U.S. Department of Education
Office of Inspector General

FY 2012
Management Challenges

Please Note:
The Inspector General's *FY 2012 Management Challenges* is available on the ED/OIG Web site at www.ed.gov/offices/oig.
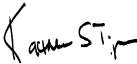
UNITED STATES DEPARTMENT OF EDUCATION
OFFICE OF INSPECTOR GENERAL

The Inspector General

October 3, 2011

MEMORANDUM

TO: Secretary Arne Duncan

FROM: Kathleen S. Tighe
            Inspector General

SUBJECT: Management Challenges for Fiscal Year 2012

The Reports Consolidation Act of 2000 requires the U.S. Department of Education (Department), Office of Inspector General (OIG), to identify and report annually on the most serious management challenges the Department faces. The Government Performance and Results Modernization Act of 2010 requires the Department to include in its agency performance plan information on its planned actions, including performance goals, indicators, and milestones, to address these challenges. To identify management challenges, we routinely examine past audit, inspection, and investigative work, as well as issued reports where corrective actions have yet to be taken; assess ongoing audit, inspection, and investigative work to identify significant vulnerabilities; and analyze new programs and activities that could pose significant challenges because of their breadth and complexity. We provided our draft challenges report to Department officials and considered all comments received.

Last year we presented four management challenges: implementation of new programs/statutory changes, oversight and monitoring, data quality and reporting, and information technology security. All of the prior management challenges remain challenges for FY 2012. The first FY 2011 challenge, implementation of new programs/statutory changes, which incorporated aspects of the American Recovery and Reinvestment Act of 2009 (Recovery Act) and the Ensuring Continued Access to Student Loans Act of 2008, has been incorporated into the oversight and monitoring challenge. In addition, we have added a new challenge related to improper payments.

The FY 2012 management challenges are:

1. Improper Payments,

2. Information Technology Security,

3. Oversight and Monitoring, and

4. Data Quality and Reporting.

We look forward to working with the Department to address the FY 2012 management challenges in the coming year. If you have any questions or would like to discuss these issues, please contact me at (202) 245-6900. You may also contact either Keith West, Assistant Inspector General for Audit, at (202) 245-7041, or William Hamel, Assistant Inspector General for Investigations, at (202) 245-6922.

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Executive Summary

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 the OIG to identify and report annually on the most serious management challenges the Department faces. The Government Performance and Results Modernization Act of 2010 requires the Department to include in its agency performance plan information on its planned actions, including performance goals, indicators, and milestones, to address these challenges.

Last year we presented four management challenges: implementation of new programs/statutory changes, oversight and monitoring, data quality and reporting, and information technology security. All of the prior management challenges remain challenges for fiscal year (FY) 2012. The first FY 2011 challenge, implementation of new programs/statutory changes, which incorporated aspects of the American Recovery and Reinvestment Act of 2009 (Recovery Act) and the Ensuring Continued Access to Student Loans Act of 2008, has been incorporated into the oversight and monitoring challenge. In addition, we have added a new challenge related to improper payments.

The FY 2012 management challenges are:

1. Improper Payments,

2. Information Technology Security,

3. Oversight and Monitoring, and

4. Data Quality and Reporting.

Improper Payments

A significant challenge for management in FY 2012 is the prevention, identification, and recapturing of improper payments. Across the Federal Government, agencies reported an estimated $125.4 billion in improper payments for FY 2010. The Department estimated that it had more than $1 billion in improper payments in the Pell Grant program alone in FY 2010. The Department, as well as other agencies, must be able to ensure that the billions of dollars entrusted to it are reaching the intended recipients. The President has established an aggressive goal to reduce government-wide improper payments by $50 billion by FY 2012. To meet these goals, various pieces of legislation were enacted and implementing guidance was issued. The Department will be

challenged to take actions to meet all the new requirements, and to intensify its efforts to prevent, identify, and recapture improper payments.

Information Technology Security

The Department collects, processes, and stores a large amount of personally identifiable information regarding employees, students, and other program participants. OIG has identified repeated problems in information technology (IT) security and noted increasing threats and vulnerabilities to Department systems and data. For the last several years, OIG's IT audits and Investigative Program Advisory Reports have identified management, operational, and technical security controls that need improvement to adequately protect the confidentiality, integrity, and availability of Department systems and data. We have identified security weaknesses in the incident handling process and procedures, personnel security controls, and configuration management. Compromise of the Department's data would cause substantial harm and embarrassment to the Department and could lead to identity theft or other fraudulent use of the information.

Oversight and Monitoring

Effective oversight and monitoring of the Department's programs and operations are critical to ensure that funds are used for the purposes intended, programs are achieving goals and objectives, and the Department is obtaining the products and level of services for which it has contracted. This is a significant responsibility for the Department given the numbers of different entities and programs requiring monitoring and oversight, the amount of funding that flows through the Department, and the impact that ineffective monitoring could have on the students and taxpayers. Five areas are included in this management challenge—student financial assistance (SFA) program participants, distance education, Recovery Act programs, grantees, and contractors.

Student Financial Assistance Program Participants

The Department must provide effective oversight and monitoring of participants in the SFA programs under Title IV of the Higher Education Act of 1965 as amended to ensure that the programs are not subject to fraud, waste, abuse, and mismanagement. Under the President's budget, the Department expects to provide more than $189 billion in grants, loans, and work-study assistance for these programs in FY 2012. An estimated 15.9 million students and their families will rely on the SFA programs to help fund their postsecondary educations. Participants in the SFA programs include postsecondary institutions, lenders, guaranty agencies, and third-party servicers. Our work has identified weaknesses in the Department's oversight and monitoring of these participants. The Department has taken corrective actions to address many of the recommendations contained in our prior reports. However, the Department needs to continue to assess and improve its oversight and monitoring of program participants and take effective actions when problems are identified.

Distance Education

Distance education refers to courses or programs offered through telecommunication, such as through Internet connection with a postsecondary institution. The flexibility offered is popular with students pursuing education on a nontraditional schedule. Many institutions offer distance education programs as a way to increase their enrollment. Management of distance

education programs presents a challenge for the Department and school officials because of limited or no physical contact to verify the student's identity or attendance. OIG audit work has found that for distance education programs, schools face a challenge in determining when a student attends, withdraws from school, or drops a course. Attendance is critical because it is used to determine the student's eligibility for Federal student aid and to calculate the return of funds if the student withdraws or drops out. Our investigative work has also identified numerous instances of fraud involving distance education programs. These cases involved the exploitation of vulnerabilities in distance education programs to fraudulently obtain Federal student aid. Also, some requirements for residential programs do not translate clearly for distance education programs, and guidance is not available to address these issues. The Department needs to develop requirements specific to distance education and to increase its oversight of schools providing programs through distance education.

Recovery Act Programs

The Recovery Act provided significant additional funding to help improve the economy and enhance education reforms. This included funding for new educational programs and existing programs. Over the last year, the challenge for the Department has moved from implementing the programs to monitoring the programs to ensure that program funds are expended for the purposes intended and that the goals and objectives of the programs are being met. In FY 2012, the Department will also be providing oversight of the winding down of the programs and funding provided. The OIG and the Government Accountability Office have conducted significant amounts of work at the Department, State agencies, and local educational agencies (LEAs). This work identified a number of control weaknesses related to the use of funds, cash management, subrecipient monitoring, and impacts on maintaining levels of funding for education programs. We made recommendations to improve implementation and monitoring of Recovery Act programs. The Department has taken proactive measures to coordinate the effective implementation and oversight of the Recovery Act and to provide technical assistance to recipients. Additional oversight and monitoring could enhance the Department's ability to ensure that Federal funds are effectively managed and that deficiencies noted in audits and other reviews are corrected timely. The Department must continue to provide guidance and assistance to recipients on these programs, identify and obtain additional resources for program monitoring, and take timely corrective actions to address issues noted in audits and other reviews.

Grantees

Effective monitoring and oversight are essential to ensure that grantees meet grant requirements and achieve program goals and objectives. In addition to our work on Recovery Act programs, our work on other grant programs has identified a number of weaknesses in grantee oversight and monitoring. We have identified pervasive fiscal control weaknesses at a number of grantees, weaknesses in a grant payback program, as well as fraud committed by LEA and charter school officials. The Department is responsible for monitoring the activities of grantees to ensure compliance with applicable Federal

requirements and that performance goals are being achieved. The Department has taken corrective actions to address many of the recommendations contained in our reports. However, the Department needs to continue to assess and improve its oversight and monitoring of grantees and take effective actions when issues are identified.

Contractors

The Department relies heavily on contractor support to accomplish its mission and to ensure the effective operations of its many systems and activities. The current value of the Department's active contracts is nearly $5.4 billion. Once a contract is awarded, the Department must effectively monitor performance to ensure that it receives the quality and quantity of products or services for which it is paying. OIG reports have included numerous deficiencies in the area of contract monitoring, and we have made recommendations for corrective action. The Department has taken action to address many of the issues noted. A critical issue hampering significant improvement, however, is the shortage of appropriately qualified staff to adequately monitor contractor performance. A concerted effort is needed to develop and implement an aggressive human capital plan to address this issue.

Data Quality and Reporting

The Department, its grantees, and its subrecipients must have controls in place and effectively operating to ensure that accurate, reliable data are reported. Data are used by the Department to make funding decisions, evaluate program performance, and support a number of management decisions. State educational agencies (SEAs) annually collect data from LEAs and report various program data to the Department. The Recovery Act places a heavy emphasis on accountability and transparency, including reporting requirements related to the awarding and use of funds. All recipients and subrecipients are mandated to provide information about their awards on a publicly available Web site authorized by the statute. The new reporting requirements required Federal, State, and local agencies to quickly develop the systems and infrastructure to collect and report the required information. The Department must educate recipients about the reporting requirements, assess the quality of the reported information, and use the collected information effectively to monitor and oversee Recovery Act programs and performance. Our work has identified a variety of weaknesses in the quality of reported data and recommended improvements at the SEA and LEA level, as well as actions the Department can take to clarify requirements and provide additional guidance. Establishing more consistent definitions for data terms will enhance reporting accuracy and comparability. For Recovery Act programs, our work noted weaknesses in controls over data quality and reporting, both externally at SEAs and LEAs, and internally at the Department. Ensuring that accurate and complete data are reported is critical to achieving the transparency goals of the Recovery Act, as well as supporting effective management decisions.

Each challenge is discussed in more detail in the sections that follow. The titles and dates of the audits, inspections, and investigations referenced in this report are noted in Appendix A.

Improper Payments

Summary

A significant challenge for management in FY 2012 is the prevention, identification, and recapturing of improper payments. Across the Federal Government, agencies reported an estimated $125.4 billion in improper payments for FY 2010. The U.S. Department of Education (Department) estimated that it had more than $1 billion in improper payments in the Pell Grant program alone in FY 2010. The Department, as well as other agencies, must be able to ensure that the billions of dollars entrusted to it are reaching the intended recipients. The President has established an aggressive goal to reduce government-wide improper payments by $50 billion by FY 2012. To meet these goals, various pieces of legislation were enacted and implementing guidance was issued. The Department will be challenged to take actions to meet all the new requirements, and to intensify its efforts to prevent, identify, and recapture improper payments.

Background

The Department stated in its FY 2010 Annual Financial Report that it needs to continue to explore additional opportunities for identifying and reducing potential improper payments and to ensure compliance with the Improper Payments Information Act of 2002 (IPIA). In March 2011, before the Committee on Appropriations, Subcommittee on Labor, Health and Human Services, Education, and Related Agencies, the Department reported that the Pell Grant program is susceptible to significant improper payments and that the program's improper payment rate was more than 3 percent, or more than $1 billion annually, including both underpayments and overpayments, as a result of incorrectly reported recipient income.

