U.S. Department of Education FY 2014 Agency Financial Report

U.S. Department of Education
Arne Duncan
Secretary

Office of the Chief Financial Officer
Thomas Skelly
Delegated to perform the functions and duties of Chief Financial Officer

November 14, 2014

This report is available on the Department's website at: http://www.ed.gov/about/reports/annual/index.html. On request, the report also is available in alternative formats, such as Braille, large print, or computer diskette. For more information, please contact our Alternate Format Center at (202) 260-0852 or by contacting the 504 coordinator via email at om_eeos@ed.gov.

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For Fiscal Year 2014, in addition to the *Agency Financial Report* (AFR), the Department will post to its website an *Annual Performance Report* (APR), and a *Summary of Performance and Financial Information* (SPFI). The APR and the Congressional Budget Justification will be posted on the Department's website at http://www.ed.gov/about/reports/annual/index.html with the FY 2016 budget.

Please submit your comments and questions regarding this plan and report and any suggestions to improve future reports, including suggestions for additional links that will increase the usefulness of the report to the public, to AFRComments@ed.gov or:

Office of the Chief Financial Officer
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Washington, D.C. 20202-0600

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About This Report

The purpose of the United States Department of Education's (the Department) Fiscal Year (FY) 2014 *Agency Financial Report* (AFR) is to inform Congress, the President, and the American people on how the Department has used federal resources entrusted to it to promote achievement and preparedness of youth entering a global environment by fostering excellence and ensuring equal access. We demonstrated our commitment to education by, among other things: improving access to early learning programs, reforming elementary and secondary education, making higher education more accessible and affordable, and working to attract talented people to the teaching profession. We also demonstrated that we are good stewards of financial resources by putting in place well-controlled and well-managed business and financial management systems and processes.

The AFR also provides high-level financial and performance highlights, assessments of controls, a summary of challenges, and a demonstration of our stewardship. This report is required by legislation and complies with the requirements of the Office of Management and Budget's Circulars A-11, *Preparation, Submission, and Execution of the Budget*, and A-136, *Financial Reporting Requirements*. The report satisfies the reporting requirements contained in the following legislation:

- Improper Payments Elimination and Recovery Act of 2010
- Government Performance and Results Act (GPRA) Modernization Act of 2010
- Federal Information Security Management Act of 2002
- Reports Consolidation Act of 2000
- Federal Financial Management Improvement Act of 1996
- Government Management Reform Act of 1994
- Chief Financial Officers Act of 1990
- Federal Managers' Financial Integrity Act of 1982

Federal Student Aid (FSA), a principal office of the Department and a designated Performance-Based Organization, also produces a separate *Annual Report* that details their financial and program performance. Summary level information about FSA activities can be found in the applicable sections of this report. For more detail on FSA's performance and financial information, refer to StudentAid.gov.

Certificates of Excellence

The Department of Education received the Association of Government Accountants' Certificate of Excellence in Accountability Reporting and a Best-in-Class Award for Best Report That Tells a Story for its FY 2013 AFR.

How This Report Is Organized

The AFR is designed to focus on use of federal resources assigned to the Department to support its mission of promoting equal access and improvement nationwide for youths in education, with a particular emphasis on the challenges ahead.

1. Management's Discussion and Analysis

This section provides information about the Department's mission and organizational structure as well as its high-level performance results, financial highlights, and management assurances regarding internal controls.

2. Financial Section

This section provides a message from the Chief Financial Officer, the financial statements and notes, required supplementary information and supplementary stewardship information, and the report from our independent auditors.

3. Other Information

This section provides improper payments reporting details, the schedule of spending, a summary of financial statement audit and management assurances, and the Office of Inspector General's Management and Performance Challenges for FY 2015 Executive Summary.

4. Appendices

This section provides a listing of selected Department web links, education resources and a glossary of acronyms, and abbreviations.

Message From the Secretary

November 14, 2014

I am pleased to present the Department of Education's FY 2014 *Agency Financial Report* (AFR). In this report, we share the Department's financial and performance highlights over the fiscal year ending September 30, 2014.

Our mission is to promote student achievement and preparation for global competitiveness by fostering educational excellence and ensuring equal access.

From improving access to early learning programs, to reforming elementary and secondary education, to making higher education more accessible and affordable, to working to attract talented people to the teaching profession, we have made an unprecedented commitment to education.

Performance Highlights

In the Department's *Strategic Plan for FY 2014–2018*, our mission is reflected in six strategic goals and 22 supporting strategic objectives, as well as six programmatic two-year Agency Priority Goals, which are posted on performance.gov. The Management's Discussion and Analysis section of this AFR contains a high-level discussion about our approach to performance management. To the best of my knowledge, the summary performance data included in this AFR are complete and reliable in accordance with federal requirements.

For those seeking additional details regarding our performance and progress toward achieving our strategic goals, I invite you to read our *Annual Performance Report*, which will be released at the same time as the President's FY 2016 budget and Congressional Budget Justifications.

Financial Management

The balance sheet of the Department now exceeds $1.0 trillion in assets. These are primarily from Credit Program Receivables (loans) and the Fund Balance with Treasury. We had $924 billion in loans outstanding at the end of the year. This included new loans made in 2014 and the balances of old loans less collections of interest and principal. The Department is the smallest of 15 cabinet-level agencies in terms of government staff, with approximately 4,100 employees, yet it has the third largest grant portfolio among the 26 federal grant-making organizations.

Good stewardship is a management imperative and priority for our Department, and I am assured that the financial data included in this AFR are complete and reliable in accordance with federal requirements. I am proud to report that we have received our 13th consecutive unmodified or "clean" audit opinion with no material internal control weaknesses and with no material instances of noncompliance with applicable laws and regulations. Last year, the Department was honored for the 10th time with a Certificate of Excellence in Accountability Reporting Award from the Association of Government Accountants, as well as a special award for producing a report that tells a compelling story about Departmental activities. The financial report includes information and assurances about the Department's financial management systems and controls as required by the *Federal Managers' Financial Integrity Act*.

Management Challenges

We remain committed to improved governance and better business processes. Management has worked closely with the Office of Inspector General (OIG) to gain its perspective about our most significant management and performance challenges, which are presented in the Other Information section of this report. The OIG's review addresses five FY 2015 management challenges: improper payments, information technology security, oversight and monitoring, data quality and reporting, and information technology system development and implementation.

The Department takes these challenges, as well as other issues identified through our own self-assessments of operations and external audits, seriously. The Department implemented initiatives to respond to the identified challenges and improve its systems and processes, including issues of grants monitoring, IT systems, and management of student loan repayments.

Outreach and Partnerships

Funding education is primarily a state and local function in the United States. Consequently, sharing information with others is an important function of the Department. On our YouTube channel, the Department shares stories about schools where reform efforts and innovations are making a difference for students. Our website, ed.gov, highlights Departmental initiatives, as well as focusing on a diversity of outside partnerships that support our mission.

Our Twitter page, @used.gov, has grown to reach more than 250,000 followers who have joined us in conversations about challenges facing their schools and communities. Twitter town halls and impromptu exchanges help to answer questions and gain feedback that help shape our outreach activities and discussions about education policy. The Department's official Facebook page shares photos, videos, and information with its active members.

Our blog, Homeroom, provides stakeholders with opportunity to learn about financing college, combating bullying, supporting teachers, and other important topics. The Department interacts with hundreds of national associations and organizations that represent the interests of prekindergarten-12 education, civil rights and advocacy, and higher education communities by keeping them apprised of program progress, policy decisions, and funding opportunities. Through e-mail and stakeholder forums, we and our national partners share updates with state and local affiliates.

Looking Ahead

Guided by our new strategic plan for FY 2014–2018, available on ed.gov and performance.gov, we have charted a road map for future success, and we will continue to evaluate our progress toward those goals and objectives. We look forward to working with our partners and colleagues in Congress, the states, and across the education community by keeping foremost in our minds why we care about education.

I am proud of the progress we are making at the Department. I salute the efforts of our dedicated employees who carry out the day-to-day work of the Department and of their continued commitment to provide every student in America with a world-class education.

Sincerely,

Arne Duncan

Contents

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Management’s Discussion and Analysis

About the Management's Discussion and Analysis

This section provides information on performance results, financial statements, systems and controls, compliance with laws and regulations, and actions taken or planned to address problems. The Department is committed to making each year's report more useful to all readers and to meet increasingly high standards for internal controls and good stewardship of federal investments. To help continue to improve the content of the *Agency Financial Report* (AFR), readers are encouraged to provide their feedback at: AFRComments@ed.gov.

The Department continues to enhance the usefulness of the AFR as a summary of the Department's activities in FY 2014 by using the report and relevant web content. Our intent is to provide users with access to useful information about the Department and its financial activities. This year, the Department concentrated on improving disclosures and continuing its commitment to reader-friendly reporting, with a particular emphasis on making the Notes to the Financial Statements more reader-friendly.

Through its performance, the Department has demonstrated its commitment to education by, among other things: improving access to early learning programs, reforming elementary and secondary education, making higher education more accessible and affordable, and working to attract talented people to the teaching profession. Through its ongoing commitment to being good stewards of its resources, the Department seeks to demonstrate that we have in place well-controlled and managed business and financial management systems and processes. In addition, we continually strive to improve our enterprise risk management methods and the means to assess and test our assumptions about risk.

Mission and Organizational Structure

This section provides information about the Department's mission, an overview of its history, and its structure. The active links include: the organization chart and principal offices, a map of its regional offices, and a description of selected offices by function, as well as a link to the full list of Department offices.

Discussion of Performance

The Department has elected to produce separate financial and performance reports for the last six years. The *Agency Financial Report* for FY 2014 provides a high-level description of performance measures and goals based on the *FY 2014–2018 Strategic Plan*, with a focus on the Agency Priority Goals (APGs) for 2014–15. A detailed discussion of performance information for FY 2014 will be provided in the Department's *Annual Performance Report* to be released at the same time as the President's FY 2016 Budget.

The section includes an overview of performance reporting, a report on the APGs for 2014–15, and high-level discussion of performance information. The Looking Ahead and Addressing Challenges section describes the challenges that the Department aims to address in order to achieve progress against the *FY 2014–2018 Strategic Plan*. The results achieved from Department expenditures are discussed at a high level in the AFR. For more details about performance, the reader should refer to the Department's budget and performance web page and performance.gov.

To view information on all Department programs, visit the Department's website.

Financial Highlights

The Department has added information in the Financial Highlights section of the report and focused on enhancing the clarity of the Notes to the Financial Statements to provide a more understandable depiction of its key financial balances and activities for FY 2014 and to identify and explain significant trends.

The Department expends a substantial amount of its budgetary resources and disburses large cash amounts on grant and loan programs intended to increase college access, quality, and completion; improve preparation for college and career from birth through 12th grade, especially for children with high needs; and ensure effective educational opportunities for all students. Therefore, the Department has included more high-level details about the sources and uses of the allotted funds and a composition of and summary of net costs by program.

The primary sources of funds are borrowings from Treasury (Debt), appropriations from Congress, and spending authority from offsetting collections. Most borrowings and collections are associated with student loans.

As a ten-time recipient of the Association of Government Accountants' Certificate of Excellence in Accountability Reporting and having earned unmodified (or "clean") audit opinions for 13 consecutive years, the Department has demonstrated its commitment to continuous improvement in its financial management, operations, and reporting.

Analysis of Controls, Systems, and Legal Compliance

To demonstrate effective stewardship of these resources, the Department has implemented effective controls over operations, systems, and financial reporting as described in the Analysis of Controls, Systems, and Legal Compliance section of the report.

The three objectives of internal controls are to ensure the effectiveness and efficiency of operations, reliability of financial reporting and systems controls, and compliance with applicable laws and regulations. The Department categorizes and assesses controls in three categories:

- internal controls over operations,
- internal controls over financial reporting, and
- internal controls over systems.

About the Department

Our Mission

The U.S. Department of Education's mission is *to promote student achievement and preparation for global competitiveness by fostering educational excellence and ensuring equal access.*

Who We Are. In 1867, the federal government recognized that furthering education was a national priority and created a federal education agency to collect and report statistical data. The Department was established as a cabinet-level agency in 1979. Today, the Department supports programs that positively impact every area and level of education.

The Department engages in four major types of activities: establishing policies related to federal education funding, including the distribution of funds, collecting on student loans, and using data to monitor the use of funds; supporting data collection and research on America's schools; identifying major issues in education and focusing national attention on them; and enforcing federal laws prohibiting discrimination in programs that receive federal funds.

Our Public Benefit. The Department is committed to helping to ensure that students throughout the nation develop skills to succeed in school, college, and the workforce. While recognizing the primary role of states and school districts in providing a high-quality education, the Department supports efforts to employ highly qualified teachers and administrators, establish challenging content and achievement standards, and monitor students' progress against those standards.

The Department's largest asset is the portfolio of student loans. Grants to states are the second largest item on the balance sheet, mostly for elementary and secondary education, awarded based on legislated formulas. The third biggest item is student aid to help pay for college through Pell Grants, Work Study, and other campus-based programs. The Department also carries out competitive grant programs to promote innovation, performs research, collects education statistics, and enforces civil rights statutes.

Offices by Function. Federal Student Aid (FSA) administers need-based financial assistance programs for students pursuing postsecondary education and makes available federal grants, direct loans, and work-study funding to eligible undergraduate and graduate students.

The offices of Elementary and Secondary Education (OESE), Special Education and Rehabilitative Services (OSERS), Innovation and Improvement (OII), English Language Acquisition (OELA), Postsecondary Education (OPE), and Career, Technical, and Adult Education (OCTAE) provide leadership, technical assistance, and financial support to state and local educational agencies and institutions of higher education for reform, strategic investment, and innovation in education.

Institute of Education Sciences (IES) is the research arm of the Department. The Department's goal is to provide rigorous and relevant evidence on which to ground education practice and policy and share this information broadly. By identifying what works, what doesn't, and why, IES aims to improve educational outcomes for all students, particularly those at risk of failure. Its goal is to transform education into an evidence-based field in which decision makers routinely seek out the best available research and data before adopting programs or practices that will affect significant numbers of students.

The Office for Civil Rights (OCR) works to ensure equal access to education and to promote educational excellence throughout the nation through vigorous enforcement of civil rights. OCR serves student populations facing discrimination and the advocates and institutions promoting systemic solutions to civil rights issues.

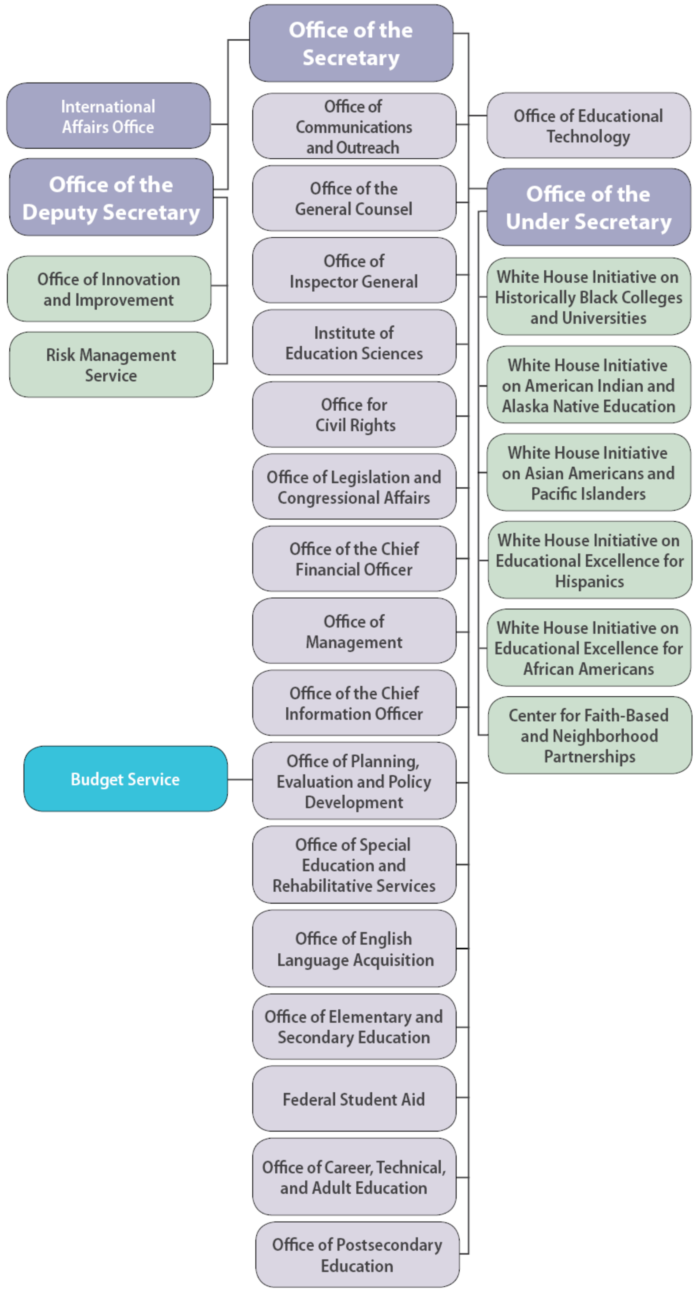
The Office of Planning, Evaluation and Policy Development (OPEPD) serves as the principal adviser to the Secretary on all matters relating to policy development and review, performance measurement and evaluation, budget processes and proposals, overseeing policy development, and reviewing policy recommendations. Two major components, the Budget Service and the Policy and Program Studies Service, are housed within OPEPD.

Regional Offices. The Department has 10 regional offices that provide points of contact and assistance for schools, parents, and citizens. Regional offices offer support through communications, civil rights enforcement, and federal student aid services to promote efficiency, effectiveness, and integrity in the programs and operations of the Department. In addition to enforcement offices in federal regions, enforcement offices are located in Washington, D.C., and Cleveland, Ohio.

Descriptions of the principal offices and overviews of the activities of the Department and its programs can be found on the Department's website.

Our Organization in Fiscal Year 2014

This chart reflects the statutory organizational structure of the U.S. Department of Education. [Interactive] and [text versions] of the coordinating structure of the Department are available.



The Department's Approach to Performance Management

Performance Management Framework

In accordance with the *GPRA Modernization Act of 2010*, the Department's framework for performance management starts with the *Strategic Plan,* including its Agency Priority Goals, which serve as the foundation for establishing long-term priorities and developing performance goals, objectives, and measures by which the Department can gauge achievement of its stated outcomes. Progress towards the Department's strategic and Agency Priority Goals is measured using data-driven review and analysis. This focus promotes active management engagement across the Department. Additional information is available in the *Department's Annual Performance Plans and Annual Performance Reports.*

Based on data available as of June 30, 2014, 18 metrics in the *FY 2014–18 Strategic Plan* showed significant progress toward the established goals, including important areas such as postsecondary degree attainment, the resolution of civil rights investigations, increased access to data, and research studies related to education.

The *FY 2014–18 Strategic Plan* is comprised of six strategic goals and six Agency Priority Goals and aims to align the Administration's yearly budget requests and the Department's legislative agenda. The Department continues to welcome input from Congress, state and local partners, and other education stakeholders about the *Strategic Plan.* Questions or comments about the *Strategic Plan* should be e-mailed to APP_APRComments@ed.gov.

FY 2014–18 Strategic Plan

AGENCY MISSION

Mission: To promote student achievement and preparation for global competitiveness by fostering educational excellence and ensuring equal access

2014–2018 STRATEGIC PLAN

Strategic Goals	Strategic Objectives	Priority Goals
Goal 1: ***Postsecondary Education, Career and Technical Education, and Adult Education.*** Increase college access, affordability, quality, and completion by improving postsecondary education and lifelong learning opportunities for youths and adults.	**Objective 1.1: *Access and Affordability.*** Close the opportunity gap by improving the affordability of and access to college and/or workforce training, especially for underrepresented and/or underprepared populations (e.g., low-income and first-generation students, English learners, individuals with disabilities, adults without high school diplomas, etc.). **Objective 1.2: *Quality.*** Foster institutional value to ensure that postsecondary education credentials represent effective preparation for students to succeed in the workforce and participate in civic life. **Objective 1.3: *Completion.*** Increase degree and certificate completion and job placement in high-need and high-skill areas, particularly among underrepresented and/or underprepared populations. **Objective 1.4: *Science, Technology, Engineering, and Mathematics Pathways.*** Increase STEM pathway opportunities that enable access to and completion of postsecondary programs.	• Increase college degree attainment in America
Goal 2: *Elementary and Secondary Education.* Improve the elementary and secondary education system's ability to consistently deliver excellent instruction aligned with rigorous academic standards while providing effective support services to close achievement and opportunity gaps, and ensure all students graduate high school college- and career-ready.	**Objective 2.1: *Standards and Assessments.*** Support implementation of internationally benchmarked college- and career-ready standards, with aligned, valid, and reliable assessments. **Objective 2.2: *Effective Teachers and Strong Leaders.*** Improve the preparation, recruitment, retention, development, support, evaluation, recognition, and equitable distribution of effective teachers and leaders. **Objective 2.3: *School Climate and Community.*** Increase the success, safety, and health of students, particularly in high-need schools, and deepen family and community engagement. **Objective 2.4: *Turn Around Schools and Close Achievement Gaps.*** Accelerate achievement by supporting states and districts in turning around low-performing schools and closing achievement gaps, and developing models of next-generation high schools. **Objective 2.5: *STEM Teaching and Learning.*** Increase the number and quality of STEM teachers and increase opportunities for students to access rich STEM learning experiences.	• Support implementation of college- and career-ready standards and assessments • Improve learning by ensuring that more students have effective teachers and leaders

2014–2018 STRATEGIC PLAN

Strategic Goals	Strategic Objectives	Priority Goals
Goal 3: *Early Learning.* Improve the health, social-emotional, and cognitive outcomes for all children from birth through 3rd grade, so that all children, particularly those with high needs, are on track for graduating from high school college- and career-ready.	**Objective 3.1: *Access to High-Quality Programs and Services.*** Increase access to high-quality early learning programs and comprehensive services, especially for children with high needs. **Objective 3.2: *Effective Workforce.*** Improve the quality and effectiveness of the early learning workforce so that early childhood educators have the knowledge, skills, and abilities necessary to improve young children's health, social-emotional, and cognitive outcomes. **Objective 3.3: *Measuring Progress, Outcomes, and Readiness.*** Improve the capacity of states and early learning programs to develop and implement comprehensive early learning assessment systems.	• Support comprehensive early learning assessment systems
Goal 4: *Equity.* Increase educational opportunities for underserved students and reduce discrimination so that all students are well-positioned to succeed.	**Objective 4.1: *Equitable Educational Opportunities.*** Increase all students' access to educational opportunities with a focus on closing achievement gaps and remove barriers that students face based on their race, ethnicity, or national origin; sex; sexual orientation; gender identity or expression; disability; English language ability; religion; socioeconomic status; or geographical location. **Objective 4.2: *Civil Rights Compliance.*** Ensure educational institutions' awareness of and compliance with federal civil rights obligations and enhance the public's knowledge of their civil rights.	• Ensure equitable educational opportunities
Goal 5: *Continuous Improvement of the U.S. Education System.* Enhance the education system's ability to continuously improve through better and more widespread use of data, research and evaluation, evidence, transparency, innovation, and technology.	**Objective 5.1: *Data Systems and Transparency.*** Facilitate the development of interoperable longitudinal data systems for early learning through employment to enable data-driven, transparent decision-making by increasing access to timely, reliable, and high-value data. **Objective 5.2: *Privacy.*** Provide all education stakeholders, from early childhood to adult learning, with technical assistance and guidance to help them protect student privacy while effectively managing and using student information. **Objective 5.3: *Research, Evaluation, and Use of Evidence.*** Invest in research and evaluation that builds evidence for education improvement; communicate findings effectively; and drive the use of evidence in decision-making by internal and external stakeholders. **Objective 5.4: *Technology and Innovation.*** Accelerate the development and broad adoption of new, effective programs, processes, and strategies, including education technology.	• Enable evidence-based decision making
Goal 6: *U.S. Department of Education Capacity.* Improve the organizational capacities of the Department to implement the *Strategic Plan*.	**Objective 6.1: *Effective Workforce.*** Continue to build a high-performing, skilled, diverse, and engaged workforce within the Department. **Objective 6.2: *Risk Management.*** Improve the Department's program efficacy through comprehensive risk management, and grant and contract monitoring. **Objective 6.3: *Implementation and Support.*** Build Department capacity and systems to support states' and other grantees' implementation of reforms that result in improved outcomes, and keep the public informed of promising practices and new reform initiatives. **Objective 6.4: *Productivity and Performance Management.*** Improve workforce productivity through information technology enhancements, telework expansion efforts, more effective process performance management systems, and state-of-the-art leadership and knowledge management practices.	

The Department's Agency Priority Goals

The Department identified six Agency Priority Goals (APGs) for FY 2014–15 that serve to focus its activities, with a particular emphasis over the next two years. These goals are consistent with the Department's five-year strategic plan, which will be used to monitor and report regularly on progress, reflect the Department's cradle-to-career education strategy, and help concentrate efforts on the importance of teaching and learning at all levels of the education system. Quarterly updates for the APGs are available on performance.gov.

Progress on the Department's FY 2014–15 Agency Priority Goals[1]

Agency Priority Goal: Increase college degree attainment in America

Goal for FY 2014–2015: By September 30, 2015, 45.6 percent of adults ages 25–34 will have an associate degree or higher, which will place the nation on track to reach the President's goal of 60 percent degree attainment by 2020.

Supports Strategic Goal 1.

Overview: In 2009, the President set a goal that, by 2020, the United States will have the highest proportion of college graduates in the world. Meeting this goal will require millions of additional Americans to earn a postsecondary degree by the end of this decade. The President's focus on the educational attainment among adults ages 25–34 allows the Department to assess progress in preparing the next generation of workers and to benchmark for international comparisons.

The Department's strategy to implement the President's College Value and Affordability Agenda comprises three areas of focus: (1) promoting evidence-based innovation and competition so that colleges offer students a greater range of affordable, high-quality options than they do today, (2) fostering institutional and student accountability in tandem with better consumer awareness, and (3) ensuring that student debt remains affordable. These strategies aim to support college attainment by reducing the cost and amount of time necessary to attain a degree, by measuring college performance and providing consumer information about cost and outcomes, by supporting the use of open educational low-cost textbooks, and by incentivizing state, institutional, and student behavior.

