Testimony of Inspector General Kathleen S. Tighe,

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Subcommittee on Labor, Health and Human Services, Education, and Related Agencies

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Chairman Cole, Ranking Member DeLauro, and members of the Subcommittee, thank you for inviting me here today to discuss the most significant management challenges facing the U.S. Department of Education (Department). For fiscal year (FY) 2017, the Office of Inspector General (OIG) identified five management challenges facing the Department. I will discuss these challenges today, as well as highlight an emerging fiscal challenge involving the Federal student aid credit subsidy estimates.

Oversight and Monitoring

The Challenge: Effective oversight and monitoring of the Department's programs and operations are critical to ensuring that funds reach the intended recipients and achieve the desired results. This is a significant responsibility for the Department as it disburses about $125 billion in student aid annually and manages an outstanding loan portfolio of nearly $1.3 trillion – making it one of the largest financial institutions in the country. In addition, the Department administers more than 100 programs that serve 55 State and territorial educational agencies, nearly 18,200 public school districts with 50 million students who attend more than 132,000 schools, more than 6,000 institutions of higher education, and numerous other grantees and subgrantees. Our work in both the Federal student aid and the K-12 areas has identified a number of weaknesses that could be alleviated through more effective oversight and monitoring.

Needed Action: For Federal student aid, the Department needs to ensure that the activities of its Program Compliance office result in effective processes to monitor program participants and reduce risk, ensure its program reviews verify that high-risk schools meet all necessary requirements, and develop and implement improved methods to prevent and detect fraud. For K-12, the Department needs to ensure that its program offices are providing risk-based oversight of grant recipients and use the single audit process to improve its monitoring efforts and help mitigate fraud and abuse in its programs.

Information Technology Security

The Challenge: The OIG has identified repeated problems in the Department's information technology (IT) security and therefore has listed it as a significant challenge for the Department since 2006. Most recently, our FY 2016 Federal Information Security Modernization Act review concluded that the Department's overall information security programs were generally not effective. Although the Department reported significant progress towards addressing long-standing IT security weaknesses, our work identified repeated weaknesses that limit the Department's ability to mitigate threats to its systems and data, leaving them vulnerable to unauthorized access and attack.

Needed Action: Implementation and management of the technical security architecture supporting the Department's and the Federal Student Aid office's (FSA) applications requires strengthening to more effectively restrict unauthorized access to information resources, and policies and procedures to manage an effective incident response policy need to be developed.

Data Quality and Reporting

The Challenge: The Department, its grantees, and its subgrantees must have controls in place and effectively operating to ensure that accurate, reliable data are reported, as data quality contributes to effective program management, funding decisions, and helps ensure the credibility of information the Department publishes. Our work has identified a variety of weaknesses in the quality of reported data, specifically in the areas of program performance and student testing.

Needed Action: The Department needs to clarify requirements to grantees and subgrantees through appropriate technical assistance. It also needs to improve its review processes to ensure that grantees and subgrantees are reporting accurate and reliable data.

IT System Development and Implementation

The Challenge: The Department faces an ongoing challenge of efficiently providing services to growing numbers of program participants and managing additional requirements with declining resources. This makes effective information systems development and implementation—and the greater efficiencies such investments can provide—critical to the success of the Department's activities. Our recent work has identified weaknesses in the Department's processes to oversee and monitor systems development that have negatively impacted operations.

Needed Action: The Department needs to monitor contractor performance to ensure that system deficiencies are corrected. It also needs to ensure that it successfully implements and complies with the Federal Information Technology Acquisition Reform Act and other related guidance.