A number of new requirements related to improper payments were enacted in FY 2010 and were effective immediately. Some of the requirements impact agency reporting for FY 2011 and subsequent years. For example, the Improper Payments Elimination and Recovery Act of 2010 (IPERA), which amends the IPIA and repeals the Recovery Auditing Act, significantly increases agency recapture efforts by expanding the types of payments that can be reviewed and by lowering the threshold of annual outlays for the requirement to perform recapture audit programs. Previously under the Recovery Auditing Act, the Department had to perform recovery efforts only in the area of contracts with a total value in excess of $500 million. Implementing IPERA is a challenge because the threshold for conducting payment recapture reviews is lowered to just $1 million in annual outlays and is expanded to cover all types of payments, including contracts, grants, loans, and benefits when the agency makes more than $1 million in such annual outlays and conducting a recapture review is deemed cost effective.

The Administration's continued efforts to reduce improper payments also imposed additional reporting requirements upon agencies through Executive Order 13520 of November 20, 2009, "Reducing Improper Payments." The Office of

Management and Budget's (OMB) implementing guidance contained in Part III to Appendix C, "Requirements for Effective Measurement and Remediation of Improper Payments," of OMB Circular A-123, "Management's Responsibility for Internal Control," requires the Department to issue quarterly reports on any high-dollar overpayments identified.

In addition, OMB designated the Pell Grant program as a high-priority program in FY 2011, pursuant to Executive Order 13520. As a result, the Department must establish semiannual or more frequent measurements for reducing improper payments in the program and prepare an Accountable Official's Annual Report.

Results of Work Performed

The Office of Inspector General's (OIG's) work related to improper payments has evolved and increased over the years to include evaluating specific Departmental controls to prevent and detect improper payments; reviewing and providing recommendations on the Department's improper payment risk assessments; auditing the Department's Federal Student Aid (FSA) office's methodology for estimating improper payments in the Federal Family Education Loan Program (FFELP); and reviewing, auditing, and investigating major recipients of Federal funds.

OIG audit and investigative work continues to identify various improper payments in the Student Financial Assistance (SFA) programs, to State educational agencies (SEA) and local educational agencies (LEA), to other grantees, and to contractors.

Many of our reviews of SFA programs continue to disclose improper payments. Our audits and investigations of postsecondary institutions routinely disclose payments resulting from ineligible students, ineligible programs, or other noncompliance. In September 2008, we issued an audit of the Department's FFELP improper payment estimation process and found that FSA used different methodologies for estimating the improper payment rates for FY 2006 and FY 2007 and planned to use another methodology for FY 2008. We also identified several significant factors that affected the reliability of the calculated improper payment rates. In a series of lender audits issued in FY 2005 through FY 2009, we noted significant improper special allowance billings. For the time periods reviewed, our five audits questioned more than $360 million in improper payments for loans that did not qualify under a special allowance rate. In addition, for one lender, we estimated that if the abuse was not stopped, an additional $882 million of improper payments would be paid over the life of the ineligible loans. As a result of our work, lenders were required to undergo independent audits to determine the eligibility of loans for certain special allowance payments. In FY 2008, these audits identified that 90 percent of the loans billed were ineligible and prevented well over a billion dollars in improper payments.

In addition to work in the SFA programs, we have performed a substantial amount of work addressing fiscal issues at SEAs and LEAs. For example, in June 2011 we issued an audit of the Camden City Public School District that identified approximately $4.5 million in contracts that were missing or inadequately executed and a total of more than $4 million in expenditures that were inadequately supported. In January 2010, we issued an audit of the Philadelphia School District in which we found that expenditures totaling more than

$138 million were either unallowable or inadequately supported. In July 2009, we compiled a report for the Department on the pervasive fiscal issues reported in more than 40 OIG audits of SEAs and LEAs. These audits collectively identified approximately $62 million in unallowable costs, $119 million in inadequately documented costs, and $1.4 billion in funds determined to be at risk. These amounts were, in most cases, a direct result of internal control weaknesses, including lack of adequate policies and procedures, policies and procedures that were not followed, and a lack of understanding regarding program regulations and guidance. To address these weaknesses, we suggested that the Department enhance its guidance to SEAs and LEAs on how to implement the administrative requirements of Federal grants and ensure that SEA and LEA officials understand the importance of complying with the requirements.

In May 2009, we issued our final audit report on the National Assessment of Educational Progress contract which noted improper payments—the most significant of which were disclosed by the contractor during our audit work. The Department recovered nearly $3.2 million in improper payments and interest from the contractor. Further investigative work identified additional overbillings by this contractor on other contracts with the Department and on contracts with four other Federal agencies. In May 2011, the contractor entered into a civil fraud settlement with the Government for an additional $1.4 million payment to the Department and also repaid the other four Federal agencies a total of more than $135,000 in improper payments.

OIG work continues in this area as we monitor the Department's quarterly reports on high-dollar overpayments and evaluate actions being taken in response to improper payments noted. For all high-dollar overpayment amounts reported on the quarterly reports through June 30, 2011, the Department has reported that it has or will recover the funds, and that it has taken action or has plans to implement adequate control activities that will mitigate the risk of future improper payments. In addition, the OIG is currently evaluating the Department's process for identifying and reporting the high-dollar overpayments. We have also started planning our evaluations of the Department's compliance with IPERA and our review of the Department's Accountable Official's Annual Report covering the Pell Grant program.

Department Actions/Plans

As reported in its FY 2010 Annual Financial Report, the Department performed its annual review and assessment of its programs and activities to identify those susceptible to significant improper payments. The Department reported the annual amount of estimated improper payments for the William D. Ford Federal Direct Loan Program (Direct Loan program), the FFELP, and the Pell Grant program, along with steps taken and actions planned to reduce improper payments. The Department continues to consult with OMB on improving and revising its processes for developing estimates for its programs and activities.

Corrective actions the Department states that it has taken or has planned include payment data analyses, implementation of various preventive controls such as the review of system edits warnings prior to approval of payments, reasonability analysis and trend analyses to evaluate changes in payment activity and levels, and focused monitoring and analysis by targeting areas of payment processing that are at an increased risk for improper payments. Specific to the Pell Grant

program, the Department has implemented an Internal Revenue Service (IRS) data retrieval tool. This process enables students to transfer certain tax information from an IRS site directly to their on-line Free Application for Federal Student Aid (FAFSA) to minimize errors and provide additional assurance of accuracy of the data included on the application.

The Department is also performing various activities related to detecting, handling, and reclaiming improper payments within some of its offices. For example, actions taken or planned as reported in the quarterly high-dollar overpayment reports include recovery of funds, automation of manual certification processes to include validation of payee codes, training, review of manual and change processes, review of refund processes, and the potential purchase of improper payment detection software.

As required by OMB Memorandum M-11-04, "Increasing Efforts to Recapture Improper Payments by Intensifying and Expanding Payment Recapture Audits," the Department also developed its payment recapture audit plan. The plan, which was submitted to OMB and the OIG in January 2011, describes the Department's current and past recapture efforts as well as planned recapture efforts for the future.

Further Actions Needed to Address the Challenge

The Department needs to continue to explore additional opportunities for preventing, identifying, and recapturing improper payments. It needs to fully implement the various activities it states that it will pursue in its payment recapture audit plan, to include the exploration of new tools, new technologies, and new administrative strategies. In addition, the Department needs to explore and implement new and effective improper payment prevention controls as part of its overall efforts to reduce the potential for improper payments.

Information Technology Security

Summary

The Department collects, processes, and stores a large amount of personally identifiable information regarding employees, students, and other program participants. OIG has identified repeated problems in information technology (IT) security and noted increasing threats and vulnerabilities to Department systems and data. For the last several years, OIG's IT audits and Investigative Program Advisory Reports (IPARs) have identified management, operational, and technical security controls that need improvement to adequately protect the confidentiality, integrity, and availability of Department systems and data. We have identified security weaknesses in the incident handling process and procedures, personnel security controls, and configuration management. Compromise of the Department's data would cause substantial harm and embarrassment to the Department and could lead to identity theft or other fraudulent use of the information.

Background

The IT infrastructure for the Department is provided through the Education Department Utility for Communications, Applications, and Technology Environment (EDUCATE) contract. Services such as email, network, desktop, security, and printers are provided under this vehicle. Additionally, the Department has a large Virtual Data Center contract that provides IT support for FSA data processing. Specifically, the Virtual Data Center serves as the host facility for FSA systems that process student financial aid applications (grants, loans, and work study), provides schools and lenders with eligibility determinations, and supports payments from and repayment to lenders.

Most of FSA's major business applications are located at the Virtual Data Center, except for one other major application called Common Origination and Disbursement. The production support/processing for this application is located at the facility of another Department contractor. The Common Origination and Disbursement processing system initiates, tracks, and disburses funds to eligible students and schools for SFA programs.

The Department has experienced sophisticated attacks to its IT systems, including hostile Internet browsing and phishing campaigns resulting in malware infections, as well as unauthorized accesses accomplished by credentials stolen through keystroke loggers. Many of the computers that are compromised are not Department systems but the home/work computers of students, contractors, and program participants such as schools, lenders, guaranty agencies, and servicers. Although the Department can specify security controls for its contractors, it has little authority in the malware detection practices of these other parties.

Results of Work Performed

Our audit work continues to identify certain control weaknesses within IT security and systems that need to be addressed. The annual financial statement audits for the Department and FSA have identified IT controls as a significant deficiency for

the past several years based on weaknesses related to access controls, noncompliant passwords, and administrator account monitoring. OIG IT audits and IPARs have noted these same issues, as well as noncompliance with certification and accreditation requirements, inadequate change controls, Privacy Act implementation, incident response, patch management, and inaccurate systems inventories. Also, as noted under the challenge related to contractor oversight, the Department has not effectively implemented a process to detect and report violations of its security requirements to ensure that its network is adequately protected. OIG has made recommendations to (1) increase areas of security awareness training; (2) enforce the contract requirement to comply with the Department's Handbook for Information Security Incident Response and Reporting Procedures when performing incident response, or develop a separate capability to perform incident response in accordance with the handbook; (3) improve controls over contractors and other outside system users, including conducting security screenings and performing background investigations; and (4) implement two-factor authentication to mitigate the risks associated with the security breaches the Department has already experienced.

OIG work continues in this area with our recent completion of an audit evaluating security controls over EDUCATE, as well as assessing the agency's overall compliance with the security provisions of the Federal Information Systems Management Act of 2002 (FISMA). The EDUCATE audit identified deficiencies in many of the same areas identified in prior IT security audits. In FY 2012, we plan to conduct an audit of the Education Central Automated Processing System (EDCAPS) to determine the effectiveness of the Department's overall information security program and practices for EDCAPS. EDCAPS is a suite of financial applications that encompass the Department's core financial management processes. EDCAPS serves approximately 2,500 internal users at the Department's headquarters and 21,000 external users across the nation and worldwide. Additionally in FY 2012, we will conduct an audit to evaluate the Department's overall compliance with FISMA requirements.

Department Actions/Plans	In response to our audits, the Department provided corrective action plans to address the recommendations, and work is in process to implement these actions. The Department has procured services to provide additional intrusion detection capabilities for its primary enterprise environment and related EDUCATE data center. The Department has also started the implementation of two-factor authentication for Government and contractor employees in an effort to comply with requirements, but significant progress is still needed.
Further Actions Needed to Address the Challenge	Vulnerabilities continue to exist in the programs intended to identify and protect critical technologies. We are still finding instances of the same deficiencies in our current audits. Security breaches have already permitted malware to be installed on end-users' computers resulting in the compromise of usernames and passwords for Department systems. Because antivirus detection software often lags behind the most current sophisticated malware by some period of time, and malware code can be rapidly changed to prevent identification, the Department must have a robust capability to identify and respond to malware installations.

The Department cannot control the security of computer systems used by its external business partners, students, and other citizen users. However, this business risk can be reduced by implementing/deploying two-factor authentication. Two-factor authentication will prevent unauthorized users (associated with keyloggers) from accessing the Department's major business applications.