Progress: Starting from a baseline of 44.0 percent in 2012, the Department projected that the annual increase of educational attainment among adults ages 25–34 would grow progressively each year above the four-year historical average of 0.7 percentage points and established performance targets of 44.7 percent for 2014 and 45.6 percent for 2015. The Department is on pace to achieve this APG as 44.8 percent of adults ages 25–34 have an associate's degree or higher, exceeding the 2014 performance target (note that the rate reflects prior year data, in this case from 2013, but is reported in 2014 when data are available). Examples of the Department's activities that support this goal include collaborating with the White House to host College Opportunity Summits that bring together superintendents and college presidents; developing and refining the College Scorecard; and redesigning existing programs to encourage efforts to improve college fit, reduce the need for remediation, increase the availability of open educational resources, and implement evidence-based practices. These activities promote

[1] The performance information reported in this section is current as of Quarter 3 of FY 2014 (April 1–June 30, 2014).

innovation, competition, and accountability in the postsecondary sector, which will boost completion rates and educational attainment.

Opportunities and Challenges: One challenge toward achieving this goal is that the Department's budgetary proposals have not received traction in Congress, and it remains unclear whether recent proposals that reflect the President's agenda will gain support. As such, success will also depend largely on the extent to which states invest in higher education. Specifically, whether and to what extent states and institutions (a) implement policies and programs to increase college access and success, (b) reduce costs and time to completion, (c) support accelerated learning opportunities, including dual enrollment, (d) develop and adopt effective and innovative practices that improve student outcomes, and (e) promote seamless transitions from secondary to postsecondary education and among higher education institutions will influence the Department's success in achieving this APG. Although the Department has some limited leverage to influence states' policies and the practices of postsecondary institutions, the Department will use its available resources, including implementation and impact of programs and technical assistance, and the ability to convene stakeholders to encourage collaboration and best practices.

Agency Priority Goal: Support implementation of college- and career-ready standards and assessments

Goal for FY 2014–2015: By September 30, 2015, at least 50 states/territories will be implementing next-generation assessments, aligned with college- and career-ready standards.

Supports Strategic Goal 2.

Overview: The adoption of internationally benchmarked college- and career-ready standards is the foundation to improving educational outcomes for all students and a fundamental step toward increasing the number of college graduates in the United States. Moreover, these standards must be coupled with high-quality formative and summative assessments that will measure the extent to which students are mastering them.

Progress: Most states have adopted college- and career-ready standards and are in the process of developing and testing the assessments aligned with those standards. The Race to the Top - Assessment (RTTA) consortia and the consortia developing alternate assessments based on alternate achievement standards completed the field testing of their assessments in preparation for operational administration in spring 2015.

Opportunities and Challenges: State capacity to implement college- and career-ready standards and assessments aligned with those standards varies. To address this challenge, the Department is developing and targeting technical assistance activities that will, in part, increase state capacity to leverage limited resources and continue to identify promising practices across multiple states. For example, the Department will build a "bank" of resources that support the implementation of college- and career-ready standards. Included in such a bank will be materials to assist in full and effective implementation of college- and career-ready standards developed or identified by offices across the Department.

The Department will continue to leverage the ESEA flexibility monitoring and renewal process to support full implementation of college- and career-ready standards and aligned, valid, and reliable assessments in states that have received ESEA flexibility. By using the ESEA flexibility monitoring process, the Department can track state implementation and identify areas where technical assistance is needed. This monitoring approach follows the different kind of relationship the Department has built internally across its offices and externally with states during the ESEA flexibility approval process, including the use of cross-Departmental teams (including staff from the Implementation and Support Unit (ISU), Office of Special Education Programs (OSEP), and the Office of School Turnaround), reducing burden and duplication, and reducing overlap between other Department programs and ESEA flexibility.

Agency Priority Goal: Improve learning by ensuring that more students have effective teachers and leaders

Goal for FY 2014–2015: By September 30, 2015, at least 37 states will have fully implemented teacher and principal evaluation and support systems that consider multiple measures of effectiveness, with student growth as a significant factor.

Supports Strategic Goal 2.

Overview: Teacher and principal evaluation and support systems enable the development and identification of effective educators and provide information to improve the educator workforce. The nation needs to do more to ensure that every student has an effective teacher, every school has an effective leader, and every teacher and leader has access to the preparation, ongoing support, recognition, and collaboration opportunities he or she needs to succeed. The Department will help strengthen the profession by focusing on meaningful feedback, support, and incentives at every stage of a career, based on fair evaluation and support systems that look at multiple measures, including, in significant part, student growth.

The Department will support states in the development and adoption of state requirements for comprehensive teacher and principal evaluations and support systems as well as in district development and implementation of comprehensive educator evaluation systems. This additional support is necessary so that teachers and educator evaluators are able, for example, to use and develop learning objectives to measure student growth and to implement new classroom observation tools.

Progress: The performance targets for this APG are based on state implementation timelines provided through original ESEA flexibility requests. These timelines indicated that 37 states expected to implement the systems by September 30, 2015. As of June 30, 2014, 10 states have fully implemented teacher and principal evaluation and support systems.[2]

Opportunities and Challenges: Providing support to states to do this work well is resource-intense. Additionally, it is difficult for the Department to maintain the momentum for reform, given districts' and states' current political situations and potential changes in leadership. However, as states continue work to implement teacher and leader evaluation systems, the Department will continue to provide robust technical assistance. In addition to monitoring, the Department has designed a one-year ESEA flexibility extension process for Window 1 and 2 states. States that are on track to meet their original ESEA flexibility commitments relating to evaluation and support systems will be able to use this process to continue their work in 2014–15. The Department will work with states that have requested changes to their timelines

[2] "Fully implemented" is defined as the school year in which teachers and principals receive effectiveness ratings.

or sequencing of events outside of the extension process to ensure that they, too, can continue their work in the 2014–15 school year and are making continuous improvement in their systems.

Agency Priority Goal: Support comprehensive early learning assessment systems

Goal for FY 2014–2015: By September 30, 2015, at least nine states will be collecting and reporting disaggregated data on the status of children at kindergarten entry using a common measure.

Supports Strategic Goal 3.

Overview: Kindergarten entry assessments (KEAs), when properly designed, are included in a state's comprehensive early learning assessment system, improve student achievement and early learning programs' effectiveness, and inform professional development to improve the early learning workforce. KEAs also can inform instruction and support students' educational success by identifying the early learning needs of each child. As such, KEAs provide an opportunity for teachers and families to understand the status of children as they are entering kindergarten and an opportunity to provide policy makers with information needed to support high-quality early learning programs that ensure children enter school prepared for success.

Progress: The Department is on track to achieve this APG. As of June 30, 2014, the Early Learning Challenge Technical Assistance Center (ELC TAC) reported that six states are collecting and reporting disaggregated data on the status of children at kindergarten entry using a common measure. Additionally, the Department's Office of Early Learning conducted an analysis of the Race to the Top - Early Learning Challenge (RTT-ELC) grantees' annual performance reports and found that four states are in the process of revising their current statewide KEAs, five other states are beginning a phased-in implementation of KEAs, and six others are pilot testing their KEAs. Although there are challenges with the implementation of KEAs, the Department is optimistic about achieving the APG.

Opportunities and Challenges: The Department plans on releasing an annual report about RTT-ELC grantees that includes information on how states are engaging stakeholders in KEA development, providing more professional development to teachers, and evaluating what is and is not working in order to improve the KEA process. The sharing of these lessons learned will advance progress toward this goal. Additionally, the Department will reach out to external organizations that share our interest in advancing quality KEAs to develop strategies that may increase our collective impact.

Because assessment in early learning is new, many states are in the early stages of developing valid and reliable measures for KEAs. Constructing and testing these instruments and implementing them across every school in the state will be challenging and will take time. In addition, new measures and systems require significant investment and state budget cuts could impact deployment. The Department will continue to convene states and share resources that support states in their collecting and reporting of disaggregated data on the status of children at kindergarten entry using a common measure.

Agency Priority Goal: Ensure equitable educational opportunities

Goal for FY 2014–2015: By September 30, 2015, the number of high schools with persistently low graduation rates will decrease by 5 percent annually. The national high school graduation rate will increase to 83 percent, as measured by the Adjusted Cohort Graduation Rate, and disparities in the national high school graduation rate among minority students, students with disabilities, English learners, and students in poverty will decrease.

***Supports Strategic Goal 4*.**

Overview: Equality of opportunity is a core American value. Young people in this country—regardless of wealth, home language, zip code, gender, sexual preference, race or disability—must have the chance to learn and achieve. Through Race to the Top (RTT), the School Improvement Grant (SIG) program, ESEA flexibility, and other federal programs, the Department is providing significant resources to improve the nation's lowest-achieving schools dramatically by using intensive turnaround models and identifying the low-achieving schools that are showing strong evidence of successfully turning around. The Department continues to focus on supporting innovation, not just compliance monitoring, and on spurring growth in achievement, not just absolute achievement measures as done in the past.

Increasing the national high school graduation rate and decreasing disparities in the graduation rate is critical to achieving the President's college graduation goal. The nation has made significant progress in increasing graduation rates, but gaps between rates for different student groups continue to persist. This APG aims to reduce that gap.

Progress: The Department announced the Excellent Educators for All initiative, a 50-state strategy to support state efforts to ensure that low income students and students of color have equal access to qualified and effective teachers and leaders. This initiative will include a new technical assistance network, educator equity data profiles, guidance for states on developing educator equity plans, and state submission of new educator equity plans. The Department expects this initiative, as well as the support provided through the programs that contribute to this APG, will result in continued improvement to the high school graduation rate and a reduction in the number of high schools with persistently low graduation rates.

Opportunities and Challenges: One key challenge in achieving this APG is providing differentiated support to states based on their current status and progress in increasing graduation rates. While all states have room for improvement, some states are farther behind than others, particularly for different subgroups of students. Recently, the Department addressed one major barrier, which was the incomparability of graduation rate data across states. All states are now required to use an adjusted cohort graduation rate, and the Department is reporting these data at the state, district, and school levels. However, differences in how states define a regular high school diploma, and other technical features of their calculations, continue to make comparisons challenging. The Department will continue to improve its data release processes to ensure that data on graduation rates are released to the public on a regular schedule and on a timely basis to help states and districts better use data to drive improvement. The Department will also use the upcoming ESEA flexibility renewal process as an opportunity to support states in continuously improving their systems of differentiated recognition, accountability, and support to ensure that they are effectively identifying and supporting schools with low graduation rates for all students and for particular subgroups of students.

Another challenge for this APG is sustaining the reforms in schools after SIG funding ends. Insufficient focus or funding for comprehensive turnaround efforts at the state and local levels compounds this challenge. As such, the Department will develop and disseminate guidance and technical assistance on sustainability strategies to help states and districts continue reforms after federal funding ends. Additionally, the Department will provide states with guidance on how to implement recent legislative changes to the SIG program that extended the length of the grants that the Department can award. The guidance will encourage states to use the additional time for both planning and sustainability activities during the grant period.

Agency Priority Goal: Enable evidence-based decision making

Goal for FY 2014–2015: By September 30, 2015, the percentage of select new (non-continuation) competitive grant dollars that reward evidence will increase by 70 percent.

***Supports Strategic Goal 5*.**

Overview: There is an increasing emphasis from the Department and among stakeholders on the importance of using evidence to support government program funding decisions. In support of this APG, the Department is increasing its internal capacity to make competitive grant awards based on the existing strength of evidence. For example, with the inclusion of a common evidence framework in the Education Department General Administrative Regulations (EDGAR), competitive grant programs may select from four tiers of evidence to use as priorities[3] or selection criteria, as appropriate. Additionally, through its mix of grants, contracts, and internal analytic work, the Department aims to support the use of research methods and rigorous study designs that provide evidence that is as robust as possible.

Progress: In FY 2014, five competitions in the Office of Innovation and Improvement (OII), the Office of Elementary and Secondary Education (OESE), and the Office of Postsecondary Education (OPE) are using evidence through eligibility requirements, competitive preference priorities, and selection criteria. As such, the Department anticipates meeting its performance target for this APG.

Opportunities and Challenges: The Department is exploring ways to support and build the capacity of program offices as they shift to evidence-based funding models. For example, the Department leverages the Regional Educational Laboratories' (RELs) resources about logic models and evaluation design by sharing them with applicants, grantees, and program offices. Although these resources support both internal and external stakeholders, the Department has limited resources to provide direct and targeted technical assistance to applicants and grantees, which vary in their comfort with and understanding of evaluation and use of evidence. To continue building the capacity of the education field to use and generate evidence, it is important that the Department is able to provide appropriate technical assistance to its grantees and applicants. The Department anticipates achieving this year's performance target for this APG based on projections about which competitive grant programs may make new awards during FY 2014.

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[3] The Department may use a priority as an absolute priority, meaning applicants must propose projects that meet it to be eligible to receive funds, or as a competitive preference priority, meaning applicants may choose to address it and could receive additional points depending on how well the priority is addressed.

Cross-Agency Priority Goals

In accordance with the *GPRA Modernization Act of 2010*, interim Cross-Agency Priority Goals (CAP Goals) were published on performance.gov in March 2014. The CAP Goals are divided into two categories:

Mission CAP Goals	Management CAP Goals
• Cybersecurity • Climate Change (federal actions) • Insider Threat and Security Clearance • Job-creating Investment • Infrastructure Permitting Modernization • STEM Education • Service Member and Veterans Mental Health	• Customer Service • IT Delivery • Strategic Sourcing • Shared Services • Benchmarking and Mission-support Operations • Open Data • Lab to Market • People and Culture

Performance.gov is updated on a quarterly basis for each CAP Goal. The website will include information required by law, such as goal leader(s), contributing agencies, organizations, programs, targets, key milestones, and major management challenges, as well as plans to address these challenges. Quarterly Performance Updates for the website on progress will be provided by the goal leader in coordination with the Performance Improvement Council, the Office of Management and Budget (OMB), corresponding government-wide management council, and contributing agencies. (A-11, Part 6, 220.5)

Each CAP Goal has a goal leader(s) and deputy goal leader(s) who will manage the processes by which goals are executed. Goal leaders are given flexibility when managing CAP Goals and are encouraged to leverage existing structures as much as practicable (e.g., existing working groups, interagency policy committees, councils). Every CAP Goal will have a governance team chaired by the goal leader, a deputy goal leader, and representatives from agencies contributing to the goal, OMB, and others as determined by the goal leader. Each governance team will develop an action plan explaining how the Federal Government will execute on the goal, including agencies' contributions, areas where cross-agency coordination is needed, and anticipated risks or obstacles. The action plan will be updated as experience is gained and new information is learned. (A-11, Part 6, 220.9)

In addition to the Agency Priority Goals, the Department contributes to CAP Goals as required by the *GPRA Modernization Act of 2010,* including:

Customer Service: Deliver world-class customer services to citizens by making it faster and easier for individuals and businesses to complete transactions and have a positive experience with government.

Science, Technology, Engineering, and Math (STEM) Education: In support of the President's goal that the United States have the highest proportion of college graduates in the world by 2020, the federal government will work with education partners to improve the quality of STEM education at all levels to help increase the number of well-prepared graduates with STEM degrees, the number of STEM teachers with corresponding undergraduate degrees, and students' access to quality STEM learning experiences.

Real time information on Cross-Agency Priority Goals is available at performance.gov.

Management Performance

The Department continues to make a substantive commitment and investment in improving its working capacity and infrastructure, to further leverage policy and programmatic aims to reform the nation's educational system. Goal 6 of the *Strategic Plan* (U.S. Department of Education Capacity: Improve the organizational capacities of the Department to implement the *Strategic Plan*) supports those aims by ensuring that the Department's hiring, staffing, training, culture, systems, and procedures enable the Department to deliver programs and resources in ways that are faster, smarter, and better year after year. Thus, the commitment and the investments are both short- and long-range in nature.

Examples of the Department's strategies are seen in the thrust for greater employee engagement, improvements and increases in diversity and inclusion, more rigorous hiring targets and goals, and expansion of its leadership and knowledge management efforts in key, cross-cutting areas, such as Information Technology (IT). These areas of focus also align with the FY 2014 President's Management Agenda. That agenda includes management goals related to customer service, benchmarking and mission support, IT delivery, Open Data, strategic sourcing, lab to market, shared services, and organizational culture.

The Department is making major efforts to bolster its impact in the people and culture element, with an enterprise-wide workgroup on employee engagement, which is also leveraging and piloting several strategic engagement initiatives throughout the Department. Those strategies include formalized supervisor and peer recognition; intensive manager training and development pilots; increased development and usage of telework policies and flexibilities; and employee wellness, lifestyle balance, and volunteerism campaigns.

IT delivery is another area of focus to which the Department has committed a considerable amount of resources. The Chief Information Officer has led a push for greater technology innovation to improve the workload capacity for employees. Efforts to improve security, gain efficiency in storage, improve network service and responsiveness, increase system speed, and increase the footprint of Wi-Fi and other wireless and mobility solutions in the Department's facilities and for those working remotely, have significantly improved the employee computing experience. These efforts have laid a foundation to clarify the Department's ongoing needs and provide a clear vision for how technology can better enable work over the next decade.

Another vital accomplishment and significant progress to date can be seen in the Department's emphasis on Cybersecurity, one of the President's mission CAP goals. During FY 2014, the Department significantly reduced the number of threats and risks, including security breaches. In another effort, the technology group reported increases in electronic signature usage at nearly 150 percent of its target. These advances in cybersecurity have been the result of steady and focused strategies to proactively seek innovation as a major resource in the campaign to improve.

Looking Ahead and Addressing Challenges

Quality education continues to be a vital component to the nation's long-term economic prosperity and recent economic gains. It is an investment that is valued highly by Americans, for both present needs and its future promise. The Department continues to support state formula grant programs while supporting the creation of models through competitive programs, including Race to the Top, Promise Neighborhoods, Investing in Innovation (i3) grants, and a redesigned School Improvement Grants program. Those commitments are bolstered by increasing the extent to which evidence is used in programs and strategic decision-making.

Going forward, the Department will build on what it has already established:

- state-driven accountability that demands progress for all children;
- high-quality early education for more low-income children;
- more flexibility for state decision-making;
- more support for principals and teachers to apply high standards to practice;
- reforming career education in high schools and community colleges; and
- reforming and simplifying the application process for student aid to help drive college affordability and completion.

Additionally, the Department will continue to strengthen the support systems necessary for all students to succeed. This includes promoting preschool access for all students, K-12 strategic reforms, and college affordability. Ultimately, the Department looks to create ladders of opportunity to help all students.

Goal 1. Postsecondary Education, Career and Technical Education, and Adult Education: Increase college access, affordability, quality, and completion by improving postsecondary education and lifelong learning opportunities for youths and adults.

Dramatically boosting completion rates for bachelor's and associate's degrees is essential for the United States to successfully compete in a global economy. A college education is one of the most important investments that Americans can make to increase the likelihood of higher earnings and lower the risk of unemployment. Unfortunately, for many low- and middle-income families, college is slipping out of reach. Over the past three decades the average tuition at a public four-year college has more than tripled, while a typical family's income has increased only modestly. Lodging, food, books, and other related expenses have also increased dramatically. More students than ever are relying on loans to pay for college.

Today, 71 percent of those earning a bachelor's degree graduate with debt, which averages $29,400. While most students are able to repay their loans, many feel burdened by debt, especially as they seek to start a family, buy a home, launch a business, or save for retirement. As such, the Department continues to focus on efforts intended to make college more affordable and loan repayments more manageable by implementing initiatives from the President's Value and Affordability Agenda.

As noted elsewhere in this report, many of the Department's initiatives depend, in large part, on the extent to which states invest in higher education and on actions taken by states and institutions. The Department will use its available resources and programs, administrative action, bully pulpit, technical assistance, and ability to convene stakeholders to drive collaboration and best practices to support states and institutions in making these investments.

Goal 2. Elementary and Secondary Education: Improve the elementary and secondary education system's ability to consistently deliver excellent instruction aligned with rigorous academic standards while providing effective support services to close achievement and opportunity gaps, and ensure all students graduate high school college- and career-ready.

The 2012 high school graduation rate—80 percent—is the highest in America's history. Graduation rate increases between 2008 and 2012 showed that an additional 100,000 Latino students and 40,000 African-American students graduated from high school. That is 140,000 students of color alone with a better chance of getting a good job, owning their own home, and supporting a family. Despite this achievement, the nation needs to push beyond 80 percent.

The adoption of internationally benchmarked college- and career-ready standards is the foundation to improving educational outcomes for all students. These standards must be coupled with high-quality formative and summative assessments to measure the extent to which students are mastering the standards. A challenge facing the Department over the next two years is supporting states both in their plans to implement these standards and aligned assessments for all students, including English learners, students with disabilities, and low-achieving students, and in their development and implementation of teacher and principal evaluation and support systems. As noted elsewhere in this report, the Department aims to address these challenges by developing and targeting technical assistance activities that will increase state capacity to leverage limited resources and by identifying and disseminating information on promising practices.

Goal 3. Early Learning: Improve the health, social-emotional, and cognitive outcomes for all children from birth through 3rd grade, so that all children, particularly those with high needs, are on track for graduating from high school college- and career-ready.

Every child should have the opportunity for a great start in life. According to recent Civil Rights Data Collection data, big opportunity gaps start at the very beginning of formal education. Nationwide, 60 percent of school districts have public preschool programs but 40 percent—almost 7,000 districts—do not offer these programs. Nearly 10,000 school districts today have a public, district-based preschool program, but more than half of those districts—57 percent—offer only part-day programs, and barely half of the school districts that have public preschool programs make them available to all children within the district.

Additionally, the most recent State Preschool Yearbook from the National Institute for Early Education Research (NIEER) shows fewer than 30 percent of 4-year-olds in the U.S. are enrolled in state-funded preschool programs; and for those who do attend, 41 percent were served in programs that met fewer than half of the NIEER quality standards benchmarks.

The Department will keep working to improve access to high-quality early learning through our implementation of the Preschool Development Grants, support of RTT-ELC state systems of early learning, Enhanced Assessment Grants (EAG) grantees that are designing and developing KEAs, and continued close partnership with the Department of Health and Human Services.

Expanding access to high-quality early learning programs and constructing, testing, and implementing assessment of early learning outcomes are challenging and resource-dependent initiatives. States are beginning the development of valid and reliable measures for KEAs. New measures and systems are expensive, and budget cuts could impact deployment. Additionally, EAG grantees that are consortia experience challenges in the coordination across states due to differences in their policies and procedures.

Goal 4. Equity: Increase educational opportunities for underserved students and reduce discrimination so that all students are well-positioned to succeed.

Identifying opportunity gaps is the first step that schools and districts should take to address educational inequities. The real power of the Civil Rights Data Collection lies not just in the numbers themselves, but in the real-world impact they can have when coupled with courage and the will to change. These data are providing—and will continue to provide—important markers and starting points for discussion within the Department and among education stakeholders. Further, as noted previously, the Department is focused on supporting innovation and efforts that demonstrate growth in student achievement.

Multiple Department programs aim to improve educational equity, and it can be challenging to ensure states and districts coordinate these efforts. Key barriers and challenges to aligning the work of these programs and improving education equity include sustaining reforms in schools after their SIG program grants end; addressing capacity challenges at state, district, and school levels; focusing on comprehensive turnaround efforts at the state and district level beyond the SIG program; ensuring alignment between SIG, RTT, ESEA flexibility, and other programs and initiatives; and accessing quality and completeness data that would allow others to define success.

Goal 5. Continuous Improvement of the U.S. Education System: Enhance the education system's ability to continuously improve through better and more widespread use of data, research and evaluation, evidence, transparency, innovation, and technology.

Through its mix of grants, contracts, and internal analytic work, the Department continues to support the use of research methods and rigorous study designs that provide robust evidence. Using evidence to award competitive grants requires a shift in culture and capacity-building across the Department and in the field. Although the Department utilizes Regional Educational Laboratories (RELs), the Education Resource Information Center (ERIC), and the What Works Clearinghouse (WWC) to make information about research and evaluation available, the Department has limited resources to provide technical assistance to applicants and grantees to support their understanding of evidence standards and conducting rigorous evaluations that would produce evidence of effectiveness.

In addition to its efforts to increase evidence-based decision-making, the Department also considers transparency, participation, and collaboration as vital to the success of improving the quality and accessibility of education. An important component of that commitment is the Department's Open Government Plan. The Department's 2014 Open Government Plan provides an update on existing programmatic work and highlights of Department actions to achieve its goals of improving student achievement and educational opportunity. The flagship initiatives of the Plan include: A fully operational beta version of the Education Data Inventory, a repository of data that the Department collects; early public participation and input in policy- and rule-making; a new version of the Federal Registry for Educational Excellence (FREE), making it easier to find digital teaching and learning resources; the Integrated Student Experience (ISE) initiative, resulting in increased financial aid awareness and a simplified application and servicing experience; and the Department's Disclosure Review Board (ED-DRB), which is responsible for the review and approval of the disclosure avoidance protections used to protect privacy in the Department's public data releases. Additionally, the Department launched an initiative called the Future Ready District Pledge, a commitment by superintendents to develop and implement technology plans that would support a transition to digital learning.

Goal 6. U.S. Department of Education Capacity: Improve the organizational capacities of the Department to implement the *Strategic Plan.*

Recently, the Department participated in a series of government-wide benchmarking exercises, as a part of the President's Management Agenda, and the findings have been very useful in key areas, including technology, real estate, and financial management. As a result of the findings, comparisons to other agencies and identifying best practices, the Department's technology group has identified the potential for greater savings in certain service sectors and found objective confirmation for many of its cost-saving plans for the future, such as driving down specific network and e-mail storage costs by transitioning services to the cloud environment. This effort has also caused the Department to consider additional shared service arrangements that may help garner more efficiency and lower costs.

