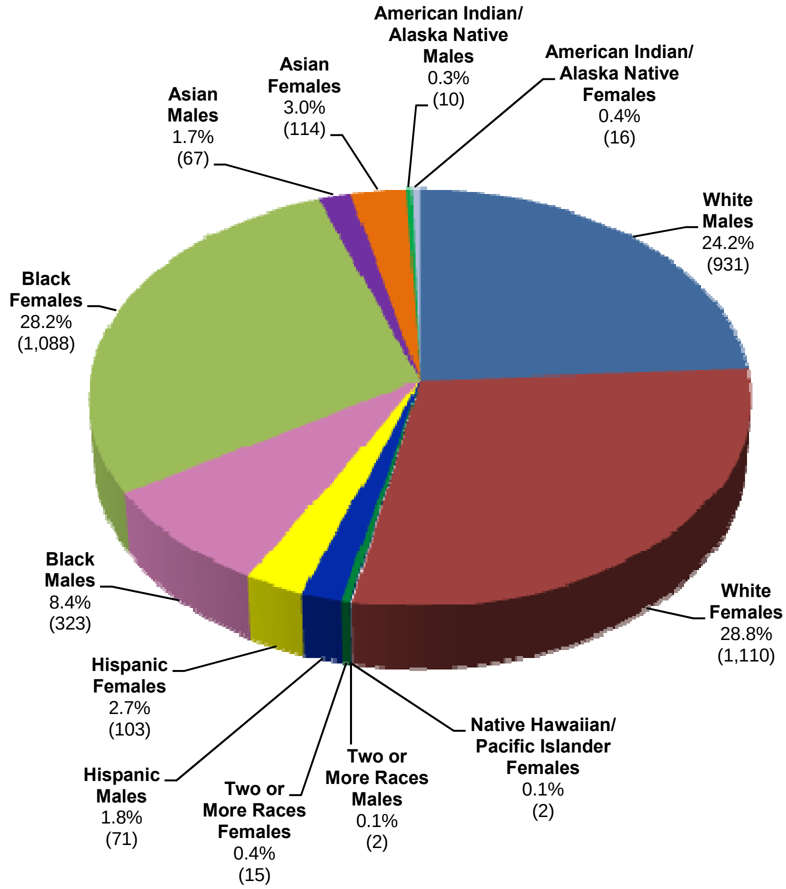
WHO WE ARE: OUR ORGANIZATION AND WORKFORCE

Department of Education Workforce Makeup

Department of Education Workforce Composition as of September 26, 2009

- Total Workforce = 4,225
- 3,852 Permanent Employees
- 373 Temporary Employees
- 62 percent (2,634) Female
- 38 percent (1,591) Male

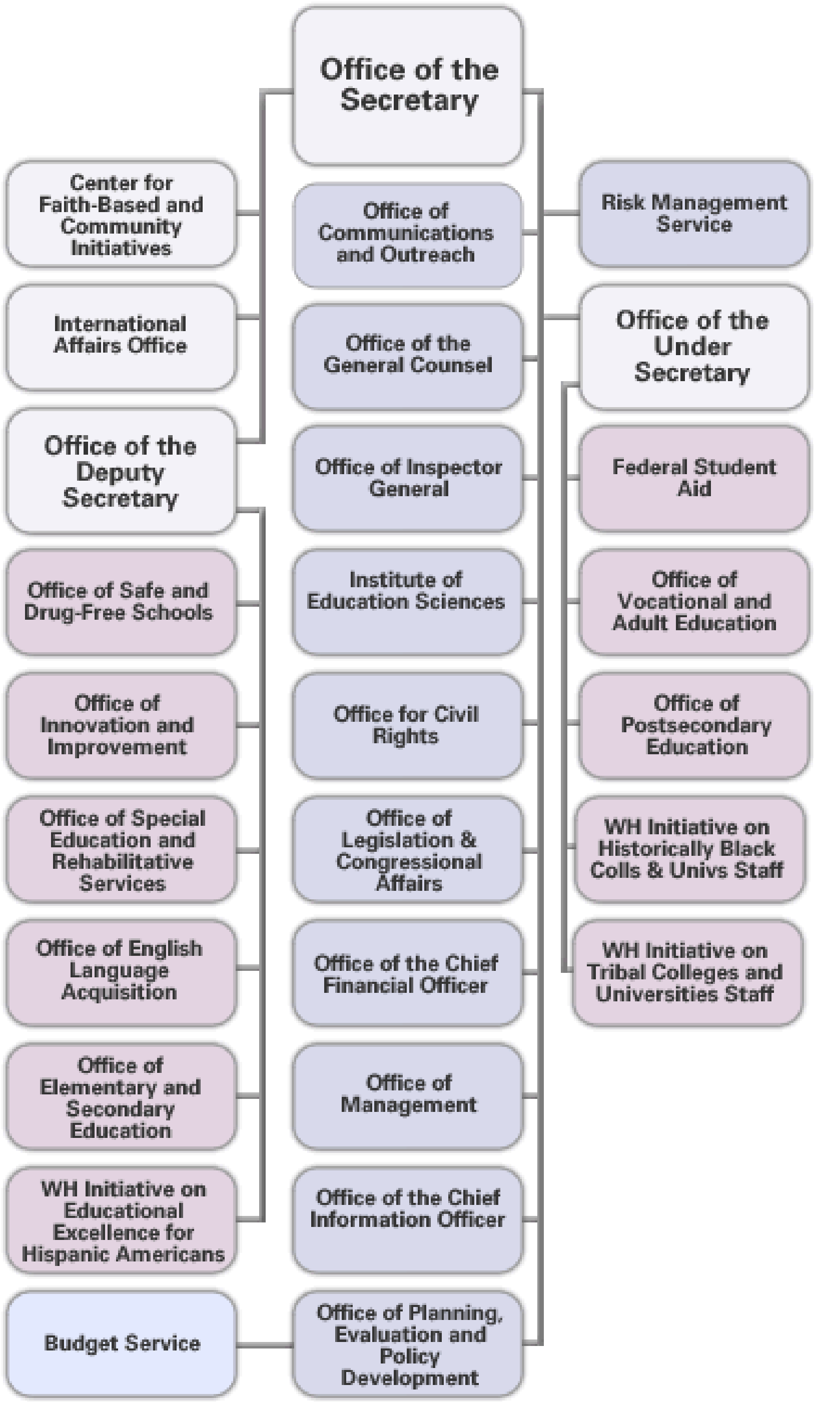
Department of Education Permanent Workforce by Ethnicity and Gender as of September 26, 2009



NOTE: Numbers may not add to 100 percent due to rounding.

Source: Annual Equal Employment Opportunity Status Report: An Equal Employment Opportunity Management Directive (MD) 715 Requirement for the Period covering October 1, 2008 Through September 26, 2009.

Department of Education Coordinating Structure FY 2009



For additional information about the principal components of the Department of Education, please go to: http://www.ed.gov/about/offices/list/index.html?src=ln.

LINKING TAXPAYER DOLLARS TO PERFORMANCE RESULTS: ACCOUNTABILITY THROUGH THE INTEGRATION OF RESULTS WITH INVESTMENT

Our emphasis on sound financial practices, performance results and program accountability reflects a strong desire to use taxpayers' dollars as effectively as possible. The Department strives to tie the performance of our programs with budget requests and to strengthen the link between financial investments and program quality.

In order to tie performance to budget submissions, federal agencies are required to identify a number of high-priority performance goals to further the administration's agenda for building a high-performing government and identify strategies and a means to achieve them. The draft goals are expected to be completed in FY 2010.

Linking Program Performance With Budget Submissions

The Department participates closely with the Performance Improvement Council (PIC) to establish guidelines and metrics to more closely align program and management performance with Budget requests. The Office of Management and Budget established the PIC in FY 2007 under *Executive Order 13450: Improving Government Program Performance* as a tool to spend taxpayers' dollars more effectively and with greater accountability.

The PIC is composed of senior staff from each federal agency who are responsible for coordinating areas of performance management activities, such as ensuring that data from annual performance plans and reports are used in agency budget justifications. Collectively, the PIC is tasked with establishing program performance standards and evaluation criteria, exchanging information among agencies, coordinating and monitoring performance assessments, keeping the public informed, obtaining advice from stakeholders and making policy recommendations.

Additionally, *GPRA* requires agencies to develop annual program performance plans that include challenging performance metrics that can be used to judge the effectiveness of each program. Programs deemed ineffective or that are not delivering results based on established performance measures are reviewed for inclusion in the Department's annual budget submission to Congress.

To further our commitment to provide more effective oversight for our fiscal resources, the Department has identified a senior manager for performance management systems in the Office of the Deputy Secretary to oversee the furtherance of accountability for results for both our strategic priorities and our internal management processes. In addition, the administration has appointed a Deputy Assistant Secretary for Performance Improvement—a position housed in the Department's Office of Management.

Performance Evaluations Improve Accountability

Each year, the Department publishes evaluations of selected programs to further demonstrate accountability for the taxpayers' investment in education spending. These evaluations serve to identify best practices as well as programs that cannot demonstrate accountability for results, as well as to inform senior management about programs in need of additional support. The Department uses evaluations to identify programs that should be eliminated from the budget or recommended for reduced funding. The Department also uses evaluations to support budget requests for increases in program funds. Several offices in the Department have the responsibility for designing and implementing evaluations of program and management activities and operations. Those offices include the Institute of Education Sciences (IES) and the Office of Planning, Evaluation and Policy Development (OPEPD). Additionally, the Department's Office of Inspector General (OIG) and the Government Accountability Office (GAO) audits and reports provide guidance and feedback on improvements in management and program operations. Finally, the Department provides guidance to grant recipients on developing evaluations based on scientifically rigorous evidence. More detail is available at: http://ies.ed.gov/ncee/pubs/evidence_based/evidence_based.asp.

Ensuring Accountability and Oversight of *Recovery Act* Funds

The Risk Management Service (RMS), in the Office of the Secretary, is responsible for Departmentwide grants policy related to identifying and working with high-risk grantees to minimize risk to federal funds that may adversely affect the advancement of the Department's priority goals.

In FY 2009 RMS took a two-phased approach to providing technical assistance to states receiving *Recovery Act* funds. The first phase targets states that received the most *Recovery Act* money and were identified as having fiscal and programmatic concerns. RMS is coordinating the provision of technical assistance to states based on basic federal grants in fiscal management requirements, such as cash management, internal controls, procurement, allowable activities, data quality and sub-recipient monitoring. In its second phase, RMS has developed a regular series of *Recovery Act* technical assistance Web conferences to enhance the ongoing provision of oversight and technical assistance to grantees receiving *Recovery Act* funds to ensure that they are held accountable to the taxpayer and that these and other Department grant funds are spent appropriately.

Cost Saving Measures Underway at the Department

A major priority of the new administration is to ensure that federal agencies control costs and conduct their internal lines of business to be as effective and efficient with the use of the taxpayers' dollar as possible. The Department has undertaken measures to evaluate and implement administrative cost-saving opportunities that have already realized immediate savings and costs avoided, as well as longer-term plans that will realize additional savings in years to come. The Department has identified a number of cost saving measures that include equipment consolidation, reduction in contract and travel costs, eliminating extraneous office space and consolidating teleconferencing facilities and conference spaces. Additional cost-saving measures are under review for FY 2010.

HOW WE VALIDATE OUR DATA

The *Government Performance and Results Act of 1993 (GPRA)* requires federal departments and agencies to clearly describe the goals and objectives of their programs, identify resources and actions needed to accomplish goals and objectives, develop a means of measuring progress made and report regularly on achievement. The goals of the act include improving program effectiveness by promoting a focus on results, service quality and customer satisfaction; improving congressional decision making by providing objective information on achieving statutory objectives; and focusing on the relative effectiveness and efficiency of federal programs and spending.

Consolidating Data Collections Through ED*Facts*

Complete, accurate and reliable data are essential for effective decision-making. Given the requirements of the *Elementary and Secondary Education Act of 1965* (*ESEA*), as amended, accuracy of state and local educational agency performance data is crucial to funding decisions and management actions are taken on the basis of this performance information.

The mandatory regulation requires states to electronically submit data to the Education Data Exchange Network Submission System (EDENS), a centralized, Internet-based system of elementary and secondary education data (K-12) from 52 state education agencies. Data are available for state and local education agencies. School data include demographics, program participation, implementation and outcomes.