Improper Payments

The Challenge: Our Improper Payments Elimination and Recovery Act (IPERA) audits for FY 2014 and FY 2015 found that the Department did not comply with IPERA as its estimated improper payments for the Direct Loan program did not meet the annual reduction target published by the Department in its Annual Financial Report (AFR). Further, although our FY 2016 IPERA audit is not yet completed, the Department stated in its most recent AFR that it anticipates the OIG will find that it did not comply with IPERA for FY 2016 because its improper payment rates did not meet the annual reduction targets for the Direct Loan or the Pell Grant programs. In May 2016, we reported that the Department's improper payment estimates for both the Direct Loan and Pell programs were inaccurate and unreliable because the Department (1) used estimation methodologies that did not include all program reviews that could identify improper payments and (2) did not include all improper payments from ineligible programs or locations identified in program reviews or other sources. As a result of these flaws, we could not conclude whether the Department actually met its reduction target for the Pell program. The Department's ability to assess progress in addressing the root causes of improper payments is limited because it relies on program reviews that identify root causes that vary from year to year.

Needed Action: In response to OIG recommendations, the Department revised its estimation methodologies for both the Direct Loan and Pell programs for FY 2106. Among the changes was the inclusion of estimates of misreported income (over and under) by Free Application for Student Aid applicants. The revised estimation methodologies resulted in significant increases in the improper payment rates for these programs: the rate for the Direct Loan program increased from 1.30 percent for FY 2015 ($1.28 billion) to 3.98 percent for FY 2016 ($3.86 billion); the rate for the Pell program increased from 1.88 percent for FY 2015 ($562 million) to 7.85 percent for FY 2016 ($2.21 billion). Although the OIG believes that the revised rates are more realistic, the significant increases emphasize the need for the Department to use a more stable estimation methodology and intensify its efforts to identify and address internal controls and oversight to address the root causes.

Emerging Fiscal Challenge – Credit Subsidy Estimates

The Challenge: An emerging fiscal challenge for the Department is developing estimates of the subsidy cost of the direct and guaranteed loan programs. These estimates are used to support budget estimates, policy decisions, and financial reporting. The Department has developed a set of complex financial and economic models that apply mathematical techniques and statistical methods to historical loan level data to develop student loan program performance assumptions and estimate the value and cost of its student loan programs. These models support the Department's estimate of the net present value of cash flows related to a nearly $1.3 trillion loan portfolio of 42 million borrowers as of September 30, 2016. The audits of the Department's and FSA's 2015 and 2016 financial statements[1] identified a significant deficiency in internal controls. The audits determined that the Department did not have a comprehensive framework for risk management or fully-developed

[1] The audits of the financial statements are conducted under contract with CliftonLarsonAllen LLP and overseen by the OIG.

critical modeling activities. Limited documentation was maintained supporting the initial design, evaluation, justification, and testing of the model for selecting a sample of borrowers used for calculating program performance assumptions; estimating future incomes for borrowers under income-driven (IDR) plans; projecting future cash flows for borrowers under IDR plans; and projecting overall program level cash flows. Given the size, growth, and changes to the IDR program, ineffective controls over the design of new models can impact the reliability of any data gleaned and presented to the public and Congress from these models. For example, in 2015, the Department's Pay as You Earn program changed IDR payment amounts on qualified loans from 15 percent of discretionary income to 10 percent. The Direct Loan program re-estimated subsidy cost was adjusted upward by $21.8 billion in FY 2016. The re-estimates reflect several updated assumptions; however, the size of the increased re-estimate was due largely to collection rates on defaulted loans and repayment plan selection. Actual collections on defaults were lower since FY 2011 than anticipated, which reduced estimated lifetime rates and increased the estimated cost to the Government by $10.1 billion. A greater percentage of borrowers chose costlier IDR plans than had been estimated and increased the estimated cost to the Government by $8.1 billion in FY 2016.

Needed Action: It is critical for the Department to update and improve both its governance and its modeling for policymakers to fully understand the long-term costs of providing Direct Loans and the impact of repayment plan options.[2] My office is currently conducting an audit of the Department's disclosures of costs related to the IDR and loan forgiveness programs. We will share the findings of this work once the audit is completed later this year.

Our FY 2017 Management Challenges Report provides more detailed information on the management challenges that I touched on today. This report is available on our Web site at www.ed.gov/oig.

[2] In November 2016, the U.S. Government Accountability Office also issued a report titled, "Education Needs to Improve Its Income-Driven Repayment Plan Budget Estimates.