The Department needs to develop more effective capabilities to respond to potential IT security incidents. Although there have been some plans to implement an incident response team, to date, no such enhanced capability has emerged. The current response process is generally limited to pulling computer systems from the network and implementing blocking of known malicious traffic. The Department needs to effectively address and eliminate IT security deficiencies where possible, continue to provide mitigating controls for vulnerabilities, and implement planned actions to correct system weaknesses.

Oversight and Monitoring
Student Financial Assistance Program Participants

Summary

The Department must provide effective oversight and monitoring of participants in the SFA programs under Title IV of the Higher Education Act of 1965 as amended (HEA) to ensure that the programs are not subject to fraud, waste, abuse, and mismanagement. Under the President's budget, the Department expects to provide more than $189 billion in grants, loans, and work-study assistance for these programs in FY 2012. An estimated 15.9 million students and their families will rely on the SFA programs to help fund their postsecondary educations. Participants in the SFA programs include postsecondary institutions, lenders, guaranty agencies, and third-party servicers. Our work has identified weaknesses in the Department's oversight and monitoring of these participants. The Department has taken corrective actions to address many of the recommendations contained in our prior reports. However, the Department needs to continue to assess and improve its oversight and monitoring of program participants and take effective actions when problems are identified.

Background

Federal SFA programs are administered under complex legal and regulatory requirements and rely on the participation of numerous non-Federal entities. Approximately 6,200 postsecondary institutions, approximately 2,900 FFELP lenders, 33 guaranty agencies, and numerous third-party servicers participate in the SFA programs. The Student Aid and Financial Responsibility Act of 2010 (SAFRA) ended the making (origination) of new FFELP loans after June 30, 2010. New loans are originated under the Direct Loan Program. Under the Direct Loan Program, funding is provided by the Federal Government through postsecondary institutions while loan origination and servicing are handled by public and private entities under contract with the Department. Although the SAFRA ended the origination of FFELP loans, lenders, guaranty agencies, and their third-party servicers will continue to service FFELP loans. There were $416 billion in outstanding FFELP loans and $221 billion in outstanding Direct Loans as of September 30, 2010. The Department projects that as of September 30, 2011, there will be $461 billion in outstanding Direct Loans and $339 billion in outstanding FFELP loans. As a result of SAFRA, about 5,500 domestic and foreign postsecondary institutions that formerly participated in the FFELP transitioned to the Direct Loan Program.

The continued poor economic situation may be limiting the ability of borrowers to repay their loans. In August 2011, the Federal Reserve Bank of New York reported that about 11 percent of student loan balances were 90 or more days delinquent, up from about 6.5 percent in 2003. By comparison, about 12 percent of credit card balances were delinquent—the highest percentage for any type of household debt and credit. Also, as a result of the economic situation, the amount of time it takes to repay loans may increase, borrowers may use more deferments and

forbearances, and more borrowers may default. These changes may increase the administrative and subsidy cost of operating the loan programs. On September 12, 2011, the Department released the official FY 2009 national student loan cohort default rate of 8.8 percent, up from 7.0 percent in FY 2008,[1] an increase of more than 25 percent. The Secretary of Education stated, "These hard economic times have made it even more difficult for student borrowers to repay their loans." We believe that the most significant financial risk to the Department is increasing loan volumes, increasing defaults, and the ability to effectively collect on loan defaults.

Results of Work Performed

Our audits and inspections have identified serious weaknesses in FSA's oversight and monitoring of SFA program participants. In FY 2011, we performed an inspection that found weaknesses in FSA's monitoring of schools' financial responsibility. In FY 2009, we reported weaknesses in FSA's monitoring of guaranty agencies, lenders, and servicers. (This audit updated a prior audit effort and found that many of the previously reported weaknesses persisted.) Issues noted in internal audits and inspections of FSA's oversight and monitoring of the SFA program participants have included the following:

FSA Control Environment Weaknesses

In our 2009 review of FSA's oversight and monitoring of lenders, guaranty agencies, and servicers, we identified internal control weaknesses in each of the Government Accountability Office (GAO) "Standards for Internal Control in the Federal Government." Improvement was needed in oversight of program participants; delegation of authority was not properly aligned with oversight and monitoring of guaranty agencies, lenders, and servicers; and potential conflicts of interest existed with the former general manager of Financial Partners Services.

Lack of Sufficient and Appropriately Qualified Staff

In the same audit, we found that FSA had not dedicated sufficient resources to effectively monitor the FFELP participants and had not established mandatory training requirements for FSA program reviewers.

Risk Assessment

Our 2009 review of FSA's Enterprise Risk Management Program noted that the organization had not fully implemented enterprise risk management. FSA's enterprise risk management function was intended to develop risk assessments and provide a more strategic view of future risks. The function was also designed to better equip senior management to anticipate, analyze, and manage risks inherent in the SFA programs. However, the program had not yet included any of the business units directly responsible for administering the SFA programs.

Monitoring Activities

In our 2009 review of FSA's oversight and monitoring of lenders, guaranty agencies, and servicers, we found that program reviews of FFELP participants

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[1] The rates represent a snapshot in time, with the FY 2009 cohort consisting of borrowers whose first loan repayments came due between October 1, 2008, and September 30, 2009, and who defaulted before September 30, 2010. More than 3.6 million borrowers from 5,900 schools entered repayment during this window of time, and more than 320,000 borrowers defaulted.

were not properly supervised or performed consistently and that FSA did not consistently quantify and document liabilities. As a result, funds that were inappropriately used were not always recovered. We also found that delegations of authority were not current with respect to FSA staff who could waive liabilities noted in program reviews, and lenders' submissions of required annual compliance audit reports were not monitored. Some of these weaknesses were also reported in the prior audit of this area, indicating that effective corrective actions were not taken.

Our 2010 audit of FSA's controls over loan purchases under the Ensuring Continued Access to Student Loans Act of 2008 (ECASLA) determined that FSA had adequate controls to reasonably ensure that it did not purchase from lenders ineligible loans under the Loan Purchase Commitment Program. We found significant weaknesses in the controls that were in place to reasonably ensure that lenders participating in the Loan Participation Purchase Program complied with loan eligibility requirements; however, we determined that these weaknesses had a minimal impact on the number and amount of ineligible loans in which the Department purchased a participation interest.

Our 2011 inspection of FSA's monitoring of schools' financial responsibility found that FSA did not always take appropriate action when it identified that a school was potentially not in compliance with the financial responsibility requirements. Specifically, FSA's procedures did not define when the failure to submit financial statements and compliance audits would result in a determination that the school was not financially responsible. Also, FSA did not enforce the requirement that schools submit a letter of credit in order to continue participating in the SFA programs.

In FY 2011, GAO reported that stronger oversight by the Department was needed to enforce the ban on incentive payments to school recruiters. Specifically, GAO found that while FSA has a process to monitor schools for violations, its methods to detect violations and track monitoring activities were limited, and FSA's policies and practices hindered its enforcement efforts. In FY 2010, GAO found that FSA lacked policy and procedures to ensure receipt and review of audited financial statements from third-party servicers for FFELP lenders. Without such reviews, FSA might not be informed of a third-party servicer's unfavorable audit opinion or significant reported findings that could affect program operations. In FY 2009, GAO found that although students must meet certain eligibility requirements to demonstrate that they have the ability to succeed in school before they receive Federal loans, weaknesses in the Department's oversight of these requirements place students and Federal funds at risk of potential fraud and abuse at proprietary schools.

We have recommended that FSA establish an effective system of internal controls to provide sufficient oversight and monitoring of SFA program participants and make certain it has staff with the appropriate knowledge and training to successfully carry out and manage its programs and operations.

Our external audits of individual SFA program participants frequently identified noncompliance, waste, and abuse of SFA program funds. The audits we performed of Community Care College, Touro College, Technical Career

Institutes, and Wilberforce University disclosed issues in a number of areas. For example, audits of these postsecondary institutions have identified disbursements of SFA funds at ineligible locations and for ineligible programs, noncompliance with institutional eligibility requirements, SFA funds awarded to ineligible students, inaccurate returns of SFA funds for students who withdraw from classes, improper manipulation of default rates, and other issues. (Also see discussion in the next section on issues that relate to distance education.) As noted previously in the Improper Payments challenge, in a series of lender audits issued in FY 2005 through FY 2009, we noted improper special allowance billings by lenders. Our review of Educational Credit Management Corporation's compliance with its agreement with the Department disclosed unallowable charges, an inadequate cost allocation plan, and cost allocation reports not provided to the Department. In FY 2011, we also issued audits of Wells Fargo Bank and Zions Bank, two custodians for FFELP loans in which the Department purchased an ownership interest under the ECASLA, and found that the custodians' monitoring and oversight of lenders and servicers needed improvement.

OIG investigations have identified various schemes by SFA program participants to fraudulently obtain Federal funds. In several recent cases, proprietary school officials created documentation in order to receive Federal grants and loans for students that did not attend the school or were enrolled in ineligible programs. In one case, proprietary school officials from Vatterott College provided false general equivalency diplomas and falsified financial aid forms to obtain Federal student grants and loans for ineligible students. Alta Colleges, an organization managing a group of schools in one State, failed to meet State licensing requirements—a requirement for receiving Federal student aid. The organization entered into a civil fraud settlement agreeing to repay $7 million to the Government for funds it was not eligible to receive. In July 2011, Kaplan Higher Education Corporation, a large proprietary school chain, entered into a civil fraud settlement agreeing to repay $1.6 million to the Government for failing to secure required training externships for students enrolled in a surgical technology program designed to prepare students to work in a surgical setting. In another recent civil fraud settlement, the owner of Cannella School of Hair Design agreed to repay more than $4.9 million for enrolling students who were ineligible because they did not have a required high school diploma or general equivalency diploma. Lastly, the former vice president of Iona College, a nonprofit college, pled guilty to embezzling more than $850,000 from the school to pay for personal expenses.

OIG work continues in this area with additional reviews related to the Department's oversight of participants in the SFA programs. This work includes a review of FSA's oversight of schools participating in the Direct Loan Program and a review of FSA's oversight of FFELP guaranty agencies. For FY 2012, we plan to conduct a number of reviews of the Department's monitoring of SFA program participants, including reviews of the implementation of the recent gainful employment regulations and prohibitions against incentive compensation and misrepresentation (see further information below), institutions' use of servicers for SFA payment processing, and further oversight of FFELP program participants.

Department Actions/Plans

Among other actions taken in response to our audits, the Department agreed to improve its control environment for oversight and monitoring, its risk assessment process, and its control activities. As discussed under the Improper Payments challenge, FFELP lenders were required to undergo independent audits to determine the eligibility of loans funded by tax-exempt obligations for certain special allowance payments. In FY 2008, these independent audits identified that 90 percent of the loans billed were ineligible and, as a result, prevented well over a billion dollars in improper payments. As a result of our work, FSA completed program reviews at 22 guaranty agencies, identifying more than $33 million in potential recoveries to the Federal fund. FSA has agreed to address the weaknesses we identified in its monitoring of schools' financial responsibility. FSA revised its system edits to reasonably ensure that only eligible loans were purchased under the ECASLA Loan Participation Purchase Program.

In January 2010, FSA changed leadership in its Enterprise Risk Management Group and hired a new chief risk officer. The FY 2012 budget justification included an increase of 91 full-time employee equivalents (FTE) across the Department for staffs that work extensively on SFA programs. The Department reported that, as of September 2010, it had more than doubled, from 13 to 29, the number of staff responsible for conducting program reviews of guaranty agencies, lenders, and servicers. FSA reported it has also filled supervisory positions, established a mandatory training program for all program review staff, and implemented program review procedures that ensure proper supervision and consistency in decision making. FSA also reported that it implemented similar procedures for its audit resolution process.

