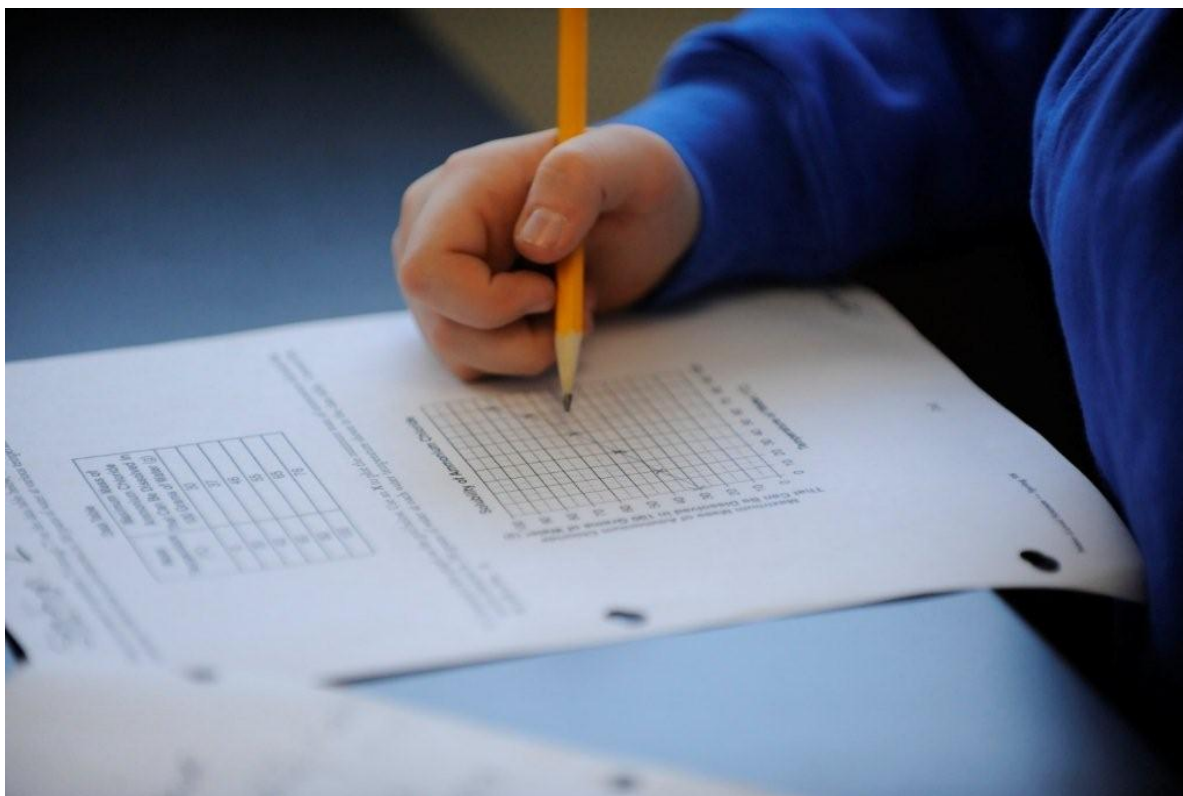

OTHER ACCOMPANYING INFORMATION



IMPROPER PAYMENTS INFORMATION ACT REPORTING DETAILS

The *Improper Payments Information Act of 2002 (IPIA)* (Public Law 107-300) and the Office of Management and Budget's (OMB) Circular A-123, Appendix C, Requirements for Effective Measurement and Remediation of Improper Payments, define requirements to reduce improper/erroneous payments made by the federal government. OMB also has established specific reporting requirements for agencies with programs that possess a significant risk of erroneous payments and for reporting on the results of recovery auditing activities. Agencies are required to annually review and assess all programs and activities to identify those susceptible to significant improper payments. The guidance in OMB Circular A-123, Appendix C, defines a significant improper payment as those in any particular program that exceed both 2.5 percent of program payments and \$10 million annually. For each program identified as susceptible and determined to be at risk, agencies are required to report to the President and the Congress the annual amount of estimated improper payments, along with steps taken and actions planned to reduce them.

