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UNITED STATES GENERAL ACCOUNTING OFFICE
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STATEMENT OF
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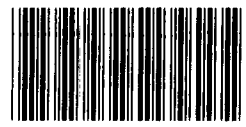
ACTING DIRECTOR
OF THE
ACCOUNTING AND FINANCIAL MANAGEMENT DIVISION
BEFORE THE
COMMITTEE ON GOVERNMENTAL AFFAIRS
UNITED STATES SENATE
ON
IMPROVING THE COLLECTION OF DEBTS
OWED THE GOVERNMENT

Mr. Chairman and Members of the Committee:

We are here at your request to discuss our work in reviewing the Health Professions and Nursing Student Loan Programs. Mr. Chairman, we appreciate your longstanding interest and support of our efforts to improve the collection of debts owed the Government. We have testified before the Committee on several occasions on problems the Federal Government has in collecting its debts, and in support of the comprehensive debt collection legislation you have introduced--S.1249. Passage of this legislation, as well as increased emphasis by agency heads on debt management, are the keys to resolving the Government's longstanding problems in this area.

Today, I will discuss the specific problems identified in an ongoing review you requested at the Department of Health and Human Services and at selected schools regarding the administration of the Health Professions and Nursing Student



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Loan programs. Before beginning, I would like to note that the problems in these programs are not new, but were previously identified by GAO in a May 1974 report titled "Congressional Objectives of Federal Loans and Scholarships to Health Profession Students Not Being Met" (B-164301). Nor are the problems unique to these two loan programs. Instead, they are representative of a general lack of priority given to debt collection by the Federal Government. In the past, emphasis was given to the disbursement of program funds and not to their collection.

PROGRAM DESCRIPTION
AND ADMINISTRATION

In response to the anticipated national shortage of doctors, nurses, and other health professions, Congress enacted the Health Professions Student Loan Program (Public Law 88-129) in 1963 and the Nursing Student Loan Program (Public Law 88-581) in 1964. Federal funds have been given to approximately 1,400 participating institutions (over 1,000 institutions are currently active in the programs), with over $700 million provided since 1963. The President has not included additional funds for the programs in the fiscal 1982 budget submitted to Congress. However, under current legislation schools are allowed to reloan, until December 1986, monies they collect from former student loan recipients.

The Department of Health and Human Services has overall management responsibility for the programs, with the Health Services Administration (HSA) responsible for program administration. These responsibilities include awarding Federal funds

to participating institutions and monitoring their program operations to assure that the funds are used in accordance with Federal program and fiscal regulations. HSA also maintains summary accounting records for the programs and prepares financial reports for use by the agency and the Department of the Treasury. Participating schools are responsible for various other administrative tasks, including making loans to eligible students, collecting repayments, processing requests for loan deferments and cancellations, and requesting writeoffs of uncollectible loans. They are also responsible for annual reporting to HSA on the financial status of their loan programs.

SUFFICIENT EMPHASIS NOT PLACED ON FINANCIAL MANAGEMENT OF THE PROGRAMS

Based on data reported to HSA by about 750 of the over 1,000 actively participating institutions, as of June 30, 1981, over 50,000, or 30 percent, of about 167,000 health professions and nursing student borrowers in loan repayment status were delinquent 90 days or more in making payments. The delinquency rate for borrowers from various disciplines ranged from a low of 6 percent for osteopathic medicine to a high of 56 percent for associate nursing student borrowers. The amount of the outstanding delinquent principal exceeded $63 million and the delinquent payments totaled over $26 million.

The 23 participating schools we reviewed generally contributed to this high rate of delinquency by not placing sufficient emphasis on the billing and collecting of outstanding loans. We found that they did not always use "due diligence" in their

collection programs as required by agency program regulations. For instance:

--promissory notes were not properly controlled,

--exit interviews were not always conducted,

--borrowers were not properly billed, and

--followup action on delinquent debts was not adequate.

We also noted that institutions held large amounts of cash at the end of the academic year; with some investing program funds, but not returning the earnings to the program.

In addition, we found that HSA had not effectively monitored either the institutions' collection activities or their accumulation of large amounts of cash. Further, agency accounting records for the programs were not reliable. At best, the agency made only token efforts to control the funds for the two programs.

I will now discuss our findings in more detail.

SCHOOLS GENERALLY DID NOT COMPLY WITH DUE DILIGENCE REQUIREMENTS

Generally schools reviewed did not comply with all requirements of due diligence and had not placed sufficient attention on collection of student loans.