On October 29, 2010, the Department published final regulations to address program integrity issues. These regulations strengthen the requirements for the SFA programs. In three of the most substantive of these amendments, the Department (1) eliminated "safe harbor" provisions that had enabled schools to evade the consequences of the HEA's prohibition on incentive payments to school's recruiters for securing enrollments; (2) published new and more detailed requirements to prevent misrepresentation by schools to students; and (3) added a definition of "credit hour," providing a much-needed metric to ensure that students receive SFA funds in amounts appropriate for the courses they are attending. As part of its program integrity initiative, on June 13, 2011, the Department also published regulations to establish a process to identify the worst performing "gainful employment" programs and to terminate their eligibility for SFA funds. Under the HEA, programs offered by proprietary schools and some public and nonprofit schools must prepare students for gainful employment in a recognized occupation. Also, as mentioned under the Improper Payments challenge, in January of 2010, the Department began offering applicants who complete their FAFSA on-line an IRS data retrieval tool, which simplifies completion of the FAFSA. Using this tool, the applicant can securely transfer IRS information into the FAFSA, significantly increasing the accuracy of the data submitted.

Further Actions Needed to Address the Challenge

FSA needs to evaluate the risks within its programs and develop strategies to address risks identified to ensure effective operations. Its programs and operations should be given priority over its internal administrative operations. FSA needs to assess its control environment, using information from OIG reviews,

internal employee surveys, and other sources as appropriate, and implement actions for improvement.

As of August 31, 2011, the Department had not yet issued its decisions on audits related to 4 of the 12 specific schools, lenders, and guaranty agencies we have identified in the appendix under this challenge that are overdue for resolution. When issued, the Department's decisions will require the entities to take corrective actions to address weaknesses related to student and program eligibility and appropriateness of lender billings. The Department should ensure that returns of program funds are made where appropriate.

Our work continues to identify serious problems with the Department's oversight of participants in the SFA programs. The Department needs to continue to assess and improve its oversight and monitoring of postsecondary institutions, FFELP guaranty agencies, lenders, and servicers, and other SFA program participants, and to act effectively when issues are identified. As part of this effort, FSA must make certain it has knowledgeable staff on board to successfully monitor and oversee participants in the SFA programs. The Department's issuance of program integrity and gainful employment regulations is a substantial step, but the Department now needs to ensure that those regulations are implemented and enforced effectively.

Oversight and Monitoring
Distance Education

Summary

Distance education refers to courses or programs offered through telecommunication, such as through Internet connection with a postsecondary institution. The flexibility offered is popular with students pursuing education on a nontraditional schedule. Many institutions offer distance education programs as a way to increase their enrollment. Management of distance education programs presents a challenge for the Department and school officials because of limited or no physical contact to verify the student's identity or attendance. OIG audit work has found that for distance education programs, schools face a challenge in determining when a student attends, withdraws from school, or drops a course. Attendance is critical because it is used to determine the student's eligibility for Federal student aid and to calculate the return of funds if the student withdraws or drops out. Our investigative work has also identified numerous instances of fraud involving distance education programs. These cases involved the exploitation of vulnerabilities in distance education programs to fraudulently obtain Federal student aid. Also, some requirements for residential programs do not translate clearly for distance education programs, and guidance is not available to address these issues. The Department needs to develop requirements specific to distance education and to increase its oversight of schools providing programs through distance education.

Background

The Higher Education Reconciliation Act of 2005 amended the HEA to allow students to receive SFA program funds for programs offered entirely through telecommunication. Previously, a school was subject to a 50-percent limitation on distance education courses and distance education enrollment. The Department does not maintain data that identify which students receive Federal student aid to attend distance education programs. However, Departmental surveys of postsecondary institutions show the use of distance education significantly increasing. More than 20 percent of undergraduates took distance education courses during the 2007–2008 academic year, up from 8 percent during the 1999-2000 academic year.

The growth in distance education—both at proprietary and nonprofit institutions—highlights the need for greater oversight and statutory or regulatory change. The primary issue is determining whether students in distance education are "regular students" as defined by the HEA and are actually in attendance for Federal student aid purposes. Institutions are obligated to return any Federal student aid received if a student does not begin attendance during the period for which aid was awarded. Determining what constitutes a class and class attendance in the on-line environment is a challenge in the absence of defined class times or delivery of instruction by instructors. On-line instruction typically consists of posted reading materials and assignments, chat-room and email exchanges, and

posting of completed student work. The point at which a student progresses from on-line registration to actual on-line academic engagement or class attendance is often not defined by institutions and is not defined by Federal statute or regulation. Without such definition, or adequate controls at the institutions themselves, Federal student aid funds are at significant risk of being disbursed to ineligible students in on-line programs, and inadequate refunds made for students who cease attendance in these programs.

Another issue is the definition of a credit hour—a critically important issue in the SFA programs, as the amount of Federal aid a student receives is based on the number of credit hours in which the student is enrolled. This issue has become even more significant as on-line education has dramatically increased in recent years. The definition of a credit hour protects students and taxpayers from inflated credit hours, the improper designation of full-time student status, the overawarding of SFA program funds, and excessive borrowing by students, especially those enrolled in distance education programs. The Inspector General provided testimony related to this issue in both FY 2010 and FY 2011.

In addition, students enrolled in distance education programs and residential programs can be eligible for the same amount of Federal student aid based on the same cost of attendance (COA). The HEA limits the COA for students engaged in correspondence courses to tuition and fees, and, if required, books, supplies, and travel. Although students in distance education and correspondence courses are both separated from their instructors, there is no similar limitation on COA for distance education students. Thus the COA for distance education students includes amounts for room and board, even though these costs may not be relevant for these students. With the explosion of distance education in recent years and the number of full-time working individuals who take these courses, a COA budget that includes an allowance for room and board for on-line learners may not be in the best interest of American taxpayers and may allow students to borrow more than is needed.

Results of Work Performed

The OIG has found that institutions did not have adequate procedures and/or information systems to capture attendance information for on-line students. In some cases, the information captured did not represent academically related activities, such as exams, tutorials, computer-assisted instruction, and/or turning in of assignments. As a result, the institutions could not correctly identify when the students began attendance to determine eligibility for Federal student aid. For students who did not officially withdraw from classes or the overall program, the institutions could not determine when the students ceased attendance to calculate the amount of aid to be returned. We recommended that FSA require the schools to review their files, return improperly retained Federal student aid, and develop and implement policies and procedures to provide reasonable assurance that funds are not disbursed to students who are not enrolled.

In our FY 2009 audit report of TUI University, we estimated that more than 10 percent of the aid disbursed was provided to either ineligible students or not earned by students that withdrew. In another report issued in FY 2011, Ashford University, we estimated that the school improperly retained at least $1.1 million of SFA program funds for students who withdrew because it did not: (1) revise the payment period end date for students who did not complete their credits

according to schedule; (2) use the correct last date of attendance as the withdrawal date; and (3) correctly project the tuition charges that would have been charged to the students if they had completed the semester. We also found that Ashford disbursed Federal student aid for students who were ineligible, because the students had not yet completed the prior payment period. Seventy-five percent of the improper disbursements to students in our sample were made to students who never became eligible. For the 2006-2007 award year, we identified more than $89,000 disbursed to students in our sample who were not eligible to receive Federal student aid and estimated that the total amount of ineligible disbursements Ashford made during the award year to be between $3.7 and $8.9 million. Although in most cases Ashford identified and corrected improper disbursements after they were made, Ashford had use of the funds and may have earned interest it was not entitled to. For both institutions, we recommended that the Department consider taking action, as appropriate, to fine, limit, suspend, or terminate the institutions' participation in the SFA programs.

Our FY 2010 inspections of three regional accrediting agencies found that none of the agencies defined a credit hour nor provided guidance on the minimum requirements for the assignment of credit hours. Based on our work, we recommended that the definition of a credit hour include a requirement that accrediting agencies evaluate the assignment of credit hours to new courses and on an ongoing basis evaluate whether courses offered by an institution have maintained the credit hour value assigned to them.

The OIG has seen a significant increase in the number of investigations involving distance education. Over the last several years, we have initiated 100 investigations of fraud rings that target distance education programs. Ringleaders recruit individuals to act as "straw students." The straw students are persons with no intention of attending school. Either the ringleaders or the straw students complete admission forms, financial aid applications, and other required documentation, often falsifying basic eligibility data such as high school completion. When the straw students receive financial aid checks, they kick back a portion of the proceeds to the ringleader. Without requirements for verifying a student's identity and for procedures to ensure that applications and attendance are completed by actual students, the schools involved in these cases, and the SFA programs overall, are vulnerable to these fraudulent schemes.

In September 2011, the OIG issued an IPAR related to the vulnerabilities noted in our investigations of distance education. We reported that nearly all the individuals identified as participants in fraud rings failed to meet the basic eligibility requirement of enrollment for the purpose of obtaining a degree, certificate, or other recognized credential. Many also did not have a high school diploma or its recognized equivalent. Lastly, some fraud rings have enrolled incarcerated inmates who are ineligible to receive Title IV funds. We made a number of recommendations to enhance controls for fraud prevention and to increase fraud detection.

Department Actions/Plans

OIG work continues in this area with a comprehensive audit of distance education requirements, Department monitoring of distance education programs at all types of postsecondary institutions, and compliance by those institutions with

requirements in administering the programs. In addition, as of September 2011, we are performing audits of two institutions that offer distance education programs.

During FY 2010 and FY 2011, FSA participated in a joint project with the OIG to identify risk indicators and schools participating in the SFA programs that may not be complying with program requirements. The project focused on schools offering distance education because of the recent, significant increase in enrollment numbers and funding. FSA and the OIG jointly performed extensive data analysis to identify potential high-volume schools offering distance education programs with potential risk of noncompliance and developed distance education program review procedures. FSA initiated program reviews and OIG initiated audits at high-risk schools identified by the joint project.

In October 2010, the Department issued regulations to improve the integrity of the SFA programs. These regulations took effect on July 1, 2011. Although not specific to distance education, the regulations provided a definition of a credit hour and clarified what constitutes attendance at an academically related activity for purposes of the return of SFA program funds when a student withdraws. We will monitor the Department's implementation of these new program integrity regulations.

Further Actions Needed to Address the Challenge

As of August 31, 2011, the Department had not yet issued its decisions on the audits related to two of the four specific schools which we have identified in the appendix under this challenge. Both of these decisions are overdue. The Department should ensure that returns of program funds are made where appropriate. FSA also needs to increase its monitoring and oversight of schools providing distance education.

The Department should gather information to identify students who are receiving SFA program funds to attend distance education programs—and gather other information as needed—in order to analyze the differences between traditional education and distance education. Based on this analysis, the Department should develop requirements specifically to address potential problems inherent in distance education and publish those requirements. These requirements should include (1) definitions of instruction and attendance in an on-line environment, (2) verification of the identities of students receiving Federal student aid for attendance in distance education courses, as well as their high school graduation status, and (3) clarification of the calculation of return of Federal student aid in a telecommunications environment.

The Department should work with Congress to reconsider the COA calculation for distance education programs to potentially reduce loan borrowing, decrease loan debt, and reduce the amount of funds available above tuition and thus obtainable by individuals who seek to defraud the Federal student aid programs through on-line fraud schemes.

Oversight and Monitoring
Recovery Act Programs

Summary

The American Recovery and Reinvestment Act of 2009 (Recovery Act) provided significant additional funding to help improve the economy and enhance education reforms. This included funding for new educational programs and existing programs. Over the last year, the challenge for the Department has moved from implementing the programs to monitoring the programs to ensure that program funds are expended for the purposes intended and that the goals and objectives of the programs are being met. In FY 2012, the Department will also be providing oversight of the winding down of the programs and funding provided. The OIG and GAO have conducted significant amounts of work at the Department, State agencies, and LEAs. This work identified a number of control weaknesses related to the use of funds, cash management, subrecipient monitoring, and impacts on maintaining levels of funding for education programs. We made recommendations to improve implementation and monitoring of Recovery Act programs. The Department has taken proactive measures to coordinate the effective implementation and oversight of the Recovery Act and to provide technical assistance to recipients. Additional oversight and monitoring could enhance the Department's ability to ensure that Federal funds are effectively managed and that deficiencies noted in audits and other reviews are corrected timely. The Department must continue to provide guidance and assistance to recipients on these programs, identify and obtain additional resources for program monitoring, and take timely corrective actions to address issues noted in audits and other reviews.