The Department has divided its improper payment activities into the following segments: Student Financial Assistance Programs, *ESEA*, Title I Program, Other Grant Programs, and Recovery Auditing.

Student Financial Assistance Programs

Risk Assessment

As required by the *IPIA*, The Department inventoried its programs during FY 2009 and reviewed program payments made during FY 2008 (the most recent complete fiscal year available) to assess the risk of improper payments. The review identified and then focused on the following key programs: Academic Competitiveness Grant (ACG) Program, William D. Ford Federal Direct Loan (Direct Loan) Program, Federal Family Education Loan (FFEL) Program, Federal Pell Grant (Pell Grant) Program, and the National Science and Mathematics Access to Retain Talent (SMART) Grant Program.

In addition to the A-123 guidance, the criteria for determining susceptible risk within the programs were defined as follows:

Programs with annual outlays that exceed \$200 million or programs that were previously required to report improper payment information under OMB Circular A-11, *Budget Submission*, former Section 57.2¹.

¹ The four original programs identified in OMB Circular A-11, Section 57, were Student Financial Assistance (now Federal Student Aid), *ESEA*, Title I, Special Education Grants to States, and Vocational Rehabilitation Grants to States. Subsequently, after further review of the program risk, OMB removed Special Education Grants to States and Vocational Rehabilitation Grants to States from the list. OMB considers Section 57 programs susceptible to significant improper payments regardless of the established thresholds. OMB Circular A-136 also applies.

Risk-Susceptible Programs

The Title IV programs that were deemed to be potentially susceptible to the risk of significant improper payments based on OMB criteria described above include ACG, Direct Loan, FFEL, Pell Grant and SMART. We have reassessed the Federal Supplemental Educational Opportunity Grant and Federal Work-Study Programs and have determined that, due to low volume and relatively low eligibility requirements, they are not risk susceptible.

As data becomes available, the Teacher Education Assistance for College and Higher Education (TEACH) Grant Program will be assessed. It is anticipated that the first assessment will take place in FY 2011.

In FY 2008, the lack of liquidity in financial markets impacted the ability of FFEL lenders and secondary markets to find cost-effective financing. As a result, Congress passed the *Ensuring Continued Access to Student Loans Act of 2008 (ECASLA)*, which was signed by the President on May 8, 2008. This gave the Department authority to purchase FFEL loans from lenders to ensure liquidity in the FFEL. The following three programs were developed under the *ECASLA* mandate:

- Loan Purchase Commitment Program.
- Loan Participation Purchase Program.
- Asset-Backed Commercial Paper (ABCP) Conduit Program.

Federal Student Aid has determined that each of these is potentially a risk-susceptible program. A risk assessment for each of these programs will be completed during FY 2010.

ACG Program. A risk assessment was completed for the ACG Program in FY 2009. Assessment of the risk of improper payments in the ACG based upon audit findings was accomplished by evaluating the results of annual audits required of schools participating in the Federal Student Aid Programs. Information on all audits was queried from the Postsecondary Education Participants System (PEPS), the management information system for all schools participating in the Federal Student Aid Programs. Audit deficiencies resulting in liabilities due to a specific ACG Program violation or due to a violation of regulations applicable to all programs were isolated. The liability amount for each deficiency applicable to the ACG was calculated and totaled and then compared with total funding. The overall improper payment rate, based on this risk analysis, was .0045 percent. Since this rate is below the threshold for reporting on improper payments, no further information on the ACG Program is included herein.

Direct Loan Program. A risk assessment was completed for the Direct Loan Program in FY 2009. There were no changes to the sampling process from prior years. The overall improper payment rate, based on this risk analysis, was 0.38 percent. Since this rate is below the threshold for reporting on improper payments, no further information on the Direct Loan Program is included herein.

FFEL Program. An ongoing risk assessment is in process for FFEL. See Footnote ⁽¹⁾ under Federal Student Aid Improper Payment Reporting Summary.