ED*Facts* became the mandatory system for states to electronically report their K–12 education data to the Department starting in school year (SY) 2008–09. The ED*Facts* system enabled the consolidation of historically separate data collection efforts, and the increased amount of data in ED*Facts* allows for even greater data collection efficiencies. The Department is using the ED*Facts* Metadata and Process System to collect each state's plan for transitioning from reporting using five racial and ethnic categories to using seven. For SY 2008–09, the collection was optional; if a state has not entered a plan, it was assumed that five categories were used for the school year.

By using the Education Data Exchange Network Submission System and ED*Facts* Metadata and Process System together, ED*Facts* is able to reduce the reporting burden for states by eliminating redundant data requests for multiple data collections. This approach also provides program offices with the ability to retire paper-based collections and improve data quality by relying solely on electronic reporting methods. In the future, the ED*Facts* initiative will employ similar strategies to increase the efficiency of data acquisition methods across the Department.

The Validation and Verification of Performance Data

OMB Circular A-11, Part 6, section 230.5, *Assessing the completeness and reliability of performance data,* requires each agency to design a procedure for verifying and validating data that it makes public in its annual performance plans and reports.

Additionally, *GPRA* prescribes the means to verify and validate measured values. Finally, the *Reports Consolidation Act of 2000* requires that the transmittal letter included in annual performance reports contains an assessment by the agency head of the completeness and reliability of the performance data included in its plans and reports.

In response, the Department has developed a guidance document to assist principal offices responsible for reporting data on strategic and program performance measures to address issues of data integrity and credibility. The guidance provides a framework for validating and verifying performance data before it is collected and reported and is used to evaluate data prior to publication for review by the public. Additionally, the Department has developed a worksheet for each program office to use to identify the validity of the data for their unique program performance measures.

The Department's data validation criteria require that program goals and measures are:

- appropriate to the mission of the organization and that measured performance has a direct relation to the goal;
- realistic and measurable, achievable in the time frame established and challenging in their targets;
- understandable to the lay person and terminology is adequately defined; and
- used in decision-making about the effectiveness of the program and its benefit to the public.

For more information on the guidance and its implementation and to review the worksheet, go to http://www.ed.gov/about/reports/annual/index.html.

The Institute of Education Sciences Data Quality Initiative

The Data Quality Initiative of the Department's Institute of Education Sciences, begun in 2006, is designed to improve the Department's program performance data and reporting in support of the goals of *GPRA.* Technical assistance is being provided to approximately 30 Department grant programs.

Activities for Department program offices include reviewing grantee evaluation plans and reports; developing annual performance reporting forms; analyzing grantee annual performance data; and developing briefings and workshops focused on evaluation strategies. In 2008 and 2009, the initiative was expanded to include programs covering a wide range of elementary and secondary education topics and populations. See http://ies.ed.gov/ncee/projects/evaluation/assistance_data.asp for more details.

The National Forum on Education Statistics

The National Forum on Education Statistics, sponsored by the Department's National Center for Education Statistics, is a voluntary, participative and cooperative federal-state-local body with a mission to develop and recommend strategies for building an education data system that will support local, state and national efforts to improve public and private education throughout the United States. See more details at http://nces.ed.gov/forum/data_quality.asp.

OUR ACCOMPLISHMENTS AND ONGOING INITIATIVES FOR FY 2009

The American Recovery and Reinvestment Act of 2009

Overview

The *Recovery Act* was signed into law by President Barack Obama on February 17, 2009. It is an unprecedented effort to jumpstart our economy, create or save millions of jobs and put a down payment on addressing long-neglected challenges so that our country can thrive in the 21st century. To see how *Recovery Act* funds are helping your state, visit http://www.ed.gov/policy/gen/leg/recovery/state-fact-sheets/index.html.

The *Recovery Act* invests heavily in education.

- The act included a total of $98.2 billion to the Department for supplemental appropriations for reforms to strengthen elementary, secondary and higher education, including money to stabilize state education budgets and to encourage states to:
  - make improvements in teacher effectiveness and ensure that all schools have highly qualified teachers;
  - make progress toward college and career-ready standards and rigorous assessments that will improve both teaching and learning;
  - improve achievement in low-performing schools, through intensive support and effective interventions; and
  - gather information to improve student learning, teacher performance and college and career readiness through enhanced data systems.
- The act provides competitive funds to spur innovation and chart ambitious reform to close the achievement gap.
- The act addresses college affordability and improves access to higher education.
- The act includes early learning programs, including child care and programs for children with special needs.

> ***Recovery Act* Successes**
>
> **Orange County Public Schools, Florida**
>
> As part of the *Recovery Act*'s efforts to impact education across the country, Florida has felt the impact of more than $3.1 billion in education funds. This includes nearly $2 billion in State Fiscal Stabilization Funds that has kept more than 25,000 teachers and staff in Florida's classrooms and maintained other essential services, over $335 million to provide special education and related services to children with disabilities under the *Individuals with Disabilities Act* (*IDEA*) and $245 million to Title I schools.
>
> Orange County Public Schools, the 11th largest school district in the nation and encompassing all of Orlando's public schools, says they have preserved more than 1,600 teachers, nurses, counselors, tutors and other essential staff due to $132 million from the *Recovery Act*.

Department Programs Receiving *Recovery Act* Funding

Race to the Top

The $4.35 billion Race to the Top Fund is the largest ever federal competitive investment in school reform. It will reward states for past accomplishments and create incentives for future improvements. The funding criteria that the Department proposes to use will challenge states to create comprehensive strategies for addressing the four central areas of reform that will drive school improvement:

- adopting internationally benchmarked standards and assessments that prepare students for success in college and in the workplace;
- recruiting, developing, retaining and rewarding effective teachers and principals;
- building data systems that measure student success and inform teachers and principals how best to improve their practices; and
- turning around our lowest-performing schools.

To read more about the Race to the Top Fund, visit http://www.ed.gov/programs/racetothetop/factsheet.html.

Recovery Act **Successes**

Richmond County School District, North Carolina

With the decline in state revenues in North Carolina, the Richmond County School District will lose over $3 million in support for education programs, staffing, professional development and other critical needs. The cuts threaten to diminish district efforts to pursue new academic models that have proven reform results. Even with recent state budget action, resource projections are on the decline.

How *Recovery Act* Funds Are Being Used: Budget reductions at the state level caused the district to face a loss of 40 positions across the system from teachers to support staff. The local educational agency's share of *Recovery Act* funds will permit the superintendent to restore a share, but not all, of these positions critical to the teaching, learning and support functions of the districts and its schools.

The one-time increase in *Individuals With Disabilities Education Act* (*IDEA*) funds is permitting the district to implement new teaching and learning strategies for students with special needs that will accelerate efforts to attain grade-level performance and academic achievement.

The one-time increase in Title I funds permits the district to invest in new strategies that promote a districtwide commitment to creating and sustaining professional learning communities. This long-range effort was in serious jeopardy of being curtailed with the loss of funds due to the downturn in the state economy.

Recovery Act funds will also be used in part to secure a state-of-the-art library facility that will be used by all district students and include access to updated technology for teaching and learning, self-directed learning and after-school programs. Without these funds, consideration of these improvements in education resources would not be possible.

Investing in Innovation

To be eligible for this $650 million competitive grant program, local educational agencies (LEAs), including charter school LEAs, and nonprofit organizations working in collaboration with one or more LEAs or a consortium of schools must have made progress in raising student achievement, significantly closing the achievement gap and made progress in other areas. For more information, see http://www.ed.gov/programs/innovation/factsheet.html.

Teacher Incentive Fund

The $200 million Teacher Incentive Fund supports state and district efforts to develop and implement performance-based teacher and principal compensation systems in high-need schools, primarily through grants to school districts and consortia of school districts. Under the compensation systems in place in virtually all school districts, teacher salaries increase based on a teacher collecting graduate credit for additional study, increasing number of years on the job or moving out of the classroom into an administrative position. These pay systems often place high-poverty schools at a disadvantage in recruiting effective teachers. The Teacher Incentive Fund supports a variety of performance-based teacher and principal compensation systems that reward teachers and principals for increases in student achievement and boost the number of effective instructors teaching in hard-to-staff subjects and in high-need schools. For more information, see http://www.ed.gov/programs/teacherincentive/factsheet.html.

Teacher Quality Partnership

The $100 million Teacher Quality Partnership program is designed to improve the quality of new teachers by creating partnerships among high-need school districts and schools or high-need early childhood education program. These partnerships create model teacher preparation programs at the pre-baccalaureate level. For more information, see http://www.ed.gov/programs/tqpartnership/index.html

State Longitudinal Data Systems

This $250 million *Recovery Act* program provides grants to states to design, develop and implement statewide longitudinal data systems to capture, analyze and use student data from preschool to high school, college and the workforce. The *Recovery Act* requires that the data systems have the capacity to link preschool, K–12 and postsecondary education as well as workforce data. To receive State Fiscal Stabilization Funds, a state must provide an assurance that it will establish a longitudinal data system that includes the 12 elements described in the *America Creating Opportunities to Meaningfully Promote Excellence in Technology, Education and Science Act* (or the *America COMPETES Act*). For more information, see http://www.ed.gov/programs/slds/factsheet.html.

Title I School Improvement Grants

Title I School Improvement Grants provide states and school districts funds to leverage change and turn around Title I schools identified for improvement, corrective action or restructuring. Authorized under *ESEA* in 2002, the program did not receive funding until FY 2007. The current $3 billion provides an unprecedented opportunity for states and school districts to implement significant reforms to transform their chronically lowest-achieving schools.

Under *ESEA,* states and school districts are required to restructure Title I schools that fail to make adequate yearly progress for five years. Reports indicate that the least rigorous interventions allowable have shown little success in turning around these chronically low-achieving schools, and that the program should be better targeted on the very lowest-performing schools. For more information, see http://www.ed.gov/programs/sif/factsheet.html.

State Educational Technology Grants

The primary goal of the $650 million Educational Technology Grants program is to improve student academic achievement through the use of technology in schools. It is also designed to help ensure that every student is technologically literate by the end of eighth grade and to encourage the effective integration of technology with teacher training and curriculum development. For more information, see http://www.ed.gov/programs/edtech/factsheet.html.

The *Recovery Act* programs provide an unprecedented opportunity for states, districts and schools to use innovative strategies to enhance instruction, facilitate teaching and learning and improve student achievement. They will enable districts to acquire new and emerging technologies, create state-of-the-art learning environments and offer new training and more support for teachers so that students acquire the range of skills they will need to compete in a global economy.

State Fiscal Stabilization Fund

The State Fiscal Stabilization Fund (SFSF) provides a total of approximately $48 billion directly to governors to help save jobs and drive education reform. The Department is awarding SFSF funds in two phases. In Phase I, states submitted applications for approximately $35.4 billion; in Phase II, states are applying for the remainder of about $12.6 billion.

In Phase I applications, state governors were required to assure that their states would take action and make progress in four areas of education reform:

- adopting internationally benchmarked standards and assessments that prepare students for success in college and the workplace;
- recruiting, developing, rewarding and retaining effective teachers and principals;
- building data systems that measure student success and inform teachers and principals how they can improve their practices; and
- turning around our lowest-performing schools.

In Phase II applications, governors are required to provide data in each of these four areas of reform. States would not need to demonstrate progress on the indicators in order to get funds; instead, states would ensure that the information is in place so that parents, teachers and policymakers know where our schools and students stand. If a state cannot provide the data, it would be required to submit a plan for ensuring that this information will be publicly reported as soon as possible. For more information, see http://www.ed.gov/programs/statestabilization/applicant.html and http://www.ed.gov/programs/statestabilization/factsheet.html.

School Modernization

Funds from the SFSF under the *Recovery Act* may be used for modernization, renovation or repair of public school facilities and institutions of higher education facilities. The School Construction Tax Credits may be used for the construction, rehabilitation or repair of a public school facility or for the acquisition of land on which such a facility is to be constructed. For more details, visit http://www.ed.gov/policy/gen/leg/recovery/modernization/index.html.

