

## ***Improper Payments Information Act Reporting Details***

The recently enacted *Improper Payments Elimination and Recovery Act of 2010 (IPERA)* (Public Law 111-204), which amends the *Improper Payments Information Act of 2002 (IPIA)* (Public Law 107-300), and the Office of Management and Budget's (OMB) Circular A-123, Appendix C, Requirements for Effective Measurement and Remediation of Improper Payments, define requirements to reduce improper/erroneous payments made by the federal government. OMB also has established specific reporting requirements for agencies with programs that possess a significant risk of erroneous payments and for reporting on the results of recovery auditing activities. Agencies are required to annually review and assess all programs and activities to identify those susceptible to significant improper payments. The guidance in OMB Circular A-123, Appendix C, defines a significant improper payment as those in any particular program that exceed both 2.5 percent of program payments and \$10 million annually. For each program identified as susceptible and determined to be at risk, agencies are required to report to the President and the Congress the annual amount of estimated improper payments, along with steps taken and actions planned to reduce them.

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

### **Student Financial Assistance Programs**

#### **Risk Assessment**

As required by the IPIA, Federal Student Aid (FSA) inventoried its programs during FY 2010 and reviewed program payments made during FY 2009 (the most recent complete fiscal year available) to assess the risk of improper payments. The review identified and then focused on the following key Title IV programs: William D. Ford Federal Direct Loan (Direct Loan) Program, Federal Family Education Loan (FFEL) Program, to include the legacy FFEL Program, the *Ensuring Continued Access to Student Loans Act (ECASLA)* programs, and servicing of FFEL loans acquired through *ECASLA*, and the Federal Pell Grant Program.

The ACG/SMART Grant Programs were deemed to be low risk programs for FY2010. These programs are budgeted together and have a five-year life, ending with the academic school year 2010-2011. A risk assessment was completed for the ACG/SMART Programs in FY 2009, and was not repeated in FY 2010 because of the prior favorable results (i.e., estimated improper payment rates of .0045 percent and .00001 percent, respectfully), and upcoming program termination. The FY 2009 improper payment risk assessment methodology is described in the *FY 2009 Agency Financial Report*. No further information on these programs is included herein.

In addition to the A-123 guidance, the criteria for determining susceptible risk within the programs were defined as those programs with annual outlays that exceed \$200 million or

programs that were previously required to report improper payment information under OMB Circular A-11, Budget Submission, former Section 57.2.<sup>2</sup>

### Risk-Susceptible Programs

The Title IV programs that were deemed to be potentially susceptible to the risk of significant improper payments based on OMB criteria described above include Direct Loan, FFEL, and Pell Grant.

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

**Direct Loan Program.** A risk assessment was completed for the Direct Loan Program in FY 2010. There were no changes to the sampling process from prior years. The overall improper payment rate, based on this risk analysis, was 0.30 percent. Since this rate is below the threshold for reporting on improper payments, no further information on the Direct Loan Program is included herein.

**FFEL Program (Legacy).** The FFEL legacy programs include Special Allowance Payment (SAP), Interest Benefits, Lender Fees, Origination Fees, Consolidation Loan Rebate Fees, Claims Paid, Account Maintenance Fee, VFA Payments, Loan Processing & Issuance Fees, and various other payments/collections to/from Guaranty Agencies (GAs). The FFEL SAP risk analyses that were undertaken last year in lieu of a measurement and described in the Department's FY 2009 AFR did not yield any result that could help inform decisions on improper payment measurement and were suspended. Accordingly, FSA did not use these risk analyses to calculate an FY 2010 error rate and no estimate of FY 2010 improper payments is provided.

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

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

FSA determined that each of these, as well as the servicing of acquired FFEL loans, constitute a risk-susceptible program. A risk assessment for each of these components and

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<sup>2</sup> The four original programs identified in OMB Circular A-11, Section 57, were Student Financial Assistance (now Federal Student Aid), *ESEA*, Title I, Special Education Grants to States, and Vocational Rehabilitation Grants to States. Subsequently, after further review of the program risk, OMB removed Special Education Grants to States and Vocational Rehabilitation Grants to States from the list. OMB considers Section 57 programs susceptible to significant improper payments regardless of the established thresholds. OMB Circular A-136 also applies.

in the aggregate was completed during FY 2010. The overall improper payment rate, based on the risk analysis, was 0.000011 percent. Since this rate is below the threshold of reporting on improper payments, no further information on *ECASLA* or servicing of FFEL loans acquired through *ECASLA* is included herein.

**Pell Grant Program.** A risk assessment was completed for Pell Grant Program in FY 2010. There were no changes to the sampling process from prior years. The overall improper payment rate, based on this risk analysis, was 3.12 percent.

### Statistical Sampling

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

**FFEL Program (Legacy).** The FFEL SAP risk analyses that were undertaken last year in lieu of a measurement as described in the *FY 2009 Agency Financial Report* did not yield any result that could help inform decisions on improper payment estimation. Accordingly, FSA did not use these risk analyses to calculate an FY 2010 error rate and no estimate of FY 2010 improper payments is provided.