Pell Grant Program. A risk assessment was completed for Pell Grant Program in FY 2009. There were no changes to the sampling process from prior years. The overall improper payment rate, based on this risk analysis, was 3.5 percent.

SMART Program. Assessment of the risk of improper payments in the SMART Program based upon audit findings was accomplished by evaluating the results of annual audits required of schools participating in the Federal Student Aid Programs. Information on all audits was queried from the PEPS, the management information system for all schools participating in the Federal Student Aid Programs. Audit deficiencies resulting in liabilities due to a specific SMART Program violation or due to a violation of regulations applicable to all programs were isolated. The liability amount for each deficiency applicable to the SMART Program was calculated and totaled and then compared with total funding. The overall improper payment rate, based on this risk analysis, was .00001 percent. Since this rate is below the threshold for reporting on improper payments, no further information on the SMART Program is included herein.

Statistical Sampling

The size and complexity of the student aid programs make it difficult to consistently define “improper” payments. The legislation and OMB guidance use the broad definition: “Any payment that should not have been made or that was made in an incorrect amount under statutory, contractual, administrative, or other legally applicable requirement.” Federal Student Aid has a wide array of programs, each with unique objectives, eligibility requirements, and payment methods. Consequently, each program has its own universe (or multiple universes) of payments that must be identified, assessed for risk, and, if appropriate, statistically sampled to determine the extent of improper payments.

FFEL Program. In FY 2009, the Department worked with OMB to target their improper payment risk analysis using data mining techniques to identify potential improper payments, with particular focus on special allowance payments (SAP) to lenders. In recent years, SAP has been among the largest categories of payments to lenders or guarantors. However, the *College Cost Reduction Act of 2007* reduced SAP rates and, combined with a historically low interest rate environment, has resulted in SAP amounts due to the Department beginning in FY 2007. This substantial decline, coupled with a significant increase in the Direct Loan Program versus FFEL and the proposed move to 100 percent Direct Loans at the end of FY 2010, have resulted in an improving risk profile related to the potential for FFEL improper payments. The agreed-upon *IPIA* targeted SAP analysis discussed above began in the fourth quarter of FY 2009 and is expected to be completed by the end of the second quarter of FY 2010. In addition to the substantial SAP decline, there is a major impact from the new *ECASLA* loan participation and loan purchase processes that needs to be evaluated with regard to the effect on payments to lenders.

Because the Department conducted a risk analysis in FY 2009 focused on identifying sources of potential improper payments, the Department will not be reporting an error rate for the FFEL program in the 2009 AFR. Rather, the Department plans to use information gained from its analysis to establish a new error measurement methodology in FY 2010 that could be used for future reporting purposes.

Pell Grant Program. The Department conducts studies with the IRS using FAFSA data. Data provided by the IRS study are used to estimate improper payments for the Pell Grant Program. The methodology for the Pell Grant Program did not change in FY 2009, and

additional details about the study can be found in the 2008 PAR under the [statistical sampling section](#).

Corrective Actions

FFEL Program. In addition to the payment data analyses mentioned above, Federal Student Aid has a number of existing internal controls integrated into its systems and activities. Program reviews, independent audits and Inspector General audits of guaranty agencies, lenders, and servicers are some of its key management oversight controls. Other control mechanisms include the following:

- **System Edits**—the system used by guaranty agencies, lenders, and servicers to submit bills and remit payments includes “hard” and “soft” edits to prevent erroneous information from being entered into the system and prevent potential erroneous payments. The edits look at a variety of factors (e.g., code combinations, reported amounts etc.) to determine either reasonableness or validity of the data. The hard edits require correction before proceeding with payment processing. The soft edits alert the user and Federal Student Aid to potential errors.
- **Reasonability Analysis**—Data reported by guaranty agencies to the National Student Loan Data System are used to determine payment amounts for account maintenance and loan issuance processing fees. Federal Student Aid also performs trend analysis of previous payments to guaranty agencies and lenders as a means of evaluating reasonableness of changes in payment activity and payment levels.
- **Focused Monitoring and Analysis**—Federal Student Aid targets specific areas of FFEL payment processing that are at an increased risk for improper payments as areas of focus for increased monitoring and oversight. In FY 2009, Federal Student Aid completed a series of audits of guaranty agencies’ establishment of the federal and operating funds in 1998 in response to an OIG recommendation. Those audits are in the resolution process.