A major effort is underway to freeze and reduce the Department's occupied space footprint in facilities across the nation. The Department's space modernization initiative will help identify and gain efficiencies in various ways, including consolidating employees and work groups into existing spaces as facilities' leases expire, for projected rent savings; reducing space requirements and related rental per square footage rates; increasing the extent and impact of telework and other mobility strategies; and redesigning workspaces to reduce the need for isolated, individual spaces while adding more collaborative ones.

In financial management, the Department continues to assess its business processes to ensure that they are effectively and efficiently supporting the mission. Those activities include process re-engineering, enhanced automation, strengthening internal controls, and expanding the use of shared service solutions where practical.

Finally, greater emphasis and development for the management and supervision cadre is an essential element of the strategy to build capacity and infrastructure. The Department continues to explore and identify innovative training and development opportunities, while also looking for tangible ways to gauge the effectiveness and return on the investments in this area. Getting this approach right is critically important to the Department's ability to sustain consistent and continuous improvement, as well as safeguarding the ability to manage the knowledge, expertise, and functionality to deliver on its strategic mission and goals.

Reporting on Progress Made on Strategic Goals and Objectives: The Department continues to use tools and processes, such as quarterly performance reviews, to assess progress toward achieving strategic goals and outcomes. Additionally, the Organizational Performance Review contributes to the Department's data-driven performance discussions by serving as a tool for principal offices to improve their efficiency and effectiveness by focusing on operational priorities and initiatives at the principal office level.

To support the tracking and reporting of progress against the goals and objectives, the Department provides regular updates to its data profile on performance.gov for key policy and programmatic topics. The effective implementation of the Department's strategic and Agency Priority Goals will depend, in part, on the effective use of high-quality and timely data, including evaluations and performance measures, throughout the lifecycle of policies and programs.

In addition, the Department's success in achieving its strategic goals is closely tied to its capacity and funding. In addressing capacity, the Department will invest in the continuous improvement of its workforce and employ comprehensive risk management to ensure prudent use of public dollars by mitigating risk through increased oversight and support of grantees and contractors.

The six Department *Strategic Plan* goals guide the day-to-day work of the Department's staff. This plan will help to align the administration's yearly budget requests and the Department's legislative agenda. Continuous improvement rests on ongoing cycles of assessing performance, examining data, and improving practices. Creating a culture of continuous improvement is at the heart of the Department's efforts to work with and support educators, administrators, and policy makers.

Accomplishing all of the priorities will require strong coordination and collaboration from Department staff working with Congress, partners at the state and local levels, and other stakeholders. This includes meeting numerous legislative challenges and acting under fiscal constraints that may impact the Department's ability to provide the necessary incentives and resources to increase quality, transparency, and accountability.

Financial Highlights

Introduction

This section provides summarized information and analyses about the Department's assets, liabilities, net position, sources and uses of funds, program costs, and related trend data. It is intended to help increase the AFR users' understanding about how the Department used the resources it was entrusted with and provides a high-level perspective of the detailed information contained in the financial statements and related notes.

The Department consistently produces accurate and timely financial information. Our financial statements and notes are prepared in accordance with accounting principles generally accepted in the United States for federal agencies issued by the Federal Accounting Standards Advisory Board (FASAB) and the format and content specified by OMB, specifically in Circular No. A-136, *Financial Reporting Requirements*. The financial statements, notes, and underlying business processes, systems, and controls are audited by an independent accounting firm with audit oversight provided by the Office of Inspector General (OIG). For thirteen consecutive years, the Department has earned an unmodified (or "clean") audit opinion. The financial statements and notes for FY 2014 are on pages 54–94 and the Independent Auditors' Report begins on page 102.

Management's assessment of internal controls in accordance with OMB Circular A-123, *Management's Responsibility for Internal Control*, provides the Department with credibility to external stakeholders and confidence that financial data produced from its underlying financial systems and business processes are complete, accurate, and reliable. This ensures the financial statements conform with applicable federal reporting requirements, the Department has trustworthy financial information for good decision-making, and various reports can be produced for both internal and external stakeholders timely and accurately. Additionally, the Department's complete and accurate financial data enables it to provide transparency pertaining to the finances of the Department and how it is spending federal funds. Further information on management's assessment of internal controls can be found in the Analysis of Controls, Systems, and Legal Compliance section that begins on page 37.

Trend Analysis

The tables below summarize trend information about components of the Department's financial condition. The Table of Key Measures summarizes trend information about components of the Department's Consolidated Balance Sheet and Statement of Net Cost, and provides a snapshot of the Department's financial condition as of September 30, 2014, compared with the end of fiscal years 2013–2010, displaying assets, liabilities, net position, and net cost, rounded to the millions. The Summarized Financial Data graphic presents the table data, as a graph, for an alternate display over the same five consecutive years, rounded to the billions.

Table of Key Measures

As of September 2014, 2013, 2012, 2011, and 2010

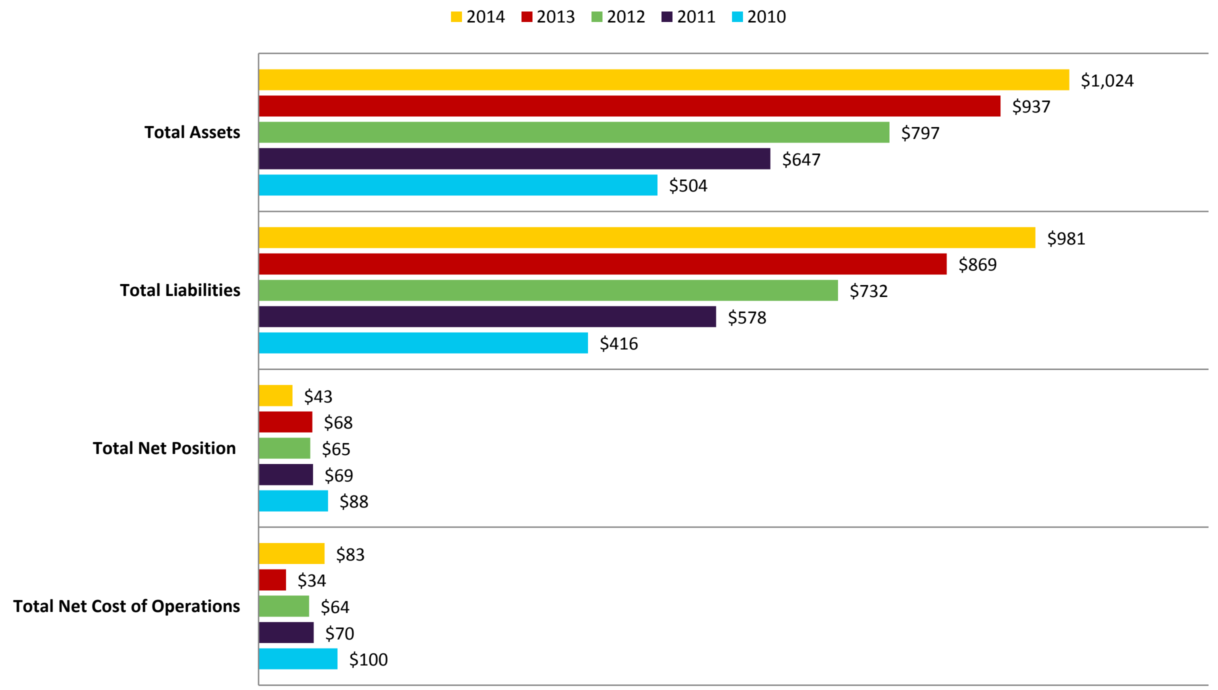
(Dollars in Millions)

	% Change FY 14 / FY 13	FY 2014	FY 2013	FY 2012	FY 2011	FY 2010
Consolidated Balance Sheet						
Fund Balance with Treasury	-9%	$ 98,696	$ 108,732	$ 121,993	$ 114,085	$ 132,259
Credit Program Receivables, Net	+12%	923,545	826,684	673,488	530,491	367,904
Other	+3%	1,685	1,642	1,446	1,966	3,501
Total Assets	+9%	**1,023,926**	**937,058**	**796,927**	**646,542**	**503,664**
Debt	+13%	966,671	852,432	715,303	547,108	374,335
Liabilities for Loan Guarantees*	+0%	-	-	1,037	10,025	14,479
Other	-13%	14,549	16,783	15,432	20,824	27,248
Total Liabilities	+13%	**981,220**	**869,215**	**731,772**	**577,957**	**416,062**
Unexpended Appropriations	-7%	66,447	71,371	72,686	71,729	94,371
Cumulative Results of Operations	-573%	(23,741)	(3,528)	(7,531)	(3,144)	(6,769)
Total Net Position	-37%	**$ 42,706**	**$ 67,843**	**$ 65,155**	**$ 68,585**	**$ 87,602**
Consolidated Statement of Net Cost						
Gross Cost	+83%	$ 112,295	$ 61,353	$ 89,263	$ 89,910	$ 116,953
Earned Revenue	+8%	(29,125)	(26,881)	(25,490)	(20,397)	(17,279)
Total Net Cost of Operations	+141%	**$ 83,170**	**$ 34,472**	**$ 63,773**	**$ 69,513**	**$ 99,674**

* The presentation of the FY 2012 and earlier Liability for Loan Guarantees is in the Liability section of the Department's Balance Sheet; however, the presentation of the same FY 2013 and FY 2014 liability is in the Credit Program Receivables, Net Balance Sheet line item, due to its negative value.

Summarized Financial Data

(Dollars in Billions)

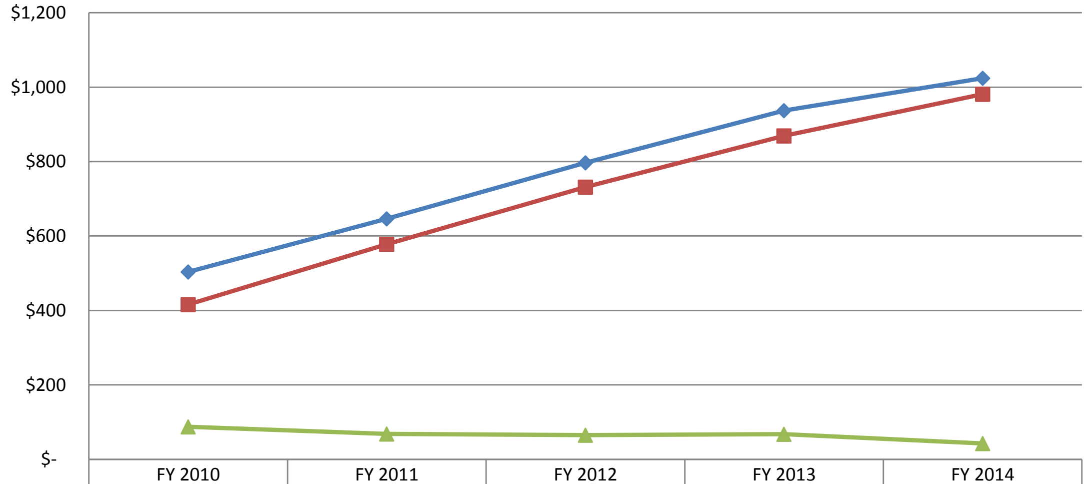


Balance Sheet

The Consolidated Balance Sheet presents, as of a specific point in time (the end of the fiscal year), the Department's total assets, total liabilities, and the difference, which is known as net position.

Comparison of Department's Assets, Liabilities & Net Position for Fiscal Years 2010–2014

(Dollars in Billions)

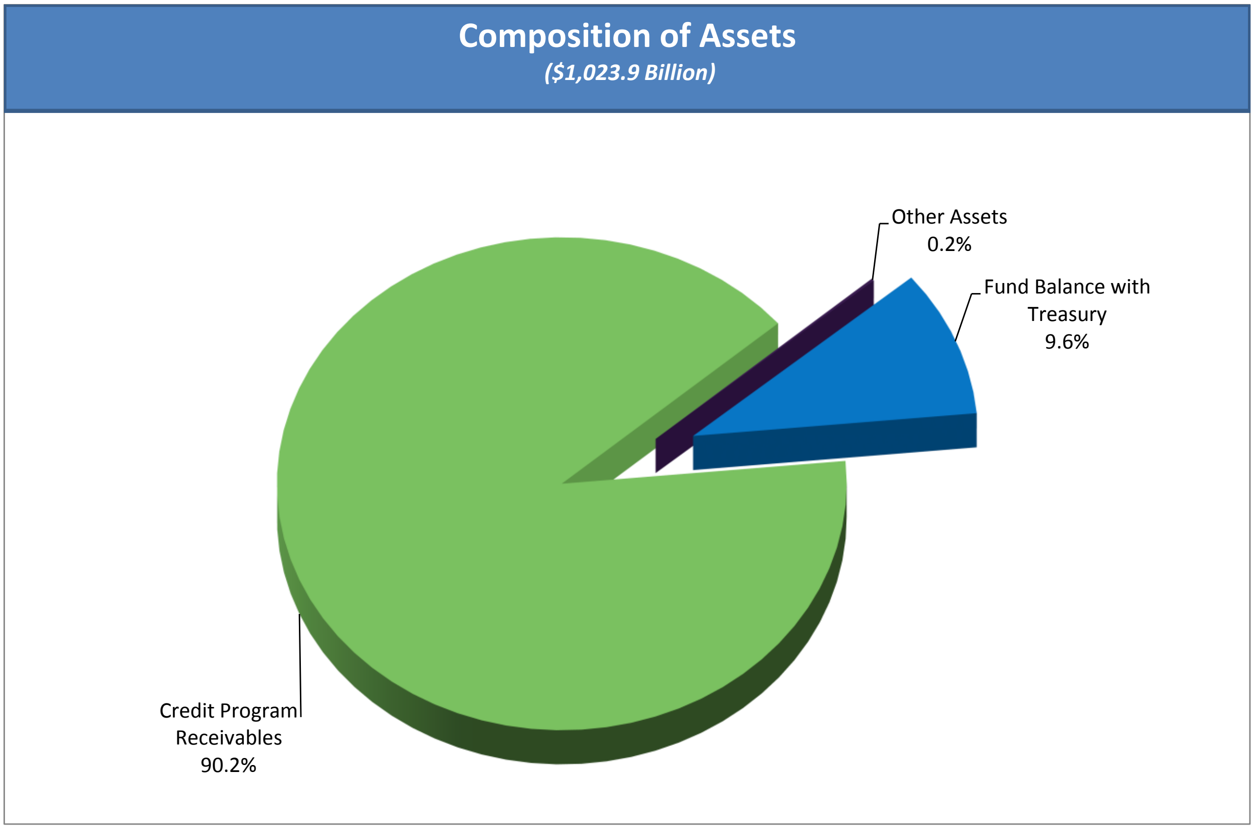


	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
Total Assets	$503,664	$646,542	$796,927	$937,058	$1,023,926
Total Liabilities	$416,062	$577,957	$731,772	$869,215	$981,220
Total Net Position	$87,602	$68,585	$65,155	$67,843	$42,706

Table amounts are presented in millions

Analysis of Assets

The Department's assets totaled $1,023.9 billion as of September 30, 2014, an increase of $86.8 billion, or approximately 9 percent, over the FY 2013 balance of $937.1 billion. The vast majority of the increase in assets relates to Credit Program Receivables, which increased to $923.5 billion, a 12 percent increase over $826.7 billion in FY 2013. The Credit Program Receivables increase is largely the result of Direct Loan disbursements for new loan originations and Federal Family Education Loan (FFEL) consolidations, net of borrower principal and interest collections, which increased the net portfolio for Direct Loans by $99.4 billion ($134 billion was disbursed for consolidated loans). The Department's total assets are composed of Fund Balance with Treasury, Credit Program Receivables, and Other Assets.

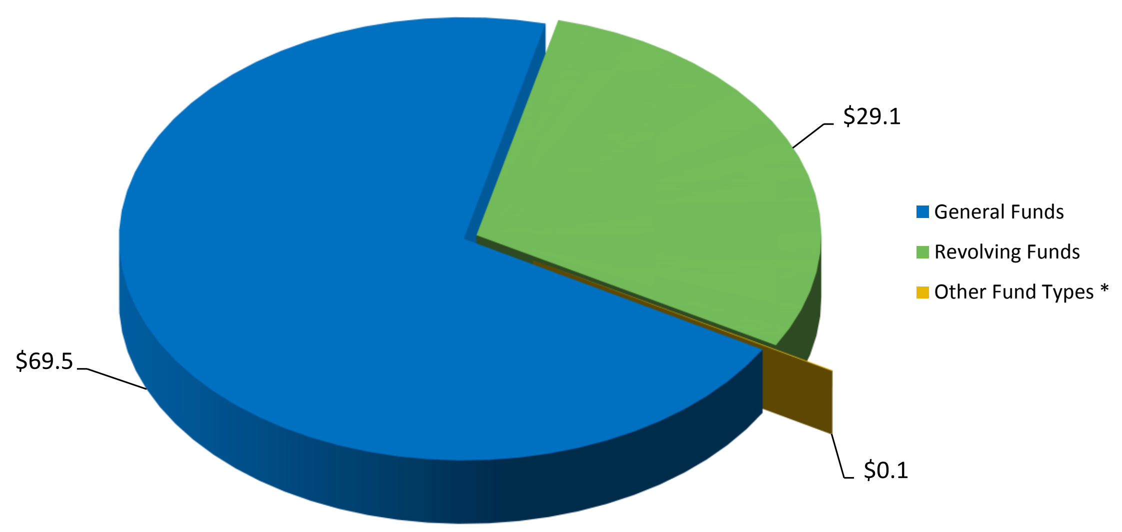


Assets as of September 30, 2014 and 2013 *(Dollars in Millions)*	**2014**	**2013**
Fund Balance with Treasury	$ 98,696	$ 108,732
Credit Program Receivables	923,545	826,684
Other Assets*	1,685	1,642
Total Assets	$ 1,023,926	$ 937,058

* The Other Assets amount includes Cash and Other Monetary Assets, Accounts Receivable, Property and Equipment, and Other.

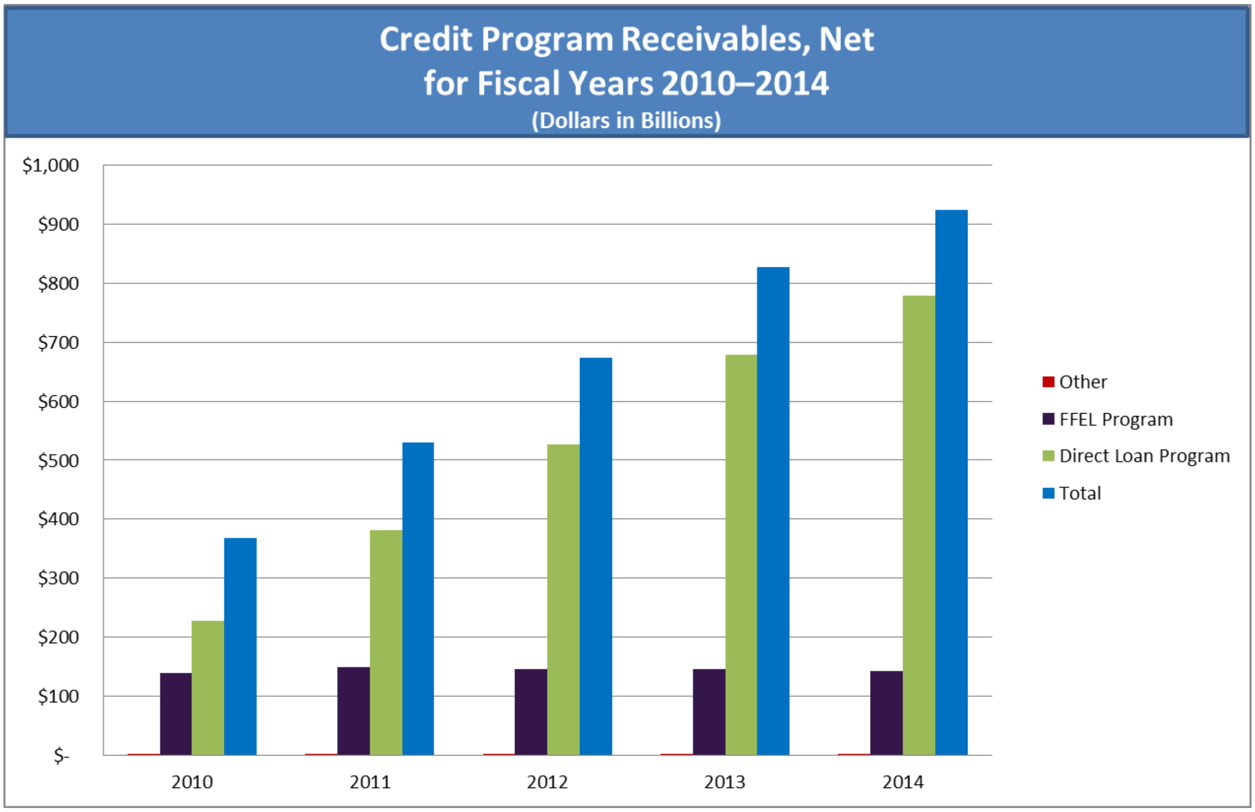
The chart below displays the composition of funds held with the U.S. Treasury (Fund Balance with Treasury) as of September 30, 2014. A portion of the general funds is provided in advance by multiyear appropriations for obligations anticipated during the current and future fiscal years. Revolving funds are derived from borrowings, as well as collections from the public and other federal agencies. Other Funds include special funds that include fees collected on delinquent or defaulted Perkins loans, and trust funds for the hurricane relief activities.

Fund Balance with Treasury
($98.7 Billion)



*Other fund types include special, trust, clearing, non-entity deposit, and receipt funds.

The chart below presents the Department's Credit Program Receivables, Net, for fiscal years 2010–2014. This chart shows the Department's shift in the composition of its loans receivable portfolio from guaranteed loans to direct loans. FFEL Guaranteed Loans Receivable have not grown during the past five years because no new loans were made after June 30, 2010. This shift in the loans receivable portfolio is consistent with the provisions of the *SAFRA Act,* which required the transition from the Department guaranteeing the loans provided by the private sector to full direct lending. As a result, there has been a pronounced increase in the Direct Loan Program. This change caused the Department's Credit Program Receivables to grow significantly, from $368 billion in FY 2010 to $924 billion in FY 2014, a $556 billion increase.



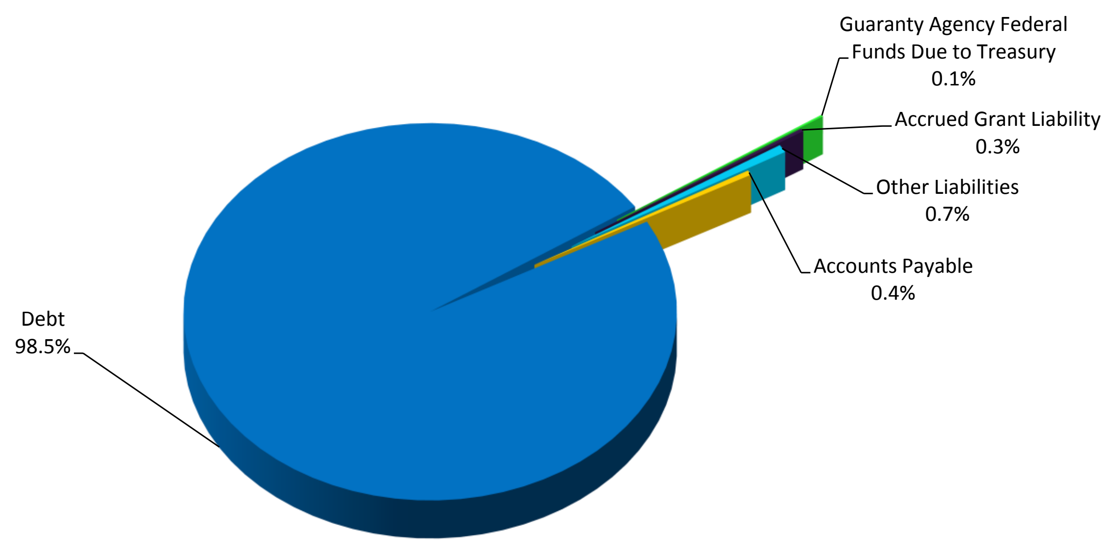
Analysis of Liabilities

Liabilities of the Department totaled $981.2 billion as of September 30, 2014, an increase of $112.0 billion, or approximately 13 percent over the FY 2013 balance of $869.2 billion. Total Liabilities are primarily made up of Debt resulting from Credit Program Receivable activity. The increase is principally related to current year borrowing from Treasury for the Direct Loan and FFEL Programs that provided funding for Direct Loan disbursements and FFEL Program payment of credit program outlays. Current year borrowing, net of repayments, resulted in a $114 billion increase in Debt.

The FY 2010–2012 Liability for Loan Guarantees are presented in the liability section of the Department's Balance Sheet, while the FY 2013 and FY 2014 Liability for Loan Guarantees are presented in the Credit Program Receivables because they resulted in a negative liability.