Title I, Part A *Recovery Act* Funds for Grants to Local Educational Agencies

The *Recovery Act* provides significant new funding for programs under Title I, Part A of *ESEA*. Specifically, the *Recovery Act* provides $10 billion in additional FY 2009 Title I, Part A funds to LEAs for schools that have high concentrations of students from families that live in poverty to help improve teaching and learning for students most at risk of failing to meet state academic achievement standards. These funds create an unprecedented opportunity for educators to implement innovative strategies in Title I schools that improve education for at-risk students and close the achievement gaps. The additional resources will enable local educational agencies to serve more students beyond the approximately 20 million currently served and boost the quality of teaching and learning. Final allocations of Title I, Part A *Recovery Act* funds to each state and local educational agency are available at http://www.ed.gov/about/overview/budget/statetables/index.html

Individuals with Disabilities Education Act (IDEA), Parts B and C

"We're here today to talk about keeping teachers in the classroom—where they belong. The ultimate foundation for our nation's future is a well-educated child. And every day, the *Recovery Act* is helping educators, parents and students work together to build the best possible foundation for the 21st century."
—Vice President Joe Biden

The *Recovery Act* appropriates significant new funding for programs under Parts B and C of the *IDEA*. Part B of the *IDEA* provides funds to state and local educational agencies to help them ensure that children with disabilities—including children aged 3 through 5—have access to a free, appropriate public education to meet each child's unique needs and prepare him or her for further education, employment and independent living.

Part C of the *IDEA* provides funds to each state lead agency designated by the state's governor to implement statewide systems of coordinated, comprehensive, multidisciplinary interagency programs and make early intervention services available to infants and toddlers with disabilities and their families.

The *IDEA* funds under the *Recovery Act* will provide an unprecedented opportunity for states, local educational agencies and early intervention service providers to implement innovative strategies to improve outcomes for infants, toddlers, children and youths with disabilities. Under the *Recovery Act*, the *IDEA* funds are provided under three authorities: $11.3 billion is available under Part B Grants to States, $400 million under Part B Preschool Grants and $500 million under Part C Grants for Infants and Families. Information about each state's allocation is available at http://www.ed.gov/about/overview/budget/statetables/index.html.

Vocational Rehabilitation State Grants

The *Recovery Act* appropriates significant new funding for the Vocational Rehabilitation (VR) State Grants program, authorized under Title I of the *Rehabilitation Act of 1973,* as amended (*Rehabilitation Act*). The VR State Grants program provides grants to states to help individuals with disabilities—especially those individuals with the most significant disabilities—prepare for, obtain and maintain employment.

The *Recovery Act* provides an unprecedented opportunity for states and vocational rehabilitation agencies to implement innovative strategies to improve employment outcomes for individuals with disabilities. Under the *Recovery Act*, $540 million is provided for the VR State Grants program. Information about each state's formula allocation is available at http://www.ed.gov/about/overview/budget/statetables/index.html.

Independent Living Services and Centers for Independent Living

The *Recovery Act* appropriates significant new funding for the Independent Living (IL) programs authorized under Title VII, Chapter 1, Part B and Part C and Chapter 2 of the *Rehabilitation Act* and for the Centers for Independent Living Program authorized under Title VII, Chapter 1, Part C of the *Rehabilitation Act*.

The Independent Living programs support services to individuals with significant disabilities and older individuals who are blind. Under the *Recovery Act*, $52 million is provided under separate authorities. Information about each state's formula allocation under these authorities is available at http://www.ed.gov/about/overview/budget/statetables/index.html.

The Centers for Independent Living Program supports nonprofit, consumer-controlled, community-based, cross-disability, nonresidential centers for independent living centers that provide an array of independent living services to individuals with significant disabilities. Under the *Recovery Act*, $87.5 million is provided under the program authority. Information about each state's allocation under the program is available at http://www.ed.gov/about/overview/budget/statetables/index.html.

McKinney-Vento Homeless Assistance

The *Recovery Act* provides $70 million under the McKinney-Vento Education for Homeless Children and Youth program, which is authorized under Title VII-B of the *McKinney-Vento Homeless Assistance Act*. The *McKinney-Vento Recovery Act* funds are a one-time source of funds that supplement the McKinney-Vento funds made available under the regular FY 2009 appropriation. These additional resources will assist states and local educational agencies in addressing the educational and related needs of some of the most vulnerable members of our society—homeless children and youth—during a time of economic crisis in the United States. For more information, see http://www.ed.gov/programs/homelessarra/index.html.

Impact Aid

The *Recovery Act* appropriated $100 million in new funding for Impact Aid under section 8007 of Title VIII of *ESEA*. After reserving 1 percent of the appropriation for management and oversight, the Department awarded $39.6 million to 179 local educational agencies that are eligible as a result of their enrollment of certain numbers and types of federally connected children for whom they receive funds under section 8003 of the Impact Aid Program (Basic Support Payments).

Payments are made based on the number of eligible federally connected children in average daily attendance who are dependents of members of the uniformed services and children living on Indian lands. For more information, see http://www.ed.gov/policy/gen/leg/recovery/factsheet/impactaid.html.

Student Financial Assistance

The *Recovery Act* appropriated $16.5 billion for Federal Pell Grants and Federal Work Study. These additional funds were part of the national effort to increase the affordability of postsecondary education for needy students.

New Initiatives in Federal Student Aid

In 2008, amid unprecedented disruptions in the private credit markets, the Department developed and successfully implemented an aggressive plan to ensure uninterrupted access to federal student loans. This plan included the use of new statutory authority to purchase FFEL loans, providing lenders with the liquidity needed to make new loans, the expansion of the Department's capacity to originate and service loans under the William D. Ford Federal Direct Student Loan Program and the strengthening of the FFEL Lender of Last Resort program. As a result of these efforts, which were continued in 2009, students and families were able to obtain over $84 billion in loans for the 2008–2009 school year smoothly and without significant disruption.

Beginning in August 2008, the Department implemented a number of programs authorized under the *Ensuring Continued Access to Student Loans Act of 2008* (*ECASLA*) to ensure credit market disruptions did not deny eligible students and parents access to federal student loans for the 2008–2009 academic year. The *ECASLA* authority, which originally expired on September 30, 2009, was subsequently extended through September 30, 2010, to continue to ensure unfettered access to loans through the 2009–2010 academic year. Programs authorized under *ECASLA* are summarized below.

Loan Participation and Loan Purchase Programs. Under these programs, lenders may access capital to make new loans either by selling eligible FFEL loans directly to the Department or by selling the Department participation interests in eligible FFEL loans. Lenders that sell loans or participation interests in loans must represent to the Department that they will continue to participate in the FFEL Program and that when funds become reasonably available from private sources on affordable terms, they will make new loans or acquire new loans made by other lenders. Participation interests on loans made for the 2008–2009 academic year had to have been redeemed, with interest, by lenders no later than October 15, 2009, either in cash or by selling the underlying loans to the Department; for loans made for academic year 2009–2010, the deadline for redemption is September 30, 2010. Through September 2009, the Department directly purchased over 5 million loans valued at approximately $24 billion. Through September 2009, the Department acquired more than $41 billion in participation interests in FFEL Program loans.

Short-Term Loan Purchase Program. From December 2008 through March 2009, the Short-Term Loan Purchase Program purchased eligible loans made for the 2007–2008 academic year. Under this program, the Department purchased 280,000 loans worth roughly $1 billion.

Asset-Backed Commercial Paper Conduit Program. The Asset-Backed Commercial Paper Conduit Program was developed to provide additional liquidity to support new lending. Under this program, which began operations mid 2009, the Department entered into forward purchase commitments with a conduit. The conduit issues commercial paper backed by qualifying student loans made between October 1, 2003 and September 30,

2009. If the conduit is unable to retire this paper as it matures, the Department commits to provide the needed funds by purchasing the underlying student loans.

Lender of Last Resort. The *Higher Education Act of 1965* requires guaranty agencies (GAs) to make loans as a Lender of Last Resort to those students who are unable to obtain FFEL loans from conventional FFEL lending sources. GAs may arrange for a conventional FFEL lender to make Lender of Last Resort loans or may make loans directly with their own resources. The Department may advance funds to a GA to make lender of last resort loans if that GA cannot arrange for such lending by another party and lacks other resources sufficient to make the needed loans. The Department will require that any federal advances be deposited in the GA's Federal Fund and that loans made from those funds be assigned to the Department promptly after they are disbursed. The Department has not made federal advances for Lender of Last Resort loans in FY 2009 and none are currently anticipated for FY 2010.

> "Time and again, when we placed our bet for the future on education, we have prospered as a result—by tapping the incredible innovative and generative potential of a skilled American workforce . . . . That's why, at the start of my administration, I set a goal for America: by 2020, this nation will once again have the highest proportion of college graduates in the world."
>
> *—President Obama*

Making College Affordable and Accessible

Today's new initiatives complement President Obama's existing agenda for higher education. At this time of economic hardship and uncertainty, the administration's agenda will build the country's capacity, innovation and confidence to drive the nation to first place in the highly skilled workforce crucial for success in the 21st century. These initiatives include:

- **Expanding Pell Grants and College Tax Credits:** The *Recovery Act* increased Pell Grants to $5,350 and created the $2,500 American Opportunity Tax Credit for four years of college tuition.
- **Reforming the Student Loan Program to Save Billions:** The administration has proposed to replace guaranteed loans with Direct Loans, which are originated and serviced by private-sector companies selected through a competitive process and paid based upon performance. Direct Loans have essentially the same terms for students and are more reliable and efficient.
- **Helping Unemployed Workers Get New Skills:** President Obama has expanded opportunities for unemployed workers to go to community colleges and learn new skills. The Department has clarified that these workers should not be denied student aid based upon incomes they no longer earn, and the Department of Labor is working with states to allow workers to keep their unemployment benefits while receiving education and training.
- **Expanding the Perkins Loan Program:** The low-cost Perkins Loan Program is an important option for students who need to borrow more than what is allowed under the larger Stafford Loan Program. The administration will expand it from $1 billion per year to $6 billion per year.
- **Helping Families Save for College:** The President's Middle Class Task Force has directed the Department of the Treasury to investigate improvements to savings plans to help families save for college more effectively and efficiently.

TEACH Grant Program. Authorized by the *College Cost Reduction and Access Act of 2007 (CCRAA)*, the Teacher Education Assistance for College and Higher Education (TEACH) Grant Program offers grants of up to $4,000 to students agreeing to teach math, science or other specialized subjects in a high-poverty school for at least four years within eight years of their graduation. If students fail to fulfill the service requirements, grants turn into Unsubsidized Stafford Loans, with interest accrued from the time of the grant award.

Because the grants turn into loans when the service obligations are not satisfied, budget and accounting treatment for TEACH Grants is consistent with the *Federal Credit Reform Act of 1990*. Subsidy costs reflecting the net present value of grant costs less the expected future loan payments are recorded in the TEACH Grant Program Account. In FY 2009, the Department disbursed approximately 15,000 grants for almost $44 million under TEACH.

Streamlining Student Financial Aid

The President has challenged the nation to once again have the highest percentage of college graduates in the world; to do that we need to send a clear message to both young people and adults that college is within their reach. More than a million students fail to apply for aid because of the application's complexity. The Department is simplifying the financial aid process by modernizing the online application, seeking legislation that will eliminate unnecessary questions and creating an easy process for students to use tax data to apply.

By developing a more user-friendly FAFSA that will make it easier to apply for college financial aid and increase postsecondary enrollment, particularly among low- and middle-income students, the Department is providing instant estimates of Pell Grant and student loan eligibility, easier navigability and seamless retrieval of tax information. See http://www.fafsa.ed.gov/ for more information.

Help for Those Burdened by Student Loan Debt

Through the *College Cost Reduction and Access Act of 2007,* Congress created the Public Service Loan Forgiveness Program. The program is designed to encourage young people to serve the public by working for federal, state or local governments, nonprofits or other public employers. Under this program, people with student loans can have their debts erased after 10 years of public service. Borrowers may qualify for forgiveness of the remaining balance due on their eligible federal student loans after they have made 120 payments under certain repayment plans while employed full-time by public service employers.