Pell Grant Program. A new IRS data retrieval process is scheduled to be implemented as a pilot on January 24, 2010. The new process will be added to the 2009-2010 FAFSA on the Web (FOTW) application. Eligible FOTW applicants and their parents will be presented a link in the financial section of the online application giving them the option to go to an IRS site, review their 2008 income information, and automatically transfer income information into the appropriate fields on the FAFSA. This process, for those who elect to use it, has the potential to significantly reduce errors on the FAFSA and thus reduce improper payments in all Federal Student Aid Programs. If successful, this data retrieval and transfer process will be implemented for the 2010–11 application year, once IRS data becomes available sometime in the summer of 2010. Federal Student Aid is also using the IRS statistical study in which financial data from a random sample of FAFSA submissions are compared with financial data reported to the IRS in annual income tax filings to identify new solutions for preventing improper payments.

Federal Student Aid Improper Payment Reporting Summary

The following table presents the improper payments outlook for the primary Federal Student Aid programs.

(\$ in millions)

Program	FY 2009 Actual			FY 2010 Estimated			FY 2011 Estimated			FY 2012 Estimated			FY 2013 Estimated		
	Outlays	IP %	IP \$	Outlays	IP %	IP \$	Outlays	IP %	IP \$	Outlays	IP %	IP \$	Outlays	IP %	IP \$
FFEL ⁽¹⁾	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Pell Grant ⁽²⁾	16,281	3.5	570	28,820	3.5	1,009	32,301	3.5	1,131	34,236	3.5	1,198	35,422	3.5	1,240

⁽¹⁾ Since the Department is completing the ongoing risk assessment for FFEL in lieu of a measurement, no error rate will be presented for FFEL in this year's *Agency Financial Report*. This work will include an examination of the error rate methodology followed by development of a new plan and measurement. In addition, the methodology will need to be expanded in the future to reflect the *ECASLA* initiatives.

⁽²⁾ The source of FY 2009 Pell outlays reflects total expenditures from FMSS. The 3.5 IP percent used for 2010-2013 is based on discussions held with OMB during FY 2007 and FY 2008. The 3.5 percent rate is being used since it is a more current target than the targets previously identified in the Federal Student Aid 2006 – 2010 Five-Year Plan.

Note: The final Pell error rate for FY 2008 was 3.69 percent. This 3.69 percent rate was reported as "preliminary" in the *FY 2008 Performance and Accountability Report*, however, it did not change.

Recovery Efforts

For Pell, recovery is achieved through assessments made during program reviews and compliance reviews. Pell also makes recoveries when overpayments to students are assigned to Federal Student Aid for collection. Pell recoveries for the period 2004 through September 30, 2009 are presented in the following table.

Pell Recoveries (Dollars in Millions)					
FY 2004 \$	FY 2005 \$	FY 2006 \$	FY 2007 \$	FY 2008 \$	FY 2009 \$
10.2	11.2	13.6	14.2	10.8	6.6

Statutory and Regulatory Barriers

There are currently no identified barriers which may limit Federal Student Aid's corrective actions in reducing improper payments and actions taken by the agency to mitigate the barriers' effects. The Department previously reported in its PAR that provisions in the Internal Revenue Code precluded it from data-matching with regard to grants made by the Department. Legislation to amend the Internal Revenue Code to allow data-matching capabilities has not been enacted, but through administrative changes, the Department and the U.S. Department of the Treasury implemented a process to verify students' (and their parents') income, tax and certain household information appearing on their tax return that they provide as part of the application for federal student aid. This initiative was cited in the "Journal of Government Financial Management" and recognized as the type of proactive approach that is vital to addressing the root causes of improper payments.