Composition of Liabilities

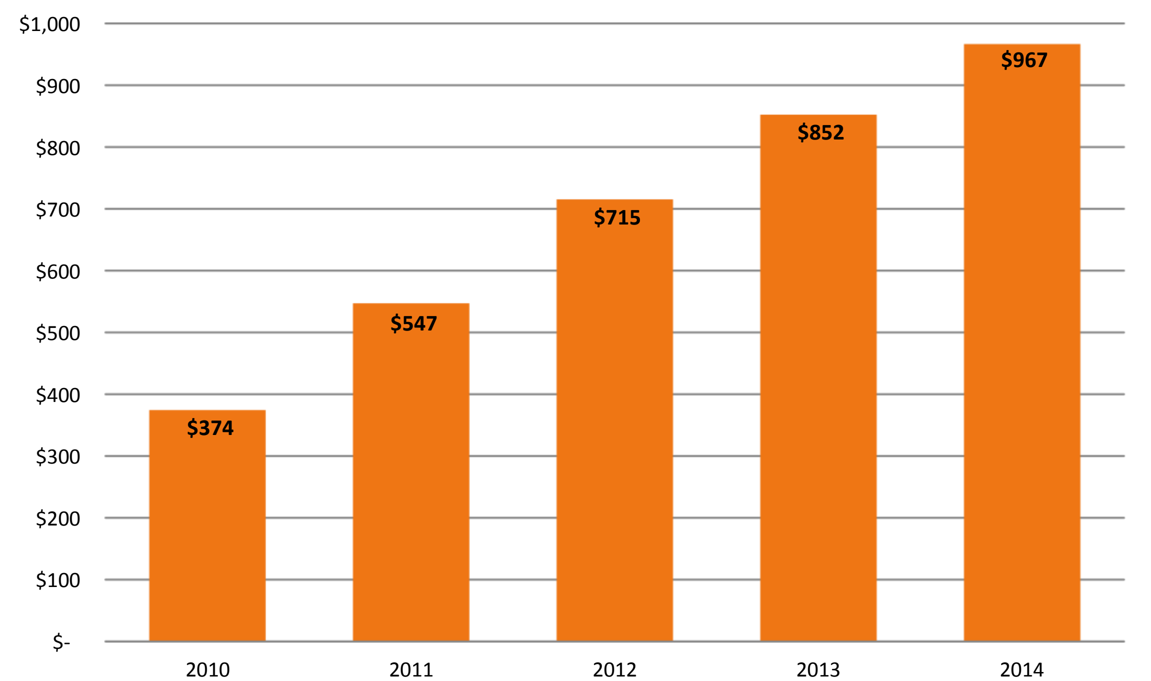
($981.2 Billion)



Liabilities as of September 30, 2014 and 2013 *(Dollars in Millions)*	**2014**	**2013**
Accounts Payable	$ 4,001	$ 4,129
Debt	966,671	852,432
Guaranty Agency Federal Funds Due to Treasury	1,471	1,482
Accrued Grant Liability	2,487	2,170
Other Liabilities	6,590	9,002
Total Liabilities	$ 981,220	$ 869,215

The Department borrows from Treasury to fund the disbursement of new loans and the payment of credit program outlays. The majority of the increase in Debt is due to the borrowing used to fund the Direct Loan Program. During FY 2014, Debt increased 13 percent from $852 billion in the prior year to $967 billion. The new financing was used to disburse new loans and make negative subsidy transfers to the Treasury's General Fund.

Debt
for Fiscal Years 2010–2014
(Dollars in Billions)

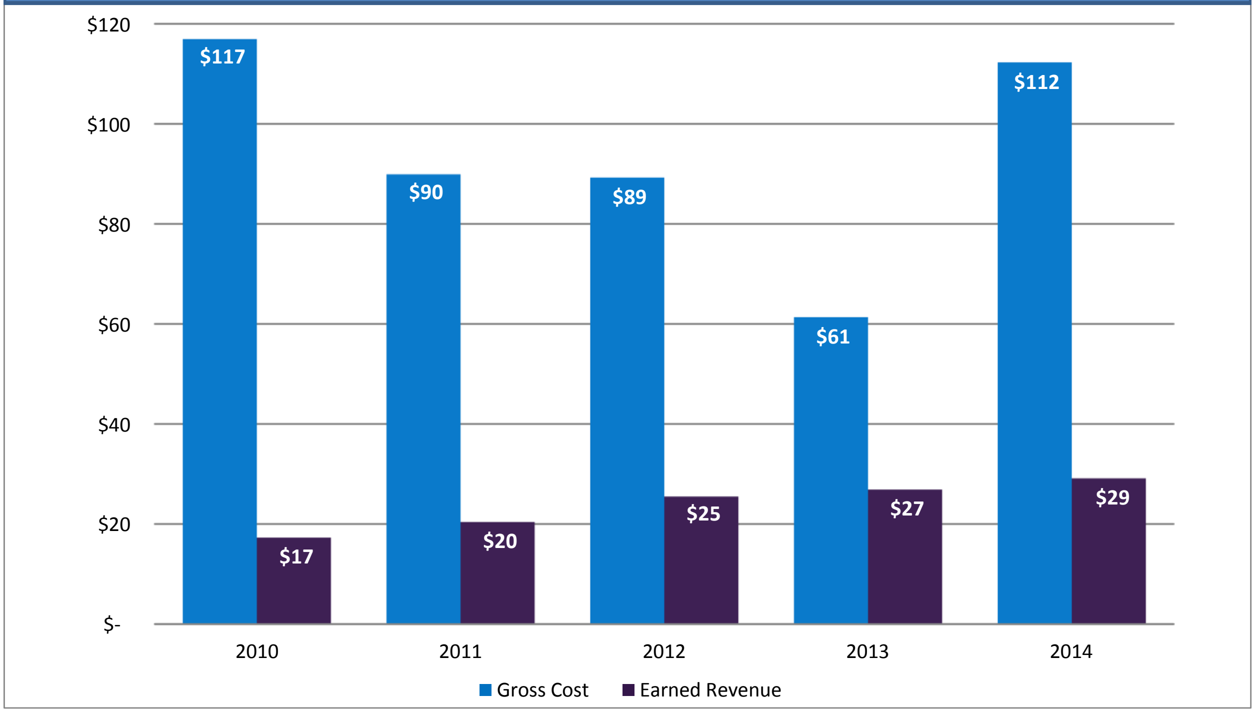


Statement of Net Cost

The Consolidated Statement of Net Cost reports the Department's components of the net costs of operations for a particular period of time (for a fiscal year). The Department's net cost of operations consists of the gross cost incurred less any exchange (i.e., earned) revenue from activities.

Net Cost of Operations totaled $83.2 billion for the year ended September 30, 2014, a $48.7 billion or 141 percent increase compared to the prior year of $34.5 billion. This increase is primarily due to an upward subsidy re-estimate of $30.2 billion for the Direct Loan Program. The primary drivers of the upward subsidy re-estimate are changes in the type and availability of repayment plans and increases in default rates.

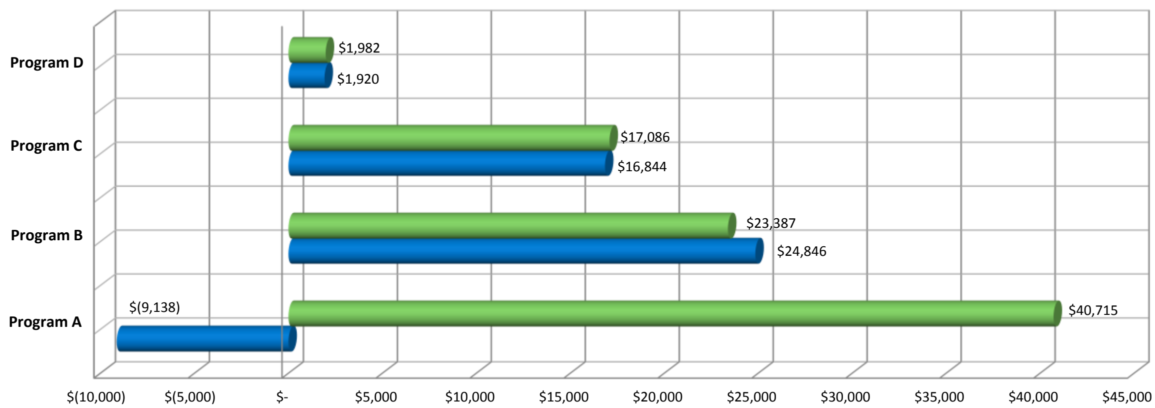
Gross Cost & Earned Revenue for Fiscal Years 2010–2014
(Dollars in Billions)



The Department's gross cost is composed of the cost of credit programs, grant programs, and operating costs. The cost of credit programs, also called subsidy, is derived using economic models that project cash inflows (net of outflows) on a net present value basis. These estimated cash flows are amortized, or spread out, over 30 years and are re-valued each year based on current economic conditions. In practical terms, a negative subsidy occurs when the interest rate and/or fees charged to the borrower are more than sufficient to cover the costs of the risk of default. Costs are tracked through "cohort" accounting, segregating loans into annual cohorts and tracking cost over the life of the loans. A cohort is a grouping of direct loans obligated or loan guarantees committed by a program in the same year even if disbursements occur in subsequent years. Factors such as interest rates charged to the borrower, interest rate on Treasury debt, default rates, fees, the re-estimate of prior subsidy cost, and other costs impact this calculation and help determine whether the result is positive or negative subsidy. In recent history, the Department's credit programs have had negative subsidy as a result of lending interest rates being greater than the rates at which the Department borrows from Treasury.

The following table presents a breakdown of net cost by program area for FY 2014 and FY 2013.

Net Cost By Program FY 2014 & FY 2013
(Dollars in Millions)



	Program A: Increase College Access, Quality, and Completion	Program B: Improve Preparation for College and Career from Birth Through 12th Grade, Especially for Children with High Needs	Program C: Ensure Effective Educational Opportunities for All Students	Program D: Enhance the Education System's Ability to Continuously Improve
2014	$40,715	$23,387	$17,086	$1,982
2013	$(9,138)	$24,846	$16,844	$1,920

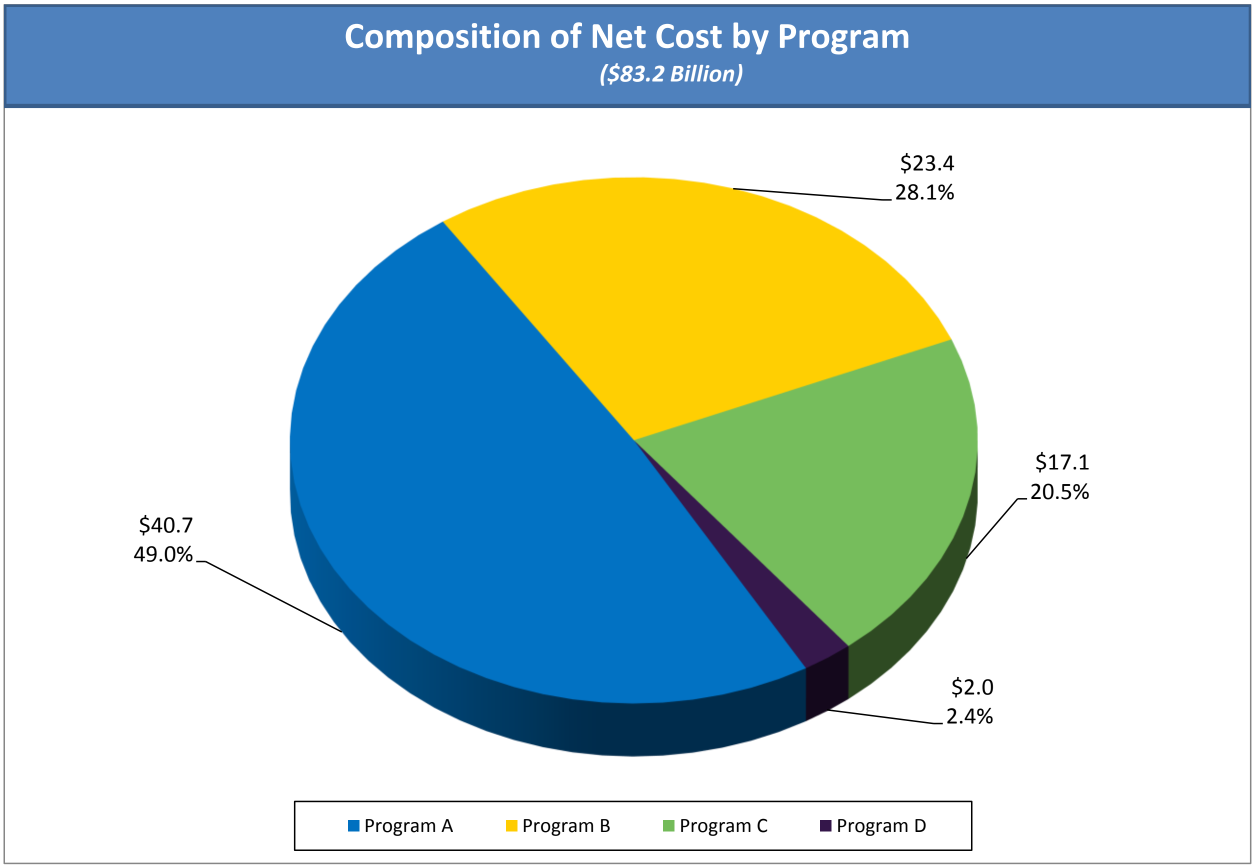
As required by the *GPRA Modernization Act of 2010*, each of the Department's reporting groups and major program offices have been aligned with the strategic goals presented in the Department's *FY 2014–2018 Strategic Plan*.

The Department has more than 100 grant and loan programs (http://www2.ed.gov/programs/gtep/gtep.pdf). In the Statement of Net Cost, they have been mapped to the Strategic Goals. The three largest grant programs are Title I, Pell, and the *Individuals with Disabilities Education Act* (IDEA) grants. Each of these programs' FY 2014 appropriations exceeded $11 billion. In addition to student loans and grants, the Department offers other discretionary grants under a variety of authorizing legislation, awarded using a competitive process, and formula grants, using formulas determined by Congress with no application process. Among the largest K-12 discretionary grants are RTT and the Teacher Incentive Fund. Among the largest formula grants are Title I Grants to LEAs (Title I, *Elementary and Secondary Education Act of 1965*, as amended) and IDEA grants.

As of FY 2014, disclosure of the *American Recovery and Reinvestment Act of 2009* (ARRA) for FY 2013 has been reclassified to present ARRA funding under the specific program offices distributing the funding.

Net Cost Program	Program Office	Strategic Goal
Program A: Increase College Access, Quality, and Completion	Federal Student Aid Office of Postsecondary Education Office of Career, Technical, and Adult Education	**Goal 1: Postsecondary Education, Career and Technical Education, and Adult Education**. Increase college access, affordability, quality, and completion by improving postsecondary education and lifelong learning opportunities for youths and adults.
Program B: Improve Preparation for College and Career from Birth Through 12th Grade, Especially for Children with High Needs	Office of Elementary and Secondary Education Hurricane Education Recovery	**Goal 2: Elementary and Secondary Education.** Improve the elementary and secondary education system's ability to consistently deliver excellent instruction aligned with rigorous academic standards while providing effective support services to close achievement and opportunity gaps, and ensure all students graduate high school college- and career-ready. **Goal 3: Early Learning.** Improve the health, social-emotional, and cognitive outcomes for all children from birth through 3rd grade, so that all children, particularly those with high needs, are on track for graduating from high school college- and career-ready.
Program C: Ensure Effective Educational Opportunities for All Students	Office of English Language Acquisition Office for Civil Rights Office of Special Education and Rehabilitative Services	**Goal 4: Equity.** Increase educational opportunities for underserved students and reduce discrimination so that all students are well-positioned to succeed.
Program D: Enhance the Education System's Ability to Continuously Improve	Institute of Education Sciences Office of Innovation and Improvement	**Goal 5: Continuous Improvement of the U.S. Education System.** Enhance the education system's ability to continuously improve through better and more widespread use of data, research and evaluation, evidence, transparency, innovation, and technology.

As further described in the Performance section of the MD&A, *Strategic Plan* Goals 1–5 are sharply defined directives that guide the Department's program offices to carry out the vision and programmatic mission; the net cost programs can be specifically associated with these five Strategic Goals. The Department also has a cross-cutting *Strategic Plan* Goal 6, U.S. Department of Education Capacity, which focuses on improving the organizational capacities of the Department to implement the *Strategic Plan*. As a result, the Department does not assign specific programs to *Strategic Plan* Goal 6 for presentation in the Statement of Net Cost.



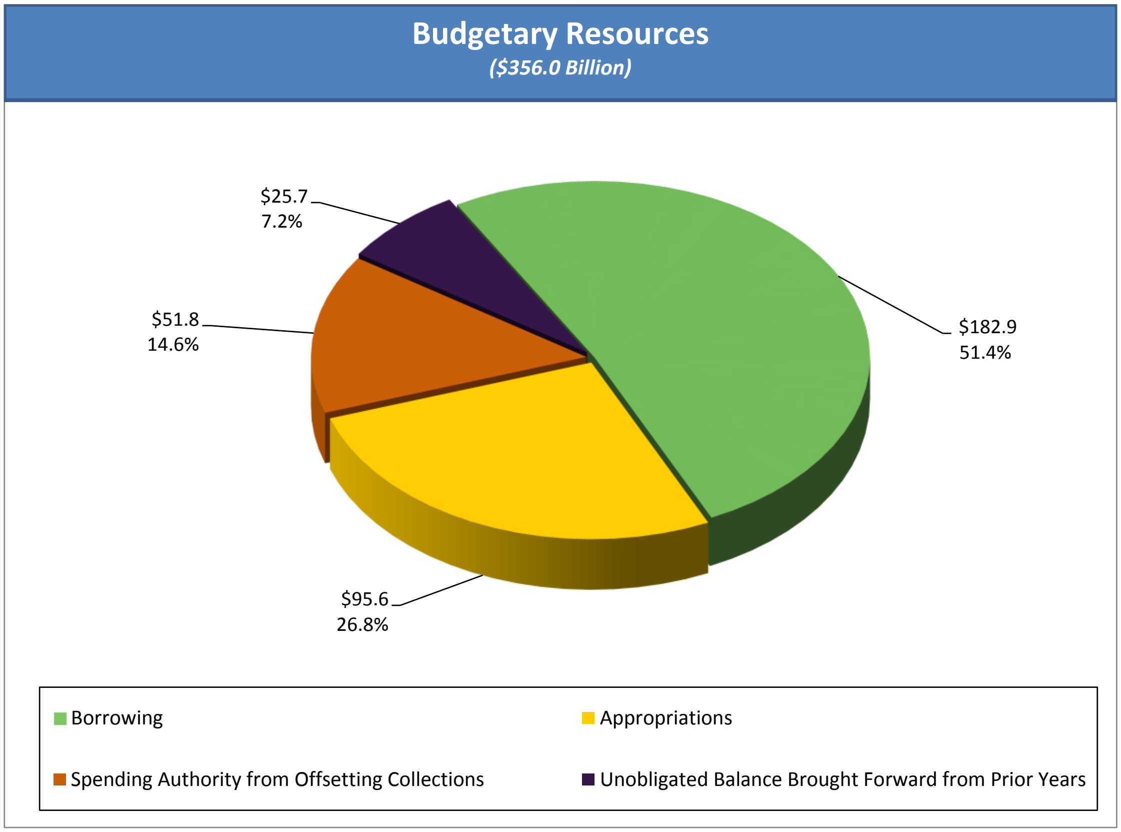
Statement of Changes in Net Position

The Consolidated Statement of Changes in Net Position reports the beginning net position, the summary effect of transactions that affect net position, presented for a particular period of time (for a fiscal year), and the ending net position. Net position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations include undelivered orders and unobligated balances for grant and administrative operations. Cumulative results of operations represent the net difference since inception between (1) expenses and (2) revenues and financing sources. Net Position of the Department totaled $42.7 billion for the year ended September 30, 2014. This reflects a 37 percent decrease over the net position of $67.8 billion from the prior fiscal year.

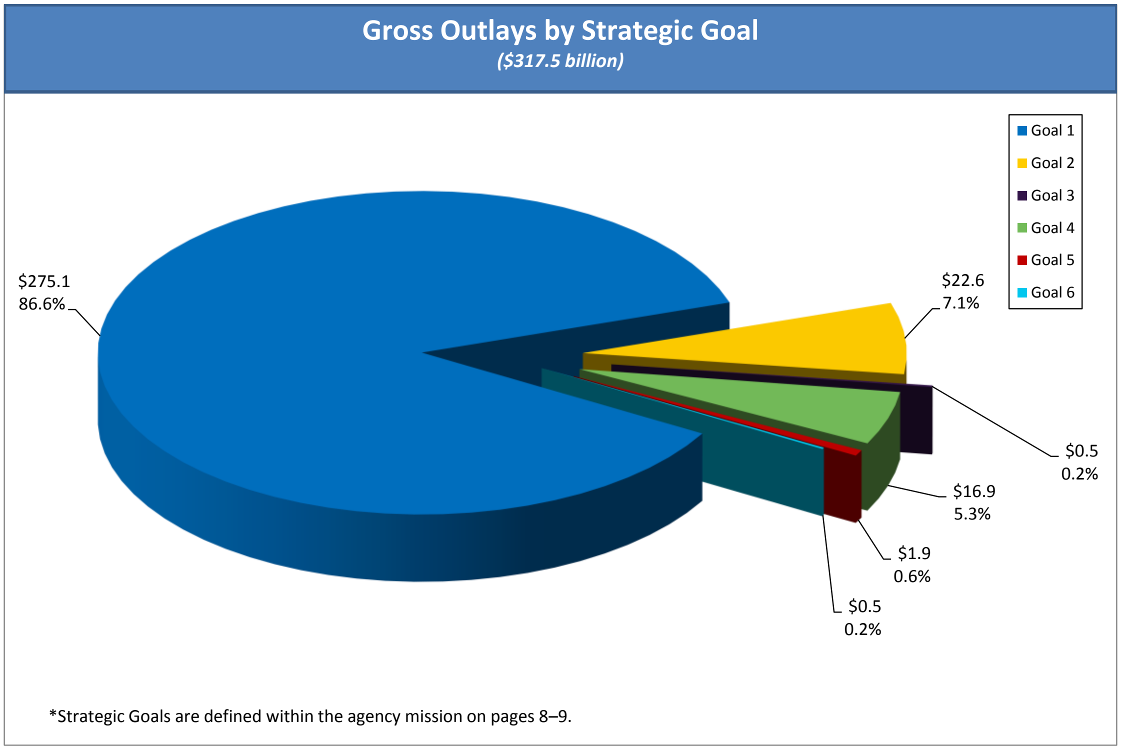
Statement of Budgetary Resources

The Combined Statement of Budgetary Resources presents information on how budgetary resources were made available and their status at the end of the fiscal year. Information in this statement is reported on the budgetary basis of accounting as prescribed by OMB and Treasury.

The Department's Budgetary Resources totaled $356.0 billion for the year ended September 30, 2014, decreasing from $359.9 billion, or approximately 1 percent from the prior year. Budgetary resources are comprised of appropriated budgetary resources of $112.4 billion and nonbudgetary credit reform resources of $243.6 billion. The nonbudgetary credit reform resources are predominantly borrowing authority for the loan programs.



Gross outlays of the Department totaled $317.5 billion for the year ended September 30, 2014, and consisted of appropriated budgetary resources of $99.9 billion and nonbudgetary credit program funding of $217.6 billion.



Gross Outlays are primarily comprised of credit program loan disbursements and claim payments, and credit program subsidy interest payments to Treasury. Additional information on the Department's sources of funds and spending is shown in the Schedule of Spending on page 137. This schedule includes sections titled, "What Money Is Available to Spend," "How Was the Money Spent," and "Who Did the Money Go To."

Limitations of the Financial Statements

Management has prepared the accompanying financial statements to report the financial position and operational results for the U.S. Department of Education for FY 2014 and FY 2013, pursuant to the requirements of Title 31 of the United States Code, section 3515(b).

While these statements have been prepared from the books and records of the Department in accordance with generally accepted accounting principles for federal entities and the formats prescribed by OMB, these statements are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records.

The statements should be read with the realization that they are a component of the U.S. Government, a sovereign entity. The implications of this are that the liabilities presented herein cannot be liquidated without the enactment of appropriations, and that ongoing operations are subject to the enactment of future appropriations.

Analysis of Controls, Systems, and Legal Compliance

The Department is the smallest of 15 cabinet-level agencies in terms of government staff, yet it manages the largest direct loan portfolio in the federal government and has the third largest grant portfolio among the 26 federal grant-making organizations. As such, the Department relies heavily on its internal controls and system frameworks to provide appropriate stewardship over funds entrusted to it by the American people.

This section provides management assurances regarding compliance with the *Federal Managers' Financial Integrity Act of 1982* (P.L. 97-255) (FMFIA) and Office of Management and Budget (OMB) revisions to Circular A-123, *Management's Responsibility for Internal Control*. It also provides an analysis of the Department's controls, systems, and legal compliance. In future years, the Department will assess compliance in accordance with GAO's recently updated *Standards for Internal Control in the Federal Government* (Green Book).

Controls Framework and Analysis

The FMFIA requires agencies to establish internal controls which provide reasonable assurance the following objectives are achieved:

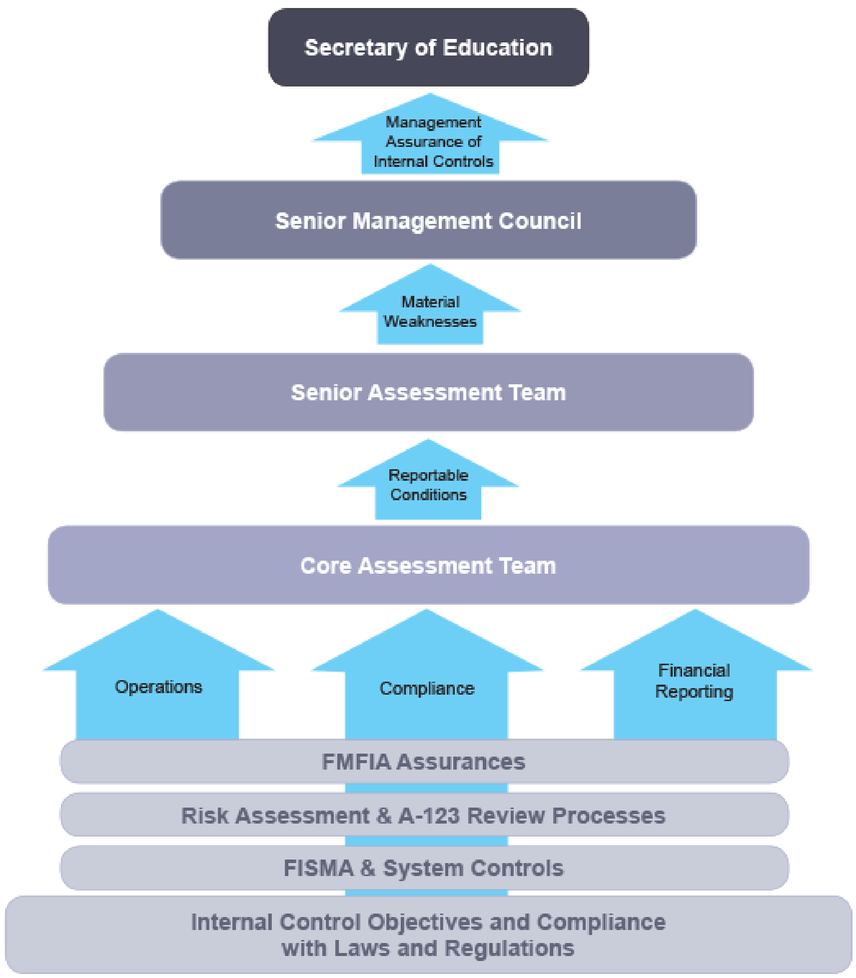
- effectiveness and efficiency of operations,
- compliance with applicable laws and regulations, and
- reliability of financial reporting.