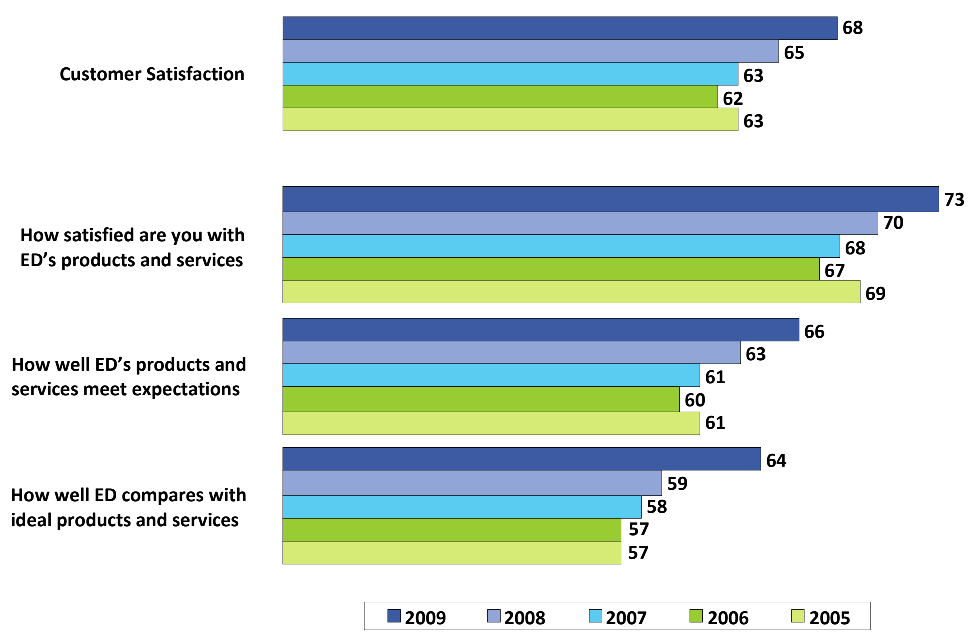
Another program that will help graduates with their student debt is the Income-Based Repayment Plan. This plan will cap the amount of the monthly federal loan payments at an amount determined by income and family size. The Department has developed an online calculator located on its student aid site to assist potential borrowers in determining their eligibility and to estimate if they would benefit from the plan. For more information, visit http://studentaid.ed.gov/PORTALSWebApp/students/english/index.jsp.

Management Improvement

Customer Satisfaction With the Department of Education

The Department strives to provide the most effective services to grantees and organizations that require support, assistance or information from the Department. Each year, the Department conducts an extensive survey of satisfaction of selected grantees and organizations. The survey is based on the American Customer Satisfaction Index, which is the national indicator of customer evaluations of the quality of goods and services and is the only uniform, cross-industry/government measure of customer satisfaction. The index is based on a scale of 100 points with a weighted average. Over a 5-year period, the Department has worked hard to provide its customers with levels of support that include quality of published guidance and documents, including online resources, effectiveness in the use of technology to deliver services, responsiveness and knowledge of Department staff and the provision of timely and quality technical assistance. In FY 2009, the Department achieved a five-point increase in customer satisfaction over the past two years. The Department saw significant increases in all drivers of customer satisfaction. For the full report, visit http://www.ed.gov/about/reports/annual/gss/index.html.

Customer Satisfaction Index 2005–2009



The Organizational Assessment

The Department's Organizational Assessment (OA) is the Departmentwide performance management system, developed in response to the requirements of Executive Order 13450, *Improving Government Program Performance,* as well as the Office of Personnel Management's requirement that each federal agency evaluate its principal offices on an annual basis. The OA operates at the principal office level and is designed to integrate and align all of the Department's performance management elements, including the *Strategic Plan,* the Secretary's annual goals and priorities, the priorities of the principal offices and other requirements of law. The OA provides a framework for communicating goals and priorities to employees and for aligning employee performance plans with the objectives of Department and principal offices.

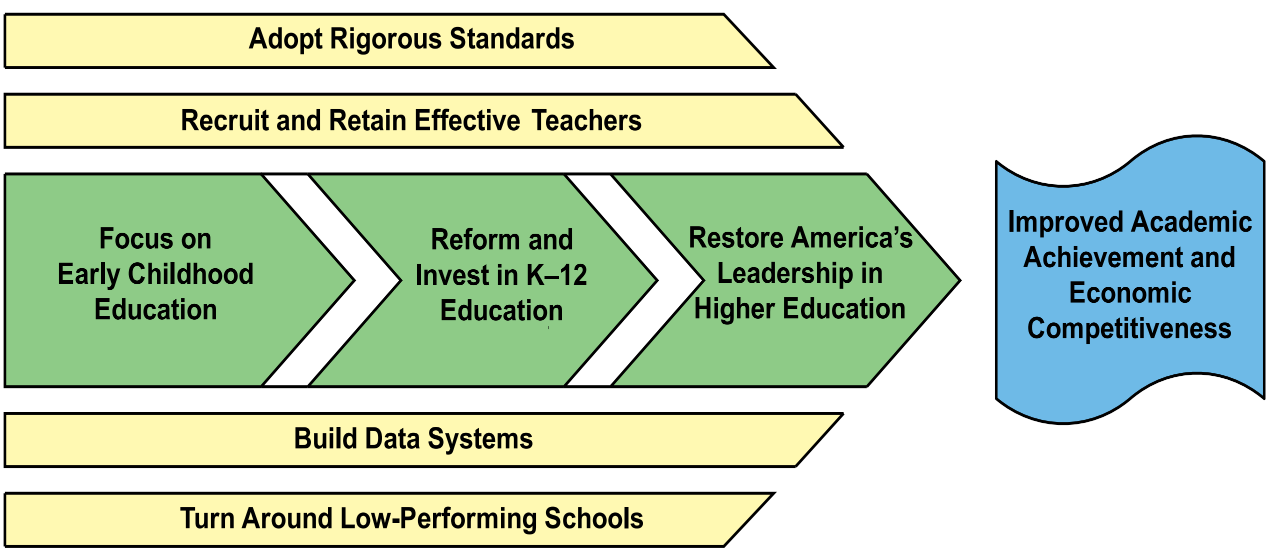
During FY 2009, the Department made significant changes to improve the transparency and accountability within its OA Initiative. These changes resulted in reducing the overall number of measures within the frameworks to better focus the Department's resources on mission-critical goals and priorities. As a result, OA leadership challenged Chief Management Officers to set ambitious goals for their Principal Operating Components. As a result, a number of steps have been implemented to ensure that the overall framework and scoring system were more rigorous in FY 2009. The goal of these changes is to improve the Department's overall performance.

A STRATEGIC FRAMEWORK FOR EDUCATION REFORM

The administration has identified four goals for education reform. These goals are to improve standards and assessments, improve teacher and principal quality, build data systems that inform educators' decisions and turn around low-performing schools.

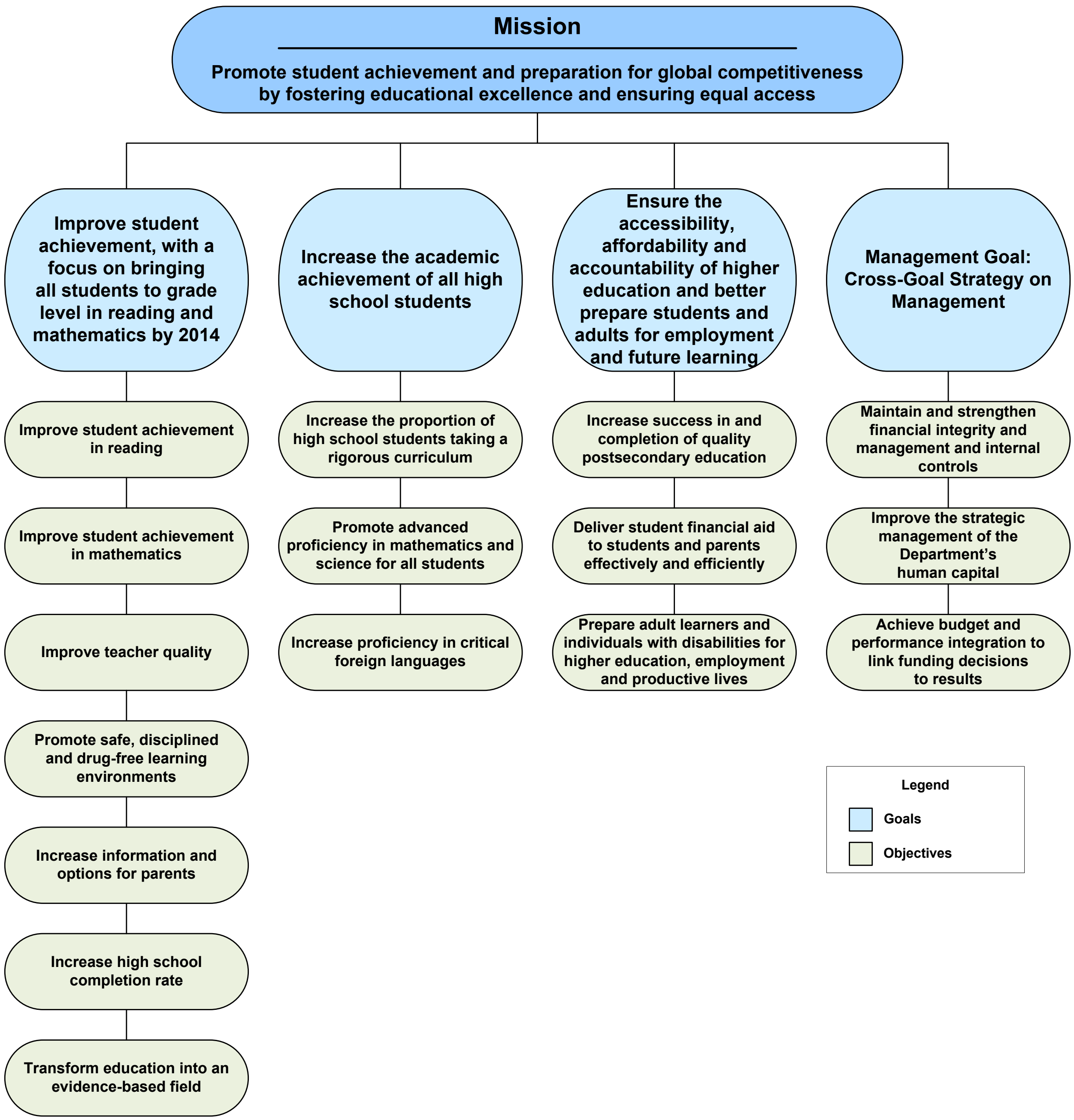
- Adopt rigorous standards and assessments that prepare students for success in college and the workforce.
- Recruit and retain effective teachers, especially in classrooms where they're needed most.
- Build data systems to track student achievement and teacher effectiveness.
- Turn around low-performing schools.

States must demonstrate a commitment to advancing education reform in these areas and agree to inform the Department of their progress to receive funding from the $48.6 billion available under the *American Recovery and Reinvestment Act's (Recovery Act)* State Fiscal Stabilization Fund (SFSF). State applications for funding are evaluated based on their assurances on these four areas of reform.



THE DEPARTMENT'S STRATEGIC PLAN

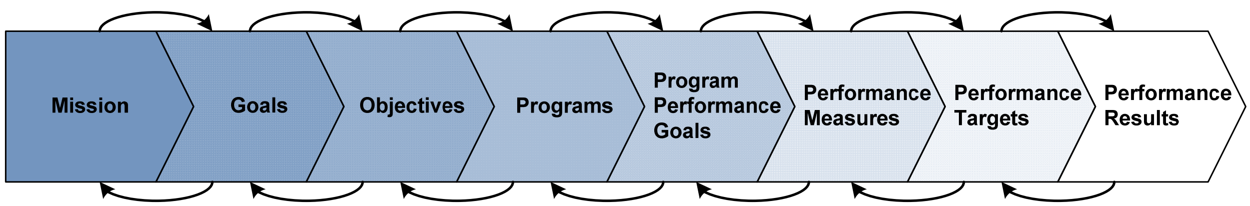
The Department reports on measures defined by the Department's *Strategic Plan for Fiscal Years 2007–2012* under the provisions of the *Government Performance and Results Act of 1993* (*GPRA*). The Department is in the process of developing a new *Strategic Plan for Fiscal Years 2010-2015*, which will replace the current plan.



OVERVIEW OF PERFORMANCE FOR FY 2009

The Department's Strategic Planning Process

The Department's strategic planning process sets high expectations for America's schools, students and for the Department. It streamlines Department goals and measures while stressing continuity. This is the process by which we ensure successful performance and management outcomes.



Challenges Linking the Program Performance to Funding Expenditures

Linking performance results, expenditures and budget for Department programs is complicated because more than 99 percent of the Department's funding is disbursed through grants and loans in which only a portion of a given fiscal year's appropriation is available to state, school, organization or student recipients during the fiscal year in which the funds are appropriated. The remainder is available at or near the end of the appropriation year or in a subsequent year.

Funds for competitive grant programs are generally available when appropriations are passed by Congress. However, the processes required for conducting grant competitions often result in the award of grants near the end of the fiscal year with funding available to grantees for future fiscal years.

Therefore, program results cannot be attributed solely to the actions taken related to FY 2009 funds but to a combination of funds from across several fiscal years. Furthermore, the results of some education programs may not be apparent for several years after the funds are expended.

There are 81 key performance measures that support the Department's mission and strategic goals under its current *Strategic Plan*. Most data for FY 2009 will be available during FY 2010. These measures will be reported on in detail in the Department's *Annual Performance Report (APR),* which will be submitted to Congress with the President's Budget Justification for FY 2011.