Lost and incomplete promissory notes

A properly completed and signed promissory note provides evidence that a debt exists, and is the legal document which commits borrowers to repay their obligations. Agency program guidelines state that promissory notes must be properly executed and safeguarded. Nevertheless, 6 of the 23 schools we reviewed could not locate or had misfiled promissory notes. At five

schools we found unsigned notes, while at two schools some borrowers signed incorrect notes. Such casual handling of the promissory notes jeopardizes the schools' ability to collect the loans.

Most schools neglect to complete exit interviews

A properly conducted exit interview is an effective tool in collecting a student loan, providing a school with a final opportunity to secure a borrower's correct address and the name and address of an employer, and to reaffirm the borrower's responsibility to repay the loan. Because of the importance of exit interviews for future collections, program guidelines specify that a written record of the interview be maintained. A July 1974 study for the Department of Health, Education, and Welfare found that schools having lower loan delinquency rates were more likely to conduct exit interviews with nearly all graduating borrowers and vice versa.

However, of the 23 schools we reviewed, only one had documentation indicating exit interviews were always conducted as required and, of about 1400 student borrower files we reviewed, over half did not have a record of a properly completed exit interview.

Borrowers not properly billed

Program regulations require that a borrower be notified approximately 15 to 30 days before the due date of the first required payment and all subsequent payments. But, eight of the schools reviewed had no evidence that borrowers were contacted prior to the due date of their first payment. More seriously,

some schools we visited did not bill all borrowers who were in repayment status or did not bill them regularly. For example:

--103 borrowers with total loans over $162,000, whom we found had graduated or left school, had not been placed on the school's billing system because the school believed the borrowers were still enrolled. For 66 of these borrowers, the first annual billing date had passed without the school having sent a bill.

--Some borrowers at another school had not been billed because the school's automated billing system did not function properly. Even though the school was aware of the problem, the bills had not been sent manually.

--Procedures at another school required annual billing; however, bills were sent sporadically when time permitted rather than on a systematic basis.

In addition, some schools failed to exhaust all means available to locate borrowers when payments were not received in a timely manner. For instance, one school, as a rule, made no additional efforts to contact borrowers once it established it had a wrong address. Furthermore, another school did not use retail credit or tracer organizations to obtain current addresses because it lacked sufficient staff. In addition to helping locate missing borrowers, these organizations can also aid the schools in determining the borrowers' ability to repay their debt.

Followup actions on delinquent loans are not adequate

Program guidelines specify that delinquent borrowers be contacted 15 days after a payment is due, to be followed by

two additional letters in 30-day intervals if the borrower still fails to make payment. We found that 12 of the 23 schools had no evidence that past due notices were sent to all delinquent borrowers and 7 schools, although mailing such notices, did so only sporadically. For example:

--One school mailed past due notices to less than 25 percent of delinquent borrowers whose files we sampled.

--Another school, although apparently contacting all delinquent students, often stopped their contacts for many months or even years even though the borrowers failed to make the required payments.

--At another school, we found no evidence of any collection activity for 7 of 30 randomly selected delinquent borrowers. Two of the seven borrowers were delinquent almost 19 months.

--Loan files at another school included complaints from borrowers stating that they had not made payments, one for over 3 years, because they had not been asked to do so by the school.

One factor contributing to these problems was that 15 of the 23 schools had no written procedures for collecting loans. The first step in establishing a viable debt collection program is development of written procedures. The lack of procedures as well as insufficient staff assigned to collection activities were, in our view, contributing factors to the high delinquency rates.

To supplement schools' collection efforts, program guidance calls for the use of collection agencies, credit bureaus, and

litigation. We found that the 23 schools generally were not using these collection tools:

--10 schools did not use the services of a collection agency.

--We found no evidence that any of the schools reviewed reported delinquent borrowers to credit bureaus, although program guidelines urge such reporting, stating that "notifying credit associations regarding an individual's credit rating has a salutory effect on most individuals whose payments are substantially overdue."

--6 schools did not refer delinquent loans to legal counsel, and our sample review of delinquent borrower files indicated that another 12 schools did so only rarely.

Many delinquent borrowers have good credit ratings in the private sector

Many borrowers with delinquent loans were able to pay. We obtained commercial credit bureau reports that indicated that many had a history of paying their private-sector creditors.

We requested credit reports from a major credit bureau for 100 randomly selected delinquent borrowers from 11 of the 23 schools. Credit reports were available for 54 borrowers--the other 46 borrowers in the sample may have had a credit report at a bureau other than the one we used. Our review of the credit reports for delinquent borrowers showed that

--39, or 72 percent, of the borrowers had what we considered good credit reports.

--31, or 57 percent, had been extended private sector credit

which exceeded the amount of their outstanding debts to the schools. Private-sector creditors had, therefore, determined that these borrowers had the ability to repay an amount at least equal to the amount of their delinquent student loans.