OMB Circular A-123 implements the FMFIA and defines management's responsibility for internal control in federal agencies. Appendix A is intended to assist federal managers with implementing a process for assessing the effectiveness of the entity's internal control over financial reporting. Appendix B prescribes policies and procedures to agencies regarding how to maintain internal controls that reduce the risk of fraud, waste, and error in government charge card programs. Appendix C acknowledges payment accuracy as a high-risk area and describes the requirements for effective measurement and remediation of improper payments. Appendix D defines new requirements for financial management systems in compliance with the *Federal Financial Management Improvement Act of 1996* (FFMIA).

The Department's internal control framework is robust. Consistent with Circular A-123, the Department established a Senior Management Council (SMC) comprised of senior leaders from across the Department to oversee the internal control framework. This oversight role includes identifying focus areas, determining when internal control deficiencies are significant, setting expectations for their correction, and monitoring the implementation of corrective actions. The Department also established a Senior Assessment Team (SAT) and Core Assessment Team (CAT) to help guide the internal control process.

Each principal office within the Department implements internal controls to achieve programmatic goals, which include internal controls over operations, financial reporting, and information technology systems. The internal control implementation begins with risk assessments of the Department's business processes and functional units. The SAT considers the potential impact of risks using a multidimensional framework comprised of numerous risk factors. The SAT then recommends processes and systems with high risk factors for more frequent and rigorous internal control evaluations. Through the evaluations, Department offices document key controls, evaluate and test the design and effectiveness of controls, and communicate results to the SAT. Each office must develop and implement corrective action plans for reported deficiencies. The CAT provides technical guidance throughout the process.

Federal Student Aid (FSA) maintains a parallel governance structure which is integrated within the Department's governance structure. FSA's Chief Operating Officer chairs FSA's SMC and participates as a member of the Department's SMC. FSA's Chief Financial Officer chairs FSA's SAT and participates as a member of the Department's SAT. The chair of FSA's CAT participates as a member of the Department's CAT. Additional information on FSA's internal control framework, assessment of controls, and related assurances can be found in the Analysis of Systems, Controls, and Legal Compliance section of the *FY 2014 Federal Student Aid Annual Report*.



The Secretary designated the Chief Financial Officer (CFO) as the Senior Internal Control Official for the Department. In this role, the office of the CFO develops and issues policies, procedures, and reporting requirements; develops and provides training and technical assistance; coordinates with the SMC, SAT, and CAT; leads selected internal control reviews; and develops and maintains internal control and audit follow-up systems.

Controls over Operations

The Department's two primary areas of operation are the administration of grants and loans. Other significant business activities include the management of contracts and interagency agreements, human capital, facilities, and legal enforcement activities. To ensure the efficient and effective implementation of these and other operations, including compliance with applicable laws and regulations, the Department issued a directive, establishing in policy that all managers are responsible for ensuring the development, maintenance, documentation, evaluation, and improvement of internal control for the programs and administrative functions for which they are responsible.

Each principal office assesses the design and operation of applicable key controls in their respective areas of responsibility and prepares an annual FMFIA assurance which highlights internal control processes, and reports identified material weaknesses and significant deficiencies. These management assurances, along with the results of internal control reviews and external audits, serve as the basis for the Secretary's assurance statement provided later in this section of the report.

In FY 2014, the Department identified no material weaknesses in internal controls over the effectiveness and efficiency of operations. The Department, however, continues to address significant deficiencies (reportable conditions) in the administration of grants, loans, and other program operations. These are consistent with OIG's report, FY 2015 Management Challenges. The Department is committed to continuous improvement, making corrections in accordance with OIG findings. A summary of the OIG report is provided in the Other Information section.

Controls over Financial Reporting

Internal Control over Financial Reporting (ICOFR) is a subset of FMFIA, section 2. The Department's assessment of the effectiveness of internal control over financial reporting is performed in accordance with Office of Management and Budget (OMB) circular A-123 Appendix A (A-123A). Additionally, the Department leverages the A-123A Implementation Guidance, which describes the process for assessing internal control over financial reporting and requires each agency to provide an annual statement of assurance on the effectiveness of internal control over financial reporting as part of its overall FMFIA assurance statement.

Planning is a critical step in our assessment of the effectiveness of internal control over financial reporting. Key decisions that drive the assessment are made during the planning phase. Management decides on the materiality threshold, risk factors, the scope of the assessments (e.g., which financial processes to review), and the test approach/methodology, as well as other key decisions. Based on this assessment, management identifies specific areas to test. For any deficiency identified during testing, OCFO staff work with process owners to facilitate the development, approval, and implementation of Corrective Action Plans (CAPs). The Department also considers the status of ongoing corrective actions and results of the financial statement audit.

In FY 2014, OCFO strengthened its framework for internal control over financial reporting by creating end-to-end process documentation for eight (8) significant business processes and 32 subprocesses that support the Department's financial statements. OCFO also catalogued controls within these processes.

Beginning in FY 2014, the Department strengthened its influence over key system controls that impact financial management operations by making OCFO the new segment owner of the

Department's Financial Management Line of Business (FMLoB). This change in ownership from the Office of the Chief Information Officer to the OCFO was intended to help guide the FM modernization strategy towards one that not only maintains tightly integrated Department-owned systems, but also seeks to make prudent investments that will yield efficient and effective financial management business processes, maximize shared services opportunities, maintain strong internal controls within the systems, ensure compliance with pertinent laws and regulations, and improve the reporting and analytic capabilities available to the FM workforce. In addition, FMLoB investments will support the FM mission of the Department, which is to provide objective financial data and performance information to its stakeholders, promote sound financial management, support data-driven decision-making, and enhance financial reporting and compliance activities.

The goals of the FMLoB Modernization Plan are:

- sustain and/or modernize Financial Management segment's integrated hardware, software, and system support,
- optimize utilization of Treasury solutions and shared services where feasible,
- ensure that IT investments support effective and efficient Financial Management business processes,
- build analytic capacity to support data-driven decision-making and enhance financial reporting and compliance activities,
- pay the Department's fair share of government-wide cost, and
- maximize interoperability between Financial Management Segment and other Department Segments.

In FY 2014, the Department identified no material weaknesses in internal controls over financial reporting.

Controls over Systems

Internal controls over systems support all three internal control objectives: operations, compliance, and financial reporting. In particular, system controls have a significant impact on financial reporting and have been the Department's and FSA's primary area of focus for addressing deficiencies in internal control.

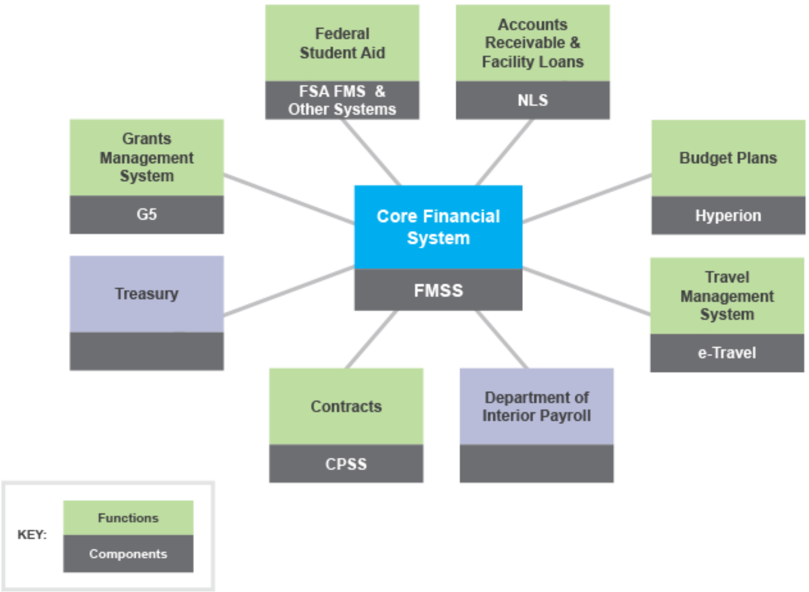
The Department has garnered significant benefits from previous years' audits and expects that implementation of the recommendations presented in FY 2014 will further improve the information security program by strengthening the associated management, technical, and operational security controls.

Among the guidance applied by the Department in assessing controls over systems during FY 2014 were FMFIA (section 4) and Appendix D of OMB A-123. We also assessed the Department's automated systems for compliance with key provisions of the *Federal Financial Management Improvement Act of 1996.*

The Department's core financial applications have been brought together under the umbrella of the Education Central Automated Processing System (EDCAPS). EDCAPS is a suite of financial applications (including commercial off-the-shelf and custom code and interfaces) that encompass the Department's core financial management processes.

The Department's financial management systems are designed to support effective internal controls and to produce accurate, reliable, and timely financial information. The current systems portfolio is depicted in the image below:

Department Systems Portfolio



The components of EDCAPS are linked through custom interfaces to provide the Department with real-time financial management capabilities. EDCAPS serves approximately 4,200 departmental users in Washington, DC, as well as 10 regional offices throughout the United States. EDCAPS also serves approximately 100,000 external users.

Components of EDCAPS

Financial Management Support System (FMSS)—The FMSS is the Department's core financial system. It provides financial management functions for the Department, including general ledger, financial statement production, funds control and budget reporting, cost accounting, and accounts receivable/administrative accounts payable functions.

Contracts and Purchasing Support System (CPSS)—The CPSS provides users with a central repository to enter, retrieve, manage, and view acquisition/contract-related data. The centralized data provides enhanced information dissemination with the ability to respond to internal and external information requests. Various other systems and processes are used to augment and supplement the business process management gaps in the current environment.

Grants Management System (G5)—G5 manages all grant activities from initial recipient contact, through grant processing, to payments and grant closeout. This single system approach provides improved grant information management, recipient response time, and accuracy of financial management information.

Travel Management System (TMS)—The Department participates in e-Travel. Under e-Travel, travel system functionality is provided under contract by E2 solutions. EDCAPS interfaces with E2 in accordance with an established memorandum of understanding.

Hyperion Budget Planning—Hyperion Budget Planning is used by the Department for preparing annual spending plans. The Plan versus Actuals Report is generated from this system.

EDCAPS also interfaces with the Department of Interior for payroll data, the Department of Treasury for payment data, and the Nortridge Loan System (NLS) for promissory note data.

2014 Internal Control Results

In FY 2014, system-level general controls tests were performed on all financially significant systems similar to those performed in FY 2013.

The Department is keenly aware of the importance of strong internal controls and adequate security controls over system access and data and continuously seeks to strengthen these controls. The Department's System Security Plan (SSP) identifies management, operational, and technical security controls for EDCAPS. The SSP is based upon a review of the environment, documentation, and interviews with information system personnel. While the Department has not eliminated all risks, management reviews confirm that all favorable actions are taken to diminish deficiencies and strengthen internal control overall. Risks are routinely monitored and contingency and mitigation plans are maintained.

EDCAPS is a moderate-impact application per Federal Information Processing Standards (FIPS) 199, and is subject to the moderate-impact baseline required by National Institute of Standards and Technology (NIST) Special Publication (SP) 800 53 Rev 4. Therefore, EDCAPS uses the moderate-impact baseline as its minimum security control requirements.

All internal EDCAPS user accounts are established using an EDCAPS Access Request Form. This form is used to grant initial access to EDCAPS subsystems and must be validated by the user's supervisor and the appropriate Information System Security Officer. Access is based on the user's role or job title. Principles of least privilege and segregation of incompatible duties are applied at all times. Access to all EDCAPS applications is protected by a user ID and password. Each application has a security administrator who is responsible for vetting individual EDCAPS access forms and for establishing their accounts. Access is granted based on the "need to know" and the least privilege the user requires performing his or her duties.

EDCAPS has been designed to deliver efficient and effective operations, while complying with FFMIA. Management considered available information from annual audit reports and other relevant, appropriate information to determine whether the Department's financial systems comply with system controls. The Department's determination leverages the results of related annual reviews. The Department is committed to continually improving all controls and acknowledges the ongoing efforts of security management to strengthen financial management systems.

Based on self-assessments and results of external audits in FY 2014, the Department has concluded that there are no material weaknesses in control over systems. However, self-assessments and external audits continue to identify control deficiencies in the areas of security management, personnel security, access controls, and configuration management across these systems. That is consistent with the management challenges OIG identified for IT security as well as system development and implementation.

Management Assurances

Based on internal control monitoring and the individual assurances provided by Principal Operating Components, the Department is able to provide reasonable assurance that the internal controls and financial management systems in effect during FY 2014 met the objectives of both sections 2 and 4 of the FMFIA.

- FMFIA section 2 explains management's responsibility for, and its role in, assessment of all internal controls, including controls over operations, compliance, and financial reporting.
- FMFIA section 4 relates to the Department's analysis of systems, controls, and legal compliance related to financial reporting, and internal controls and system frameworks, including FMFIA, FFMIA, and the *Federal Information Security Management Act* (FISMA), as well as OMB Circular A-123, including Appendix D, as addressed in previous sections of this report.

Statement of Assurance

The Department of Education's management is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the *Federal Managers' Financial Integrity Act of 1982* (FMFIA) and OMB Circular A-123, *Management's Responsibility for Internal Control*. The Department evaluated its internal controls to support (1) effective and efficient programmatic operations, (2) compliance with applicable laws and regulations, and (3) reliable financial reporting.

Internal Control Over Operations

For all program areas, the Department provides reasonable assurance that internal controls were in place and operating to meet the objectives of section 2 of FMFIA, no material weaknesses were identified, and we were in compliance with applicable laws and regulations as of September 30, 2014, with the exception noted in the Legal Compliance section below.

Internal Control Over Financial Reporting

The Department conducted its assessment of the effectiveness of internal controls over financial reporting, which includes safeguarding of assets and compliance with applicable laws and regulations, in accordance with the requirements of Appendix A of OMB Circular A-123. The Department has reasonable assurance that internal controls over financial reporting as of September 30, 2014, were operating effectively and there were no material weaknesses in the design or operation of the controls.

Internal Control Over Systems

The Department is required to implement and maintain financial management systems that substantially comply with federal financial management systems requirements, federal accounting standards, and the United States Government Standard General Ledger at the transaction level. Based on the results of the Department's assessment in accordance with the requirements of section 4 of FMFIA, the Department's financial management systems substantially comply with the *Federal Financial Management Improvement Act* as of September 30, 2014.

Notwithstanding the aforementioned assertions, I acknowledge that we have internal control- and compliance-related issues, such as those identified by our auditors and the management challenges raised by the Office of Inspector General in other sections of this report. We are committed to resolving them.

Arne Duncan
November 14, 2014

Financial Management Systems Strategy

The *Federal Information Security Management Act of 2002* (FISMA) requires federal agencies to implement a mandatory set of processes and system controls designed to ensure the privacy, confidentiality, integrity, availability, and security of system-related information. The Department has been implementing a multiyear process to improve its reporting activities, as described in the Controls over Systems section.

The Department has designated the FMSS as a mission-critical system that provides core financial management services. The Department expects to improve the following performance outcomes: control and accountability over financial management services, including financial management system controls and practices that include cross-validation rules to prevent erroneous accounting transactions from being processed; and financial system reporting capabilities that continue to respond quickly to internal and external financial information inquiries. Additional areas of emphasis are the continued tight integration and streamlining with the office of Federal Student Aid and business processes; reduced manual reconciliation efforts for the Office of the Chief Financial Officer; reduction of errors and improved funds control; better data sharing and centralized data edits and controls that could otherwise get out of synchronization between the FMSS and its feeder systems; and budget planning that integrates with the general ledger.

Currently, the FMSS resides on an Oracle database and uses the Oracle Federal Financial Software Version 11.5.10 (11i). Oracle has issued version Release 12 of its software as a replacement for the 11i version. Release 12 has passed the necessary testing and is federally compliant for financial management. The Department is examining solutions for migrating to the Release 12 version. The Office of Management and Budget (OMB) has directed agencies to explore the possibility of utilizing a federal shared service provider (FSSP) for financial management before implementing or migrating to new versions of financial applications. During FY 2015, the Department expects to explore potential options pertaining to using an FSSP solution for core financial management services.

Legal Compliance

Compliance with applicable laws and regulations is an integral component of the Department's internal control program. This section is a partial list of those applicable laws for which the Department's internal controls ensure compliance, with the exceptions noted below.

***Federal Financial Management Improvement Act* (FFMIA)—**requires that agency financial management systems comply with federal financial management systems requirements, applicable federal accounting standards and the U.S. Standard General Ledger (USSGL) at the transaction level in order to provide uniform, reliable, and more useful financial information. Agencies are required to assess and report on whether these systems comply with FFMIA on an annual basis.

The results of tests of FFMIA section 803(a) requirements disclosed no instances in which the Department's financial management systems did not substantially comply with (1) federal financial management systems requirements, (2) applicable federal accounting standards, or (3) the USSGL at the transaction level.

The Improper Payments Information Act of 2002, as amended by the Improper Payments Elimination and Recovery Act of 2010 (IPERA) and the Improper Payments Elimination and Recovery Improvement Act of 2012 **(IPERIA)—**requires agencies to annually report information on improper payments to the President and Congress, focusing on risk assessments, statistical sampling, and corrective actions. The statute requires OMB to provide guidance to agencies on reimbursement of costs between agencies, retention and timely destruction of records, and prohibiting the duplication and disclosure of records, including creation and maintenance of a Do Not Pay list to facilitate federal agencies' review of payment or award eligibility for purposes of identifying and preventing improper payments.

Federal Information Security Management Act of 2002 **(FISMA)—**requires federal agencies to implement a mandatory set of processes and system controls designed to ensure the confidentiality, integrity, and availability of system-related information.

***Prompt Payment Act of 1982*—**requires federal agencies to make timely payments to vendors. When a payment is not processed within the timeframes specified in the act, payment of interest is required.

***Anti-Deficiency Act of 1870 (with amendments in 1982)*—**prohibits federal agencies from obligating or expending federal funds in advance or in excess of an appropriation, apportionment, or certain administrative subdivisions of those funds. The act also prohibits agencies from accepting voluntary services.

***Debt Collection Improvement Act of 1996*—**enacted into law as part of the *Omnibus Consolidated Rescissions and Appropriations Act of 1996.* The primary purpose of the *Debt Collection Improvement Act* (DCIA) is to increase the collection of nontax debts owed to the federal government.

> The *Digital Accountability and Transparency Act* (DATA Act), Public Law 113-101, enacted on May 9, 2014, amended the DCIA to require referral of delinquent debt to the Department of Treasury's Offset Program within 120 days. The Department is in communication with Treasury regarding implementation of the DCIA, and is working to determine the best course of action, including, as needed, modifications to existing regulations and/or systems and processes, to fully comply with the DCIA. This determination of noncompliance with this provision of the DCIA does not represent a material weakness in the Department's internal controls.

***Federal Credit Reform Act of 1990*—**enacted to provide a more realistic picture of the cost of U.S. government direct loans and loan guarantees. The purposes of Title V of the act are to measure more accurately the costs of federal credit programs; place the cost of credit programs on a budgetary basis equivalent to other federal spending; encourage the delivery of benefits in the form most appropriate to the needs of beneficiaries; and improve the allocation of resources among credit programs and between credit and other spending programs (See Notes 1 and 6 in the Financial Section).

***The Cash Management Improvement Act of 1990*—**The purpose of this law is to improve the transfer of federal funds between the federal government, the states, territories, and the District of Columbia. The law focuses on two recurrent intergovernmental issues: states drawing federal funds in advance of need; and the federal government providing late grant awards to states.

***Single Audit Act of 1984*—**The *Single Audit Act of 1984* (with amendment in 1996) and OMB Circular A-133 ("Audits of State, Local Governments, and Non-Profit Organizations") provide audit requirements for ensuring that grant funds to state, local, and tribal governments, colleges, universities and other nonprofit organizations (nonfederal entities) are expended properly.

Government Performance and Results Act of 1993 as amended by the GPRA Modernization Act of 2010—The GPRA of 1993 established strategic planning, performance planning, and reporting as a framework for agencies to communicate progress in achieving their missions. The *GPRA Modernization Act of 2010* established important changes to these existing requirements.

The foundations of GPRA are: (1) agencies are required to develop five-year strategic plans that must contain a mission statement as well as long-term, results-oriented goals covering each of its major functions; (2) agencies are required to prepare annual performance plans that establish the performance goals for the applicable fiscal year, a brief description of how these goals are to be met, and a description how these performance goals can be verified; and (3) agencies must prepare annual performance reports that review the agency's success or failure in meeting its targeted performance goals.

Elementary and Secondary Education Act—The current reauthorization of ESEA is the *No Child Left Behind Act* of 2001. It emphasizes equal access to education, sets high standards for academic performance, and demands a rigorous level of accountability from schools and districts. ESEA authorizes an important group of education programs administered by the states. These programs support eligible schools and districts eager to raise the academic achievement of struggling learners, and address the complex challenges that arise among students who live with disability, mobility problems, learning difficulties, poverty, transience, and the need to learn a second language.

Higher Education Opportunity Act of 2008—intended to strengthen the educational resources of our colleges and universities and to provide financial assistance for students in postsecondary and higher education. It increased federal money given to universities, created scholarships, and gave low-interest loans for students.

Individuals with Disabilities Education Act of 2004—governs how states and public agencies provide early intervention, special education, and related services to children with disabilities.

General Education Provisions Act—provides general administrative requirements that govern the implementation of all Department grant programs.

Department of Education Organization Act—established the Department, defines its mission, and sets out key components of its organizational structure.

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Financial Section

Message From the Chief Financial Officer

Our FY 2014 *Agency Financial Report* (AFR) demonstrates the Department of Education's firm commitment to financial management excellence. In compiling the AFR this year, we made a concerted effort to provide information at a high level while providing web links for many details.

We made the Notes more reader-friendly and tried to build on our success in telling the financial story of the Department, for which we were recognized by the Association of Government Accountants in 2013 as the best in federal government.

FY 2014 was not easy. We overcame a multi-week government shutdown and tight operating budgets for the entire year, while still carrying out many complex programs. Despite these challenges, I am extremely pleased that we have attained our 13th consecutive unmodified or "clean" opinion. The consistency in our accounting and reporting is a tribute to the excellent work of our employees and contract partners.

The Department is the smallest of the 15 cabinet-level agencies in terms of government staff, with approximately 4,100 employees, yet we have large financial responsibilities whether the measure is assets, obligations, or outlays.

The balance sheet of the Department now exceeds $1 trillion. Our largest asset is a portfolio of student loans. Our employees and contractors collect principal and interest on the loans, provide services to students and schools, and implement ways to make it easier for borrowers to repay.

The second largest item on the balance sheet is grants to states, most of which go toward elementary and secondary education and get awarded on a legislated formula basis.

The third biggest item is student aid, which helps students and families pay for college through Pell Grants, Work Study, and other campus-based programs.

The Department also carries out competitive grant programs to promote innovation, performs research, collects education statistics, and enforces civil rights statutes.

Our annual spending is another way of looking at the financial picture. We made almost $200 billion in new obligations in FY 2014. This included approximately $100 billion in new student loans, $32 billion in Pell Grants for needy college students, $14.5 billion for Title I of the *Elementary and Secondary Education Act,* $11.5 billion for the Grants to States under the *Individuals with Disabilities Education Act, and* $2.5 billion for Improving Teacher Quality State Grants. With all those large activities and over 100 smaller programs, we still spent less than 1 percent of the annual obligations on administrative costs.

In addition to providing an unmodified opinion for FY 2014, our auditors reported that there were no material internal control weaknesses and no material instances of noncompliance with applicable laws and regulations. They did, however, note one item involving the *Debt Collection Improvement Act* as discussed in the Legal Compliance section of the MD&A.

We realize that our administrative processes and internal controls are never perfect. There are always areas in need of improvement, including those identified by our independent auditors in their report and by the Office of Inspector General in its assessment of our management challenges. We are working on these issues and on issues related to our internal self-assessments in areas such as grant monitoring, IT systems, and management of student loan repayments. We will use their suggestions and findings as guides as we strive for continuous improvement.

Thomas P. Skelly
Delegated to perform the functions and duties of the Chief Financial Officer
November 14, 2014

About the Financial Section

In FY 2014, the Department has expended significant time and energy to make the Financial Section more reader-friendly for a general audience. Because so many details in the Section are critical to understanding the report, we placed a high priority on cutting through jargon and repetitive statements, and used graphic examples to illustrate points of discussion. While we recognize each year that there is always room for improvement, we believe that this year's Financial Section represents our most user-friendly report to date. In addition, we have put in place a team-based continuous improvement process with reviews by our readers. As such, we welcome comments from readers to further improve the report and make it easier to use.

The Financial Section is the AFR's center core. It begins with a concise statement of the Department's financial condition and extends to the Notes to the Financial Statements, which provide specific detail, including calculations and assumptions in key areas, as defined in OMB Circular A-136. The section also presents the Report of the Independent Auditors as well as supplemental information on human capital and program outcomes.

In FY 2014, we revamped the Notes to make them more reader-friendly. We did so using a peer review process among teams of content experts within the Department, benchmarking against other agencies, and with a careful eye to plain language to attract a broader audience to material that is often viewed as the fine print, but is, in reality, the assumptions under which the Department operates.

Financial Statements

Financial statements included are: Consolidated Balance Sheet As of September 30, 2014 and 2013, Consolidated Statement of Net Cost For the Years Ended September 30, 2014 and 2013, Consolidated Statement of Changes in Net Position For the Years Ended September 30, 2014 and 2013, and Combined Statement of Budgetary Resources For the Years Ended September 30, 2014 and 2013.