ESEA, Title I Program

The Department performed a risk assessment of the *Elementary and Secondary Education Act of 1965* Title I Program, Grants to Local Educational and Agencies, during FY 2009. The assessment, based on FY 2007 single audit data (the most recent available), yielded an estimated improper payment rate of 0.23 percent or \$29 million. This confirms previously reported data indicating that the risk of improper payments under current statutory requirements is very low. To validate the assessment data, the Department conducts on-site monitoring reviews on a three-year review cycle that encompass all states and territories receiving Title I funds. There were no findings in the monitoring reviews with questioned costs that contradicted the data in the risk assessment.

The Department is continuing to review and monitor for data quality. A key element of the monitoring process involves the wide use of the number of children who qualify for free and reduced-price meals to determine an individual school's Title I eligibility and allocation by local educational agencies. The Title I statute authorizes local educational agencies to use these data, provided under the U.S. Department of Agriculture's national School Lunch Program, for this purpose. In many districts these data are the only indicator of poverty available at the individual school level.

The U.S. Department of Agriculture is working with states and localities to improve program integrity, within the existing statutory and regulatory framework, through enhanced monitoring and auditing. The U.S. Department of Agriculture is also working with the Department and other federal agencies that have programs that make use of these data to explore long-term policy options.

Risk Assessment for Other Grant Programs

The Department's approach to the risk assessment process for non-Federal Student Aid grant programs was to develop a methodology to produce statistically valid measures that

could be applied uniformly across the Department's programs. The intent was to use the same methodology across all non-Federal Student Aid grant programs to establish a level of quality control for all programs and, at the same time, produce a cost-effective measure. The Department deemed it cost effective to utilize the results of the thousands of single audits already being conducted by independent auditors on grant recipients.

In FY 2007, the Department worked with the Department of Energy's Oak Ridge National Laboratory to perform data mining on information available in the Federal Audit Clearinghouse's Single Audit Database, the Department's Grant Administration and Payment System, and the Department's Audit Accountability and Resolution Tracking System to assess the risk of improper payments in its remaining grant programs. To conduct the risk assessment screening, Oak Ridge National Laboratory augmented the Audit Accountability and Resolution Tracking System database with imputed values for the likely questioned costs for grants that were not audited. The imputed and real questioned costs could then be tabulated to provide a reasonable upper-bound estimate of the rate of erroneous payments for each of the functional programs of interest.

If the computed upper-bound percentage was below 2.5 percent, then the actual value would be lower than 2.5 percent. If the computed upper-bound percentage was greater than 2.5 percent, then the actual value may be greater or less than 2.5 percent, but the Department would need additional information to determine the appropriate estimate.

The most striking result of the analysis was the generally low rate of questioned costs. The key finding of this analysis was that for the most recent year for which data were available (FY 2005), none of the functional programs exceeded the threshold value of 2.5 percent. Consequently, none of the programs would be labeled as susceptible to significant erroneous payments.

In accordance with OMB Circular A-123, Appendix C, programs deemed low risk only require a risk assessment every three years unless a program experiences a significant change in legislation and/or a significant increase in funding level. Since the Oak Ridge National Laboratory risk assessments have not indicated any significant risk of improper payments, the Department did not task Oak Ridge National Laboratory to perform the risk assessment for FY 2009. However, the Department is taking the following actions to further improve its monitoring efforts.

Migrant Education Grants to States. The Review of the Migrant Education Program (MEP) focused on the Office of Migrant Education's (OME's) monitoring of child eligibility under Title I, Part C, of the *ESEA*. On December 4, 2007, the Office of Inspector General (OIG) sent an audit closeout memorandum to the Assistant Secretary for Elementary and Secondary Education (OESE), informing her that OIG terminated its audit of the MEP at OME. OIG decided to terminate its audit based on ". . . ongoing changes to Department monitoring, and proposed changes to the migrant law. . ." The memorandum points out, however, that the termination of OIG's review ". . . does not preclude the Department of Education from taking action concerning any aspect of the entities reviewed." Five external audit reports had relevancy to the MEP eligibility issue. Four of the reports have been either resolved or closed.