GOAL 1: Improve Student Achievement, With A Focus On Bringing All Students To Grade Level In Reading And Mathematics By 2014

Our Public Benefit

In education, the bottom line is student learning. The *Elementary and Secondary Education Act of 1965* (*ESEA*) revolutionized federal support for elementary and secondary education by establishing a national commitment to bring all children up to grade level in reading and mathematics and holding schools, districts and states accountable for making annual progress toward that goal. The *ESEA* promotes effective action to turn around schools that consistently fail to educate their students to high standards and provides students enrolled in those schools better choices and options.

Because student achievement depends on the efforts of well-prepared teachers, the Department is working with state educational agencies to devise and implement appropriate strategies for ensuring that teachers become highly qualified.

Also, teaching and learning to high standards require that our nation's schools be safe and drug free. The Department promotes practices that create safe, secure and healthy school climates.

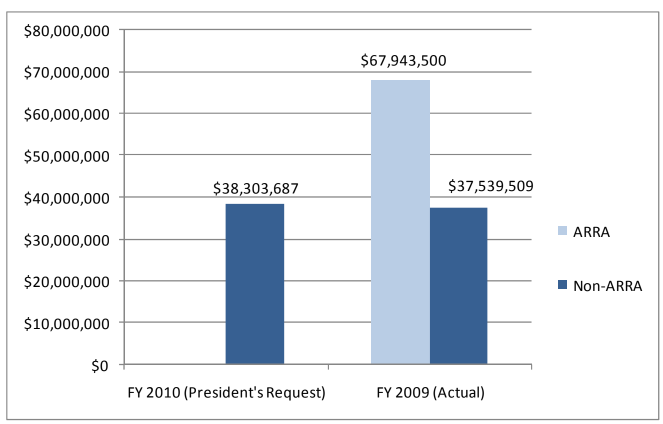
Parents are children's first and most important teachers. The Department promotes parental involvement in their children's schools, and encourages states and communities to provide information on additional options to parents.

The Department has developed the following objectives in support of Goal 1. Additionally, the Department has identified 37 key strategic performance measures for this goal.

Strategic Objectives:

- Improve student achievement in reading
- Improve student achievement in mathematics
- Improve teacher quality
- Promote safe, disciplined and drug-free learning environments
- Increase information and options for parents
- Increase high school completion rate
- Transform education into an evidence-based field

Goal 1 Resources
($ in thousands)



Strategies that support the Department in meeting its strategic objectives for Goal 1 include:

- assisting states and school districts in turning around low performing schools;
- collecting and disseminating student information;
- assisting states to ensure that their teachers are highly qualified;

- encouraging districts to reform teacher compensation systems to reward their most effective teachers and to create incentives to attract their best teachers;
- identifying and disseminating information about the most effective practices that create a safe, disciplined and drug free school climate;
- supporting high-quality charter schools; and
- improving the high school completion rate.

GOAL 2: Increase the Academic Achievement of All High School Students

Our Public Benefit

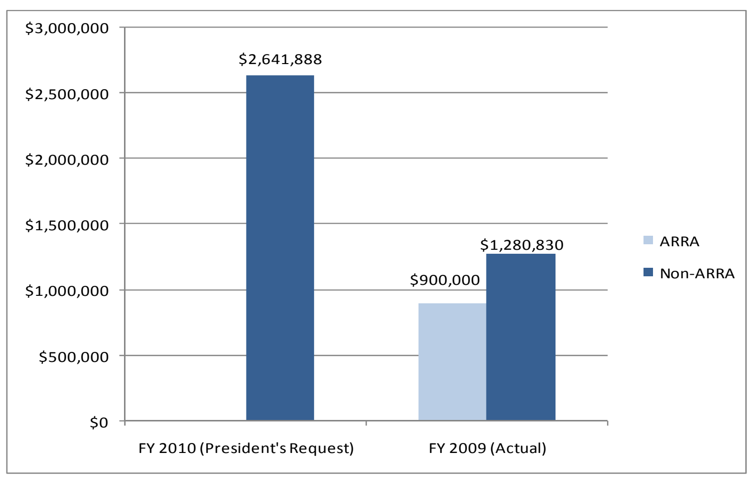
To better equip our students to compete in the global economy, the Department encourages states to adopt high school course work and programs of study that prepare all students for a postsecondary credential and facilitate a seamless transition from high school to college or the workforce. The Department will continue to enhance and promote achievement in mathematics, science and critical foreign languages through incentives for teachers to teach advanced courses, thus providing opportunities for students to be well prepared for postsecondary education or the workforce following high school. The Department encourages increased access to, and participation in, Advanced Placement (AP) or International Baccalaureate (IB) classes by low-income and other disadvantaged students. To offer challenging courses, schools must have qualified teachers to teach them. The Department promotes efforts to increase the number of teachers who have the academic content knowledge needed to teach advanced classes.

The Department will pursue the following objectives in support of Goal 2. Additionally, the Department has identified 11 key strategic performance measures for this goal.

Strategic Objectives:

- Increase the proportion of high school students taking a rigorous curriculum
- Promote advanced proficiency in mathematics and science for all students
- Increase proficiency in critical foreign languages

Goal 2 Resources ($ in thousands)



Strategies that support the Department in achieving its objectives for Goal 2 include:

- increasing access to AP courses nationwide;
- increasing the number of teachers qualified to teach AP and IB classes; and
- supporting projects expanding offerings and participation in advanced mathematics and science classes.

GOAL 3: Ensure the Accessibility, Affordability and Accountability of Higher Education and Better Prepare Students and Adults for Employment and Future Learning

Our Public Benefit

America's institutions of higher education have long been engines of innovation, helping the nation to achieve a level of economic prosperity experienced by few other countries throughout history. The dynamics of rapid technological change over time have required greater levels of education to sustain the global competitiveness of the American economy. As a result, an increasing proportion of Americans have enrolled in and completed a program of postsecondary education in order to secure high-quality employment in competitive industries.

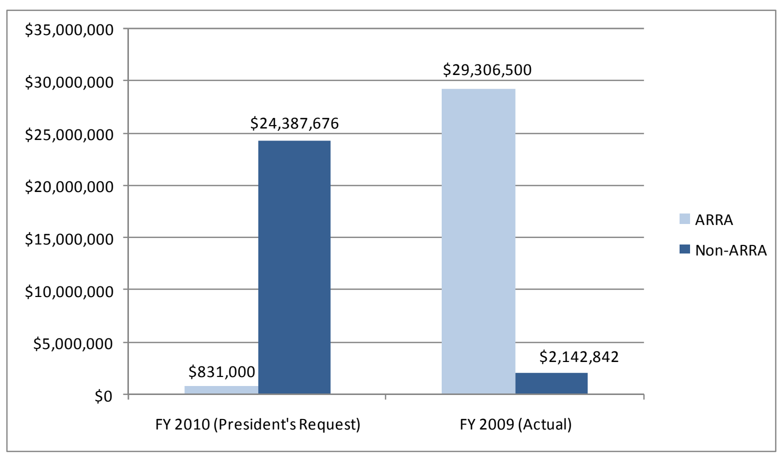
Financial aid must be made available to students in a more simplified manner and be more focused on students with the greatest financial need. Furthermore, adult education and vocational rehabilitation programs must provide increasingly effective services to improve the skills and employment prospects of those they serve.

The Department will pursue the following objectives in support of Goal 3. Additionally, the Department has identified 20 key strategic performance measures for this goal.

Strategic Objectives:

- Increase success in and completion of quality postsecondary education
- Deliver student financial aid to students and parents effectively and efficiently
- Prepare adult learners and individuals with disabilities for higher education, employment and productive lives

Goal 3 Resources
($ in thousands)



Strategies that support the objectives of Goal 3 include:

- maintaining high levels of college enrollment and persistence, while increasing the affordability of and accessibility to higher education through effective college preparation and grant, loan and campus-based aid programs;
- promoting and disseminating information regarding promising practices in community colleges;
- strengthening the accountability of postsecondary education institutions through accreditation, evaluation and monitoring;
- creating an efficient and integrated student financial aid delivery system;
- reducing the cost of administering federal student aid programs;

- improving federal student aid products and services to provide better customer service; and
- strengthening technical assistance to state vocational rehabilitation agencies through improved use of data, dissemination of information and solidified partnerships.

Cross-Goal Strategy on Management

Our Public Benefit

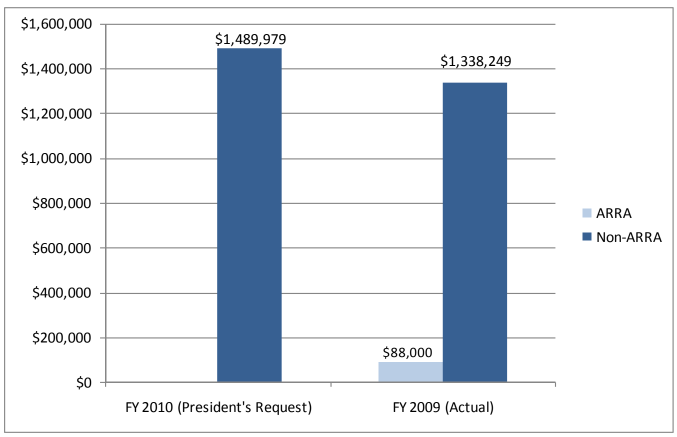
The Department carries out its mission and attains results for its goals through a commitment to excellent management practices. Through strong leadership, fiscal responsibility and strategic deployment of human capital, the Department ensures that all Americans have access to quality programs and benefit from successful outcomes.

The Department will pursue the following objectives in support of the cross-goal management strategy. Additionally, the Department has identified 13 key strategic performance measures for this goal.

Strategic Objectives:

- Maintain and strengthen financial integrity and management and internal controls
- Improve the strategic management of the Department's human capital
- Achieve budget and performance integration to link funding decisions to results

Cross-Goal Resources ($ in thousands)



Strategies that support the achievement of this strategic objective include:

- implementing risk mitigation activities to strengthen internal control and the quality of information used by managers;
- improving formula and discretionary grant management processes;
- improving compliance with information security requirements;
- fostering leadership and accountability;
- improving the Department's hiring process;
- holding people and programs accountable for budget and performance integration;
- improving performance measurement and data collection; and
- using performance information to inform program management and performance.

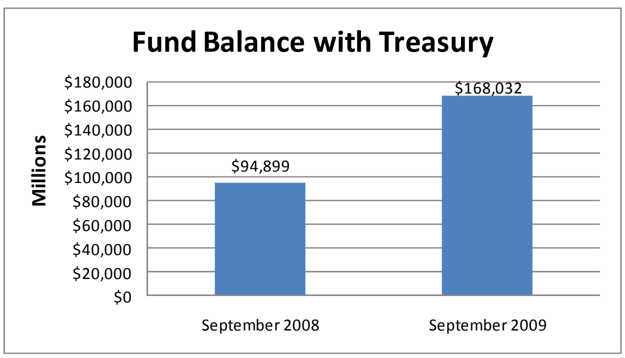
FINANCIAL HIGHLIGHTS

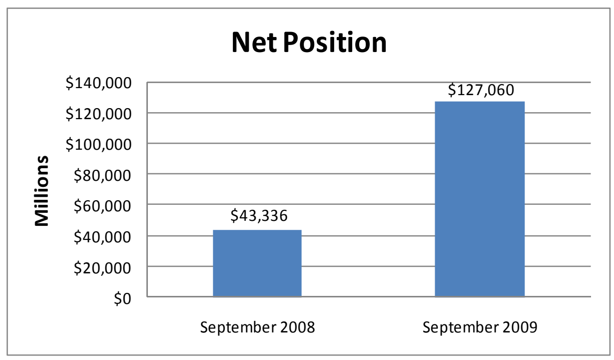
The Department consistently produces accurate and timely financial information that is used by management to inform decision-making and drive results in key areas of operation. For the eighth consecutive year, we achieved an unqualified (clean) opinion from independent auditors on the annual financial statements. Since 2003, the auditors have found no material weaknesses in the Department's internal control over financial reporting. In accordance with the Office of Management and Budget's (OMB) Circular No. A-123, *Management's Responsibility for Internal Control,* the Department continues to test and evaluate findings and risk determinations uncovered in management's internal control assessment.