Notes to the Financial Statements

Note 1. Summary of Significant Accounting Policies
Note 2. Non-Entity Assets
Note 3. Fund Balance with Treasury
Note 4. Accounts Receivable
Note 5. Cash and Other Monetary Assets
Note 6. Credit Programs for Higher Education: Credit Program Receivables, Net and Liabilities for Loan Guarantees
Note 7. Property and Equipment, Net and Leases
Note 8. Other Assets
Note 9. Accounts Payable
Note 10. Debt
Note 11. Other Liabilities
Note 12. Accrued Grant Liability
Note 13. Net Position
Note 14. Intragovernmental Cost and Exchange Revenue by Program
Note 15. Interest Expense and Interest Revenue
Note 16. Statement of Budgetary Resources

Note 17. Reconciliation of Net Cost of Operations to Budget
Note 18. Incidental Custodial Collections
Note 19. Contingencies

Required Supplementary Information

This section contains the Combining Statement of Budgetary Resources For the Years Ended September 30, 2014 and 2013.

Required Supplementary Stewardship Information

Stewardship Expenses summarize spending and stakeholder relationships with state and local educational agencies. Stewardship resources are substantial investments by the federal government for the long-term benefit of the nation. Because costs of stewardship resources are treated as expenses in the financial statements in the year the costs are incurred, they are reported as RSSI to highlight the benefit nature of the costs and to demonstrate accountability.

Boosting completion rates for bachelor's and associate degrees is essential for Americans to compete in a global economy. Education is the stepping stone to higher living standards for American citizens, and is vital to economic growth. Economic outcomes, such as wage and salary levels, have historically correlated with the educational attainment of individuals and the skills employers expect of those entering the labor force.

Report of the Independent Auditors

The results of the audit of the Department's financial statements for FY 2014 and FY 2013 to comply with the *Chief Financial Officers Act of 1990,* as amended, are presented to be read in conjunction with the Financial Section in its entirety. The Department's Office of Inspector General contracted with the independent certified public accounting firm of CliftonLarsonAllen, LLP to audit the financial statements of the Department as of September 30, 2014 and 2013, and for the years then ended.

United States Department of Education
Consolidated Balance Sheet
As of September 30, 2014 and 2013
(Dollars in Millions)

	FY 2014	FY 2013
Assets:		
Intragovernmental:		
Fund Balance with Treasury (Note 3)	$ 98,696	$ 108,732
Accounts Receivable (Note 4)	3	2
Other Intragovernmental Assets (Note 8)	55	22
Total Intragovernmental	98,754	108,756
Cash and Other Monetary Assets (Note 5)	1,471	1,482
Accounts Receivable, Net (Note 4)	136	121
Credit Program Receivables, Net (Note 6)	923,545	826,684
Property and Equipment, Net (Note 7)	7	2
Other Assets (Note 8)	13	13
Total Assets (Note 2)	**$ 1,023,926**	**$ 937,058**
Liabilities:		
Intragovernmental:		
Accounts Payable (Note 9)	$ 1	$ 2
Debt (Note 10)	966,671	852,432
Guaranty Agency Federal Funds Due to Treasury (Note 5)	1,471	1,482
Other Intragovernmental Liabilities (Note 11)	6,413	8,855
Total Intragovernmental	974,556	862,771
Accounts Payable (Note 9)	4,000	4,127
Accrued Grant Liability (Note 12)	2,487	2,170
Other Liabilities (Note 11)	177	147
Total Liabilities (Note 11)	**$ 981,220**	**$ 869,215**
Commitments and Contingencies (Note 19)		
Net Position:		
Unexpended Appropriations (Note 13)	$ 66,447	$ 71,371
Cumulative Results of Operations (Note 13)	(23,741)	(3,528)
Total Net Position (Note 13)	**$ 42,706**	**$ 67,843**
Total Liabilities and Net Position	**$ 1,023,926**	**$ 937,058**

The accompanying notes are an integral part of these statements.

United States Department of Education
Consolidated Statement of Net Cost
For the Years Ended September 30, 2014 and 2013
(Dollars in Millions)

	FY 2014	FY 2013
Program Costs:		
Increase College Access, Quality, and Completion		
Gross Costs	$ 69,746	$ 17,606
Earned Revenue	(29,031)	(26,744)
Net Program Costs	40,715	(9,138)
Improve Preparation for College and Career from Birth Through 12th Grade, Especially for Children with High Needs		
Gross Costs	$ 23,402	$ 24,871
Earned Revenue	(15)	(25)
Net Program Costs	23,387	24,846
Ensure Effective Educational Opportunities for All Students		
Gross Costs	$ 17,101	$ 16,870
Earned Revenue	(15)	(26)
Net Program Costs	17,086	16,844
Enhance the Education System's Ability to Continuously Improve		
Gross Costs	$ 2,046	$ 2,006
Earned Revenue	(64)	(86)
Net Program Costs	1,982	1,920
Net Cost of Operations (Notes 14 & 17)	**$ 83,170**	**$ 34,472**

The accompanying notes are an integral part of these statements.

United States Department of Education
Consolidated Statement of Changes in Net Position
For the Years Ended September 30, 2014 and 2013

(Dollars in Millions)

	FY 2014 Cumulative Results of Operations	FY 2014 Unexpended Appropriations	FY 2013 Cumulative Results of Operations	FY 2013 Unexpended Appropriations
Beginning Balances:				
Beginning Balances	**$ (3,528)**	**$ 71,371**	**$ (7,531)**	**$ 72,686**
Budgetary Financing Sources:				
Appropriations Received	$ -	$ 95,293	$ -	$ 90,993
Appropriations Transferred – In/Out	-	76	-	-
Other Adjustments (Rescissions, etc.)	-	(619)	-	(2,824)
Appropriations Used	99,674	(99,674)	89,484	(89,484)
Nonexchange Revenue	12	-	10	-
Donations and Forfeitures of Cash and Cash Equivalents	2	-	1	-
Other Financing Sources:				
Imputed Financing from Costs Absorbed by Others	$ 36	$ -	$ 34	$ -
Negative Subsidy Transfers, Downward Subsidy Re-Estimates, and Other	(36,767)	-	(51,054)	-
Total Financing Sources	**$ 62,957**	**$ (4,924)**	**$ 38,475**	**$ (1,315)**
Net Cost of Operations:	**$ (83,170)**	**$ -**	**$ (34,472)**	**$ -**
Net Change:	**$ (20,213)**	**$ (4,924)**	**$ 4,003**	**$ (1,315)**
Ending Balances (Note 13)	**$ (23,741)**	**$ 66,447**	**$ (3,528)**	**$ 71,371**

The accompanying notes are an integral part of these statements.

United States Department of Education
Combined Statement of Budgetary Resources
For the Years Ended September 30, 2014 and 2013

(Dollars in Millions)

	FY 2014 Budgetary	FY 2014 Non-Budgetary Credit Reform Financing Accounts	FY 2013 Budgetary	FY 2013 Non-Budgetary Credit Reform Financing Accounts
Budgetary Resources:				
Unobligated Balance, Brought Forward, October 1	$ 16,207	$ 11,315	$ 12,622	$ 18,993
Recoveries of Prior Year Unpaid Obligations	1,131	97,274	1,191	35,425
Other Changes in Unobligated Balance (+ or -)	(372)	(99,811)	(428)	(39,189)
Unobligated Balance from Prior Year Budget Authority, Net	$ 16,966	$ 8,778	$ 13,385	$ 15,229
Appropriations (Discretionary and Mandatory)	95,004	581	88,380	5
Borrowing Authority (Discretionary and Mandatory) (Note 16)	-	182,860	-	195,185
Spending Authority from Offsetting Collections (Discretionary and Mandatory)	473	51,347	779	46,976
Total Budgetary Resources (Note 16)	**$ 112,443**	**$ 243,566**	**$ 102,544**	**$ 257,395**
Status of Budgetary Resources:				
Obligations Incurred (Note 16)	$ 97,606	$ 233,457	$ 86,337	$ 246,080
Unobligated Balance, End of Year:				
Apportioned	12,125	69	13,700	-
Unapportioned	2,712	10,040	2,507	11,315
Total Unobligated Balance, End of Year	14,837	10,109	16,207	11,315
Total Status of Budgetary Resources (Note 16)	**$ 112,443**	**$ 243,566**	**$ 102,544**	**$ 257,395**
Change in Obligated Balance:				
Unpaid Obligations				
Unpaid Obligations, Brought Forward, October 1	$ 59,630	$ 161,747	$ 65,057	$ 172,230
Obligations Incurred	97,606	233,457	86,337	246,080
Outlays (Gross) (-)	(99,886)	(217,614)	(90,573)	(221,138)
Recoveries of Prior Year Unpaid Obligations (-)	(1,131)	(97,274)	(1,191)	(35,425)
Unpaid Obligations, End of Year	**$ 56,219**	**$ 80,316**	**$ 59,630**	**$ 161,747**
Uncollected Payments				
Uncollected Payments, Federal Sources, Brought Forward, October 1 (-)	$ (3)	$ (25)	$ (2)	$ (26)
Change in Uncollected Payments, Federal Sources (+ or -)	2	(1)	(1)	1
Uncollected Payments, Federal Sources, End of Year (-)	$ (1)	$ (26)	$ (3)	$ (25)
Memorandum (Non-add) Entries				
Obligated Balance, Start of Year (+ or -)	**$ 59,627**	**$ 161,722**	**$ 65,055**	**$ 172,204**
Obligated Balance, End of Year (+ or -)	**$ 56,218**	**$ 80,290**	**$ 59,627**	**$ 161,722**
Budget Authority and Outlays, Net:				
Budget Authority, Gross (Discretionary and Mandatory)	$ 95,477	$ 234,788	$ 89,159	$ 242,166
Actual Offsetting Collections (Discretionary and Mandatory) (-)	(624)	(97,463)	(935)	(72,672)
Change in Uncollected Customer Payments from Federal Sources (Discretionary and Mandatory) (+ or -)	2	(1)	(1)	1
Budget Authority, Net (Discretionary and Mandatory)	**$ 94,855**	**$ 137,324**	**$ 88,223**	**$ 169,495**
Outlays, Gross (Discretionary and Mandatory)	$ 99,886	$ 217,614	$ 90,573	$ 221,138
Actual Offsetting Collections (Discretionary and Mandatory) (-)	(624)	(97,463)	(935)	(72,672)
Outlays, Net (Discretionary and Mandatory)	99,262	120,151	89,638	148,466
Distributed Offsetting Receipts (-) (Note 16)	(39,652)	-	(48,725)	-
Agency Outlays, Net (Discretionary and Mandatory) (Note 16)	**$ 59,610**	**$ 120,151**	**$ 40,913**	**$ 148,466**

The accompanying notes are an integral part of these statements.

Notes to the Financial Statements
For the Years Ended September 30, 2014 and 2013

Note 1. Summary of Significant Accounting Policies

Reporting Entity and Programs

The United States (U.S.) Department of Education (the Department), a cabinet-level agency of the Executive Branch of the U.S. Government, was established by Congress under the *Department of Education Organization Act* (Public Law 96-88), which became effective on May 4, 1980. The mission of the Department is to promote student achievement and preparation for global competitiveness by fostering educational excellence and ensuring equal access. The Department is responsible for administering federal student loan and grant programs, as discussed below.

Federal Student Loan Programs. The Department administers direct loan, loan guarantee and other student aid programs to help students and their families finance the cost of postsecondary education. These include the William D. Ford Federal Direct Loan Program (Direct Loan) and the Federal Family Education Loan Program (FFEL).

The Direct Loan Program, added to the *Higher Education Act of 1965* (HEA) in 1993 by the *Student Loan Reform Act of 1993,* authorizes the Department to make loans through participating schools for eligible undergraduate and graduate students and their parents. The FFEL Program, authorized by the HEA, operated through state and private nonprofit guaranty agencies which provided loan guarantees and interest subsidies on loans made by private lenders to eligible students. The *SAFRA Act*, formerly the *Student Aid and Fiscal Responsibility Act* that was included in the *Health Care and Education Reconciliation Act of 2010* (HCERA), effective July 1, 2010, stated that no new FFEL loans would be made.

The Department also administers loans for the Historically Black Colleges and Universities (HBCU) Capital Financing Program, the Health Education Assistance Loan Program (HEAL), the Teacher Education Assistance for College and Higher Education Grant Program (TEACH), along with low-interest loans to institutions of higher education for the building and renovating of their facilities through the facilities loan programs.

Grant Programs. The Department administers numerous grant programs, including: grants to state and local entities for elementary and secondary education; special education and rehabilitative services grants; grants to support institutions of higher education; educational research and improvement grants; grants to assist low-income and first-generation college students to prepare for and transition into college; grants to improve our global awareness and competitiveness; and fellowships for college and graduate students. Among the largest K-12 discretionary grants are the Federal TRIO Program (TRIO), Race to the Top, and Teacher Incentive Fund. Among the largest formula grant programs are the Title I grants issued under the *Elementary and Secondary Education Act of 1965*, as amended, grants issued under the *Individuals with Disabilities Education Act* (IDEA), and grants to local education agencies.

The Department also administers the Federal Pell Grant (Pell Grant) Program to provide need-based grants that provide access to postsecondary education for low-income undergraduate and certain post-baccalaureate students.

Major Program Offices

The Department has three major program offices that administer loan and grant programs. They are:

- Federal Student Aid (FSA)
- Office of Elementary and Secondary Education (OESE)
- Office of Special Education and Rehabilitative Services (OSERS)

In addition, there are other offices that administer programs, including the Office of Career, Technical, and Adult Education (OCTAE), Office of Postsecondary Education (OPE), Institute of Education Sciences (IES), Office of English Language Acquisition (OELA), Office of Innovation and Improvement (OII), Office of Management, Office for Civil Rights (OCR), and Hurricane Education Recovery (HR) activities. (See Notes 12 and 14)

Basis of Accounting and Presentation

These financial statements have been prepared to report the financial position, net cost of operations, changes in net position, and budgetary resources of the Department, as required by the *Chief Financial Officers Act of 1990* and the *Government Management Reform Act of 1994*. The financial statements were prepared from the books and records of the Department, in accordance with Generally Accepted Accounting Principles (GAAP) accepted in the U.S. for federal entities, issued by the Federal Accounting Standards Advisory Board (FASAB), and the Office of Management and Budget (OMB) Circular No. A-136, *Financial Reporting Requirements*, as revised. These financial statements are different from the financial reports prepared by the Department pursuant to OMB directives that are used to monitor and control the use of budgetary resources. FSA also issues audited stand-alone financial statements which are included in their annual report.

The Department's financial statements should be read as a component of the U.S. Government, a sovereign entity. One of the many implications of this is that the liabilities cannot be liquidated without legislation providing resources and legal authority to do so.

The accounting structure of federal agencies is designed to reflect both accrual and budgetary accounting transactions. Under the accrual method of accounting, revenues are recognized when earned and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash. Budgetary accounting facilitates compliance with legal constraints and controls over the use of federal funds.

Intradepartmental transactions and balances have been eliminated from the consolidated financial statements.

Intragovernmental Transactions

The Department's financial activities are interlinked and dependent upon the financial activities of the centralized management functions of the federal government. Due to financial regulation and management control by OMB and the U.S. Department of Treasury (Treasury), operations may not be conducted and financial positions may not be reported as they would if the Department were a separate, unrelated entity.

Accounting for Federal Credit Programs

The purpose of the *Federal Credit Reform Act of 1990* (FCRA) is to record the lifetime cost of direct loans and loan guarantees at the time the loan is disbursed. Under the FCRA, subsidy cost is estimated using the net present value of future cash flows to and from the Department. In accordance with the FCRA, credit programs either estimate a cost to the government (a "positive" subsidy to borrowers), breakeven (zero subsidy cost), or estimate a negative subsidy cost. Credit programs have negative subsidies when the estimated cost to the government of providing credit is less than the estimated collections from repayments, interest, and fees, on a present value basis. The estimates are affected by the cost of borrowing (at Treasury's rates) and the estimated risk of default. In practical terms, a negative subsidy occurs when the interest rate and/or fees charged to the borrower are more than sufficient to cover the costs of the risk of default.

The cost of direct loan and loan guarantee programs are budgeted and tracked by the fiscal year in which the loan award is made or the funds committed. Such a grouping of loans or guarantees are referred to as a "cohort." A cohort is a grouping of direct loans obligated or loan guarantees committed by a program in the same year even if disbursements occur in subsequent years.

In order to account for the change in the net present value of the loan portfolio over time, the subsidy cost is "amortized" each year. Amortization of subsidy is interest expense on debt with Treasury minus interest income from borrowers and interest on uninvested fund balance with Treasury. It is calculated as the difference between interest revenue and interest expense. Amortized amounts are recognized as an increase or decrease in interest income. Amortization accounts for the differences in interest rates, accruals, and cash flows over the life of a cohort, insuring that cost is reflected in subsidy estimates and re-estimates. For direct loans, the allowance for subsidy is adjusted with the offset to interest revenue. For guaranteed loans, the liability for loan guarantees is adjusted with the offset to interest expense.

The FCRA establishes the use of Program, Financing, and General Fund Receipt Accounts for loan guarantees committed and direct loans obligated after September 30, 1991. The Program Account is a budget account that receives and obligates appropriations to cover the subsidy cost of a direct loan or loan guarantee and disburses the subsidy cost to the Financing Account. A Program Account also receives appropriations for administrative expenses. Appropriations for new subsidy and subsidy re-estimates are received in Program Accounts and transferred to the Financing Accounts. Financing Accounts borrow funds from Treasury, make direct loan disbursements, pay claims on guaranteed loans, collect principal and interest from borrowers, collect fees and other program income, pay interest to Treasury on borrowings, collect interest from Treasury on uninvested funds, and collect funds for positive subsidy or transfer negative subsidy to a General Fund Receipt Account. The Financing Account receives the subsidy cost payment from the Program Account. The General Fund Receipt Account, a budget account, is used by Treasury for the receipt of amounts paid from the Financing Account when there are negative subsidies for original cost estimates or downward re-estimates of prior subsidy costs. The budgetary resources and activities for these accounts are presented separately in the Combined Statement of Budgetary Resources (SBR) and the Budget of the United States Government and are excluded from the determination of the budget deficit or surplus. Program accounts are classified as either budgetary or non-budgetary in the Combined SBR. The budgetary accounts include the Program and Liquidating Accounts, while Financing Accounts are non-budgetary. FCRA establishes Liquidating Accounts for activity relating to any loan guarantees committed or direct loans obligated before October 1, 1991.

Components of subsidy costs for loans and guarantees include defaults (net of recoveries); contractual payments to third-party private loan collectors who receive a set percentage of amounts collected; and, as an offset, origination and other fees collected. For direct loans, the difference between interest rates incurred by the Department on its borrowings from Treasury and interest rates charged to particular borrowers is also subsidized (or may provide an offset to subsidy if the Department's rate is less). The corresponding interest subsidy in loan guarantee programs is the payment of interest supplements to third-party lenders in order to pay down the interest rates on loans made by those lenders.

As of July 1, 2014, consistent with the *Consolidated Appropriations Act, 2014* (P.L. 113-76), the Department of Health and Human Services (HHS) transferred all HEAL program loans to the Department. This was accomplished through Treasury guidance on obligated and non-obligated balance transfers. (See Note 6)

Budget Authority

Budget authority is the authorization provided by law for the Department to incur financial obligations that will result in outlays. The Department's budgetary resources include unobligated balances of resources from prior years; recoveries of prior-year obligations; and new resources, which include appropriations, authority to borrow from Treasury, and spending authority from collections.

Borrowing authority is an indefinite budgetary resource authorized under the FCRA. This resource, when realized, finances the unsubsidized portion of the Direct Loan, FFEL, TEACH, and other loan programs. In addition, borrowing authority is requested in advance of expected collections to cover negative subsidy cost. Treasury prescribes the terms and conditions of borrowing authority and lends to the Financing Account amounts as appropriate. Amounts borrowed, but not yet disbursed, are included in uninvested funds and earn interest. Treasury uses the same weighted average interest rates for both the interest charged on borrowed funds and the interest earned on uninvested funds. Treasury calculates a different interest rate to be used for each loan cohort. The Department may carry forward borrowing authority to future fiscal years provided that cohorts are disbursing loans. All borrowings from Treasury are effective on October 1 of the current fiscal year, regardless of when the Department borrowed the funds, except for amounts borrowed to make annual interest payments.

Authority to borrow from Treasury provides most of the funding for disbursements made under the Direct Loan Program, FFEL, TEACH, and other loan programs. Subsidy and administrative costs of the programs are funded by appropriations. Borrowings are repaid using collections from borrowers, fees, and interest on uninvested funds.

Unobligated balances represent the cumulative amount of budget authority that is not obligated and that remains available for obligation under law, unless otherwise restricted. Resources expiring at the end of the fiscal year remain available for five years, but only for upward adjustments of prior year obligations, after which they are canceled and may not be used. Resources that have not expired at year-end are available for new obligations, as well as upward adjustments of prior-year obligations. Funds are appropriated on an annual, multi-year, or no-year basis. Appropriated funds shall expire on the last day of availability and are no longer available for new obligations. Amounts in expired funds are unavailable for new obligations, but may be used to adjust previously established obligations.

Permanent Indefinite Budget Authority. The Direct Loan, FFEL, TEACH, and other loan programs have permanent indefinite budget authority through legislation. Parts B and D of the HEA pertain to the existence, purpose, and availability of permanent indefinite budget authority for these programs.

Reauthorization of Legislation. Funds for most Department programs are authorized, by statute, to be appropriated for a specified number of years, with an automatic one-year extension available under Section 422 of the *General Education Provisions Act*. Congress may continue to appropriate funds after the expiration of the statutory authorization period, effectively reauthorizing the program through the appropriations process. The current *Budget of the United States Government* presumes all programs continue in accordance with congressional budgeting rules. (See Note 16)

Use of Estimates

Department management is required to make certain estimates while preparing consolidated financial statements in conformity with GAAP. These estimates are reflected in the assets, liabilities, net cost, and net position of the financial statements and may differ from actual results. The Department's estimates are based on management's best knowledge of current events, historical experiences, and other assumptions that are believed to be reasonable under the circumstances. Significant estimates reported on the financial statements include allocation of Department administrative overhead costs, annual credit program re-estimates and modifications of subsidy cost (general program administration cost), as well as grant liability and advance accruals. (See Notes 6, 12, and 14)

Entity and Non-Entity Assets

Assets are classified as either entity or non-entity assets. Entity assets are those that the Department has authority to use for its operations. Non-entity assets are those held by the Department but are not available for use in its operations. Non-entity assets are offset by liabilities to third parties and have no impact on net position. The Department combines its entity and non-entity assets on the Balance Sheet and discloses its non-entity assets in the notes. (See Note 2)

Fund Balance with Treasury

Fund Balance with Treasury includes five types of funds in the Department's accounts with Treasury available to pay current liabilities and finance authorized purchases, as well as funds restricted until future appropriations are received: (1) General funds consist of expenditure accounts used to record financial transactions arising from congressional appropriations, as well as receipt accounts; (2) Revolving funds, which include Financing Accounts, manage the activity of self-funding programs whether through fees, sales, or other income; (3) Special funds are receipts from sources that are authorized by law for a specific purpose—these receipts are available for expenditure for special programs; (4) Trust funds are used for the acceptance and administration of funds contributed from public and private sources and programs and are in cooperation with other federal and state agencies or private donors; and (5) Other funds include deposit funds, receipt funds, and clearing accounts. Treasury processes cash receipts and cash disbursements for the Department. The Department's records are reconciled with Treasury's. (See Note 3)

Accounts Receivable

Accounts Receivable are amounts due to the Department from the public and other federal agencies. Receivables from the public result from overpayments to recipients of grants and other financial assistance programs, as well as disputed costs resulting from audits of educational assistance programs. Amounts due from federal agencies result from reimbursable agreements entered into by the Department with other agencies to provide various goods and services. Accounts receivable are reduced to net realizable value by an allowance for uncollectible amounts. The estimate of an allowance for loss on uncollectible accounts is based on the Department's experience in the collection of receivables and an analysis of the outstanding balances.

Accounts Receivable are established as claims to cash or other assets against other entities. At the Department, accounts receivable originate through legal provisions or program requirements to return funds due to noncompliant program administration, regulatory requirements, or individual service obligations. Further, the Department utilizes the opportunity to reduce the accounts receivable balances through the Treasury referral program.

The Department calculates the allowance for loss from uncollectable accounts receivable by applying a collection rate based on historical trends against gross accounts receivable. The collection rate is determined based on a rolling average of actual collection rates for the prior seven fiscal years. (See Note 4)

Cash and Other Monetary Assets

Cash and Other Monetary Assets consist of guaranty agency reserves that represent the federal government's interest in the net Federal Fund assets of state and nonprofit FFEL Program guaranty agencies. Guaranty agency Federal Fund reserves are classified as non-entity assets with the public and are offset by a corresponding liability due to Treasury. Guaranty agency reserves include initial federal start-up funds, receipts of federal reinsurance payments, insurance premiums, guaranty agency share of collections on defaulted loans, investment income, administrative cost allowances, and other assets.

Sections 422A and 422B of the HEA required FFEL guaranty agencies to establish a Federal Student Loan Reserve Fund (Federal Fund) and an Operating Fund. The Federal Fund and the non-liquid assets developed or purchased by a guaranty agency, in whole or in part with federal funds, are the property of the U.S. and are reflected in the *Budget of the United States Government*. Ownership by the federal government is independent of the actual control of the assets.