In June 2009, staff from the Internal Controls Evaluation Group (ICEG) met with personnel from OME to discuss the ramifications of discontinuing tracking the Federal Managers' Financial Integrity Act (FMFIA) deficiencies in relation to OIG's internal audit of the MEP.

Due to the termination of the audit, and after conferring with OME personnel, ICEG concluded there would be no justification for continuing to track the FMFIA deficiencies in this audit. Therefore, OESE need not report these internal control deficiencies in its FY 2009 FMFIA annual certification.

Risk Management Service. The goal of the Risk Management Service in the Office of the Secretary is to identify and take effective action to manage and mitigate risks in the area of grants management that may adversely affect the advancement of the Department's mission. To achieve this objective, the Risk Management Service develops and coordinates a Departmentwide risk management strategy and coordinates and supports consistent, high-quality management of formula and discretionary grants Departmentwide.

The office focuses on identifying potential high-risk grantees before problems begin to occur. Program office and Risk Management Service staff members provide assistance to those grantees regarding their grants and financial management practices to help strengthen the grantees' management of federal funds. In the case of grantees identified as high risk, resources are directed toward solving and managing issues of misuse, abuse, or waste of federal funds. The Risk Management Service has developed a Decision Support System that analyzes available information on grants and grantees, and makes this information available to support decisions on where the Department should deploy resources for oversight and technical assistance. The Decision Support System will continue to develop and expand over the next few years. This year, in response to the risk associated with the large amount of grant funding made available by the *American Recovery and Reinvestment Act of 2009*, the Risk Management Service is also leading Departmentwide technical assistance to the recipients of the largest amount of funds under the Act. Finally, the office also provides customer service in the form of training and responses to inquiries on policy interpretations to grantees, grant applicants, and program offices awarding and monitoring grants.

Managing Risk in Discretionary Grants. In FY 2009, the Department managed more than 10,000 discretionary grant awards. Due to the vast legislative differentiation and the complexity of the Department's grant award programs, ensuring that program staff are fully aware of potentially detrimental issues relating to individual grantees is a significant challenge. Program offices designate specific grants as high risk in accordance with Departmental regulations. The Department uses the Grants High-Risk Module housed within the Department's Grant Administration and Payment System, to track grants and grantees that are designated high risk. Program office staff are required to review and certify their awareness of the high-risk status of applicable grantees before making awards.

Manager Accountability. The Department categorized OMB Circular A-133 single audit findings to provide feedback to program managers regarding the frequency and type of findings within their programs. This assists managers in tailoring their program monitoring efforts to the type of findings that most frequently occur. Additionally, post-audit follow-up courses have been developed to associate audit corrective actions with monitoring to minimize future risk and audit findings. Managerial compliance with monitoring procedures is reviewed and tested during the assurance process under OMB Circular A-123, *Management's Responsibility for Internal Control*.

Planned Corrective Actions. In addition to the actions previously outlined under the Student Financial Assistance Programs and *ESEA*, Title I Program sections, the Department will periodically update any corrective action plans based on the results of the

initiatives outlined above. The Department will record and maintain corrective action plans as required, which will include due dates, process owners and task completion dates.

Information Systems and Infrastructure. The Department has submitted budget requests of \$250,000 for FY 2010 and FY 2011 for information system infrastructure improvements. A portion of the funds will be used to continue the refinement of the Oak Ridge National Laboratory data mining effort. It is also anticipated that the Department will incur costs related to mitigation activities.

American Recovery and Reinvestment Act (Recovery Act) Programs. For FY 2009 and FY 2010, the *Recovery Act* supplemented the Department of Education's appropriations by \$98.2 billion. The law created the new \$48.6 billion State Fiscal Stabilization Fund grant program. The *Recovery Act* also supplemented existing programs, including *ESEA* Title I and *IDEA* Part B and Part C, nearly doubling the funds available for some major grant programs at the Department. Immediately following the enactment of *Recovery Act*, the Department conducted a systematic assessment of the risks presented by the law and concluded that recipient expenditures under all *Recovery Act* grants should be monitored because of the high level of funding. Further, the Department concluded that the State Fiscal Stabilization Fund program should receive a particularly high level of oversight because the program is both new and funded at an extremely high level.

