GAO
Accountability * Integrity * Reliability

United States General Accounting Office
Washington, DC 20548

June 9, 2003

The Honorable Rod Paige
The Secretary of Education

Subject: *Response to the Department of Education's Request to Reconsider the High-Risk Designation of Federal Student Aid Programs*

Dear Mr. Secretary:

This letter is in response to your May 2, 2003, letter requesting that we make a commitment to reconsider by early this summer our high-risk designation of the Department of Education's Student Financial Aid (SFA) programs. In that letter you outlined how the department has addressed many of the concerns we have identified and the plans it has underway for continued improvements, as well as its plans to update Federal Student Aid's (FSA) Five-Year Performance Plan. In order to help ensure that planned and completed actions address the issues raised in our recent High-Risk and Performance and Accountability reports, you offered to provide a series of briefings to our key managers on:

- plans and progress for sustaining the clean opinion on the department's financial statements;
- FSA progress on its modernization efforts and FSA Data Strategies Framework;
- FSA program integrity initiatives, including FSA default prevention and collection strategies; and
- progress on One-ED (the department's human capital planning initiative).

We accept the offer to attend these briefings and look forward to the opportunity to keep informed of significant progress toward resolving management issues and sustaining improvement in SFA programs.

In 1990, we began our program of reporting on government operations that we identified as high risk. Since then, generally coinciding with the start of each new Congress, we have periodically reported on the status of progress to address high-risk areas and updated our high-risk list. In our January 2003 update[1] for the new 108th Congress, we identified the following actions related to SFA programs as remaining to be completed by the department:

- continue with systems integration and improve plans and reports to better demonstrate progress,
- make comprehensive improvements to address financial management and internal control weaknesses,
- improve plans and reports to clearly explain strategies for achieving default management goals, and
- continue implementation of strategic human capital measures, including succession planning and staff development.

Previously, at the department's request, specific actions needed to address each of these areas were provided to the department in the attached copy of our letter of August 1, 2001, to Deputy Secretary William Hansen. In that letter we compiled a summary of major actions that are critical in addressing the underlying root causes that have resulted in the high-risk designation of SFA programs measured against criteria we use for designation of programs as high risk. For example, the attachment to that letter lays out the following three key measurements of sound financial management for the department and FSA:

- an unqualified audit opinion on the department's financial statements,
- full compliance with the Federal Financial Management Improvement Act (FFMIA) of 1996, and
- correction of material internal control weaknesses identified in the financial statement audit

The department has taken actions over the last several years to improve its financial management and the weaknesses identified. Significant progress was made recently when the department received an unqualified – or "clean" – opinion on its financial statements for fiscal year 2002. While this is an important milestone, significant management weaknesses remain that must be addressed in the other two key measurements we identified, which are discussed in more detail below. In addition, it is important that the department demonstrate that it can sustain the clean opinion, as well as other improvements that are made. As you know, the department first received an unqualified audit opinion on its fiscal year 1997 financial statements, but was not able to sustain that result, nor repeat it until this year.

The first key measure that remains a weakness is compliance with FFMIA. FFMIA requires agencies to institute financial management systems that substantially comply with federal financial management systems requirements, applicable accounting standards, and the federal government's *Standard General Ledger*. Every year since FFMIA was enacted, the department's auditors have reported that the department's

[1]U.S. General Accounting Office, *High-Risk Series: An Update*, GAO-03-119 (Washington, D.C.: January 2003).

systems did not substantially comply with the act's requirements. This continued for fiscal year 2002. According to the auditors, although the department implemented a new financial management system during fiscal year 2002, issues associated with the transition to the new system contributed to difficulties in providing reliable, timely information for managing current operations and timely reporting of financial information to central agencies. The auditors also reported that the department needs to address identified computer security weaknesses in its financial management and other information systems.

The second key measure that remains uncorrected is material internal control weaknesses identified in the financial statement audits. The department's auditors have consistently reported major internal control weaknesses related to financial management systems and financial reporting. In fiscal year 2002, the auditor again reported that significant financial management issues continued to impair the department's ability to accumulate, analyze, and present reliable financial information. While the auditor reported improvements in the latter part of the fiscal year, they reported that they continue to believe that the department needs to place additional focus on reconciliation procedures, account analysis, and financial reporting. Until these issues are fully resolved, the department's ability to produce timely, accurate, and useful financial information for its managers and stakeholders will be greatly impeded.

Designations of programs as high risk because of their greater vulnerabilities to waste, fraud, abuse, and mismanagement, as well as removal of programs' high-risk designations, are the independent and objective judgment of GAO professionals. One of the key factors that enters into the judgment regarding removal of the designation is whether the corrective measures are effective and can be sustained. We have developed and will continue to refine the criteria we use to form judgments on removing high-risk designations. At the time of our January 2003 update to the Congress, agencies were required to have accomplished the following steps before a program's high-risk designation could be removed:

- a demonstrated strong commitment and top leadership support to address the risk(s);
- the capacity (that is, the people and other resources) to resolve the risk(s);
- a corrective action plan(s) that defines the root causes, identifies effective solutions, and provides for substantially completing corrective measures near term, including but not limited to, steps necessary to implement solutions we recommended;
- a program to monitor and independently validate the effectiveness and sustainability of corrective measures; and
- the ability to demonstrate progress in implementing corrective measures.