The Department disburses funds to a guaranty agency. A guaranty agency, through its Federal Fund, pays lender claims and pays default aversion fees into its own Operating Fund. The Operating Fund is the property of the guaranty agency and is used to fulfill responsibilities that include repaying money borrowed from the Federal Fund and performing default aversion and collection activities. Payments made to the Department from Guaranty Agency Federal Fund through a statutory recall or agency closures represent capital transfers and are credited to the Department's Fund Balance with Treasury account. (See Note 5)

Credit Program Receivables, Net and Liabilities for Loan Guarantees

The financial statements reflect the Department's estimate of the long-term cost of direct and guaranteed loans in accordance with the FCRA. Loans and interest receivable are valued at their gross amounts less an allowance for the present value of amounts not expected to be recovered and thus having to be subsidized—called an "allowance for subsidy." The difference between the gross amount and the allowance for subsidy is the present value of the cash flows to, and from, the Department that are expected from receivables over their projected lives. Similarly, liabilities for loan guarantees are valued at the present value of the cash outflows from the Department less the present value of related inflows. The estimated present value of net long-term cash outflows of the Department for subsidized costs is net of recoveries, interest supplements, and offsetting fees. The Department also values all pre-1992 loans, loan guarantees, and direct loans at their net present values. If the Liability for Loan Guarantees is positive, the amount is reported as a component of Credit Program Receivables, Net.

The Liability for Loan Guarantees presents the net present value of all future cash flows from currently insured FFEL loans including claim payments, interest assistance, allowance payments, and recoveries from assigned loans. Guaranteed loans that default are initially turned over to guaranty agencies for collection. Defaulted FFEL loans are accounted for and reported in the financial statements under credit reform rules, similar to direct loans, although they are legally not direct student loans. Negative balances are reported as a component of Credit Program Receivables, Net. Credit Program Receivables, Net includes default FFEL loans owned by the Department and held by the Department or guaranty agencies. In most cases, after approximately four years, defaulted guaranteed loans not in repayment are turned over to the Department for collection.

Credit program receivables for activities under the temporary loan purchase authority include the present value of future cash flows related to purchased loans. Subsidy was transferred, which may have been prior to loan purchase, and is recognized as subsidy expense on the

Balance Sheet and Statement of Net Cost. The cash flows of these authorities also include inflows and outflows associated with the underlying or purchased loans and other related activities, including any positive or negative subsidy transfers. (See Note 6)

Property and Equipment, Net and Leases

The Department capitalizes single items of property and equipment with a cost of $50,000 or more that have an estimated useful life of two years or more. Additionally, the Department capitalizes bulk purchases of property and equipment with an aggregate cost of $500,000 or more. A bulk purchase is defined as the purchase of like items related to a specific project, or the purchase of like items occurring within the same fiscal year that have an estimated useful life of at least two years. Property and equipment are depreciated over their estimated useful lives using the straight-line method of depreciation. Internal Use Software meeting the above cost and useful life criteria is also capitalized. Internal Use Software is either purchased off the shelf, internally developed, or contractor developed solely to meet the Department's needs.

The Department adopted the following useful lives for its major classes of depreciable property and equipment:

Depreciable Property and Equipment

(In Years)

Major Class	Useful Life
Information Technology, Internal Use Software, and Telecommunications Equipment	3
Furniture and Fixtures	5

The Department leases buildings, along with information technology and telecommunications equipment, as part of a contractor-owned, contractor-operated services contract. Lease payments associated with the equipment have been determined to be operating leases and, as such, are expensed as incurred. The non-cancellable lease term is one year, with the Department holding the right to extend the lease term by exercising additional one-year options. (See Note 7)

Liabilities

Liabilities represent actual and estimated amounts to be paid as a result of transactions or events that have already occurred. However, no liabilities can be paid by the Department without budget authority. Liabilities for which an appropriation has not been enacted are classified as liabilities not covered by budgetary resources, and there is no certainty that an appropriation will be enacted. The government, acting in its sovereign capacity, can abrogate liabilities that arise from activities other than contracts. FFEL Program and Direct Loan Program liabilities are entitlements covered by permanent indefinite budget authority. (See Note 11)

Accounts Payable

Accounts Payable include amounts owed by the Department for goods and services received from other entities, as well as payments not yet processed. (See Note 9)

Debt

The Department borrows from Treasury to provide funding for the Direct Loan, FFEL, TEACH, and other loan programs. The liability to Treasury from borrowings represents unpaid principal at year-end. The Department repays the principal based on available fund balances. Interest on the debt is calculated and paid at fiscal year-end using rates set by Treasury. These are rates generally fixed based on the rate for 10-year Treasury securities. In addition, the Federal Financing Bank (FFB) holds bonds issued by a designated bonding authority, on behalf of the

Department, for the HBCU Capital Financing Program. The Department reports the corresponding liability for full payment of principal and accrued interest on bonds as a payable to the FFB. (See Note 10)

Accrued Grant Liability

Disbursements of grant funds are recognized as expenses at the time of disbursement. Some grant recipients incur allowable expenditures as of the end of an accounting period but have not yet been reimbursed by the program. The Department will accrue a liability for these allowable expenditures incurred that have not yet been reimbursed. The amount is estimated using statistical sampling, as well as information on recent grant expenditures and unliquidated balances. (See Note 12)

Other Liabilities

Other Liabilities include liabilities in miscellaneous receipts and capital transfers. Liabilities in miscellaneous receipt accounts are recorded for downward subsidy re-estimates that are accrued at year end and for amounts of future capital transfers from Liquidating Accounts. Miscellaneous receipt accounts are a mechanism used by Treasury to facilitate the elimination of receivables and payables within the government, and the Department follows the guidance for using miscellaneous receipt accounts in recording specific events. Upon execution of a downward re-estimate or an actual capital transfer, the liabilities in the miscellaneous receipt accounts are satisfied and removed from the general ledger. Liabilities in miscellaneous receipt accounts are unfunded liabilities. (See Note 11)

Net Cost

Net cost consists of gross costs and earned revenue. Gross costs and earned revenue are classified as intragovernmental (exchange transactions between the Department and other entities within the federal government) or with the public (exchange transactions between the Department and non-federal entities).

Net program costs are gross costs less revenue earned from activities. The Department determines gross cost and earned revenue by tracing amounts back to the specific program office. Administrative overhead costs of funds unassigned are allocated based on full-time employee equivalents of each program. (See Note 14)

Interest Expense and Interest Revenue

The Department accrues interest receivable and records interest revenue on performing Direct Loans and FFEL loans purchased by the Department. The Department recognizes interest income when interest is accrued on loans to the public for the Direct Loan, FFEL, and TEACH Programs. FFEL Financing and Liquidating Accounts accrue interest as part of allowance for subsidy. Interest due from borrowers is accrued at least monthly and is satisfied upon collection or capitalization into the loan principal.

Interest expense and interest revenue are equal for all credit programs due to subsidy amortization. If interest revenue is greater than expense or interest expense is greater than revenue, the difference is recorded to revenue with the offset to allowance for subsidy. Subsidy amortization is required by the FCRA and accounts for the difference between interest accruals and interest cash flows. (See Note 15)

Net Position

Net position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations include undelivered orders and unobligated balances, except for amounts in Financing Accounts, Liquidating Accounts, and trust funds. Cumulative results of operations represent the net difference since inception between (1) expenses and (2) revenues and financing sources. (See Note 13)

Personnel Compensation and Other Employee Benefits

Annual, Sick, and Other Leave. The liability for annual leave, compensatory time off, and other vested leave is accrued when earned and reduced when taken. Each year, the accrued annual leave account balance is adjusted to reflect current pay rates. Sick leave and other types of non-vested leave are expensed as taken. Annual leave earned but not taken, within established limits, is funded from future financing sources.

Retirement Plans and Other Retirement Benefits. Employees participate in either the Civil Service Retirement System (CSRS), a defined benefit plan, or the Federal Employees Retirement System (FERS), a defined benefit and contribution plan. For CSRS employees, the Department contributes a fixed percentage of pay.

FERS consists of Social Security, a basic annuity plan, and the Thrift Savings Plan. The Department and the employee contribute to Social Security and the basic annuity plan at rates prescribed by law. In addition, the Department is required to contribute to the Thrift Savings Plan a minimum of 1 percent per year of the basic pay of employees covered by this system, match voluntary employee contributions up to 3 percent of the employee's basic pay, and match one-half of contributions between 3 percent and 5 percent of the employee's basic pay. For FERS employees, the Department also contributes the employer's share of Medicare.

Contributions for CSRS, FERS, and other retirement benefits are insufficient to fund the programs fully and are subsidized by the Office of Personnel Management (OPM). The Department imputes its share of the OPM subsidy, using cost factors provided by OPM, and reports the full cost of the programs related to its employees.

Federal Employees' Compensation Act. The *Federal Employees' Compensation Act* (FECA) provides income and medical cost protection to covered federal civilian employees injured on the job, employees who have incurred work-related occupational diseases, and beneficiaries of employees whose deaths are attributable to job-related injuries or occupational diseases. The FECA Program is administered by the U.S. Department of Labor (DOL), which pays valid claims and subsequently seeks reimbursement from the Department for these paid claims.

The FECA liability consists of two components. The first component is based on actual claims paid and recognized by the Department as a liability. Generally, the Department reimburses DOL within two to three years once funds are appropriated. The second component is the estimated liability for future benefit payments based on unforeseen events, such as death, disability, medical, and miscellaneous costs as determined by DOL annually. (See Note 11)

Reclassifications

Certain reclassifications were made to the Fiscal Year (FY) 2013 financial statements and notes to conform to the current year presentation. These changes had no effect on total assets, liabilities, net position, net cost of operations, or budgetary resources. The *American Recovery and Reinvestment Act of 2009* (ARRA) funding is winding down, thereby diminishing the materiality of the program. Therefore, the separate ARRA presentation on the financial statements and note disclosures has been removed. The Consolidated Statement of Net Cost and related note disclosures for FY 2013 have been reclassified to present ARRA funding under the specific program offices distributing the funding. (See Notes 12 and 14)

Note 2. Non-Entity Assets

As of September 30, 2014 and 2013, non-entity assets consisted of the following:

Non-Entity Assets

(Dollars in Millions)

	2014	2013
Non-Entity Assets		
Intragovernmental:		
Fund Balance with Treasury	$ 44	$ 40
Total Intragovernmental	**44**	**40**
With the Public:		
Cash and Other Monetary Assets	1,471	1,482
Credit Program Receivables, Net	387	369
Accounts Receivable, Net	63	61
Total With the Public	**1,921**	**1,912**
Total Non-Entity Assets	**1,965**	**1,952**
Entity Assets	1,021,961	935,106
Total Assets	$ 1,023,926	$ 937,058

The Department's FY 2014 assets are predominantly entity assets (99.8 percent), leaving the small portion of assets remaining as non-entity assets. Non-entity intragovernmental assets primarily consist of deposit fund and clearing account balances. Non-entity assets with the public primarily consist of guaranty agency reserves (76.6 percent), reported as Cash and Other Monetary Assets, and related Federal Perkins Loan Program loan receivables (20.1 percent), reported as Credit Program Receivables, Net. Federal Perkins Loan Program is a non-entity asset because the assets are held by the Department but are not available to the Department. The corresponding liabilities for these non-entity assets are reflected in various accounts, including Intragovernmental Accounts Payable, Guaranty Agency Federal Fund Due to Treasury, and Other Liabilities. (See Notes 5, 9, and 11)

Note 3. Fund Balance with Treasury

Fund Balance with Treasury by status of funds and fund type, as of September 30, 2014 and 2013, consisted of the following:

Fund Balance with Treasury

(Dollars in Millions)

	2014					
	General Funds	Revolving Funds	Special Funds	Trust Funds	All Other Funds	Total
Status of Funds						
Unobligated Balance:						
Available	$ 12,125	$ 69	$ -	$ -	$ -	$12,194
Unavailable	1,230	10,040	11	-	-	11,281
Obligated Balance, Not Yet Disbursed	56,208	18,964	4	1	-	75,177
Other	-	-	-	-	44	44
Fund Balance with Treasury	**$ 69,563**	**$29,073**	**$ 15**	**$ 1**	**$ 44**	**$98,696**

	2013					
	General Funds	Revolving Funds	Special Funds	Trust Funds	All Other Funds	Total
Status of Funds						
Unobligated Balance:						
Available	$ 13,700	$ -	$ -	$ -	$ -	$ 13,700
Unavailable	1,010	11,315	15	-	-	12,340
Obligated Balance, Not Yet Disbursed	59,619	23,028	2	3	-	82,652
Other	-	-	-	-	40	40
Fund Balance with Treasury	**$ 74,329**	**$ 34,343**	**$ 17**	**$ 3**	**$ 40**	**$108,732**

Composition of Funds

A portion of the general funds is provided in advance by multiyear appropriations for obligations anticipated during the current and future fiscal years. Revolving funds are derived from borrowings, as well as collections from the public and other federal agencies. Special funds include fees collected on delinquent or defaulted Perkins loans that have reverted back to the Department from the initial lenders. Trust funds generally consist of remaining undisbursed donations for the hurricane relief activities.

Status of Funds

Available unobligated balances represent amounts that are apportioned for obligation in the current fiscal year. Unavailable unobligated balances represent amounts that are not apportioned for obligation during the current fiscal year and expired appropriations no longer available to incur new obligations. Total unavailable unobligated balances ($11,281 million) differs from unapportioned amounts on the SBR ($12,752 million) due to the Cash and Other Monetary Assets ($1,471 million). Obligated balances not yet disbursed include undelivered orders and unpaid expended authority. (See Note 5)

Note 4. Accounts Receivable

Accounts Receivable, as of September 30, 2014 and 2013, consisted of the following:

Accounts Receivable
(Dollars in Millions)

	2014		
	Gross Receivables	Allowance	Net Receivables
Intragovernmental	$ 3	$ -	$ 3
With the Public	324	(188)	136
Total	**$ 327**	**$ (188)**	**$ 139**

	2013		
	Gross Receivables	Allowance	Net Receivables
Intragovernmental	$ 2	$ -	$ 2
With the Public	306	(185)	121
Total	**$ 308**	**$ (185)**	**$ 123**

Gross Receivables by type, as of September 30, 2014 and 2013, are presented below.

Gross Receivables
(Dollars in Millions)

	2014	2013
Category		
Institutional	$ 209	$ 194
Individual	72	72
State and Local	43	40
Intragovernmental	3	2
Total	**$ 327**	**$ 308**

Accounts receivable consist of institutional debt resulting from external audit or program review; program scholarship grant repayments; employee debt; and intragovernmental debts due from other federal agencies through interagency agreements.

Note 5. Cash and Other Monetary Assets

Cash and Other Monetary Assets consist of reserves held in the FFEL guaranty agency Federal Fund. Changes in the valuation of the Federal Fund increase or decrease the Department's Cash and Other Monetary Assets with a corresponding change in Guaranty Agency Federal Fund Due to Treasury. The table below presents Cash and Other Monetary Assets for the years ended September 30, 2014 and 2013.

Cash and Other Monetary Assets
(Dollars in Millions)

	2014	2013
Beginning Balance, Cash and Other Monetary Assets	**$ 1,482**	**$ 1,307**
Increase/(Decrease) in Guaranty Agency Federal Fund, net	(11)	175
Ending Balance, Cash and Other Monetary Assets	**$ 1,471**	**$ 1,482**

The $11 million net decrease in the Federal Fund in FY 2014 represents the change in the estimated value of net assets held in the FFEL guaranty agency Federal Fund. This decrease reflects the impact of guaranty agencies' operations.

Note 6. Credit Programs for Higher Education: Credit Program Receivables, Net and Liabilities for Loan Guarantees

The Department currently operates two major student loan programs, Direct Loan and FFEL. The Direct Loan Program offers four types of loans: Stafford, Unsubsidized Stafford, PLUS, and Consolidation. Evidence of financial need is required for an undergraduate student to receive a subsidized Stafford loan. The other three loan programs are available to borrowers at all income levels. Loans can be used only to meet qualified educational expenses.

The Department holds $924 billion in outstanding student loan net receivables. This outstanding balance is comprised primarily of Direct Loan, FFEL, and loans purchased using authority provided in *Ensuring Continued Access to Student Loans Act of 2008* (ECASLA), but there are several other loan programs that the Department administers—including the Federal Perkins Loan Program, the TEACH Grant Program, HEAL Program, and the Facilities Loan Programs.

Credit Program Receivables, as of September 30, 2014 and 2013, consisted of the following:

Credit Program Receivables, Net
(Dollars in Millions)

	2014	2013
Direct Loan Program Loan Receivables, Net	$ 778,516	$ 679,107
FFEL Program Loan Receivables:		
FFEL Guaranteed Loan Program, Net (Pre-1992)	1,904	2,231
FFEL Program (Post-1991):		
FFEL Guaranteed Loan Program, Net	37,969	35,144
Temporary Loan Purchase Authority:		
Loan Purchase Commitment, Net	36,556	38,946
Loan Participation Purchase, Net	64,513	67,546
ABCP Conduit, Net	1,922	1,864
Federal Perkins and Other Loan Program Loan Receivables, Net	387	369
TEACH Program Loan Receivables, Net	536	453
HEAL Program Loan Receivables, Net	115	
Facilities Loan Programs Loan Receivables, Net	1,127	1,024
Total	**$ 923,545**	**$ 826,684**

Due to Congressional legislation, HHS will report all prior year HEAL Program information on their financial statements. Thus, the Department will not report FY 2013 HEAL Program information on the comparable financial statements in FY 2014.

The federal student loan programs provide students and their families with the funds to help meet postsecondary education costs. Funding for these programs is provided through permanent indefinite budget authority. What follows is a comprehensive description of the student loan programs at the Department, including summary financial data and subsidy rates.

William D. Ford Federal Direct Loan Program. The federal government makes loans directly to students and parents through participating institutions of higher education under the Direct Loan Program. Direct Loans are originated and serviced through contracts with private vendors. As of September 30, 2014 and 2013, total principal balances outstanding of Direct Loans were approximately $694 billion and $585 billion, respectively.

The Department disbursed approximately $134 billion in Direct Loans to eligible borrowers in FY 2014 and approximately $130 billion in FY 2013. Of the $134 billion disbursed in Direct Loans, new loans were $99 billion and consolidation loans were $35 billion. Loans are typically disbursed in multiple installments over an academic period; as a result, loan disbursements for an origination cohort year often cross fiscal years. Half of all loan volume is obligated in the fourth quarter of a fiscal year. Regardless of the fiscal year in which they occur, disbursements are tracked by cohort as determined by the date of obligation rather than disbursement.

Approximately 8.5 percent of Direct Loan obligations made in a fiscal year are never disbursed. Loan obligations are established at a summary level based on estimates of schools' receipt of aid applications. The loan obligation may occur before a student has been accepted by a school or before the student begins classes. For Direct Loans obligated in the 2014 cohort, an estimated $12.6 billion will never be disbursed. Eligible schools may obtain advances from the Department to fund Direct Loans awards or request subsequent reimbursement from the Department.

Direct Loan Program loan receivables are defaulted and non-defaulted loans owned and held by the Department. The following schedule summarizes the principal and related interest receivables, net of the allowance for subsidy:

Direct Loan Program Loan Receivables, Net

(Dollars in Millions)

	2014	2013
Principal Receivable	$ 694,006	$ 584,528
Interest Receivable	37,152	29,332
Total	731,158	613,860
Allowance for Subsidy	47,358	65,247
Direct Loan Program Loan Receivables, Net	**$ 778,516**	**$ 679,107**

Of the $731.2 billion in receivables, as of September 30, 2014, $33.9 billion (4.6 percent) in loan principal was in default and had been transferred to the Department's defaulted loan servicer, compared to $28.9 billion (4.7 percent) as of September 30, 2013. As of September 30, 2014 and 2013, an additional $0.5 billion and $1.1 billion, respectively in defaulted loans held by servicers had not yet been transferred to the Department's defaulted loan servicer; this amount includes defaulted Direct Loans and defaulted loans from other loan programs.

Negative allowance for subsidy is a factor of interest rates, default rates, fees, and other costs. Negative subsidy is an estimate of future cash inflows exceeding future cash outflows. Subsidy, either positive or negative, provides resources for the Department to carry on its loan origination and loan servicing activities under the Direct Loan Program.

The following schedule provides a reconciliation between the beginning and ending balances of the allowance for subsidy for the Direct Loan Program:

Direct Loan Program Reconciliation of Allowance for Subsidy

(Dollars in Millions)

	2014	2013
Beginning Balance, Allowance for Subsidy	**$ 65,247**	**$ 32,076**
Activity		
Fee Collections	(1,623)	(1,557)
Loan Cancellations	2,068	1,890
Subsidy Allowance Amortization	(11,319)	(7,719)
Other	1,111	1,000
Total Activity	**(9,763)**	**(6,386)**
Components of Negative Subsidy Transfers		
Interest Rate Differential	33,161	37,063
Defaults, Net of Recoveries	(1,409)	(1,887)
Fees	1,756	1,801
Other	(11,418)	(9,967)
Current Year Negative Subsidy Transfers	**22,090**	**27,010**
Components of Subsidy Re-estimates		
Interest Rate Re-estimates	(8,344)	11,754
Technical and Default Re-estimates	(21,872)	793
(Upward)/Downward Subsidy Re-estimates	**(30,216)**	**12,547**
Ending Balance, Allowance for Subsidy	**$ 47,358**	**$ 65,247**

Loan cancellations include write-offs of loans because the primary borrower died, became disabled, or declared bankruptcy. The Other components of current year negative subsidy transfers consist of contract collection costs, program review collections, fees, and other accruals. The interest rate re-estimate relates to subsidy associated with establishing a fixed rate for the Department's borrowing from Treasury.

The following schedule summarizes the Direct Loan Financing Account interest expense and interest revenue for the years ended September 30, 2014 and 2013:

Direct Loan Program Interest Expense and Revenue

(Dollars in Millions)

	2014	2013
Interest Expense on Treasury Borrowing	$ 25,152	$ 22,661
Total Interest Expense	**$ 25,152**	**$ 22,661**
Interest Revenue from the Public	$ 32,801	$ 26,972
Amortization of Subsidy	(11,319)	(7,720)
Interest Revenue on Uninvested Funds	3,670	3,409
Total Interest Revenue	**$ 25,152**	**$ 22,661**

The following schedule summarizes the Direct Loan Financing Account subsidy expense for the years ended September 30, 2014 and 2013:

Direct Loan Program Subsidy Expense

(Dollars in Millions)

	2014	2013
Components of Negative Subsidy Transfers		
Interest Rate Differential	$ 33,161	$ 37,063
Defaults, Net of Recoveries	(1,409)	(1,887)
Fees	1,756	1,801
Other	(11,418)	(9,967)
Negative Subsidy Transfers	**22,090**	**27,010**
(Upward)/Downward Subsidy Re-estimates	(30,216)	12,547
Direct Loan Subsidy Expense	**$ (8,126)**	**$ 39,557**

The change in Direct Loan Subsidy Expense of $47.7 billion from FY 2013 to FY 2014 is primarily due to the change in subsidy re-estimates. Direct Loan re-estimated subsidy cost was adjusted upward by $30.2 billion in FY 2014. Updated discount rates for the 2013 and 2012 cohorts decreased cost by $4.4 billion. Changes in the availability of repayment plans increased cost by $18.6 billion. Costs increased $2.9 billion due to increases in default rates. Changes in prepayment rates reflect slower than expected prepayment activity, leading to increased interest earnings resulting in $3.2 billion in downward subsidy cost. Other assumption updates produced offsetting costs, with the remainder attributable to interest on the re-estimate. In June 2014, President Obama announced a new initiative to expand the Pay As You Earn repayment plan to all borrowers. The modified cost for subsidy of this plan for cohort years 1994-2013 is $8.3 billion. This planned initiative will be negotiated with interested parties in 2015. The subsidy rate is sensitive to interest rate fluctuations; for example, a 1 percent increase in projected borrower base rates would reduce projected Direct Loan subsidy cost by $3.5 billion. Re-estimated costs only include those cohorts that are 90 percent disbursed; cohort years 1994–2013.

Direct Loan re-estimated subsidy cost was adjusted downward by $12.5 billion in FY 2013. Updated discount rates for the 2012 and 2011 cohorts decreased cost by $11.8 billion. Deferment and forbearance rate changes decreased cost by $1.5 billion. Costs increased $1.5 billion due to increases in default and disability rates. Changes in prepayment rates reflect slower than expected prepayment activity, leading to increased interest earnings resulting in $1.1 billion in downward subsidy cost. Other assumption updates produced offsetting costs, with the remainder attributable to interest on the re-estimate. The subsidy rate is sensitive to interest rate fluctuations; for example, a 1 percent increase in projected borrower base rates would reduce projected Direct Loan subsidy cost by $1.8 billion. Re-estimated costs only include those cohorts that were 90 percent disbursed; cohort years 1994–2012.

The subsidy rates applicable to the 2014 loan cohort year follow:

Direct Loan Subsidy Rates—Cohort 2014

	Interest Differential	Defaults	Fees	Other	Total
Stafford	(4.86)%	0.15%	(1.07)%	6.37%	0.59%
Unsubsidized Stafford	(25.51)%	0.27%	(1.07)%	7.77%	(18.54)%
PLUS	(34.89)%	0.51%	(4.29)%	6.99%	(31.68)%
Consolidation	(6.59)%	1.58%	0.00%	11.14%	6.13%
Total	**(18.08)%**	**0.59%**	**(1.25)%**	**8.20%**	**(10.54)%**

The subsidy rate represents the subsidy expense of the program in relation to the obligations or commitments made during the fiscal year and are weighted on gross volume. The subsidy expense for new direct loans reported in the current year relates to disbursements of loans from both current and prior years' cohorts. Subsidy expense is recognized when the Department disburses direct loans. The subsidy expense reported in the current year may include re-estimates. The subsidy rates shown above, which reflect aggregate negative subsidy in the FY 2014 cohort, cannot be applied to direct loans disbursed during the current reporting year to yield the subsidy expense, nor are these rates applicable to the portfolio as a whole. The Department does not re-estimate student loan cohorts until they are at least 90 percent disbursed. As a result, the financial statement re-estimate does not include a re-estimate of the current year cohort. The first re-estimate of this cohort will take place upon execution of the 2016 President's Budget.

The costs of the Department's student loan programs, especially the Direct Loan Program, are highly sensitive to changes in actual and forecasted interest rates. The formulas for determining program interest rates are established by statute; the existing loan portfolio has a mixture of borrower and lender rate formulas. Interest rate projections are based on probabilistic interest rate scenario inputs developed and provided by OMB.