In FY 2009, Federal Student Aid worked with OMB to target their improper payment analysis using data mining techniques to identify potential improper payments, with particular focus on special allowance payments (SAP) to lenders. In recent years, SAP has been among the largest categories of payments to lenders or guarantors. However, the *College Cost Reduction Act of 2007* reduced SAP rates and, combined with a historically low interest rate environment, has resulted in SAP amounts due to the Department beginning in FY 2007. This substantial decline, coupled with a significant increase in the Direct Loan Program versus FFEL and the move to 100 percent Direct Loans at the end of FY 2010, have resulted in an improving risk profile related to the potential for FFEL improper payments.

**Pell Grant Program.** The Department conducts studies with the IRS using FAFSA data. Data provided by the IRS study are used to estimate improper payments for the Pell Grant Program. The methodology for the Pell Grant did not change in FY 2010 and additional details about the study can be found in the FY 2009 AFR, under Corrective Actions.

### Corrective Actions

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

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

**Pell Grant Program.** FSA implemented the 2009-10 Internal Revenue Service (IRS) data retrieval process, as a pilot on January 28, 2010, as planned. As of June 2010, over 600,000 users had gone to the IRS Web site to retrieve their income information. Approximately half of those users then transferred their income tax return data to the FAFSA on the Web (FOTW) application.

As a follow up to the successful 2009–10 pilot, the IRS data retrieval process for initial and renewal applications is enabled on the 2010–2011 FOTW site. This went live in September 2010. The IRS data retrieval process again enables Title IV student aid applicants and parents of dependent applicants to transfer certain tax return information from an IRS Web site directly to their 2010–2011 FOTW application. For 2010–2011, FSA is also expanding the availability of the IRS data retrieval process to include applicants using the Spanish version of the FOTW application. For the 2011–12 cycle year, the data match will be implemented in late January 2011 with hopes that the 2011–12 applicants and parents of dependent students can access and transfer IRS data earlier in the year directly into their 2011–12 FOTW.

FSA will continue to explore ways to facilitate the detection of error, based on the results of the FAFSA/IRS Data Statistical Study. Additionally, FSA continues to simplify the application process, which now includes real-time access for applicants and their parents to previously filed IRS tax information. These enhancements, coupled with improved error detection, should allow FSA to further reduce improper payments.

## Federal Student Aid Improper Payment Reporting Summary

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

Program	FY 2010 Actual			FY 2011 Estimated			FY 2012 Estimated			FY 2013 Estimated			FY 2014 Estimated		
	Outlays \$	IP %	IP \$	Outlays \$	IP %	IP \$	Outlays \$	IP %	IP \$	Outlays \$	IP %	IP \$	Outlays \$	IP %	IP \$
Pell Grant <sup>(1)</sup>	32,215	3.12	1,005	32,454	3.3	1,071	35,058	3.3	1,157	35,630	3.3	1,176	36,639	3.3	1,209

<sup>(1)</sup> The source of FY 2010 Pell outlays reflects total expenditures from FMSS. These numbers are considered estimates because the Pell rate is preliminary.

The chart above uses a preliminary Pell improper payment (IP) percentage for FY 2010. The FY 2010 IP percentage is scheduled to be finalized after issuance of the Department's AFR. The target 3.3 IP percentage used for 2011–2014 is based on potential improvements over the FY 2009 rate. Analysis of the FY 2010 data will be performed through early 2011 to determine whether the decrease from FY 2009 is statistically significant, and if so, what caused it. The IRS data retrieval study may affect the rate in FY 2012, but should not affect the rate for FY 2011 because the process went live late in the award year.

Note: The final Pell error rate for FY 2009 was 3.5 percent. This 3.5 percentage rate was reported as “preliminary” in the FY 2009 AFR; however, it did not change.

### Recovery Efforts

For Pell, recovery is achieved through assessments made during program reviews and compliance reviews. Pell also makes recoveries when overpayments to students are assigned to Federal Student Aid for collection. Pell recoveries for the period 2005 through September 30, 2010, are presented in the following table.

<b><u>Pell Recoveries</u></b> <b>(Dollars in Millions)</b>					
<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>
11.2	13.6	14.2	10.8	6.6	6.7

### Statutory and Regulatory Barriers

There are currently no identified barriers which may limit Federal Student Aid's corrective actions in reducing improper payments.

## ***Elementary and Secondary Education Act of 1965, Title I, Part A Program***

The Department performed a risk assessment of the *Elementary and Secondary Education Act of 1965* Title I Grants to Local Educational Agencies, during FY 2010. The assessment, based on FY 2008 single audit data (the most recent available), yielded an estimated improper payment rate of 0.04 percent or \$4.7 million. This confirms previously reported data indicating that the risk of improper payments under current statutory requirements is very low. To validate the assessment data, the Department conducts on-site monitoring reviews on a three-year review cycle that encompass all states and territories receiving Title I funds. There were no findings in the monitoring reviews with questioned costs that contradicted the data in the risk assessment.