Background

The Recovery Act was signed into law on February 17, 2009, authorizing $787 billion in Government spending and tax cuts to stimulate the economy, save and create jobs, and invest in education reforms. The Department received $96.8 billion for new and existing programs. This additional funding represented more than one and one-half times the Department's FY 2009 regular budget of $62.6 billion.

More than 80 percent of the Department's Recovery Act funding was designated for five programs:

- State Fiscal Stabilization Fund (SFSF)—$48.6 billion for this new program to stabilize State and local budgets and advance education reforms;

- Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA) as amended (Title I)—$13 billion in education for the disadvantaged;

- Part B of the Individuals with Disabilities Education Act (IDEA)— $12.2 billion for special education programs;

- Race to the Top—$4.35 billion for this new program to advance education reforms; and

- Investing in Innovation—$650 million for this new program to expand innovative practices and bring promising reforms to scale.

In August 2010, Public Law 111-226 authorized a new Federal program, the Education Jobs Fund Program (Ed Jobs). The Ed Jobs program provided $10 billion in assistance to States to save or create education jobs for the 2010-2011 school year. Jobs funded under this program included those that provided educational and related services for early childhood, elementary, and secondary education.

Although responsible for distributing and monitoring significantly more than funding than it received from the regular FY 2009 appropriation, the Department did not receive significant additional resources to accomplish this task. The fact that many recipients of Recovery Act funds are facing difficult economic situations increases the risk that Federal funds could be misused. The increased risk requires additional monitoring and oversight efforts by the Department. For the three largest programs, recipients generally must obligate all funds by September 30, 2011. The Department is charged with working with SEAs and LEAs to ensure that Recovery Act funds are spent timely while also exercising prudent oversight. This challenge will become more important as the deadlines for spending and liquidating Recovery Act funds approach and pass.

Results of Work Performed

The OIG has performed audit work at States and LEAs related to the Recovery Act. We have also been coordinating closely with GAO on its work related to Recovery Act education programs. The OIG's first phase of audit work, initiated in FY 2009, involved eight States and Puerto Rico and evaluated internal control activities of prime recipients and subrecipients over use of funds, cash management, subrecipient monitoring, and data quality. The OIG initiated its second phase of audit work in FY 2010 in 11 States, evaluating the use of funds and data quality for compliance with applicable laws, regulations, and guidance. Work is still underway in two States from this second phase. We also evaluated maintenance of effort (MOE) requirements (related to maintaining minimum levels of education funding) under the SFSF program and corrective actions taken to address prior audit findings in programs that subsequently received Recovery Act funding. Issues noted with respect to data quality are discussed under the Data Quality and Reporting challenge. The results of our reviews in the other areas are summarized below:

Use of Funds

Our first phase of audits found weaknesses in most recipients' controls over uses of funds. We identified the need for the Department to work with recipients to ensure that: (1) Recovery Act funds are accounted for separately from other Federal and non-Federal funding sources; (2) effective controls are in place over payroll processing and documentation; (3) written policies and procedures are in place; and (4) Recovery Act contracts are effectively monitored. Our second phase of audits also identified internal control weaknesses over the use of Recovery Act funds as well as several questioned cost findings related to unsupported and unallowable expenditures. These findings were typically small dollar amounts, but they represented

weaknesses that States and LEAs have in accounting for and using funds appropriately.

Cash Management

Our first phase audits identified instances of weak controls over cash management by recipients and subrecipients of education grants that could result in additional borrowing costs to the Federal Government. Specifically, our work found that SEAs did not always have effective controls in place to minimize the time between the receipt and disbursement of funds. We also found that SEAs did not always have policies and procedures in place to correctly calculate and timely remit interest earned on Federal cash advances to the Federal treasury. We issued an alert memorandum to the Department to provide advance notice of this area of concern. Our second phase audits showed that some recipients and subrecipients still do not have appropriate controls in place over cash management.

Subrecipient Monitoring

The Department has overall responsibility for monitoring its programs; however, prime recipients must monitor subrecipient activities to ensure compliance with applicable Federal requirements. Our Recovery Act audits have identified that the Department needs to ensure that prime recipients: (1) modify monitoring methods to include oversight of Recovery Act funds that adequately address fiscal issues, (2) review supporting documentation or verify on a risk basis to ensure that allowable expenditures were made before Recovery Act payments were made to subrecipients, and (3) establish clear responsibilities for monitoring SFSF funds. We issued a management information report on issues that the Department should consider in its future risk assessments and monitoring visits.

Maintenance of Effort

Flexibility inherent in the SFSF program MOE requirements may result in SEAs reducing funding for public education. The MOE assurances provide flexibility for States in various budget situations. A State facing a large deficit can avoid reductions in total education funding while a State with a stronger budget situation can increase total education spending to work toward the education reforms of the Recovery Act. However, we concluded that this flexibility may be resulting in a reduction in some States' funding for public education. We issued an alert memorandum to the Department on the potentially adverse impact to the achievement of the education reform objectives of the SFSF program. We recommended that the Department take action to address these potential consequences by tracking SEA funding for public education and using these data to ensure compliance with the MOE assurances in their SFSF applications. GAO also issued a report in this area, recommending that the Department require States to include in their SFSF applications an explanation of any changes and the reasons for changes to the calculations or MOE levels.

Corrective Actions to Address Prior Audit Findings

We evaluated the Department's progress in implementing corrective actions for the OIG prior audits of programs that subsequently received Recovery Act funding. We found that although some resolution activities for these audits

were underway, the Department had not made significant progress in issuing its management decisions to resolve the findings. As a result, weaknesses noted in prior audits may have continued in the administration of additional program funding. We recommended that the Department expedite corrective actions for these prior audits to safeguard Recovery Act and other program funds.

The OIG has also evaluated the Department's implementation of the SFSF program, focusing on the formula grant portion of the program, which comprises more than 90 percent of the funding. We found that the Department's initial implementation of the program was generally appropriate. The Department calculated State allocations in accordance with statutory requirements, and the funding applications we sampled included all required information and underwent multiple levels of review. We did note that although the Department's process indicated that reviewers had verified that all required data and related information were provided, the process did not provide assurance that steps were taken to assess whether the data were reasonably supported. This could impact the Department's ability to determine whether States are complying with MOE requirements. In our sample of 16 States, we noted that 3 States appeared to have insufficient or questionable supporting data. Department officials stated that they believed that current staff, plus planned contractor assistance, would be adequate to manage the SFSF program and monitor recipients. Although it appears that staffing has been adequate during the initial implementation of the program, the time required to implement and monitor the SFSF program could impact the Department's ability to effectively manage existing programs.

In June 2011, GAO reported that the Department had provided extensive support to Race to the Top grantees and has begun its monitoring efforts. GAO also reported that the Department facilitated information sharing, but grantees wanted more information and nongrantees were unaware of plans to share lessons learned. In July 2011, GAO reported that the Department is monitoring the implementation of School Improvement Grant (SIG) program awards and plans to collect performance data to identify and disseminate high quality practices. However, GAO found that time frames for planning and implementing interventions were challenging. GAO further reported that despite the Department's efforts to address these issues, late approval of State applications remained an issue for school year 2011–2012. GAO recommended that the Department consider options to have SIG grants awarded earlier, such as using an earlier deadline for State applications or approving State applications that include timelines for earlier awards to districts.

OIG investigations continue to examine allegations of waste, fraud, and abuse involving Recovery Act funds and to take appropriate action to ensure that anyone who steals or intentionally misuses Recovery Act funds is held accountable for those unlawful actions. The Recovery Act increased funding for the Pell Grant program—one of the SFA programs. A recent investigation resulted in the sentencing of a former official from American Institute for his role in a fraudulent high school diploma scam. The former official created false high school diplomas in order to make students appear eligible for admission to the school and to support false applications for Federal student aid. As a result of his fraudulent

efforts, ineligible students at the school received approximately $156,000 to which they were not entitled, of which approximately $5,100 involved Recovery Act funds. Other Recovery Act investigations involve the use of funds by local school districts and their contractors.

OIG work continues in our third phase of Recovery Act audit work, initiated in FY 2011, with our review of 22 LEAs in 22 States to provide a national perspective on how LEAs are using Recovery Act and Ed Jobs funds. We also have audits in process for Recovery Act programs related to SEA monitoring of the SIG program, Teacher Incentive Fund program awards, and the MOE flexibility under IDEA. Because funds for many of the Recovery Act programs must be expended by early FY 2012, our fourth phase of Recovery Act audits will focus on determining whether recipients expended final funding appropriately. We also plan to review the Race to the Top and Investing in Innovation programs. The State and local deadlines for obligations of the funds under these latter programs extend into FY 2014 and FY 2015, respectively. We will continue to coordinate with GAO on its efforts in these programs.

Department Actions/Plans

The Department has taken a number of actions to ensure the successful implementation of the Recovery Act. The Department issued extensive guidance on each of the programs funded under the Recovery Act. These guidance documents included information on appropriate uses of funds and reporting requirements along with other program specific issues. In June 2010, the Department sent a memorandum to all Department grant and cooperative agreement recipients reminding them of cash management requirements and to ensure that subrecipients are also aware of the requirements. The Department also issued guidance explaining the cash management requirements in more detail. In August 2011, the Department issued letters to each Governor notifying them of their current Recovery Act grant balances and reminding them of the approaching obligation and liquidation deadlines.

The Department also conducted a series of technical assistance webinars to communicate with recipients and subrecipients on how to successfully administer Recovery Act programs. Webinar topics included issues such as internal controls, cash management, allowable activities, subrecipient monitoring, and data quality. Past webinars are available for viewing on the Department's Web site. The Department established an internal Metrics and Monitoring Team that meets weekly to discuss issues in Recovery Act program areas. The team includes representatives from all of the program offices that received Recovery Act funding, as well as other key functions such as Budget Service, the Office of the Chief Financial Officer, the Office of the Chief Information Officer, and Risk Management Service. The Department also required all staff that review grant applications or oversee grants to attend fraud awareness training developed and presented by OIG staff.

In accordance with OMB guidance, Risk Management Service developed a risk mitigation plan for Recovery Act implementation. This plan analyzes both programmatic and financial risk factors associated with implementing the Recovery Act through all levels of the grant process. Risk Management Service has a risk assessment tool for its regular programs that is also being applied to recipients of Recovery Act funds.

The Department reported that it requires States to include in their SFSF applications explanations of the changes to calculations to MOE, as recommended by GAO, and it posts on its Web site when a State files an amended application. With respect to the issues noted in our SFSF audit, the Department reported that it has a detailed monitoring schedule and protocol for SFSF monitoring and that it has competed and awarded a contract to provide additional support to this effort. In addition, the Department stated that it is conducting on-site monitoring and has added five additional staff members that spend a substantial portion of their time monitoring the program.

The Department established the Implementation and Support Unit within the Office of the Deputy Secretary with primary responsibility for administering the SFSF, Race to the Top, and Ed Jobs Fund programs. The Implementation and Support Unit provides support for comprehensive reform implementation at the State level and acts as a primary point of contact for these three programs, all of which require involvement from Governors and Chief State School Officers. In FY 2011, the Department focused its Title I monitoring on the SIG program because that program received $546 million in FY 2010 and an additional $3 billion in Recovery Act funding. GAO reported that the Department used a variety of strategies to oversee State and district implementation of the SIG program.

Further Actions Needed to Address the Challenge

Further guidance and technical assistance are required to address issues as they arise with specific programs and recipients. These issues are likely to center on the need for recipients to obligate and spend funding by statutory deadlines and ensure appropriate use of funds. Effective oversight and monitoring are needed to ensure that the goals of the Recovery Act and those of previously established programs are achieved and that Federal funds are expended in accordance with Federal requirements.