American Recovery and Reinvestment Act of 2009

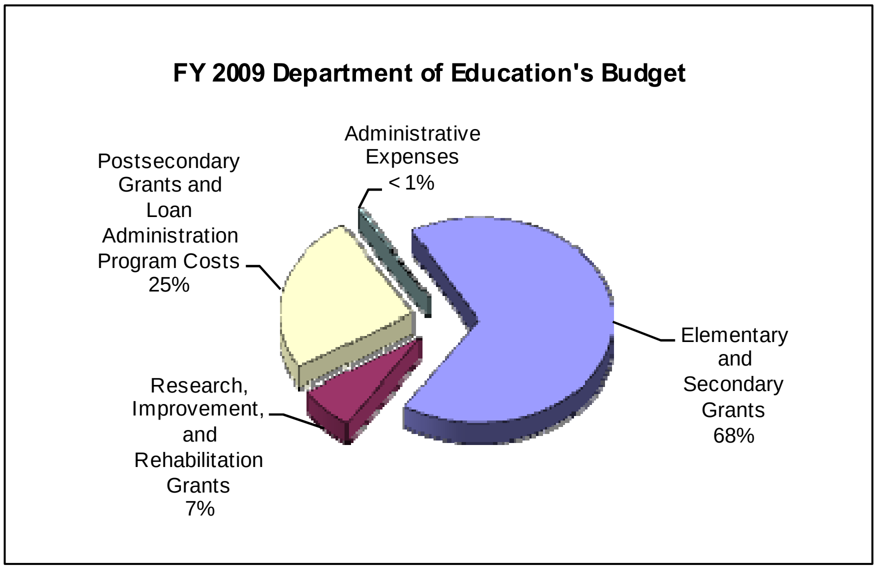
The *Recovery Act* provides $98.2 billion in additional funding to the Department. A significant portion of *Recovery Act* funding, $53.6 billion, is for the State Fiscal Stabilization Fund whose purpose is to minimize and avoid reductions in education and other essential services and to promote reform. The remaining funds will be used for currently authorized federal education activities. These activities include Impact Aid, Higher Education, Institute of Education Sciences, Student Aid Administration, Student Financial Assistance, Innovation and Improvement, Special Education, Rehabilitative Services and Disability Research, Education for the Disadvantaged, Office of Inspector General and School Improvement Programs.

This significant increase in funding is evident from a comparison of the Department's financial statements as of September 30, 2009, and September 30, 2008. The increases in Fund Balance with Treasury and Net Position were 77 percent and 193 percent, respectively, which are due to effects of the *Recovery Act* funding.





Sources of Funds



The Department managed a budget in excess of $140.5 billion during FY 2009, of which 68 percent supported elementary and secondary education grant programs.

Postsecondary education grants and administration of student financial assistance accounted for 25 percent, including loan programs costs that helped almost 13 million students and their parents to better afford higher education during FY 2009. An additional 7 percent went toward programs and grants encompassing research, development and dissemination, as well as vocational rehabilitation services. Administrative expenditures were less than 1 percent of the Department's appropriations.

Nearly all of the Department's non-administrative appropriations support three primary lines of business: grants, guaranteed loans and direct loans. The original principal balances of the Federal Family Education Loan (FFEL) Program and Federal Direct Student Loan Program loans, which compose a large share of federal student financial assistance, are funded by commercial banks and borrowings from the Treasury, respectively.

The Department's four largest grant programs are SFSF, Title I grants for elementary and secondary education, Pell Grants for postsecondary financial aid and Special Education Grants to States under the *Individuals with Disabilities Education Act.* In addition, this was the first full year of the Teacher Education Assistance for College and Higher Education (TEACH) Grant Program. This program awards annual grants to students who agree to teach in a high-need subject area in a public or private elementary or secondary school that serves low-income students.

The FFEL Program ensures that the loan capital for approximately 2,900 private lenders is available to students and their families. Through loan guarantees issued by 35 active state and private nonprofit Guaranty Agencies, backed by federal reinsurance provided by the Department, the FFEL Program protects lenders against losses from borrower default. As of the end of September 2009, the total principal balance of outstanding guaranteed loans held by lenders was approximately $457 billion. The government's estimated maximum exposure for defaulted loans was approximately $445 billion.

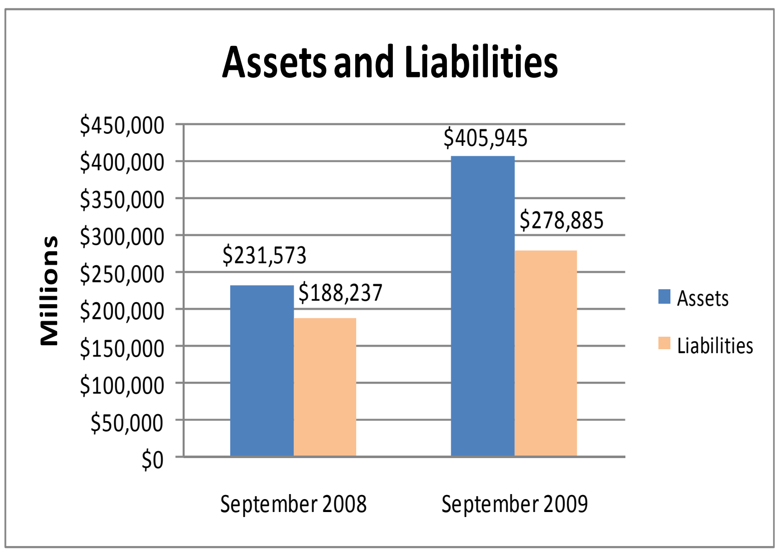
The *Ensuring Continued Access to Student Loans Act of 2008* (*ECASLA*) amended the FFEL Program to authorize the secretary to purchase or enter into forward commitments to purchase FFEL loans. The Department has implemented three activities under this temporary loan purchase authority. These activities are: (1) loan purchase commitments under which the Department agrees to purchase loans directly from FFEL lenders; (2) loan participation interest purchases in which the Department purchases participation interests in FFEL loans; and (3) an Asset-Backed Commercial Paper (ABCP) Conduit program in which the Department enters into a forward commitment to purchase FFEL loans from a student loan-backed conduit, as needed, to allow the conduit to repay short-term liquidity loans used to re-finance maturing commercial paper.

The William D. Ford Federal Direct Student Loan Program, created by the *Student Loan Reform Act of 1993,* provides an alternative method for delivering assistance to students. This program uses Treasury funds to provide loan capital directly to eligible undergraduate and graduate students and their parents through participating schools. These schools then disburse loan funds to students. As of September 30, 2009, the value of the Department's direct loan portfolio was $152.8 billion.

Financial Position

The Department's financial statements are prepared in accordance with established federal accounting standards and are audited by the independent accounting firm of Ernst & Young, LLP. Financial statements and footnotes for FY 2009 appear on pages 48-96. An analysis of the principal financial statements follows.

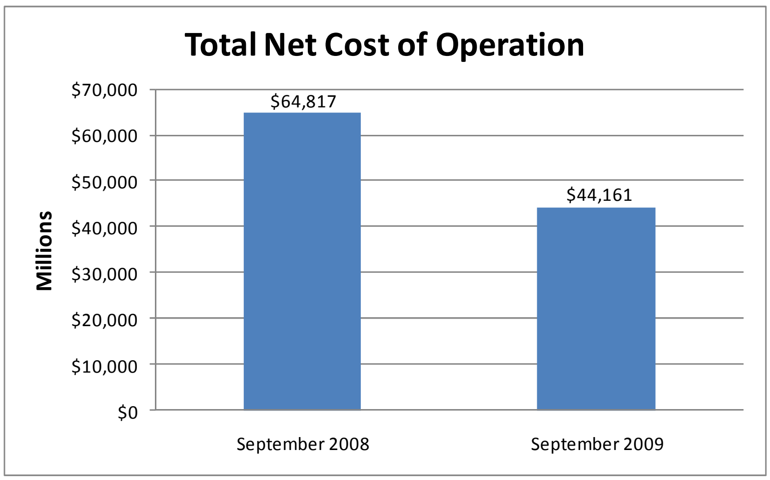
Balance Sheet. The Balance Sheet presents, as of a specific point in time, the recorded value of assets and liabilities retained or managed by the Department. The difference between assets and liabilities represents the net position of the Department. The Balance Sheet displayed on page 48 reflects total assets of $406 billion, a 75 percent increase over FY 2008. The majority of this increase is due to both the American *Recovery and Reinvestment Act* and to *ECASLA*. Credit Program Receivables increased by $99.5 billion, a 74 percent increase over FY 2008. This increase is largely due to an increase in direct loan disbursements, and activity related to loan purchase commitments and loan participation purchases under the Federal Family Education Loan (FFEL) program. The majority of this loan portfolio is principal and interest owed by students on direct loans. The remaining balance is related to defaulted guaranteed loans purchased from lenders under terms of the FFEL Program and to loan purchase commitments and loan participation purchases under the FFEL Program. The net portfolio for direct loans increased by over $42.9 billion due to increased direct loan disbursements. FFEL Program loans increased by $56.4 billion during FY 2009, due primarily to loan



volume and activity related to loan purchase commitments and loan participation purchases. The Fund Balance with Treasury increased by $73.1 billion, a 77 percent increase from FY 2008. The vast majority of this increase is due to the *Recovery Act*.

Total Liabilities for the Department increased by $90.6 billion, a 48 percent increase over FY 2008. The increase is primarily due to the fact that borrowing increased for the Direct Loan Program and to provide funds for the loan purchase commitments and loan participation purchases activities under the FFEL Program. Liabilities for Loan Guarantees for the FFEL Program decreased $22.8 billion, a 53 percent decrease due primarily to subsidy transfers, re-estimates and modifications. These liabilities present the estimated costs, on a present-value basis, of the net long-term cash outflows due to loan defaults and interest subsidies net of offsetting fees.

The Department's Net Position as of September 30, 2009 was $127.1 billion, an $83.8 billion increase over the $43.3 billion Net Position as of September 30, 2008. This 193 percent increase was largely due to the *Recovery Act.*



Statement of Net Cost. The Statement of Net Cost presents the components of the Department's net cost, which is the gross cost incurred less any revenues earned from the Department's activities. The Department's total program net costs, as reflected on the Statement of Net Cost, page 49, were $44.2 billion, a 32 percent decrease from September 30, 2008. This change largely reflects the effects of both the $2.6 billion downward modification and the $21.7 billion downward re-estimate in the guarantee loan portion of the FFEL Program, and the $5.2 billion downward re-estimate for Direct Loans.

The Statement of Net Cost is presented to be consistent with the Department's strategic goals. As required by the *Government Performance and Results Act of 1993*, each of the Department's Reporting Organizations has been aligned with the major goals presented in the Department's *Strategic Plan 2007–2012*.

Net Cost Program	Reporting Organizations/ Groups	Strategic Goal
Ensure Accessibility, Affordability and Accountability of Higher Education and Career and Technical Advancement	• Federal Student Aid • Office of Postsecondary Education • Office of Vocational and Adult Education	3 Ensure the accessibility, affordability and accountability of higher education, and better prepare students and adults for employment and future learning
Promote Academic Achievement in Elementary and Secondary Schools	• Office of Elementary and Secondary Education • Office of English Language Acquisition • Office of Safe and Drug-Free Schools • Hurricane Education Recovery	1 Improve student achievement, with the focus on bringing all students to grade level in reading and mathematics by 2014 2 Increase the academic achievement of all high school students
Transformation of Education	• Institute of Education Sciences • Office of Innovation and Improvement	1 Improve student achievement, with the focus on bringing all students to grade level in reading and mathematics by 2014
Special Education	• Office of Special Education and Rehabilitative Services	Cuts across Strategic Goals 1, 2 and 3
American Recovery and Reinvestment Act	• *Recovery Act*	Cuts across Strategic Goals 1, 2 and 3

Strategic Goals 1, 2 and 3 are sharply defined directives that guide reporting organizations to carry out the Department's vision and programmatic mission, and the net cost programs can be specifically associated with these three strategic goals. The Department has a Cross-Goal Strategy on Management, which is considered a high-level premise on which the Department establishes its foundation for the three goals. As a result, we do not assign specific programs to the Cross-Goal Strategy for presentation in the Statement of Net Cost.

Statement of Budgetary Resources. This statement provides information about the provision of budgetary resources and their status as of the end of the reporting period. The statement displayed on page 51 shows that the Department had $437.8 billion in total budgetary resources for the 12 months ended September 30, 2009. These budgetary resources were composed of $170.1 billion in appropriated budgetary resources and $267.7 billion in non-budgetary credit reform resources, which primarily consist of borrowing authority for the loan programs. Of the $46.6 billion that remained unobligated at year end, $12.1 billion represents funding provided in advance for activities in future periods that were not available at year end. These funds will become available in following fiscal years.