Some specific examples of delinquent borrowers with good commercial credit reports are as follows:

--One borrower, delinquent for over 7 years on a student loan with a balance of $3,288, had recently obtained a loan of $220,000 to purchase real estate.

--Another borrower, delinquent over 3 years on a student loan with a balance of $2,940, had paid off 2 commercial loans for $13,200, was current on a $56,000 loan to purchase real estate, and had a line of credit for $7,700 with several banks and department stores.

--A third borrower, with a Health Professions Student Loan balance of $7,000, delinquent for 10 months, was current on a $25,000 home improvement loan and a $12,400 automobile loan. In addition, three banks and a department store reported that the borrower had a line of credit amounting to $9,900.

These examples illustrate that many borrowers with delinquent student loans are repaying their commercial debts, and that schools have allowed them to ignore the repayment of their student loans with apparently little fear of reprisal, or any of the adverse actions which would normally result from not paying debts they owe to private-sector creditors.

SCHOOLS HELD LARGE AMOUNTS OF IDLE PROGRAM FUNDS

Institutions participating in the two programs have been allowed to accumulate Federal funds in excess of their immediate needs. This is contrary to legislation for the programs and to Federal fiscal regulations, and, more importantly, costs the Treasury millions in interest annually.

In reviewing year-end cash balances reported by the 23 institutions we visited, we found that the amounts reported on the latest available annual operating reports ranged from a low of $1,000 to a high of $1.1 million, totaling $7.3 million for the 23 institutions. We also reviewed cash balances reported by 80 randomly selected schools and, based on that sample review, estimated that all schools actively participating in the two programs held a total of not less than $63 million in year-end cash balances. Allowing schools to hold this much cash could cost the Treasury about $6.3 million interest annually.

We found that annual program funds awarded to the schools were not based on need, and before June 1980, schools were actually encouraged to withdraw all Federal funds made available to them regardless of their current needs. For example,

--One school had unused program funds of about $613,000 at the beginning of the year and, during the same year, collected over $450,000 from prior loans made to students, increasing its loan fund to over $1 million. Although the school only made about $630,000 in new loans, it drew down $176,000 in additional Federal funds for that year.

--Another school had a beginning cash balance of almost $20,000. Although it only loaned about $15,500 during that year, it was given over $31,000 more in Federal funds for that year.

--Yet another school had a beginning cash balance of $176,000 for one of the loan programs. During the year the school loaned a total of $160,000 to eligible students, $16,000 less than the funds available at the start of the year. Nevertheless, the school withdrew an additional $90,000 of available Federal monies for the program during that same year.

In reviewing the 23 schools, we found that 10 of the schools left Federal program funds idle in non-interest bearing accounts. Of the 13 schools that invested program funds, only 1 school returned all and 2 schools returned part of the interest earnings from investments to the appropriate program. The remaining 10 schools used the interest income from invested Federal monies to finance other operations rather than making loans to eligible students. This does not meet the requirements of the law which states that any earnings of the fund must be returned to the program.

HEALTH AND HUMAN SERVICES HAS NOT ADEQUATELY MANAGED THE PROGRAMS

In our view, the Department of Health and Human Services' inadequate administration of the programs is one of the primary reasons for the problems at the schools. Our May 1974 report outlined debt collection problems at participating schools for the Health Professions Loan program similar to those identified

during our current review. We recommended that the Department (1) encourage schools to aggressively collect loans, and (2) closely monitor the schools' collection efforts. The agency said that it would more aggressively monitor the program, acknowledging it had depended too heavily on the schools to use good management procedures, and that it had devoted inadequate resources to monitor the schools.

However, it did not follow through. Program officials attributed their continued failure to properly oversee the two programs to the lack of staff resources, and to the low priority placed on the collection function.

Few onsite assessments have been performed

Onsite assessments of the schools' program administration have been sporadic and few. After we issued our May 1974 report showing that some schools were not properly administering their loan programs, the agency planned to perform onsite program assessments at each school every 3 years, or about 400 assessments annually. Less than 400 assessments, however, were performed during 1977 and 1978, and agency officials told us that very few assessments were completed during the following 2 years. The officials said that the primary cause for not doing the onsite assessments as planned was lack of sufficient resources. Of the 23 schools we reviewed, only 5 schools had an onsite assessment prior to June 1981, when the agency again resumed its onsite monitoring effort. We also found that the programs at 7 of the 23 schools had never been audited by anyone. Since June 1981, about 130 onsite assessments have been completed, with the

assessment reports currently being evaluated by agency staff.