We are impressed with the level of commitment to addressing the factors that resulted in this high-risk designation, and progress has clearly been made. However, in our independent and professional judgment as of January 2003, the SFA programs did not fully satisfy the criteria for removal from the high-risk list, largely because of the remaining financial management issues. In addition, it is not our policy to address high-risk designations "out of cycle." One key reason for this is to allow enough time between assessments to demonstrate the sustainability of corrective measures. Furthermore, providing for an out of cycle assessment for the Department of Education would set a precedent that would result in other agencies asking for such interim determinations. This would result in a significant unplanned use of resources that would adversely affect our ability to meet congressional mandates and requests on time.

Thus, although we decline to commit to reconsider our January 2003 decision to classify the SFA program as high risk at this time, we will continue to work with the department to ensure that we are informed about and have validated the progress made in resolving these issues and sustaining improvement in all three areas. This proactive approach, which includes consideration of our ongoing work as well as that of the department's outside auditors and the Inspector General, will enable us to promptly assess progress made and challenges that remain in preparation for the next high-risk cycle. In this regard, our next high-risk list is scheduled for publication in January 2005.

We are sending copies of this report to the Secretary of Education and the department's congressional oversight committees. We are also sending copies to the Subcommittee on Government Efficiency and Financial Management, House Committee on Government Reform, the Senate Committee on Governmental Affairs, and other interested parties.

We remain encouraged by the department's commitment to addressing these important challenges. We look forward to continuing to work with you in the future on these very important issues.

Sincerely yours,

David M. Walker
Comptroller General
of the United States

Enclosure

(190099)

GAO
Accountability * Integrity * Reliability
United States General Accounting Office
Washington, DC 20548

August 1, 2001

Mr. William D. Hansen
Deputy Secretary
Department of Education

Dear Mr. Hansen:

It was a pleasure meeting with you last week, and we look forward to working with you on a proactive basis to help the Department of Education address its major management challenges. Key among these management challenges is addressing the issues that have resulted in our "high-risk" designation of Education's Student Financial Assistance (SFA) programs. As you know, in 1990 we designated SFA's programs as high-risk due to long-standing conditions that make the program highly susceptible to fraud, waste, abuse, or mismanagement. While many of the conditions we have identified in our series of reports on high-risk programs have been addressed, significant issues remain and therefore our high-risk designation continues.[1]

As you requested, we have compiled the attached summary of the major actions that need to be taken in order for SFA's programs to be removed from our high-risk list. This summary includes recommendations and other actions that are critical to addressing the underlying root causes that have resulted in the high-risk designation of SFA's programs. These issues generally center around the need to

- Strengthen financial management and internal controls such that relevant, reliable, timely information is available to efficiently and effectively manage day-to-day operations and provide adequate stewardship and accountability
- Implement an integrated set of information systems that will enable SFA to efficiently manage and effectively control post secondary education assistance programs and administer high quality related services to students, colleges and universities, and financial institutions

[1] High Risk Series: An Update(GAO-01-263, January 2001)

- Maintain a balanced management approach that seeks to minimize noncompliance and default rates while still promoting the widespread use of the program

In addition, we currently have on-going work that will result in recommendations that are likely to be of significance to the high-risk designation, including our improper payments review, management review of SFA, and review of SFA's systems integration efforts. As this work progresses, we will keep you and your team informed of issues that need to be added to the list we are providing today.

We have found that the only way for an agency to be successful in addressing serious management challenges and therefore to be removed from the high risk list is to have (1) a demonstrated strong commitment and top leadership support to address the risks, (2) the capacity to resolve the risks, (3) a comprehensive corrective action plan, (4) a program instituted to monitor and independently validate the effectiveness and sustainability of corrective measures, and (5) the ability to demonstrate progress in having implemented corrective measures. We are encouraged by your sense of urgency and commitment to addressing the Department's management challenges. We commend you for your efforts to date and look forward to working with you in the future on these very important issues.

Sincerely yours,

Marnie S. Shaul for

Cornelia Ashby
Director, Education, Workforce, and Income Security

Linda Calbom

Linda Calbom
Director, Financial Management and Assurance

David McClure

David McClure
Director, IT Management Issues

Page 2

ATTACHMENT

ACTIONS NEEDED FOR REMOVAL FROM GAO'S HIGH RISK LIST

Given that managing SFA is similar to operating a financial institution, strengthening financial management systems and controls is key to reducing SFA's exposure to fraud, waste, error and mismanagement. A collective set of key measurements of sound financial management include

- An unqualified audit opinion on the Department's financial statements
- Full compliance with the Federal Financial Management Improvement Act
- Correction of all material internal control weaknesses identified in the financial statement audit

The ultimate goal of good financial management is to have strong systems and controls that produce timely, relevant, reliable information throughout the year so that it is available to program managers for informed decision making purposes. The recommendations listed under items 1-3 below were made by the agencies' outside auditors and are key to achieving this goal. The recommendations were made to address identified material internal control weaknesses, which are also listed. While these recommendations relate to the agency as a whole, they are generally applicable to SFA and therefore are key to it's removal from the high risk list.