The Department needs to ensure that external entities take timely corrective actions to resolve weaknesses reported in audits related to the use of funds, cash management, and subrecipient monitoring. As of August 31, 2011, we noted the following:

- The Department had not issued its decisions on the corrective actions that should be taken for 12 of the 14 external audit reports that are overdue for resolution from our first and second phases of Recovery Act audits (see Appendix A for listing). The Department needs to continue to provide guidance and outreach to leverage the audit results so that issues are proactively being addressed in all States, SEAs, and LEAs.

- The Department had not yet developed the corrective actions it plans to take to address the recommendations made in our alert memorandum related to the potential impact on maintaining levels of funding for education programs, or the audit of the SFSF program. Both reports are overdue for resolution.

Oversight and Monitoring
Grantees

Summary

Effective monitoring and oversight are essential to ensure that grantees meet grant requirements and achieve program goals and objectives. In addition to our work on Recovery Act programs included in the previous section, our work on other grant programs has identified a number of weaknesses in grantee oversight and monitoring. We have identified pervasive fiscal control weaknesses at a number of grantees, weaknesses in a grant payback program, as well as fraud committed by LEA and charter school officials. The Department is responsible for monitoring the activities of grantees to ensure compliance with applicable Federal requirements and that performance goals are being achieved. The Department has taken corrective actions to address many of the recommendations contained in our reports. However, the Department needs to continue to assess and improve its oversight and monitoring of grantees and take effective actions when issues are identified.

Background

The Department is responsible for administration, oversight, and monitoring of more than 200 different programs awarded through grants to 56 SEAs, 13,800 public school districts, and 99,000 public elementary and secondary schools. The Department is responsible for ensuring that the grants are executed in compliance with requirements and that program objectives are being met. The funding for many grant programs flows through primary recipients such as SEAs, to subrecipients such as LEAs or other entities. The primary recipients are responsible for oversight and monitoring of the subrecipients' activities to ensure compliance with Federal requirements.

In recent years, the Department received a large increase in the amount of grant funding and number of programs that it is responsible for managing. The Department's annual budget increased from $44 billion in FY 2000 to almost $70 billion in FY 2011, while at the same time the number of FTEs decreased 13 percent. The funds provided under the Recovery Act nearly doubled the annual appropriations for these programs. As discussed above, the Department did not receive significant additional resources to absorb the workload created by the Recovery Act—its already limited resources were further stretched to accommodate these additional responsibilities.

GAO has identified "Improving Student Achievement in Elementary and Secondary Schools" as a management challenge for the Department. GAO stated that many States have struggled to meet key requirements of the No Child Left Behind Act, including implementing provisions designed to improve student achievement in low-performing schools, increasing the number of highly qualified teachers, and implementing Statewide assessment systems. GAO stated the Department has not taken sufficient action to ensure that States and school districts help low-performing schools improve student achievement.

OIG work has identified a number of weaknesses in grantee oversight and monitoring. These weaknesses involve LEA fiscal control issues, payback program weaknesses, and fraud perpetrated by SEA, LEA, and charter school officials as follows:

LEA Fiscal Control Issues

During FY 2009, we issued a management information report that summarized a series of LEA audits which reported fiscal control issues representing approximately $182 million in questioned costs and an additional $1.4 billion in funds determined to be at risk in 41 LEA reports. In 27 of these LEAs, we found pervasive fiscal issues such as unallowable or inadequately documented expenditures. During FY 2010 and FY 2011, we issued five audit reports on operations at four LEAs that identified fiscal control issues representing more than $33.6 million in questioned costs and more than $128 million in unsupported costs. We also issued an alert memorandum to the Department recommending that one LEA be considered high-risk and that special conditions be applied to its funding. Despite the amount of guidance available to SEAs and LEAs, we suggested that the guidance be enhanced given the high percentage of audits that included the pervasive issues.

Payback Program Weaknesses

In FY 2010, we found significant weaknesses with the Department's management and oversight of the Indian Education Professional Development Grant payback program. This program required individuals who received funding for training under the program to perform work related to the training received (work payback) or repay all or a prorated part of the financial assistance received (cash payback). We found the program office did not maintain adequate records on students receiving assistance under the program and subsequently did not ensure that these students fulfilled their payback obligations.

Fraud by SEA/LEA Officials

Since the beginning of FY 2008, we have opened 65 investigations of either SEA or LEA officials related to allegations of fraud and corruption related to Department programs. These investigations have identified fraud schemes that included: (1) bribery and kickbacks involving consultants, contractors, and employees; (2) use of fictitious vendors to generate payments; (3) false expenditure reports and checks; (4) use of dormant or unknown bank accounts; and (5) misuse of procurement credit cards. More effective internal control systems at the SEAs and LEAs could have mitigated the risk of these fraud schemes. For example, a former school district superintendent from Pharr-San Juan-Alamo Independent School District, and five school district board trustees were sentenced for their roles in a bribery and extortion scheme. The former school officials accepted bribes in exchange for favorable votes on district construction contracts. Another example involved the former director of the school bus division of the American Samoa Department of Education who pled guilty to conspiracy to commit bribery. This official admitted to participating in a scheme that involved other American Samoa Department of Education employees as well as the owner and operator of a company that sold school bus parts to the American Samoa

government. The official and others arranged to order "phantom" bus parts that were never received and parts that were purchased at inflated prices. In exchange for these fraudulent orders, the official and the co-conspirators received approximately $300,000.

Fraud by Charter School Officials

Charter schools generally operate as independent entities that fall under oversight of an LEA or authorizing chartering agency. Our investigations have found that LEAs or chartering agencies often fail to provide adequate oversight to ensure that Federal funds are properly used and accounted for. In March 2010, we provided a management information report to the Department that highlighted vulnerabilities in this area. Over the last several years, OIG has opened more than 50 charter school investigations. To date, these investigations have resulted in 21 indictments and 17 convictions of charter school officials. The cases that have been fully settled have resulted in more than $5.8 million in restitution, fines, forfeitures, and civil settlements. The type of fraud identified generally involved some form of embezzlement of funds from the school by school officials.

GAO has also conducted work related to grantee oversight and monitoring. In February 2011, GAO reported that the Department improved its strategic workforce planning and performance management systems, but a lack of reliable data on workload limited its ability to accurately estimate resource needs and inform workforce planning efforts.

In FY 2011, GAO issued a report that addressed the Department's monitoring of its largest program, ESEA, Title I—Improving the Academic Achievement of the Disadvantaged. GAO reported that the Department generally monitored State implementation of the Title I program and evaluated the extent that States ensure district and school compliance with Title I requirements. GAO reported that the Department covered two to three school districts in each State being reviewed and that the Department did not conduct detailed reviews of the district's Title I expenditures to identify unallowable expenses but primarily relied on other sources of oversight, such as OIG audits, for this purpose.

In its November 2009 report, GAO reported that Department monitoring staff has limited financial expertise and training, which hindered effective monitoring of grantees' compliance with requirements. GAO found the Department has monitoring tools that aid in reviewing basic financial compliance, but the lack of staff expertise limited the ability to probe more deeply into grantees' use of funds. In addition, GAO reported that the Department lacked a systematic means of sharing information on grantees and on promising practices in grant monitoring. GAO recommended that the Department increase financial expertise among its grants monitoring staff and develop an accessible mechanism to share information.

OIG work continues in this area as we are currently reviewing the Department's and/or SEAs' oversight of charter schools, the 21st Century Community Learning Centers Program, and Centers for Independent Living. We are also performing an inspection of the Department's process to identify and monitor high-risk grantees. In FY 2012, we plan a significant amount of work related to the Department's

oversight and monitoring of grantees, as well as further reviews of SEA oversight of subgrantees. In addition to Recovery Act programs, our planned FY 2012 work includes reviews of Department and SEA oversight of charter schools and Charter Management Organizations or Educational Management Organizations, oversight of LEA/school adequate yearly progress determinations, and the Department's oversight of other grant programs.

Department Actions/Plans

The Department developed financial monitoring training for program staff members that is designed to complement other resources that the agency uses to provide financial monitoring. The Department also established a dedicated group of financial monitoring experts. The Department's program offices are currently increasing their coordination through activities including a forum for ongoing discussion of their monitoring strategies. The Department developed a discretionary grant monitoring tool that is being pilot tested during FY 2011. The tool, which is intended to make it easier for the Department to evaluate potential risk to grant funds for specific programs at the recipient level, is supported by the Decision Support System. The Decision Support System is a suite of software tools and support services used to perform risk analysis and reveal to the Department information that can be used to effectively administer grants. Appropriate uses of the information are to inform the work of: (1) identifying fiscal or performance risks with the Department's applicants or grant recipients; (2) determining whether special conditions are needed for the award; and (3) developing risk-based monitoring and technical assistance plans.

The Department is also developing a technical assistance plan and training curricula to provide enhanced guidance and training to SEAs and LEAs. The technical assistance plan and training curricula will include administrative requirements for implementation of Federal grants and will convey the importance of complying with those requirements. The Department has also participated in a number of conferences, training workshops, and webinars to provide additional technical assistance to SEAs and LEAs.

The Department implemented a new process for applying risk management principles to all key stages of the discretionary grant process, including the process for new and continuation awards. According to the new policy described in a May 16, 2011, Grant Bulletin, prior to making awards, program offices must assess an entity's risk by reviewing, at a minimum, prior and/or current financial and performance information, information on compliance with Federal audit requirements, relevant findings in audit reports and monitoring reports, and progress on corrective actions to resolve audit findings. Program offices, on the basis of these reviews and in consultation with the Department's Office of the General Counsel, should determine whether any action needs to be taken at the time the award is made, such as designating the applicant as high-risk or imposing special conditions on the grantee. Program offices should continue to conduct risk assessments during the performance period.

GAO reported that the Department planned to conduct on-site Title I monitoring in 12 States during FY 2011. As of September 27, 2011, 10 State monitoring reports have been completed. GAO also reported that the Department is developing criteria for selecting States for Title I monitoring in future years. The

Department is working with the States that have been monitored to correct issues that have been identified and to provide needed technical assistance.

Further Actions Needed to Address the Challenge

The Department should continue to improve its monitoring efforts for recipients of formula and discretionary grant funds. This includes pursuing efforts to enhance risk management, increase financial expertise among its grants monitoring staff, and develop mechanisms to share information regarding risks and monitoring results. The Department plans to continue to work toward developing and implementing a workload analysis system that integrates human capital, operations, and cost data. The Department is also working to develop workload guidance to be used across the Department.

As of August 31, 2011, the Department had not yet issued its management decision as to the corrective actions needed for all three external audits that are overdue for resolution. The Department needs to continue to complete corrective actions related to the alert memorandum on the Philadelphia School District, and the internal audit report related to the Office of Indian Education's management of the Professional Development Grant program.

The ESEA does not address minimum requirements for SEA monitoring of LEA administration of ESEA programs. The Education Department General Administrative Regulations (EDGAR) require grantees to monitor grant and subgrant-supported activities to ensure compliance with applicable Federal requirements achievement of performance goals; however, the regulations do not address minimum requirements for monitoring. IDEA does address some minimum monitoring requirements and establishes requirements for SEA monitoring, enforcement, and annual reporting. Similar to requirements under the Recovery Act, the Department should consider adding language to its regulations, so that prime recipients are fully cognizant of their responsibilities related to and minimum requirements for monitoring subrecipients.

The Department should include a reporting requirement for fraud and criminal misconduct in connection with all ESEA-authorized programs when EDGAR is revised. Modeled on reporting requirements for programs administered by FSA, such a regulatory provision would require any government entity, grantee, or subgrantee participating in an ESEA program to refer to the OIG for investigation any information related to fraud or other criminal misconduct.