Large backlog in reviewing
annual operating reports

An annual operating report is required for each Health Professions and Nursing Student Loan program a school participates in. The report, if properly used, can be an effective monitoring tool to evaluate an institution's administration of the programs. Agency officials told us that they have not timely reviewed the annual operating reports received from participating schools because the agency lacked staff.

For example, as of March 1981, only 50 percent of the 300 health professions reports and only about 30 percent of the 1,100 nursing student reports for the 1980 school year had been reviewed. In addition, according to agency officials, many annual reports from previous years with "problems", such as discrepancies in the amount of program funds a school had withdrawn during the year, also had not been reviewed. The agency stopped reviewing reports in March 1981 and had not resumed the task by mid-November 1981 even though by that time it also had received 1981 annual reports for the approximately 1100 active institutions.

In December 1980, an agency task group recommended that an automated system be developed to process the schools' annual operating reports immediately upon receipt. It found that the manual review process the agency was using was painstakingly slow and that following up on errors found during the review was equally slow. To date, such a system has not been developed.

Uncollectible loans not reviewed

Before October 1980, program guidelines erroneously stated that legislation did not allow uncollectible loans to be written off until the end of the programs. Although the agency had changed its policy on this matter many years ago, it did not inform the schools of this change until October 1980. As a result, schools have submitted few requests to write off loans considered uncollectible.

As part of the request to write off an uncollectible loan, a school must document that it has followed due diligence in collecting the outstanding loan. By reviewing such evidence, the agency has an opportunity to monitor the schools' collection efforts. As of November 1981, however, only 23 schools had ever requested permission to write off a loan. In total, since inception of the programs nearly 20 years ago, only 150 uncollectible loans amounting to $190,000 have been submitted to the agency for permission to write off, and of these, only 55 loans amounting to $40,000 have been written off. Although well aware that only few schools had asked to write off loans, agency officials did not plan to encourage such requests, because they lack staff for reviewing loan writeoff requests.

Programs are rarely audited

The law (P.L. 95-623, November 9, 1978) requires that schools provide for a biennial audit of the Health Professions Student Loan Program to determine the fiscal condition of their programs and the adequacy of their management practices. This would provide the agency another tool to monitor the programs.

The first such audit was to have been completed by September 1, 1980, with audit reports submitted to the Department of Health and Human Services after completion. Program guidelines strongly recommend that the schools also provide for periodic audits of the Nursing Student Loan Program and that reports of such audits also be submitted to the agency.

However, as of November 1981, the agency had received reports from only 8 of the 300 schools participating in the Health Professions Program and from only 18 of the 1,100 schools in the Nursing Student Program. The agency has so far not followed up on the audit requirements and does not know if the schools have provided for the audits.

CURRENT FINANCIAL STATUS OF THE LOAN PROGRAMS IS UNKNOWN

Compounding the agency's lack of program oversight was the fact that the agency's accounting records did not accurately show the financial status of the loan programs. We found that the loans receivable balance--reported to be about $695 million as of July 1981--was overstated by many millions because:

--The agency had not recorded the Government's share of cancelled loans--estimated to be $66 million. As provided for under the programs, schools may cancel loans upon the death or permanent and total disability of a borrower, if borrowers practice their profession in an area designated as a shortage area, or, in the case of the Nursing Student Loan Program, for employment in a nonprofit agency. Although schools continually reported the amounts of annual loan cancellations, the agency recorded very few of

these cancellations in its accounting system.

--As discussed previously, the agency had written off only $40,000 in loans as uncollectible, even though some loans were delinquent more than 8 years and their collection in the future is unlikely, and

--The agency had not established an allowance for the amount of loans that will be cancelled and those that will be uncollectible in the future.

On the other hand, the loans receivable balance was understated by an undeterminable amount because the agency did not record interest earned on loans made to students. Schools are required to report the amount of their annual interest earnings on loan repayments. The agency, however, did not record this data in its accounting system and, therefore, had no idea of the amount of interest due the Government from the programs.

Further, distortions of the loans receivable balance occurred because schools were allowed to transfer monies--up to 20 percent of the annual award--from the loan funds to corresponding scholarship funds and vice versa. However, necessary adjustments to the agency accounting records may not be recorded until many years after the transfer of funds, and there was no assurance that all adjustments were made. In addition, we found that the agency had not recorded as a liability $3 million owed to participating schools in payment for their share of loans cancelled during the past several years.

In summary, the Department of Health and Human Services must continuously and effectively monitor how the schools administer the loan programs, and take the required measures to assure

that only those schools that adhere to program guidelines are allowed to continue in the programs. The agency also must improve its accounting for the two loan funds. Otherwise, the agency will have no assurance that all monies due the Government are properly repaid.

This concludes my prepared statement. We would be happy to respond to any questions.