### **Risk Assessment for Other Grant Programs**

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

In FY 2010, the Department worked with the Department of Energy's Oak Ridge National Laboratory to perform data mining on information available in the Federal Audit Clearinghouse's Single Audit Database, the Department's Grant Administration and Payment System, and the Department's Audit Accountability and Resolution Tracking System to assess the risk of improper payments in its remaining grant programs. To conduct the risk assessment screening, Oak Ridge National Laboratory augmented the Audit Accountability and Resolution Tracking System database with imputed values for the likely questioned costs for grants that were not audited. The imputed and real questioned costs could then be tabulated to provide a reasonable upper-bound estimate of the rate of erroneous payments for each of the functional programs of interest.

The most striking result of the analysis was the generally low rate of questioned costs. The key finding of this analysis was that for the most recent year for which data were available (FY 2008), none of the functional programs exceed the threshold value of 2.5 percent. Consequently, none of the programs would be labeled as susceptible to significant erroneous payments.

**Managing Risk in Discretionary Grants.** In FY 2010, the Department managed more than 10,000 discretionary grant awards. Due to the vast legislative differentiation and the complexity of the Department's grant award programs, ensuring that program staff are fully aware of potentially detrimental issues relating to individual grantees is a significant challenge. Program offices designate specific grants as high risk in accordance with Departmental regulations. The Department uses the Grants High-Risk Module housed within the Department's Grant Administration and Payment System, to track grants and grantees that are designated high risk. Program office staff are required to review and certify their awareness of the high-risk status of applicable grantees before making awards.

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

**Planned Corrective Actions.** In addition to the actions previously outlined under the Student Financial Assistance Programs, the Department will periodically update any corrective action plans based on the results of the initiatives outlined above. The Department will record and maintain corrective action plans as required, which will include due dates, process owners, and task completion dates.

**Information Systems and Infrastructure.** The Department has submitted budget requests of \$250,000 for FY 2011 and FY 2012 for information system infrastructure improvements. A portion of the funds will be used to continue the refinement of data mining efforts and the possible extension of recapture auditing efforts. It is also anticipated that the Department will incur costs related to mitigation activities.

**American Recovery and Reinvestment Act (Recovery Act) Programs.** For FY 2009 and FY 2010, the *Recovery Act* supplemented the Department of Education's appropriations by \$97.4 billion. The law created the new \$53.6 billion State Fiscal Stabilization Fund grant program. The *Recovery Act* also supplemented existing programs, including *ESEA* Title I and *IDEA* Part B and Part C, nearly doubling the funds available for some major grant programs at the Department. Immediately following the enactment of the *Recovery Act*, the Department conducted a systematic assessment of the risks presented by the law and concluded that recipient expenditures under all *Recovery Act* grants should be monitored because of the high level of funding. Further, the Department concluded that the State Fiscal Stabilization Fund program should receive a particularly high level of oversight because the program is both new and funded at an extremely high level.

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

The Department has also automated the review of the expenditure and activities data that recipients are reporting into [FederalReporting.gov](http://FederalReporting.gov) under the requirements of *Recovery Act* Section 1512. The staff across the Department is reviewing exception reports for inconsistencies between expenditures reported by recipients and the information in the Department's finance system. The staff is also reviewing the reports to gauge the reasonableness of reported expenditures and the relationship of prime recipient draws on

their grants to the amount expended by their subrecipients, to monitor for cash management issues.

## Recovery Auditing Progress

To effectively address the risk of improper administrative payments, the Department continued a recovery auditing initiative to review contract payments. The Department performed a review on a statistical sample of payment transactions. No improper payments were indicated in the review. The following chart presents the results of the Department's recovery auditing program.

Recovery Auditing Summary (in millions)								
Agency Component	Amount Subject to Review for CY Reporting	Actual Amount Reviewed and Reported CY	Amounts Identified for Recovery CY	Amounts Recovered CY	Amounts Identified for Recovery PYs	Amounts Recovered PYs	Cumulative Amounts Identified for Recovery (CY + PYs)	Cumulative Amounts Recovered (CY + PYs)
All	\$1,033	\$19.1	\$0	\$0	\$0.3	\$0.1	\$0.3	\$0.1

## Summary

The Department is enhancing its efforts for identifying and reducing the potential for improper payments to comply with the *IPERA*. Although there are still challenges to overcome, the Department is committed to ensuring the integrity of its programs.

The Department is focused on identifying and managing the risk of improper payments and mitigating the risk with adequate control activities. In FY 2011, we will continue to work with OMB and the Inspector General to explore additional opportunities for identifying and reducing potential improper payments and to ensure compliance with the *IPERA*.