Oversight and Monitoring
Contractors

Summary

The Department relies heavily on contractor support to accomplish its mission and to ensure the effective operations of its many systems and activities. The current value for the Department's active contracts is nearly $5.4 billion. Once a contract is awarded, the Department must effectively monitor performance to ensure that it receives the quality and quantity of products or services for which it is paying. OIG reports have included numerous deficiencies in the area of contract monitoring, and we have made recommendations for corrective action. The Department has taken action to address many of the issues noted. A critical issue hampering significant improvement, however, is the shortage of appropriately qualified staff to adequately monitor contractor performance. A concerted effort is needed to develop and implement an aggressive human capital plan to address this issue.

Background

Contract monitoring is an integral part of the Federal acquisition life cycle. Proper oversight is necessary to ensure that contractors meet the terms and conditions of each contract; fulfill agreed-upon obligations pertaining to quality, quantity, and level of service; and comply with all applicable regulations. The Department contracts for many services that are critical to its operations. These services include the following primary areas: (1) systems development, operation, and maintenance; (2) loan servicing and debt collection; (3) technical assistance for grantees; (4) administrative and logistical support; and (5) education research and program evaluations. Responsibility for oversight and monitoring of contracts and contractor performance at the Department is shared by staff in the program offices and the Department's Contracts and Acquisition Management, a component of the Office of the Chief Financial Officer. The FSA program office has delegated authority for its own procurement function. FSA follows the policies and procedures established by Office of the Chief Financial Officer and Contracts and Acquisition Management, as well as applicable Federal requirements in conducting their contracting operations. The Department's Chief Acquisition Officer is the Chief Financial Officer, who is responsible for oversight management for all procurement activities at the Department.

Results of Work Performed

OIG has identified issues relating to the lack of effective oversight and monitoring of contracts and contractor performance, primarily related to the appropriateness of contract prices and payments and the effectiveness of contract management. OIG investigations have noted inappropriate activities by contractor employees that resulted in improper billings and payments.

Appropriateness of Contract Prices and Payments
We have noted issues with respect to the prices paid under contracts and with the review of contractors' invoices for payment. For the EDUCATE contract, we found that the Department may not have effectively established contract

pricing. As a result, the prices charged under the contract may not be reasonable. In addition, we became aware that the Department did not act timely to resolve issues impacting performance validation and payment calculations after the execution of a contract modification. As a result, the Department may have paid the EDUCATE contractor money it was not entitled to receive under the terms of the contract. In another audit, we found more than $100,000 in unallowable and unsupported costs charged to the National Assessment of Educational Progress contract.

Additional work related to the EDUCATE contract included a review of the Department's processes for validating contractor performance prior to invoice payment. The final report for this audit, which was issued in May 2011, noted that the Department does not have adequate controls in place for validating contractor performance. Specifically, the Department does not have assurance that the EDUCATE contractor is performing as required, will improve performance when necessary, and is being paid appropriately for the level of service provided. We recommended improvements in the Department's validation processes, to include the use of independent data and better assurance of the quality of data being relied upon to assess performance, improvements in the processes for identifying and assigning personnel to validate contractor-submitted performance data, improvements in processes to validate unit-based expenses, as well as actions to improve the use of contract incentives/disincentives to encourage contractor performance.

Contract Management

In other work related to the EDUCATE contract, we found that the Department had not effectively implemented a contract to identify, respond to, and report security incidents regarding the security processes related to the Department's IT infrastructure. Specifically, the Department terminated the initial contract because of contractor performance problems, and the subsequent contractor has been unable to provide the level of service required by the contract. As a result, the Department has paid for services it has not received and has still not ensured that its IT network is adequately protected.

OIG investigative work resulted in settlements of nearly $1 million in FY 2010 as a result of illegal actions taken by employees of NCO Financial Systems, Inc., a contractor involved in servicing loans. We found that the employees had fraudulently consolidated $3.8 million of Federal student loans. The contractor received a collection fee from the Department for the consolidations, and the employees earned bonuses from the contractor. Recoveries were also made from the guaranty agency for monies it received from the Department as a result of the unlawful consolidations. Also, as mentioned under the Improper Payments challenge, OIG investigations resulted in recoveries of $1.4 million from another contractor for inappropriate billings.

OIG work continues in this area as we conduct additional work on the EDUCATE contract related to controls over cost management. We are in the process of performing work related to the Department's management of the Title IV Additional Servicers contracts to ensure appropriate contractor performance and accountability.

Department Actions/Plans

The Department has provided corrective action plans to address the issues noted in our audit work above. The Department revised its Contracting Officer's Representative Training Program to incorporate more stringent certification, training, and recordkeeping requirements. The Department also stated it would work with applicable principal offices to ensure that all future performance-based contracts include appropriate contractor incentives and disincentives to enhance contract management. In August 2009, the Department updated its Directive on Contract Monitoring for Program Officials.

The Department implemented a procedure requiring that contract monitoring plans be developed for all new and existing contracts. It also developed a training program reinforcing the Department's contracting processes and applicable laws and regulations. Senior managers, contracting personnel, and relevant program office personnel were required to attend this training. Program offices were directed to implement immediate steps and take personal responsibility for ensuring that contracts are awarded properly and effectively monitored.

In FY 2010, the Department implemented training of all EDUCATE contract administration team members to address roles and responsibilities and to assure understanding of contract deliverable processes. It also developed procedures documenting formal steps to be taken to timely address contract concerns relating to performance validation and payment calculations. In FY 2011, the Department completed and documented analyses of EDUCATE desktop services pricing, clarified contract requirements related to IT network security services, considered alternatives, and subsequently procured applicable services.

The Department also has corrective actions underway to improve processes for validation of contractor performance and unit-based expenses on the EDUCATE contract, to ensure contract staff have the appropriate technical expertise to monitor assigned contract areas, and to modify its incentives and disincentives to effectively encourage improvements in contractor performance. The Department is in the process of procuring analytical services to evaluate the EDUCATE contract and provide strategies for achieving cost and operational efficiencies for IT and infrastructure services. This includes fully assessing the contract services provided, services required, and costs associated with those services and comparing the costs and services to other available options, in terms of innovative technical solutions and contractual alternatives.

Further Actions Needed to Address the Challenge

Because the Department relies on its contractors to help run its various programs and operations, effective contract management is critical for ensuring effective performance by the contractors, that the Department receives the specified level and quality of products or services, and that payments made are appropriate. As reported in the FY 2011 Management Challenges Report, the numbers of Department staff responsible for contract oversight and monitoring are limited. The Department still needs to work to ensure that it has an appropriately qualified staff in place and in sufficient numbers to provide effective oversight of its contracts. In addition, it will need to address significant concerns regarding its performance and invoice validation processes.

Data Quality and Reporting

Summary

The Department, its grantees, and its subrecipients must have controls in place and effectively operating to ensure that accurate, reliable data are reported. Data are used by the Department to make funding decisions, evaluate program performance, and support a number of management decisions. SEAs annually collect data from LEAs and report various program data to the Department. The Department evaluates program data to make critical funding and other management decisions. The Recovery Act places a heavy emphasis on accountability and transparency, including reporting requirements related to the awarding and use of funds. All recipients and subrecipients are mandated to provide information about their awards on a publicly available Web site authorized by the statute. The new reporting requirements required Federal, State, and local agencies to quickly develop the systems and infrastructure to collect and report the required information. The Department must educate recipients about the reporting requirements, assess the quality of the reported information, and use the collected information effectively to monitor and oversee Recovery Act programs and performance.

Our work has identified a variety of weaknesses in the quality of reported data and recommended improvements at the SEA and LEA level, as well as actions the Department can take to clarify requirements and provide additional guidance. Establishing more consistent definitions for data terms will enhance reporting accuracy and comparability. For Recovery Act programs, our work noted weaknesses in controls over data quality and reporting, both externally at SEAs and LEAs, and internally at the Department. Ensuring that accurate and complete data are reported is critical to achieving the transparency goals of the Recovery Act.

Background

The Department operates systems to collect data regarding its programs. SEAs submit data from LEAs and SEA programs through the Education Data Exchange Network (EDEN) to the EDFacts system. EDFacts is a central repository that consolidates kindergarten through 12th grade education information collected from SEAs. This Internet-based collection process simplifies reporting and improves the timeliness of the kindergarten through 12th grade education information that is required for annual and final grant reporting, and specific program mandates. Some of the data included in Department systems involve the number of persistently dangerous schools, graduation and dropout rates, State academic assessments, and the number of schools identified in need of improvement. The Department has also collaborated with SEAs and other industry partners to centralize the SEA-reported data with other Department data, such as financial grant information. This collaboration enables better analysis and use of the data in policy development, planning, and program management at the Federal, State, and local levels.

The Department uses data in a number of other systems and from a number of other sources for funding allocation, performance evaluation, and other management decisions. States are required to implement a set of annual academic assessments. The assessments are used as the primary means of determining Adequate Yearly Progress of the State and each of its LEAs and schools in enabling all children to meet the State's student academic achievement standards. Assessments are used to hold schools accountable for student achievement and, as such, must meet requirements for accuracy, reliability, and quality. Funding to LEAs may be directly impacted by the results of the scoring assessments. Funding for other programs, such as the Migrant Education Program, is allocated based on the numbers of students eligible for the programs.

To ensure transparency and accountability of Recovery Act spending, recipients are required to submit quarterly reports on awards, spending, and job impact. According to OMB, the reports, which contain specific detailed information on the projects and activities funded by the Recovery Act, provide the public with an unprecedented level of transparency into how Federal dollars are being spent. The reports will also help drive accountability for the timely, prudent, and effective spending of Recovery Act funds. OMB is the lead agency responsible for implementing the requirements by defining the required data elements and the reporting process. Each agency that is charged with administering Recovery Act funds must work with its recipients to ensure that the reported data are as accurate and complete as possible. The Department is also required to draft and publish implementation plans and periodic updates on the implementation status for all of the Recovery Act programs that it administers.

Results of Work Performed

OIG and GAO have identified weaknesses in controls over data accuracy and reliability, as well as inconsistent definition and application of data terminology, as follows:

Inadequate Controls Over Data Accuracy and Reliability

In FY 2010, we reported that internal controls were not always sufficient to ensure that accurate, reliable data are reported. The Georgia Department of Education (GaDOE) underreported the numbers of dropouts and discipline incidents and did not have adequate controls to ensure the accuracy of data reported by LEAs. One LEA reviewed provided inaccurate or unsupportable data to GaDOE, which GaDOE then included in its reports to the Department.

Annual Academic Assessments

During FY 2009, we issued reports regarding the quality of controls over the scoring of annual academic assessments in three States—Florida, Wyoming, and Tennessee. In each State, we found areas of concern regarding the reliability of the assessment data, including a lack of sufficient monitoring of contractor activities and insufficient written policies and procedures. In September 2009, GAO also issued a report on academic assessments that questioned the ability of States to ensure valid and reliable assessment data because of the capacity of staff to provide vendor oversight, the administration of alternate assessments, and gaps in assessment security.

We also conducted work to evaluate compliance with Recovery Act reporting requirements by the Department, SEAs, and LEAs. GAO has also performed work

in this area. A number of issues were noted related to data quality and reporting by recipients, disclosure of known data deficiencies, Department actions to ensure data quality, and guidance on data quality as follows:

Data Quality and Reporting by Recipients

As previously mentioned under the Oversight and Monitoring—Recovery Act challenge, OIG's first phase of audits of Recovery Act implementation involved eight States and Puerto Rico. We evaluated internal control activities of prime recipients and subrecipients of Recovery Act education grants, including controls over data quality. Our work identified several data quality issues including lack of separate tracking of Recovery Act funds for reporting, lack of changes made to tracking and reporting systems to accommodate new reporting requirements, inadequate planning and guidance on the collection of data and systems to monitor data for accuracy and completeness, and lack of policies and procedures to ensure that known data deficiencies are disclosed to the Department. OIG's second phase of audits included testing of the required data to see whether the SEAs and LEAs data were accurate, reliable, and complete. The most common findings were related to the calculations of jobs saved/created and expenditures that were not reported as transparently as possible because of timing issues or challenges in tracking Recovery Act funds appropriately.