The Department has established an elevated level of oversight for *Recovery Act* grants in order to avoid improper payments. Monitoring for potential excessive draws against these grants began immediately after the Department made the funds available to grantees. The Department quickly automated this process so that the finance system automatically notifies the Federal program officer any time a grantee requests payment of a large sum or a large proportion of a grant. The program officer then contacts the grantee to ensure the payment is in compliance with program rules and federal financial assistance management requirements. The program officer approves the large payment requests before they are processed.

The Department has also automated the review of the expenditure and activities data that recipients are reporting into FederalReporting.gov under the requirements of *Recovery Act* Section 1512. The staff across the Department is reviewing exception reports for inconsistencies between expenditures reported by recipients and the information in the Department's finance system. The staff is also reviewing the reports to gauge the reasonableness of reported expenditures and the relationship of prime recipient draws on their grants to the amount expended by their subrecipients, to monitor for cash management issues.

Recovery Auditing Progress

To effectively address the risk of improper administrative payments, the Department continued a recovery auditing initiative to review contract payments. The Department performed a review of payments based on a statistical sample of FY 2008 payment transactions. No improper payments were indicated in the review. The Department's purchase and travel card programs remain subject to monthly reviews and reconciliations to identify potential misuse or abuse.

Recovery Auditing Summary (in millions)								
Agency Component	Amount Subject to Review for CY Reporting	Actual Amount Reviewed and Reported CY	Amounts Identified for Recovery CY	Amounts Recovered CY	Amounts Identified for Recovery PYs	Amounts Recovered PYs	Cumulative Amounts Identified for Recovery (CY + PYs)	Cumulative Amounts Recovered (CY + PYs)
All	\$1,569	\$29.3	\$0	N/A	\$0.3	\$0.1	\$0.3	\$0.1

Summary

The Department is continuing its efforts to comply with the *IPIA*. Although there are still challenges to overcome, the Department is committed to ensuring the integrity of its programs.

The Department is focused on identifying and managing the risk of improper payments and mitigating the risk with adequate control activities. In FY 2010, we will continue to work with OMB and the Inspector General to explore additional opportunities for identifying and reducing potential improper payments and to ensure compliance with the *IPIA*.

SUMMARY OF FINANCIAL STATEMENT AUDIT AND MANAGEMENT ASSURANCES

The following tables provide a summarized report on the Department's financial statement audit and its management assurances. For more details the auditor's report can be found on pages 103–122 and the Department's Management assurances on pages 42–43.

Summary of Financial Statement Audit					
Audit Opinion	Unqualified				
Restatement	No				
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Ending Balance
Total Material Weaknesses	0	0	0	0	0
Summary of Management Assurances					
Effectiveness of Internal Control over Financial Reporting - <i>Federal Managers' Financial Integrity Act (FMFIA) 2</i>					
Statement of Assurance	Unqualified				
Material Weaknesses	Beginning Balance	New	Resolved	Reassessed	Ending Balance
Total Material Weaknesses	0	0	0	0	0
The Department had no material weaknesses in the design or operation of the internal control over financial reporting.					
Effectiveness of Internal Control over Operations - <i>FMFIA 2</i>					
Statement of Assurance	Unqualified				
Material Weaknesses	Beginning Balance	New	Resolved	Reassessed	Ending Balance
Information Technology Security	1		1		0
Total Material Weaknesses	1	0	1	0	0
Conformance with Financial Management System Requirements - <i>FMFIA 4</i>					
Statement of Assurance	The Department systems conform to financial management system requirements.				
Non-Conformance	Beginning Balance	New	Resolved	Reassessed	Ending Balance
Total Non-Conformance	0	0	0	0	0
Compliance with <i>Federal Financial Management Improvement Act</i>					
	Agency		Auditor		
Overall Substantial Compliance	Yes		No		
1. System Requirements	Yes		No		
2. Federal Accounting Standards	Yes		Yes		
3. United States Standard General Ledger at Transaction Level	Yes		Yes		