Limitations of Financial Statements

Management has prepared the accompanying financial statements to report the financial position and operational results for the U.S. Department of Education for FY 2009 and FY 2008 pursuant to the requirements of Title 31 of the United States code, section 3515(b).

While these statements have been prepared from the books and records of the Department in accordance with generally accepted accounting principles for federal entities and the formats prescribed by OMB, these statements are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records.

The statements should be read with the realization that they are a component of the U.S. Government, a sovereign entity. One implication of this is that the liabilities presented herein cannot be liquidated without the enactment of appropriations, and ongoing operations are subject to the enactment of future appropriations.

MEMORANDUM FROM THE OFFICE OF INSPECTOR GENERAL

UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF INSPECTOR GENERAL

THE INSPECTOR GENERAL

MEMORANDUM

TO:	Secretary Arne Duncan
FROM:	Mary Mitchelson, Acting Mary Mitchelson
RE:	Management Challenges for Fiscal Year 2010
DATE:	October 30, 2009

Pursuant to the *Reports Consolidation Act of 2000*, we provide the attached report, Management Challenges for the U.S. Department of Education for Fiscal Year 2010. We look forward to working with you to address these challenges and improve the efficiency and integrity of the Department's programs and operations.

400 MARYLAND AVE., S.W. WASHINGTON, D.C. 20202-1510

Our mission is to ensure equal access to education and to promote educational excellence throughout the Nation.

OFFICE OF INSPECTOR GENERAL'S MANAGEMENT CHALLENGES FOR FISCAL YEAR 2010

The Office of Inspector General (OIG) works to promote efficiency, effectiveness and integrity in the programs and operations of the U.S. Department of Education (Department). Through our audits, inspections, investigations and other reviews, we continue to identify areas of concern within the Department's programs and operations and recommend actions the Department should take to address these weaknesses.

The *Reports Consolidation Act of 2000* requires OIG annually to identify and summarize the top management challenges facing the Department and provide information on the Department's progress in addressing those challenges. In recent years, we have focused our Management Challenges reports on six operational areas that our work identified as most vulnerable to waste, fraud and abuse: (1) student financial assistance programs; (2) information technology (IT) security and management; (3) grantee monitoring and oversight; (4) grant and contract awards, performance and monitoring; (5) data reliability; and (6) human resources. While our previous Management Challenges reports have noted some progress by the Department in addressing these challenges, with passage of the *American Recovery and Reinvestment Act of 2009* (*Recovery Act*) and the *Ensuring Continued Access to Student Loans Act of 2008* (*ECASLA*), there is an immediate need for the Department to increase its efforts to ensure that Federal education programs are operating effectively, efficiently and as required by statute. It is with that goal in mind that we focus this report on three overall challenges that impact virtually every operational aspect of the Department: (1) the *Recovery Act*; (2) student financial assistance programs/*ECASLA*; and (3) information security and management.

The Department has voiced its commitment to tackling these challenges and addressing the underlying problem of internal controls. "Internal controls" are plans, methods and procedures an entity employs to provide reasonable assurance that it meets its goals and achieves its objectives while minimizing operational problems and risks. By establishing effective internal controls, the Department can be an effective steward of the billions of taxpayer dollars supporting its programs and operations. America's students and taxpayers deserve nothing less.

Challenge: Implementing the *Recovery Act*

The *Recovery Act* was signed into law on February 17, 2009, and includes approximately $98.2 billion in new funding for federal education programs and operations. This includes funding for programs within the *Elementary and Secondary Education Act of 1965,* as amended (*ESEA*); the *Higher Education Act of 1965,* as amended (*HEA*); the *Individuals with Disabilities Education Act of 2004,* as amended; and the *Rehabilitation Act of 1973.* With 55 state and territorial educational agencies, more than 16,000 school districts and thousands of schools, colleges and universities potentially eligible to receive these funds, the Department faces a formidable challenge in ensuring that *Recovery Act* funds reach the intended recipients and achieve the desired results. To do so, the Department must: (1) provide effective oversight and monitoring of its grantees and subrecipients; (2) ensure that the information reported to the Department and by the Department is accurate and reliable; and (3) make certain it has knowledgeable staff on board to successfully carry out and manage its programs and operations. While our specific *Recovery Act* work is underway, previous OIG audits, inspections and investigations have uncovered problems in these three areas, making each a significant challenge for the Department.

Grantee and Subrecipient Oversight and Monitoring

Ineffective monitoring and oversight can have a significant impact on a grantee's ability to meet statutory requirements and ensure critical education funds reach the intended recipients. Recent OIG audits, inspections and investigations have uncovered problems with program control and oversight of a number of grantees, almost all of which are eligible to receive *Recovery Act* funds. Further complicating this issue is the requirement that grantees receiving *Recovery Act* funds closely monitor subrecipients' use of and account for the funds. Our previous audit and investigation work identified a number of weaknesses in grantee oversight and monitoring of its subrecipients. For example, some state educational agencies' (SEA) subrecipient monitoring efforts lacked a fiscal oversight component, while other SEAs were found to conduct on-site program monitoring of subrecipients infrequently. Other grantees were found to rely too heavily on local educational agency single audits, which often times are too late for early detection of inappropriate use of funds. In addition, preliminary *Recovery Act* work has shown that some grantees are relying on existing monitoring procedures that do not appear adequate to ensure their subrecipients use of and accounting for *Recovery Act* funds appropriately, and do not cover new program funding, including dollars from the *Recovery Act*'s State Fiscal Stabilization Fund. These factors make it a challenge for the Department to ensure that adequate and timely monitoring of *Recovery Act* funds is taking place at both the SEA and subrecipient levels.

The Department's Progress. *The Department has expressed its commitment to improving oversight of its grantees and subrecipients. As an example, the Department has been working closely with the Michigan Department of Education and Detroit Public Schools to aggressively address significant financial and performance problems which left the school system on the verge of collapse. The Department's plan includes provisions for a structurally balanced budget, accountability and systemic controls and deficit elimination. With regard to the* Recovery Act, *the Department has issued a number of policy guidance documents and fact sheets to assist grantees in implementing* Recovery Act *programs. It is also developing a technical assistance plan and training curricula for grantees that will include administrative requirements for implementation of federal grants and will convey the importance of complying with those requirements. The Department also intends to conduct outreach efforts, such as conferences, workshops and Webinars, to provide additional technical assistance to* Recovery Act *grantees.*

Data Reliability

The Department, its grantees and subrecipients must have controls in place and effectively operate to ensure that accurate, reliable data is reported. This is particularly important with regard to *Recovery Act* funds, as recipients must submit regular reports detailing the projects and activities funded with those dollars. They are also required to submit quarterly reports, which include new data elements that must be submitted within 10 days of the close of each fiscal quarter. Our preliminary *Recovery Act* work has determined that some SEAs are planning to use existing data systems to collect, compile and report *Recovery Act* data, but had not yet modified their systems to reflect new reporting requirements. Also, some SEAs expressed concern that they had not received adequate guidance, or that their states might not have enough staff and funding resources to meet all of the new reporting requirements and timelines. In addition, the *Recovery Act* requires that all fund recipients register in the Central Contractor Registration database, which means the Department must ensure that all of these recipients are registered in time to meet reporting requirements. As previous OIG work has identified issues of noncompliance with data collection and reporting requirements, it will be a challenge for the Department to ensure that data received from *Recovery Act* fund recipients is accurate, reliable and complete.

The Department's Progress. *The Department has collected data and has developed a risk-assessment model for technical assistance that will allow its staff to provide more guidance to states and other grantees that are at increased risk for problems. Department staff has also been using conference calls with states to provide targeted technical assistance to meet each state's specific needs. The Department established a Metrics and Monitoring Team that is charged with ensuring transparency, accountability and oversight of* Recovery Act *dollars. The team meets weekly to coordinate oversight efforts and develop new reports that are required for posting on the Recovery.gov Web site.*

Human Resources

Like most federal agencies, the Department will see a significant percentage of its workforce eligible for retirement in 2010. Compounding the situation is the immediate demand for staff to address the requirements of the *Recovery Act*. Prior OIG work in the area of grants monitoring has shown that staff handled a large number of grants and were not able to closely monitor all necessary activities. Human resources is a challenge that the Department must immediately address, as current staff will be further stretched to monitor the unprecedented levels of new funding available to state and local governments and other entities under the *Recovery Act*.

The Department's Progress. *The Department has devoted significant resources to implement requirements related to the* Recovery Act. *Teams have been formed to issue guidance and provide technical assistance and outreach on various topics to ensure* Recovery Act *fund recipients are aware of their responsibilities, all at a time when a number of critical positions have not yet been filled due to the change in administration. While efforts to date have been significant, Department staff may not be able to maintain the current pace without additional resources as its* Recovery Act *efforts move from implementation to monitoring.*

Challenge: Student Financial Assistance Programs/*ECASLA*

The federal student financial assistance programs involve more than 6,200 postsecondary institutions, more than 2,900 lenders, 35 guaranty agencies and many third party servicers. In 1998 and in response to the growing complexity, increased demand and the likelihood for waste, fraud and abuse associated with the student financial assistance programs, Congress established a Performance Based Organization (PBO) in the Department to manage and administer the student financial assistance programs authorized under Title IV of the *HEA*. In the decade since becoming the PBO, the Federal Student Aid (FSA) office's responsibilities have increased as the programs have grown substantially. In 2009, FSA disbursed $18.4 billion in Pell Grants averaging approximately $2,973 to 6.2 million students. In fulfilling its program responsibilities, FSA directly manages or oversees almost $622 billion in outstanding loans, representing over 111 million student loans to more than

32 million borrowers. Further, with the significant disruptions in the credit markets, in early 2008, lenders in the Federal Family Education Loan (FFEL) Program expressed concerns that there would be insufficient private capital to fund FFEL loans to meet the demands of Stafford and PLUS loan borrowers. To address these concerns, Congress passed the *ECASLA*, which provided the Department with the authority to purchase or enter into forward commitments to purchase student loans from lenders to ensure that loans are available for all students. Colleges and universities also expanded participation in the William D. Ford Federal Direct Loan (Direct Loan) program due to uncertainty over FFEL availability. Prior to 2008, the Direct Loan program has accounted for about 20 percent of new student loan volume. However, the Direct Loan program's new loan volume is expected to increase to about 60 percent for the 2009–2010 academic year, and the administration has proposed a transition to 100 percent direct lending for the 2010–2011 academic year.

In order to fulfill all of its responsibilities as a PBO, as well as sufficiently administer the Title IV and *ECASLA* programs, FSA must: (1) have a system of effective internal controls in place; (2) provide sufficient oversight and monitoring of Title IV program participants; (3) provide effective contract monitoring to ensure that it receives quality goods and services from its vendors; and (4) make certain it has knowledgeable staff on board to successfully carry out and manage its programs and operations. Our specific *ECASLA*-related work is ongoing, but previous OIG efforts found that FSA does not have sufficient capacity or resources necessary to provide effective oversight for all aspects of the student financial assistance programs, leaving programs vulnerable to waste, fraud and abuse.

Internal Controls

Establishing effective internal controls has long been a challenge for Federal Student Aid, and three recent OIG reports show that problems in this area continue. First, an OIG audit that sought to determine whether FSA was meeting its responsibilities as a PBO in three key areas found that FSA had not done so, and as a result, the Congress, the Secretary and the public have not been clearly informed about FSA's progress toward achieving its purposes as a PBO or whether it has reduced its program costs since becoming a PBO more than a decade ago. Second, an OIG review of FSA's oversight of GAs, lenders and loan servicers found that improvements were needed in each of the five areas of internal control: control environment, risk assessment, information and communications, control activities and monitoring. This was a follow-up report to a 2006 audit that contained similar findings, many of which had not been fully addressed. Third, OIG performed an inspection of FSA's Enterprise Risk Management Group, an effort initiated by FSA in 2006 with the goal of developing risk assessments and providing a more strategic view of future risks. The OIG inspection found that FSA had not fully implemented enterprise risk management, leaving its programs vulnerable to waste, fraud and abuse. Based on these findings, the passage of *ECASLA* and the expansion of the Direct Loan Program, it is vital that FSA leaders take on this challenge and implement effective internal controls.