Department Actions to Ensure Data Quality

In October 2009, as part of the Recovery Accountability and Transparency Board's data quality initiative, we issued an audit and reported that the Department had established a process to perform limited data quality reviews of recipient reporting to identify material omissions and/or significant reporting errors. It has also established processes to notify the recipients of the need to make appropriate and timely changes. We subsequently performed a limited evaluation of the data submitted for the first reporting period and identified categories where data appeared to be unreasonable or incomplete. We also noted some instances where correlations between jobs and expenditure data did not appear to be reasonable and where some data relationships appeared to be unusual and may warrant further review. The number of occurrences noted within each area was limited; however, the occurrences could increase in number in future reporting cycles. Our results were provided to the Department in an internal memorandum with the suggestion that it consider appropriate measures to enhance its related controls in order to provide greater assurance over the quality of Recovery Act recipient reporting.

In FY 2011, we performed an additional audit to determine the effectiveness of the Department's data quality review processes. This audit found that the Department's processes to ensure the accuracy and completeness of recipient-reported data were generally effective. However, the audit also found recipient-reported data that were inconsistent with existing Department data and/or other recipient-reported data. We recommended that the Department ensure that the automated reports that are used for data validation are technically accurate and effectively used. Additionally, we recommended that the Department ensure that all applicable staff have

access to the appropriate system in order to conduct the necessary data validations.

Guidance on Data Quality

In two separate reports, GAO recommended that the Department and/or OMB improve the consistency of FTE calculations by issuing clarifying guidance to recipients. (Note: This guidance was issued by OMB in December 2009.)

OIG work continues in this area. In FY 2012, we are planning a review of the accuracy of reported improvements in Adequate Yearly Progress results under Title I of the ESEA.

Department Actions/Plans

The Department now requires some management certifications regarding the accuracy of SEA-submitted data. When SEAs submit data to the Department's EDEN system and for their annual Consolidated State Performance Report, the Department requires an authorized SEA official to certify that the reported data are accurate. For migrant child counts, the official must also certify that the data are true, reliable, and valid. The Department has also instituted data validation and verification steps and requires States to address their data issues before it will officially accept an SEA's data in the EDEN system.

In 2008, the Department released new regulations to address some of the migrant education program issues identified in our audits. The regulations provided enhanced definitions regarding program eligibility and a requirement for SEAs to re-document the eligibility of all program participants.

To address concerns related to the accuracy of academic assessments, the Department has provided technical assistance through meetings, written guidance, user guides, and direct contact with Department staff. The Department also conducts an ongoing peer review process to evaluate State assessment systems, and it includes a review of test security practices during its scheduled program monitoring visits. In June 2011, the Secretary sent a letter to Chief State School Officers suggesting steps that could be taken to help ensure the integrity of the data used to measure student achievement.

The Department did establish a process to conduct data quality reviews of Recovery Act data. In addition to this ongoing process, the Department issued several guidance documents to all recipients of Recovery Act education funds concerning issues relating to data quality, including the issue of FTE calculations identified in the GAO reports. These guidance documents answered questions and clarified issues that specifically pertain to Recovery Act education programs and the related required reports. The Department issued clarifying guidance on Recovery Act reporting requirements that instructed recipients to report any known data deficiencies to the Department along with actions being taken to correct the deficiencies. In July 2010, the Department issued policy regarding action on recipients that have failed to comply with reporting requirements.

Along with guidance, the Department has provided and continues to provide technical assistance to recipients. The Department conducted technical assistance webinars addressing data reporting and data quality issues. These webinars are available on the Department's Recovery Act Web site. Department

representatives also continue to provide technical assistance to recipients that contact the Department with specific questions.

As previously mentioned, the Department has established a Metrics and Monitoring Team that meets weekly to discuss issues, including data quality issues, in Recovery Act programs across the Department. The Department stated that its data quality review process documents decreasing occurrences of suspect or incorrect data since the OIG reviews were conducted. The Department has also established a Data Strategy Team to share ideas to inform Department processes and policies related to data, coordinate Department data initiatives, and improve transparency in all matters surrounding ED's collection of data. The team's goal is to improve the public's understanding of and access to data and coordinate work across multiple Department offices. The Data Strategy Team will support States' use of data through data Web sites and technical assistance to grantees.

Further Actions Needed to Address the Challenge

As of August 31, 2011, the Department has not yet resolved the audit related to the EDFacts program. The Department should issue its decision to GaDOE on the corrective actions to be taken to address deficiencies identified with respect to controls over data accuracy, reliability, and completeness. In addition, the Department has not yet issued its decision on one of the three audits of controls over State assessment scoring. The audit is overdue for resolution. In addition, the Department should continue to monitor corrective action taken by the other two States.

As mentioned earlier, the Department should timely issue its decisions regarding corrective actions needed to address the external Recovery Act audits. As of August 31, 2011, the Department had issued its decision on only 2 of the 14 reports from our first and second phases of audits that are overdue for resolution, detailing the actions needed to address OIG findings related to improvements in controls over the accuracy and reliability of data and reporting, and disclosing known deficiencies in data reported.

Although the Department has increased its use of data certifications, there is not a general requirement for management certifications for all submitted data. In addition, further guidance and clarification may be needed to ensure that consistent data definitions are used. Our work continues to find problems with reported data, further supporting the need for the Department and grantees to implement controls to ensure data accuracy and reliability.

The Department is working to ensure that required data are reported as accurately and completely as possible, but there is still work that can be accomplished. The Department must continue to identify recipients that fail to report and prepare to take appropriate actions to ensure compliance with requirements. Along with new requirements, Recovery Act funds will continue to be spent and more data will be reported, requiring more quality control reviews and technical assistance. The Department should continue to enhance its controls and reviews of data quality to ensure data reported are accurate and reliable.

Appendix A. Work Discussed Under the Challenges

The following audits, inspections, investigative cases and other work are discussed under the challenge areas.[2]

Challenge: **Improper Payments**	

OIG Internal Reports

- Management Information Report—Fiscal Issues Reported in ED-OIG Work Related to LEAs and SEAs, July 2009

- Federal Student Aid's Estimation of Improper Payments in the Federal Family Education Loan Program, September 2008

OIG External Reports

- Camden City Public School District's Administration of Federal Funds, June 2011

- Philadelphia School District's Controls Over Federal Expenditures, January 2010

- National Assessment of Educational Progress Contract, May 2009

- Series of Audits on Improper Special Allowance Billings by Lenders:

  ο Special Allowance Payments to Sallie Mae's Subsidiary, Nellie Mae, for Loans Funded by Tax-Exempt Obligations, August 2009

  ο Special Allowance Payments to the Kentucky Higher Education Student Loan Corporation for Loans Made or Acquired with the Proceeds of Tax-Exempt Obligations, May 2009

  ο Special Allowance Payments to the Pennsylvania Higher Education Assistance Agency for Loans Funded by Tax-Exempt Obligations, November 2007

  ο Special Allowance Payments to Nelnet for Loans Funded by Tax-Exempt Obligations, September 2006

  ο Special Allowance Payments to New Mexico Educational Assistance Foundation for Loans Funded by Tax-Exempt Obligations, May 2005

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[2] OIG reports may be found on our Web site at this link: http://www2.ed.gov/about/offices/list/oig/reports.html. Unless otherwise noted, dates referenced for investigative activities relate to the ending period for the OIG Semiannual Reports to Congress where the activities are discussed: http://www2.ed.gov/about/offices/list/oig/sarpages.html. Investigative press releases noted are available at this link: http://www2.ed.gov/about/offices/list/oig/ireports.html. GAO reports may be found on GAO's Web site, www.gao.gov.

OIG Investigations

- Educational Testing Service, Press Release, May 2011

Challenge: Information Technology Security

Because of the sensitivity of IT security issues, some OIG reports have been redacted.

- Investigative Program Advisory Report (IPAR) Incident Response and Reporting Procedures, July 2011

- IPAR—Weaknesses in the Process for Handling Compromised Privileged Accounts, September 2010

- Security Controls for Data Protection over the Virtual Data Center (Plano, Texas), September 2010

- Security over Certification and Accreditation for Information Systems, October 2009

- Incident Handling and Privacy Act Controls over External Web Sites, June 2009

Challenge: Oversight and Monitoring—SFA Program Participants

OIG Internal Reports

- Review of Federal Student Aid's Monitoring of Financial Responsibility, March 2011

- Federal Student Aid's Controls Over Loan Purchases Under the Ensuring Continued Access to Student Loans Act of 2008, July 2010

- Management Information Report—Review of Federal Student Aid's Enterprise Risk Management Program, May 2009

- Federal Student Aid's Oversight and Monitoring of Guaranty Agencies, Lenders, and Servicers Needs Improvement, April 2009

OIG External Reports

- Educational Credit Management Corporation's 2006 Agreement with the United States Department of Education, March 2011

- Wells Fargo Bank, National Association's Management of Collection Account Funds and Oversight Activities under the Ensuring Continued Access to Student Loans, February 2011

- Zions First National Bank's Management of Collection Account Funds and Oversight Activities Under the ECASLA Loan Participation Purchase Program, October 2010

- Community Care College's Administration of Title IV Federal Student Aid Programs, August 2009

- Touro College's Title IV, Higher Education Act Programs, Institutional and Program Eligibility, October 2008

- Technical Career Institutes, Inc.'s Administration of the Federal Pell Grant and Federal Family Education Loan Programs, May 2008

- Wilberforce University's Administration of the Title IV, Higher Education Act Programs, March 2008

- Series of Audits on Improper Special Allowance Billings by Lenders:

  o Special Allowance Payments to Sallie Mae's Subsidiary, Nellie Mae, for Loans Funded by Tax-Exempt Obligations, August 2009

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- Georgia Department of Education's Controls Over Performance Data Entered in EDFacts, April 2010

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- See also listing of OIG External Reports under Oversight and Monitoring— Recovery Act challenge above, first and second phases of OIG Recovery Act work.

GAO Reports

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- Recovery Act: One Year Later, States' and Localities' Uses of Funds and Opportunities to Strengthen Accountability, March 2010

- No Child Left Behind Act: Enhancements in the Department of Education's Review Process Could Improve State Academic Assessments, September 2009

Appendix B. Abbreviations and Acronyms Used in this Report

COA	Cost of Attendance
Department	U.S. Department of Education
Direct Loan Program	William D. Ford Federal Direct Loan Program
EDCAPS	Education Central Automated Processing System
ECASLA	Ensuring Continued Access to Student Loans Act of 2008
EDEN	Education Data Exchange Network
EDGAR	Education Department General Administrative Regulations
Ed Jobs	Education Jobs Fund Program
EDUCATE	Education Department Utility for Communications, Applications, and Technology Environment
ESEA	Elementary and Secondary Education Act of 1965
FAFSA	Free Application for Federal Student Aid
FFELP	Federal Family Education Loan Program
FISMA	Federal Information Security Management Act of 2002
FSA	Federal Student Aid
FTE	Full-Time Employee Equivalent
GAO	Government Accountability Office
GaDOE	Georgia Department of Education
HEA	Higher Education Act of 1965
IDEA	Individuals with Disabilities Education Act
IPAR	Investigative Program Advisory Report

IPERA	Improper Payments Elimination and Recovery Act of 2010
IPIA	Improper Payments Improvement Act of 2002
IRS	Internal Revenue Service
IT	Information Technology
LEA	Local Educational Agency
MOE	Maintenance of Effort
OIG	Office of Inspector General
OMB	Office of Management and Budget
Recovery Act	American Recovery and Reinvestment Act of 2009
SAFRA	Student Aid and Financial Responsibility Act of 2010
SEA	State Educational Agency
SFA	Student Financial Assistance
SFSF	State Fiscal Stabilization Fund
SIG	School Improvement Grants
Title I	Title I of ESEA

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