1. Financial Management Systems and Financial Reporting Need to Be Strengthened

Recommendations:

- Complete the implementation plan for the replacement of the general ledger software package and ensure the transition occurs in a timely and documented manner. In addition, the Department should ensure that the new general ledger software package will meet its financial reporting needs, including an automated closing process and interim reporting capabilities, thereby facilitating the preparation of financial statements by reporting group and at the consolidated level.

- Develop and enhance procedures for account analysis to ensure that periodic analyses are completed that will detect errors and irregularities in a timely manner.

- Enhance policies and procedures surrounding the preparation and review of adjustments and provide training to ensure that individuals preparing and reviewing the adjustments receive sufficient guidance to meet financial reporting objectives.

1

ATTACHMENT

- Search for duplicate payments and research improper payments that are identified. In addition, the Department should enhance its current control procedures to ensure that duplicate payments are prevented and/or detected in a timely manner.

- Review and enhance current policies and procedures for controlling the disbursement process. The policies and procedures should ensure that an adequate segregation of duties exists, supervisory reviews are appropriately implemented, and all transactions are properly processed and supported with documentation.

- Assess the roles and responsibilities of each Departmental office (including OCFO, SFA, and Budget Service) involved with the financial reporting process to ensure that appropriate resources and tools are available to achieve the financial reporting objectives established by management.

2. Reconciliations Need to be Improved

Recommendations:

- Update current policies and procedures surrounding reconciliations of all significant accounts and programs, including budgetary accounts and the reconciliation of subsidiary ledgers or feeder systems to FMSS. These policies and procedures should be specific in order to provide sufficient guidance to the Department's personnel. The Department should review its policies and procedures on a regular basis to ensure that they remain current and are achieving management's objectives.

- Perform reconciliations of all significant accounts and programs, both proprietary and budgetary, on at least a monthly basis. Reconciliations should also be performed between subsidiary ledgers or feeder systems and FMSS on a monthly basis. The reconciliations should include documentation of the research performed and the resolution of the issue. All differences identified should be researched and resolved in a timely manner. In addition, a supervisory review of the reconciliations should be performed. Pertinent reconciliations performed by SFA and other Department offices should be coordinated with the Financial Management Office within OCFO.

- Resolve unreconciled differences specific to the Budget Clearing and suspense accounts on a timely basis. In addition, determine the disposition of the funds that will be placed in the Treasury receipt account.

ATTACHMENT

3. Controls Surrounding Information Systems Need Enhancement

Recommendations:

- Finalize development of the business continuity and disaster recovery plans for the EDCAPS applications and the underlying infrastructure. Once developed, the plans should be tested and updated regularly to assess their effectiveness.
- Finalize the implementation of effective logging and monitoring controls for the Windows NT platform that supports EDCAPS to allow effective detection and resolution of security relevant events.
- Strengthen the system software change management process to provide effective controls over authorization, testing and documentation of system software changes.
- Complete corrective actions on the information technology security program noted in the fiscal year 2000 FNVU report.

4. A balanced management approach should be pursued. This includes

- vigorously pursuing default management and prevention strategies,
- striking an appropriate balance between providing technical assistance to schools and program monitoring to ensure compliance with laws and regulations, and
- obtaining the human capital and other resources needed to ensure the sustained availability of required data, information systems, and sound management.

GAO's Mission

The General Accounting Office, the audit, evaluation and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through the Internet. GAO's Web site (www.gao.gov) contains abstracts and full-text files of current reports and testimony and an expanding archive of older products. The Web site features a search engine to help you locate documents using key words and phrases. You can print these documents in their entirety, including charts and other graphics.

Each day, GAO issues a list of newly released reports, testimony, and correspondence. GAO posts this list, known as "Today's Reports," on its Web site daily. The list contains links to the full-text document files. To have GAO e-mail this list to you every afternoon, go to www.gao.gov and select "Subscribe to daily E-mail alert for newly released products" under the GAO Reports heading.

Order by Mail or Phone

The first copy of each printed report is free. Additional copies are $2 each. A check or money order should be made out to the Superintendent of Documents. GAO also accepts VISA and Mastercard. Orders for 100 or more copies mailed to a single address are discounted 25 percent. Orders should be sent to:

U.S. General Accounting Office
441 G Street NW, Room LM
Washington, D.C. 20548

To order by Phone:	Voice:	(202) 512-6000
	TDD:	(202) 512-2537
	Fax:	(202) 512-6061

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Web site: www.gao.gov/fraudnet/fraudnet.htm
E-mail: fraudnet@gao.gov
Automated answering system: (800) 424-5454 or (202) 512-7470

Public Affairs

Jeff Nelligan, Managing Director, NelliganJ@gao.gov (202) 512-4800
U.S. General Accounting Office, 441 G Street NW, Room 7149
Washington, D.C. 20548