The Department's Progress. *FSA has agreed to improve the management of its programs. It is restructuring and improving its chief compliance officer organization for the oversight of the FFEL Program. FSA is also in the process of implementing the authorities provided by* ECASLA *for the Loan Participation/Purchase programs, and establishing internal controls to provide for accountability and monitoring and ensure compliance with the requirements of the law.*

Participant Oversight and Monitoring

FSA has always faced a significant challenge in conducting effective monitoring and oversight of the thousands of entities participating in its programs. Recent OIG efforts have revealed cases of lenders violating the inducement provision of the *HEA* or overbilling the Department for loans under the 9.5 percent special allowance payment (SAP); guaranty agencies that did not comply with *HEA* requirements regarding the Federal Fund and Operating Fund; and schools that did not comply with Title IV requirements for institutional and program eligibility, the 90-10 rule and other criteria. With *ECASLA*, the need for FSA to conduct effective oversight and monitoring has only intensified. FSA estimated that about 75 percent of FFEL new loan volume for the 2008–2009 academic year would be financed through *ECASLA* programs, and significant increases in student loan volume were expected in the Direct Loan program. FSA must make improvements in oversight and monitoring to ensure that the entities participating in the federal student financial assistance programs are adhering to statutory, regulatory and program requirements. Still another challenge facing both FSA and schools participating in the Title IV programs involves identity verification of students receiving federal student financial assistance. FSA does not yet require schools to verify the identity of students receiving aid, which leaves the programs vulnerable to identity theft and other fraudulent schemes, particularly distance education programs.

The Department's Progress. *FSA has agreed to develop and implement consistent oversight procedures of the entities participating in the federal student financial assistance programs. As an example, in response to our audit work on 9.5 percent SAP, the Department has required all lenders wishing to bill at the 9.5 percent SAP rate to undergo audits to determine the eligibility of loans for payments at the 9.5 percent rate. With* ECASLA*, FSA has conducted outreach efforts to inform industry participants of* ECASLA-*related programs and operations, and developed testing and certification requirements for industry participants with the advice of OIG. Additionally, FSA has executed Lender of Last Resort Agreements with 30 guaranty agencies. To increase the capacity of the Direct Loan Program, FSA has expanded the capacity of the Common Origination and Disbursement system used to originate Direct Loans. To handle the increased need for servicing Direct Loans and loans purchased under the* ECASLA-*related programs, FSA contracted with four additional entities to service loans. In addition, as part of its corrective action to the recommendations made in our 2007 inspection report on guaranty agency compliance with the establishment of a Federal Fund and Operating Fund at each agency, FSA contracted for program reviews at 22 guaranty agencies. FSA hired contractors to carry out these efforts. These program reviews identified more than $33 million in potential recoveries to the Federal Fund. Finally, FSA is aware of the issues involving identity verification of students receiving federal student financial assistance and may discuss the issue at its next negotiated rulemaking session.*

Contract Awards, Monitoring and Performance

In 2005, the Secretary of Education delegated authority to the Chief Operating Officer in FSA to procure property and services in the performance of functions managed by FSA as a PBO. Since that time, more than 50 percent of the contracts entered into and paid by the Department are done so by and through FSA. A 2007 audit by OIG found that FSA's contract monitoring process did not always ensure contractors adhered to contract requirements and FSA received the products and services intended. We found that FSA staff did not always ensure appropriate review and approval of invoices, appropriately communicate acceptance/rejection of deliverables, issue modifications for contract changes and appropriately issue or sign necessary appointment letters. This occurred because of resource limitations and because FSA staff was not always familiar with applicable policies and procedures. FSA must expand its oversight and monitoring to new contractors, such as the four new contractors hired to service loans.

The Department's Progress. *In 2008 FSA hired consultants to review its acquisition processes and make recommendations for improvement. In addition, FSA revised its Contracting Officer's Representative Training Program to incorporate more stringent certification, training and recordkeeping requirements.*

Human Resources

Due to the complexities of the student financial assistance programs, FSA personnel must have the necessary skills and training for effective program monitoring and oversight. During the course of our 2007 inspection report on guaranty agency compliance with the establishment of the Federal and the Operating Funds, Department officials acknowledged that FSA did not have sufficient staff with the qualifications and knowledge needed to monitor guaranty agencies, lenders and other participants. Further, our 2009 audit of FSA's oversight of guaranty agencies, lenders and loan servicers noted that staff resources were not sufficient to adequately provide oversight of those participants, and core competencies had not been developed to ensure proper qualifications for staff conducting program reviews. We also found that FSA staff did not complete adequate training related to their duties. FSA must take the steps necessary to ensure it has knowledgeable staff so it has the capacity to successfully carry out the student financial assistance programs.

The Department's Progress. *To address the human resource weaknesses identified in recent OIG audit and inspection reports, FSA has contracted for services, including program reviews. In addition, FSA agreed with OIG recommendations that it ensure that its staff have the requisite knowledge to sufficiently evaluate programs; that it dedicate sufficient staff resources to provide oversight of the FFEL program; and that it develop core competencies and implement mandatory training for responsible staff.*

Challenge: Information Security and Management

The *Federal Information Security Management Act* (*FISMA*) requires each federal agency to develop, document and implement an agencywide program to provide information security and develop a comprehensive framework to protect the government's information, operations and assets. To ensure the adequacy and effectiveness of information security controls, Igs conduct annual independent evaluations of the agencies' information security programs and report the results to the Office of Management and Budget. OIG work conducted since 2004 has revealed numerous system security internal control weaknesses, all of which increase the risk for inappropriate disclosure or unauthorized use of sensitive and personally identifiable information (PII). The Department's challenges in the area of IT security and management involve the *Recovery Act*; oversight and monitoring of its multimillion-dollar IT contracts; addressing cybersecurity threats; and administering its IT capital investment portfolio. It is vital that the Department addresses these challenges to ensure that its IT and information security projects are appropriately managed so they meet their technical and functional goals on time and on budget.

Recovery Act Funds

Through the *Recovery Act*, an additional $98.2 billion will flow through the Department's systems. These systems must simultaneously administer and process transactions for the *Recovery Act* as well as existing programs. As a result, it is essential that the Department implement and maintain appropriate systems security controls over IT assets used to administer *Recovery Act* funds.

The Department's Progress. *The Department has agreed to improve its managerial, operational and technical security controls to adequately protect its data. While we are currently conducting work related to the* Recovery Act, *previous* FISMA*-related reports identified critical risks and vulnerabilities in the Department's systems. Our findings have provided management with key recommendations for tightening of security awareness and incident handling, ensuring adequate maintenance of the Department's systems and damage assessment.*

Contract Awards, Monitoring and Performance

In 2007, the Department awarded a 10-year, nearly $500 million contract to a single vendor to acquire IT network services and improve all services provided to the Department customers and to lower costs to the Department through IT integration. While OIG is currently reviewing this contract, previous OIG work revealed that improvement was needed in the Department's IT contract management. A 2007 OIG audit of the previous IT network services contract revealed a number of weaknesses, including that the Department did not provide effective performance incentives or disincentives to allow for timely enforcement of an acceptable level of performance, and that contract modifications were not fully evaluated to consider whether a reduction in cost was appropriate for the reduced level of effort required by the contractor to meet acceptable levels of performance. We also found that the Department's controls did not ensure the contractor provided the quality and services required by the contract. As a result, the Department paid for a quality or level of services it did not receive.

The Department's Progress. *The Department agreed to take action on a number of the recommendations made in our 2007 IT audit, which included: ensuring that future performance-based contracts include appropriate incentives and disincentives to motivate contractor performance; providing a correlation between performance and payments to the contractor; and assuring minimum quality levels for all critical services. It also agreed to require contractors to provide the Department with alternatives to address unsatisfactory contractor performance and allow for execution of option years for achievement of satisfactory performance levels if such continuation is in the best interest of the Department. The Department also agreed to develop and implement an internal contract-deliverables tracking system.*

Ongoing Cybersecurity Threats

The nature of the ongoing cybersecurity threat has shifted. Historically the threat was from the outside "hacker" conducting attacks to compromise systems for bragging rights or use of resources. Now the primary threat is from criminal elements, including organized crime and even terrorist organizations. The threat vector most commonly used by these parties is to influence regular users to go to malicious Web sites or open malicious files and compromise the computer. The consequences of security incidents from these threats can include disclosure of sensitive information and PII, lost staff hours, damaged or altered records, extensive financial damage and the loss of the public's confidence in its government.

The Department's Progress. *The Department is making progress in establishing policies to protect sensitive information and PII and has implemented enhanced security monitoring to protect users' computers within the Department's network. More needs to be done, however, to reduce the threats posed by external business partners who have remote access to Department systems. For example, while the Department is working hard to implement two-factor authentication within the Department's network, little progress has been made on strengthening remote access from business partners.*

IT Capital Investment Portfolio

The Department's IT capital investment portfolio for FY 2009 was $656.9 million and for FY 2010 is expected to be $920.8 million, with many resource-intensive projects pending. It is critical that the Department have a sound IT investment management control process that can ensure that technology investments are appropriately evaluated, selected, justified and supported. This oversight and monitoring process must address IT investments as an agency-wide portfolio.

The Department's Progress. *The Department has recently strengthened the IT capital investment program by expanding membership of two of its review groups, the Investment Review Board and the Planning and Investment Review Working Group. The Department continues its efforts to strengthen individual business cases and to map proposed investments to an agencywide enterprise architecture strategy.*

MANAGEMENT'S ASSURANCES

Federal Managers' Financial Integrity Act

As required under the *Federal Managers' Financial Integrity Act of 1982* (*FMFIA*)*,* the Department reviewed its management-control system. The objectives of the management-control system are to provide reasonable assurance that the following occur:

- Obligations and costs are in compliance with applicable laws.
- Assets are safeguarded against waste, loss, unauthorized use or misappropriation.
- The revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and maintain accountability over assets.
- Programs are efficiently and effectively carried out in accordance with applicable laws and management policy.

Managers throughout the Department are responsible for ensuring that effective controls are implemented in their areas of responsibility. Individual assurance statements from senior management serve as a primary basis for the Department's assurance that management controls are adequate. The assurance statement provided on page 43 is the result of our annual assessment and is based upon each senior officer's evaluation of controls.

Department organizations that identify material deficiencies are required to submit plans for correcting the cited weaknesses. These corrective action plans, combined with the individual assurance statements, provide the framework for continual monitoring and improving of the Department's management controls.

Material Weakness Reported in FY 2008 Resolved. Corrective actions have been implemented to resolve the "Information Technology (IT) Security" material weakness reported in the *FY 2008 Performance and Accountability Report*. The Office of the Chief Information Officer implemented corrective actions in response to OIG audits and reviews of IT security. These actions have led to a significant improvement in IT security internal controls.

Inherent Limitations on the Effectiveness of Controls. Department management does not expect that our disclosure on controls over financial reporting will prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable—not absolute—assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints. The benefits of the controls must be considered relative to their associated cost. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Federal Financial Management Improvement Act

The Secretary has determined that the Department is in compliance with the *Federal Financial Management Improvement Act of 1996* (*FFMIA*), although the auditors have identified instances in which the Department's financial management systems did not substantially comply with the act.

The Department is cognizant of its auditor's concerns relating to instances of noncompliance with *FFMIA* as noted in the Compliance with Laws and Regulations Report located on pages 118-120 of this report. The Department continues to strengthen and improve its financial management systems.

The *FFMIA* requires that agencies' financial management systems provide reliable financial data in accordance with generally accepted accounting principles and standards. Under *FFMIA*, the financial management systems substantially comply with the three following requirements under *FFMIA*—federal financial management system requirements, applicable federal accounting standards and the use of the U.S. Government Standard General Ledger at the transaction level.

FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT

Management for the Department of Education is responsible for establishing and maintaining effective internal control and financial management systems that meet the intent and objectives of the *Federal Managers' Financial Integrity Act of 1982* (*FMFIA)*. The Department conducted its assessment of the effectiveness of internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations in accordance with the Office of Management and Budget Circular No. A-123, *Management's Responsibility for Internal Control*. Based on the results of this evaluation, the Department of Education can provide reasonable assurance that its internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations as of September 30, 2009, was operating effectively and no material weaknesses were found in the design or operations of the internal controls.

In addition, the Department conducted an assessment of the effectiveness of internal control over financial reporting, which includes safeguarding of assets and compliance with applicable laws and regulations, in accordance with the requirements of Appendix A of the Office of Management and Budget's Circular No. A-123. In accordance with the results of this assessment, the Department of Education can provide reasonable assurance that its internal control over financial reporting as of June 30, 2009, was operating effectively and that no material weaknesses were found in the design or operation of the internal control over financial reporting.

/s/

Arne Duncan
November 16, 2009