The following schedule summarizes the Direct Loan Program loan disbursements by loan type for the years ended September 30, 2014 and 2013:

Direct Loan Program Expenditures by Loan Type

(Dollars in Millions)

	2014	2013
Stafford	$ (25,877)	$ (26,530)
Unsubsidized Stafford	(54,740)	(56,122)
PLUS	(18,910)	(19,388)
Consolidation	(34,525)	(27,472)
Total Expenditures	**$ (134,052)**	**$ (129,512)**

The allocation of disbursements for the first three loan types is estimated based on historical trend information.

Student and parent borrowers may prepay existing loans without penalty through a new consolidation loan. Under the FCRA and requirements provided by OMB regulations, the retirement of Direct Loans being consolidated is considered a collection of principal and interest. This receipt is offset by the disbursement related to the newly created consolidation loan. Underlying direct or guaranteed loans, performing or nonperforming, are paid off in their original cohort; new consolidation loans are originated in the cohort in which the new consolidation loan was obligated. Consolidation activity is taken into consideration in establishing subsidy rates for defaults and other cash flows. The cost of new consolidations is included in subsidy expense for the current-year cohort; the effect of prepayments on existing loans could contribute to re-estimates of prior cohort costs. The net receivables include estimates of future prepayments of existing loans through consolidations; they do not reflect costs associated with anticipated future consolidation loans.

Direct Loan consolidations increased from $28 billion during FY 2013 to $35 billion during FY 2014. Under the FCRA, the subsidy costs of new consolidation loans are not reflected until the future fiscal year in which they are disbursed. The effect of the early payoff of the existing loans—those being consolidated—is recognized in the future projected cash flows of the past cohort year in which the loans were originated.

Federal Family Education Loan Program. As a result of the *SAFRA Act*, the Department and private lenders did not originate or guarantee any new loans in FY 2014 or FY 2013. Federal guarantees on FFEL Program loans and commitments remain in effect for loans made before July 1, 2010, that were sold to the Department through an ECASLA program, consolidated into a direct loan, or otherwise satisfied, discharged, or cancelled. As of September 30, 2014 and 2013, total principal balances outstanding of guaranteed loans held by lenders were approximately $242 billion and $264 billion, respectively. As of September 30, 2014 and 2013, the estimated maximum government exposure on outstanding guaranteed loans held by lenders was approximately $236 billion and $258 billion, respectively. Of the insured amount, the Department would pay a smaller amount to the guaranty agencies, based on the appropriate reinsurance rates, which range from 100 to 95 percent.

FFEL Program Loan Receivables, Net

(Dollars in Millions)

	2014	2013
FFEL Program (Pre-1992)		
Principal Receivable	$ 4,707	$ 5,040
Interest Receivable	5,810	5,563
Total	10,517	10,603
Allowance for Subsidy	(8,586)	(8,356)
Liabilities for Loan Guarantees	(27)	(16)
FFEL Guaranteed Loan Program, Net (Pre-1992)	**1,904**	**2,231**
FFEL Program (Post-1991)		
FFEL Guaranteed Loan Program:		
Principal Receivable	34,251	32,649
Interest Receivable	5,273	4,849
Total	39,524	37,498
Allowance for Subsidy	(5,773)	(6,614)
Liabilities for Loan Guarantees	4,218	4,260
FFEL Guaranteed Loan Program, Net (Post-1991)	**37,969**	**35,144**
Temporary Loan Purchase Authority:		
Loan Purchase Commitment:		
Principal Receivable	29,401	31,899
Interest Receivable	1,927	1,859
Total	31,328	33,758
Allowance for Subsidy	5,228	5,188
Loan Purchase Commitment, Net	**36,556**	**38,946**
Loan Participation Purchase:		
Principal Receivable	52,782	56,041
Interest Receivable	3,358	3,297
Total	56,140	59,338
Allowance for Subsidy	8,373	8,208
Loan Participation Purchase, Net	**64,513**	**67,546**
ABCP Conduit:		
Principal Receivable	2,036	2,208
Interest Receivable	218	193
Total	2,254	2,401
Allowance for Subsidy	(332)	(537)
ABCP Conduit, Net	**1,922**	**1,864**
FFEL Program Loan Receivables, Net	**$ 142,864**	**$ 145,731**

ECASLA gave the Department temporary authority to purchase FFEL loans and participation interests in those loans. The Department implemented three activities under this authority: loan purchase commitments; purchases of loan participation interests; and a put, or forward purchase commitment, with an Asset-Backed Commercial Paper (ABCP) Conduit. This authority expired after September 30, 2010; as a result, loan purchase commitments and purchases of loan participation interests concluded. However, under the terms of the Put Agreement with the conduit, ABCP Conduit activity ceased operations in January 2014.

The asset-backed commercial paper vehicle, the Conduit, closed in early FY 2014, resulting in a $71 billion recovery of prior year obligations and the cancellation of unused borrowing authority.

The FFEL Guaranteed Student Loan Financing Account has a negative estimated Liability for Loan Guarantees of $4.2 billion and $4.3 billion as of September 30, 2014 and 2013, respectively. This indicates that expected collections on anticipated future defaulted loans will be in excess of default disbursements, calculated on a net present value basis. Under GAAP, the negative estimated liability has been classified as a component of Credit Program Receivables on the Consolidated Balance Sheet. The following schedule provides a reconciliation between the beginning and ending balances of the liability for loan guarantees for the insurance portion of the FFEL Program:

FFEL Program Reconciliation of Liabilities for Loan Guarantees

(Dollars in Millions)

	2014	2013
Beginning Balance, FFEL Financing Account Liability for Loan Guarantees	**$ 4,260**	**$ (1,013)**
Activity		
Interest Supplement Payments	1,094	1,336
Claim Payments	8,914	9,125
Fee Collections	(2,156)	(2,239)
Interest on Liability Balance	1,843	1,783
Other	(13,785)	(12,564)
Total Activity	**(4,090)**	**(2,559)**
Components of Loan Modifications		
Loan Modification Costs	4,020	-
Modification Adjustment Transfers	(581)	-
Loan Modifications	**3,439**	**-**
(Upward)/Downward Subsidy Re-estimates	**609**	**7,832**
Ending Balance, FFEL Financing Account Liability for Loan Guarantees	**4,218**	**4,260**
FFEL Liquidating Account Liability for Loan Guarantees	(27)	(16)
Liabilities for Loan Guarantees	**$ 4,191**	**$ 4,244**

Other activity includes negative special allowance collections, collections on defaulted FFEL loans, expenditures, and loan cancellations due to death, disability, or bankruptcy.

The following schedules provide reconciliations between the beginning and ending balances of the allowance for subsidy for the Loan Purchase Commitment component and the Loan Participation Purchase component of the FFEL Program. Loans in these programs are loans acquired by the Department. Acquired loans are reported at their net present value of future cash flows.

Loan Purchase Commitment Reconciliation of Allowance for Subsidy

(Dollars in Millions)

	2014	2013
Beginning Balance, Allowance for Subsidy	**$ 5,188**	**$ 5,258**
Activity		
Subsidy Allowance Amortization	(749)	(771)
Loan Cancellations	116	106
Contract Collection Cost and Other	72	51
Total Activity	**(561)**	**(614)**
(Upward)/Downward Subsidy Re-estimates	**601**	**544**
Ending Balance, Allowance for Subsidy	**$ 5,228**	**$ 5,188**

Loan Participation Purchase Reconciliation of Allowance for Subsidy

(Dollars in Millions)

	2014	2013
Beginning Balance, Allowance for Subsidy	**$ 8,208**	**$ 8,910**
Activity		
Subsidy Allowance Amortization	(1,304)	(1,319)
Loan Cancellation	224	197
Contract Collection Cost and Other	93	43
Total Activity	**(987)**	**(1,079)**
(Upward)/Downward Subsidy Re-estimates	**1,152**	**377**
Ending Balance, Allowance for Subsidy	**$ 8,373**	**$ 8,208**

The following schedule provides FFEL Program subsidy expense for the years ended September 30, 2014 and 2013, respectively:

FFEL Program Subsidy Expense

(Dollars in Millions)

	2014	2013
FFEL Guaranteed Loan Program Subsidy Re-estimates	$ 609	$ 7,832
Loan Purchase Commitment Subsidy Re-estimates	601	544
Loan Participation Purchase Subsidy Re-estimates	1,152	377
ABCP Conduit Subsidy Re-estimates	203	-
FFEL Program (Upward)/Downward Subsidy Re-estimates	**2,565**	**8,753**
FFEL Guaranteed Loan Program Modification Costs	4,020	-
FFEL Program Subsidy Expense	**$ 6,585**	**$ 8,753**

FFEL Guaranteed re-estimated subsidy cost was adjusted downward by $0.6 billion in FY 2014. Costs decreased $411 million due to updated economic assumptions, including probabilistic deterministic rates, which reflected historically low commercial paper rates, resulting in substantially higher negative special allowance payments than were previously projected. Costs decreased $111 million due to maturity and debt distribution assumption updates. Other assumption updates produced offsetting costs, with the remainder attributable to interest on the re-estimate. The subsidy rate is sensitive to interest rate fluctuations; for example, a 1 percent increase in borrower interest rates and the guaranteed yield for lenders would increase projected FFEL costs by $18 billion.

FFEL Guaranteed re-estimated subsidy cost was adjusted downward by $7.8 billion in FY 2013. Costs decreased $5.2 billion due to updated economic assumptions, including probabilistic deterministic rates, which reflected historically low commercial paper rates, resulting in substantially higher negative special allowance payments than were previously projected. Costs increased $1 billion due to increases in bankruptcy and disability rates. Other assumption updates produced offsetting costs, with the remainder attributable to interest on the re-estimate. The subsidy rate is sensitive to interest rate fluctuations; for example, a 1 percent increase in borrower interest rates and the guaranteed yield for lenders would increase projected FFEL costs by $12.3 billion.

Modification of Subsidy Cost. Recorded subsidy cost of a loan is based on a set of assumed future cash flows. Government actions that change these assumed future cash flows change subsidy cost and are recorded as loan modifications. Loan modifications are recognized under the same accounting principle as subsidy re-estimates. Modification adjustment transfers are required to adjust for the difference between current discount rates used to calculate modification costs and the discount rates used to calculate cohort interest expense and revenue. Separate amounts are recorded for modification costs and modification adjustment transfers. The Department modified loans in FY 2014, but not in FY 2013.

FY 2014 Modification. The *Bipartisan Budget Act of 2013* eliminated guaranty agencies' retention share of original defaulted student loan amounts, and reduced the maximum fee they can charge a borrower on the borrower's outstanding balance from 18.5 to 16 percent. The Act required these agencies to send rehabilitated loans to the Department if they cannot find a private lender buyer. These technical changes resulted in a $4 billion downward subsidy cost modification and a $581 million modification adjustment transfer loss for the FFEL Financing Account.

Other Credit Programs for Higher Education

Federal Perkins Loan Program. The Federal Perkins Loan Program provides low-interest loans to eligible postsecondary school students. In some statutorily defined cases, funds are provided to reimburse schools for loan cancellations. For defaulted loans assigned to the Department, collections of principal, interest, and fees, net of amounts paid by the Department to cover contract collection costs, are transferred to Treasury annually.

As of September 30, 2014 and 2013, loan and interest receivables, net of allowance for losses, were $387 million and $358 million, respectively. These receivables are valued at net realizable value with estimated allowance for losses of $161 million and $154 million as of September 30, 2014 and 2013, respectively.

TEACH Grant Program. The Department awards annual grants of up to $4,000 to eligible undergraduate and graduate students who agree to serve as full-time mathematics, science, foreign language, bilingual education, special education, or reading teachers at high-need schools for four years within eight years of graduation. The maximum lifetime grant for students is $16,000 for undergraduate programs and $8,000 for graduate programs. For students failing to fulfill the service requirement, the grants are converted to Direct Unsubsidized Stafford

Loans. Since grants can be converted to direct loans, for budget and accounting purposes, the program is operated as a loan program under the FCRA.

As of September 30, 2014 and 2013, loan receivables were $536 million and $453 million, respectively. The receivable balance is net of allowance for subsidy of $120 million and $106 million as of September 30, 2014 and 2013, respectively.

The subsidy rates applicable to the 2014 loan cohort year follow:

TEACH Subsidy Rates—Cohort 2014

	Interest Differential	Defaults	Fees	Other	Total
Total Subsidy Rates	**6.96%**	**0.24%**	**0.00%**	**6.55%**	**13.75%**

HEAL Program. The Department assumed responsibility for the HEAL program and the authority to administer, service, collect, and enforce the program. The HEAL Program is structured as required by the FCRA. A Liquidating Account is used to record all cash flows to and from the government resulting from guaranteed HEAL loans committed prior to 1992. Credit program receivables, net of allowance for subsidy and liabilities for loan guarantees, were $115 million for FY 2014. All loan activity for 1992 and beyond is recorded in corresponding Financing Accounts.

Facilities Loan Programs. The Department also administers the HBCU Capital Financing Program. Since 1992, this program has given HBCUs access to financing for the repair, renovation, and, in exceptional circumstances, the construction or acquisition of facilities, equipment, and infrastructure through federally insured bonds. The Department has authorized a designated bonding authority to make loans to eligible institutions, charge interest, and collect principal and interest payments. In compliance with HEA, as amended, the bonding authority maintains an escrow account to pay the principal and interest on bonds for loans in default.

The total amount of support for HBCU programs, along with any accrued interest and unpaid servicing fees, will be capitalized to principal and be reamortized through the original maturity date of June 1, 2037. The Department has approximately $1.3 billion in outstanding borrowing from the FFB to support loans made to HBCU institutions and approximately $213 million obligated to support near term lending as of September 30, 2014.

The Department administers the College Housing and Academic Facilities Loan Program (CHAFL), the College Housing Loan Program, and the Higher Education Facilities Loan Program. From 1952 to 1993, these programs provided low-interest financing to institutions of higher education for the construction, reconstruction, and renovation of housing, academic, and other educational facilities.

The following schedule summarizes the principal and related interest receivables, net of the allowance for subsidy:

Facilities Loan Programs Loan Receivables, Net
(Dollars in Millions)

	2014	2013
Principal Receivable	$ 1,324	$ 1,211
Interest Receivable	12	10
Total	1,336	1,221
Allowance for Subsidy/Loss	(209)	(197)
Facilities Loan Programs Loan Receivables, Net	**$ 1,127**	**$ 1,024**

Administrative Expenses

Administrative expenses, for the periods ended September 30, 2014 and 2013, consisted of the following:

Administrative Expenses
(Dollars in Millions)

	2014		2013	
	Direct Loan Program	FFEL Program	Direct Loan Program	FFEL Program
Operating Expense	$ 604	$ 390	$ 639	$ 413
Other Expense	22	14	25	16
Total	**$ 626**	**$ 404**	**$ 664**	**$ 429**

Note 7. Property and Equipment, Net and Leases

Property and Equipment, as of September 30, 2014 and 2013, consisted of the following:

Property and Equipment, Net
(Dollars in Millions)

	2014		
	Asset Cost	Accumulated Depreciation	Net Asset Value
Information Technology, Internal Use Software, and Telecommunications Equipment	$ 181	$ (174)	$ 7
Furniture and Fixtures	3	(3)	-
Property and Equipment, Net	**$ 184**	**$ (177)**	**$ 7**

	2013		
	Asset Cost	Accumulated Depreciation	Net Asset Value
Information Technology, Internal Use Software, and Telecommunications Equipment	$ 177	$ (175)	$ 2
Furniture and Fixtures	3	(3)	-
Property and Equipment, Net	**$ 180**	**$ (178)**	**$ 2**

The Depreciation expense for the years ended September 30, 2014 and 2013 was $1 million and $6 million, respectively.

The major drivers of fixed assets at the Department are improvements to information technology, including financial management and program management systems. Specifically, recent enhancements have been made to the Department's automated grant management and financial reporting systems for the Department and FSA. The Department has acquired more robust information technology to augment its significant capabilities to manage student loan and grant operations. In addition, the Department has very limited or no acquisition cost associated with furniture and fixtures. The Department owns and maintains a few school buildings on various military bases.

All Department and contractor staff are housed in leased buildings. The Department does not own real property for the use of its staff. The Department leases office space from the General Services Administration (GSA). The lease contracts with GSA for privately and publicly owned buildings are operating leases. Future lease payments are not accrued as liabilities, and are expensed as incurred. The Department leases 22 privately owned and 8 publicly owned buildings in 19 cities. Building lease expense, as of September 30, 2014 and 2013, was $70 million and $80 million, respectively. The majority of leases is for information technology, telecommunications equipment, and leased buildings.

Estimated future minimum lease payments for the privately and publicly owned buildings are presented below.

Future Minimum Lease Payments

(Dollars in Millions)

2014		2013	
FY	**Amount**	**FY**	**Amount**
2015	78	2014	80
2016	83	2015	90
2017	88	2016	93
2018	91	2017	96
2019	97	2018	100
After 2019	100	After 2018	103
Total	**$ 537**	**Total**	**$ 562**

Note 8. Other Assets

Other Intragovernmental Assets primarily consist of advance payments to the U.S. Department of Interior's (DOI) Bureau of Indian Education under terms of an interagency agreement. Under this agreement, funds are transferred from DOI to fund initiatives that include, but are not limited to: (1) Improving Basic Programs Operated by Local Education Agencies; (2) Comprehensive School Reform; (3) Teacher Quality Improvement Formula Grants; (4) Enhancing Education through Technology; and (5) 21st Century Community Learning Centers. Other Intragovernmental Assets were $55 million and $22 million as of September 30, 2014 and 2013, respectively.

Other Assets with the public consist of payments made to grant recipients in advance of their expenditures and in-process invoices for interest benefits and special allowances for the FFEL Program. Other Assets with the public were $13 million as of September 30, 2014 and 2013.

Note 9. Accounts Payable

Accounts Payable, as of September 30, 2014 and 2013, consisted of the following:

Accounts Payable
(Dollars in Millions)

	2014	2013
Accrual for Unreimbursed Loan Disbursements	$ 3,027	$ 2,923
In Process Disbursements:		
Direct Loans	312	573
Grants	264	366
FFEL Claim Payments	311	52
Contractual Services	212	228
Other	(126)	(15)
Accounts Payable to the public	**4,000**	**4,127**
Intragovernmental Accounts Payable	1	2
Total Accounts Payable	**$ 4,001**	**$ 4,129**

Accounts Payable to the public primarily consists of in-process grant and loan disbursements, including an accrued liability for schools that have disbursed loans prior to requesting funds. The Department pays vendor invoices according to the Prompt Payment Act rules that are built into the financial system as a control mechanism, generally within 25–30 days of receipt of goods and proper invoicing. The Department also monitors and leverages vendor discount opportunities by processing payments to coincide with discount terms when possible.

FY 2014 Accounts Payable Other abnormal balance of $(126) million is primarily due to a temporary adjustment related to FFEL Guaranteed Loan Program collections of fees, principal, and interest on defaulted loans.

Note 10. Debt

Debt, as of September 30, 2014 and 2013, consisted of the following:

Debt
(Dollars in Millions)

	2014			
	Beginning Balance	Borrowing	Repayments	Ending Balance
Treasury Debt				
Direct Loan Program	$ 698,361	$ 171,227	$ (50,581)	$ 819,007
FFEL Program				
Guaranteed Loan Program	43,254	-	-	43,254
Loan Purchase Commitment	38,598	976	(3,303)	36,271
Loan Participation Purchase	68,017	790	(4,505)	64,302
ABCP Conduit	2,543	203	(773)	1,973
TEACH Program	485	99	(29)	555
Facilities Loan Programs	37	-	-	37
Total Treasury Debt	**851,295**	**173,295**	**(59,191)**	**965,399**
Debt to the FFB				
HBCU	1,137	156	(21)	1,272
Total Debt to the FFB	**1,137**	**156**	**(21)**	**1,272**
Total	**$ 852,432**	**$ 173,451**	**$ (59,212)**	**$966,671**

	2013			
	Beginning Balance	Borrowing	Repayments	Ending Balance
Treasury Debt				
Direct Loan Program	$ 549,332	$ 177,682	$ (28,653)	$ 698,361
FFEL Program				
Guaranteed Loan Program	43,254	-	-	43,254
Loan Purchase Commitment	42,341	602	(4,345)	38,598
Loan Participation Purchase	77,292	519	(9,794)	68,017
ABCP Conduit	1,735	1,000	(192)	2,543
TEACH Program	370	128	(13)	485
Facilities Loan Programs	45	-	(8)	37
Total Treasury Debt	**714,369**	**179,931**	**(43,005)**	**851,295**
Debt to the FFB				
HBCU	934	225	(22)	1,137
Total Debt to the FFB	**934**	**225**	**(22)**	**1,137**
Total	**$ 715,303**	**$ 180,156**	**$ (43,027)**	**$ 852,432**

The Department borrows from Treasury to fund the disbursement of new loans and the payment of credit program outlays and related costs. During FY 2014, debt increased 13 percent from $852 billion in the prior year to $967 billion. The Department makes periodic principal payments after considering the cash position and liability for future outflows in each cohort of loans, as mandated by the FCRA.

Over 84 percent of the Department’s debt, as of September 30, 2014, is attributable to the Direct Loan Program. The majority of the net borrowing activity (borrowing less repayments) for the year was designated for funding new Direct Loan disbursements. Net borrowing in the Direct Loan Program for FY 2014 totaled $121 billion. The new financing was used to disburse new loans and make negative subsidy transfers. The Department also borrowed funding to execute the downward subsidy re-estimate on the entire portfolio and to pay its interest to Treasury at year-end. Principal payments were made during the year. FFEL and some Facilities Loan Programs are no longer offering new financing to public borrowers or entering into guaranty agreements with lending authorities.

The Department also borrows from Treasury for activity in the TEACH and HBCU Programs. During FY 2014, TEACH net borrowing of $70 million was used for the advance of new grants and repayments of principal made to Treasury. In FY 2014, debt in HBCU increased by $135 million, or 12 percent. This total represents the aggregate of new bonds administered and repayments made on previously issued bonds.

Note 11. Other Liabilities

Other Liabilities, as of September 30, 2014 and 2013, consisted of the following:

Other Liabilities

(Dollars in Millions)

	2014		2013	
	Intragovern-mental	With the Public	Intragovern-mental	With the Public
Liabilities Covered by Budgetary Resources				
Current				
Advances From Others	$ 26	$ -	$ 29	$ -
Employer Contributions and Payroll Taxes	3	-	6	-
Liability for Deposit Funds and Clearing Accounts	(22)	74	7	37
Accrued Payroll and Benefits	-	13	-	28
Deferred Revenue	-	50	-	31
Liabilities in Miscellaneous Receipt Accounts	3,783	-	6,074	-
Total Other Liabilities Covered by Budgetary Resources	**3,790**	**137**	**6,116**	**96**
Liabilities Not Covered by Budgetary Resources				
Current				
Accrued Unfunded Annual Leave	-	38	-	36
Non-Current				
Accrued Unfunded FECA Liability	3	-	4	-
Custodial Liability	2	-	2	-
Liabilities in Miscellaneous Receipt Accounts	376	-	358	-
Capital Transfers	2,242	-	2,375	-
Accrued FECA Actuarial Liability	-	2	-	15
Total Other Liabilities Not Covered by Budgetary Resources	**2,623**	**40**	**2,739**	**51**
Other Liabilities	**$ 6,413**	**$ 177**	**$ 8,855**	**$ 147**

Other liabilities include current and non-current liabilities. The current liabilities covered by budgetary resources primarily consist of $3.7 billion for downward subsidy re-estimates, which, when executed, will be paid to the General Fund of the Treasury.

The non-current liabilities not covered by budgetary resources primarily relate to capital transfers, excess unanticipated collections on defaulted loans in liquidating accounts in the amount of $2.2 billion, and the student loan receivables of the Federal Perkins Loan Program in the amount of $376 million.

Liabilities Not Covered by Budgetary Resources

Liabilities not covered by budgetary resources include liabilities for which congressional action is needed before budgetary resources can be provided. Although future appropriations to fund these liabilities are likely, it is not certain that appropriations will be enacted to fund these liabilities. Liabilities not covered by budgetary resources totaled $2.6 billion and $2.7 billion as of September 30, 2014 and 2013, respectively.

As of September 30, 2014 and 2013, liabilities totaled $981.2 billion and $869.2 billion, respectively. Of this amount, liabilities covered by budgetary resources totaled $978.6 billion and $866.4 billion as of September 30, 2014 and 2013, respectively.

Note 12. Accrued Grant Liability

The Accrued Grant Liability by major program office, as of September 30, 2014 and 2013, consisted of the following:

Accrued Grant Liability
(Dollars in Millions)

	2014	2013
FSA	$ 1,719	$ 1,727
OESE	386	145
OSERS	182	120
Other	200	178
Accrued Grant Liability	**$ 2,487**	**$ 2,170**

The majority of Accrued Grant Liability is composed of Pell Grants. The remaining Accrued Grant Liability also includes Discretionary, Formula, and Campus-Based Student Aid Grants.

Note 13. Net Position

Unexpended appropriations, as of September 30, 2014 and 2013, consisted of the following:

Unexpended Appropriations
(Dollars in Millions)

	2014	2013
Unobligated Balances:		
Available	$ 12,078	$ 13,700
Not Available	1,169	909
Undelivered Orders	53,200	56,762
Unexpended Appropriations	**$ 66,447**	**$ 71,371**

Cumulative Results of Operations. The Cumulative Results of Operations of $(23,741) million and $(3,528) million as of September 30, 2014 and 2013, respectively, consists mostly of unfunded upward subsidy re-estimates for Direct and FFEL Loan Programs, other unfunded expenses, and net investments of capitalized assets.

Other Financing Sources. Negative Subsidy Transfers, Downward Subsidy Re-estimates, and Other in the Other Financing Sources section of the Statement of Changes in Net Position was $(36,767) million and $(51,054) million as of September 30, 2014 and 2013, respectively. The amount was primarily comprised of Direct Loan and FFEL Program activity.

Appropriations Received. Appropriations Received was $95,293 million and $90,993 million as of September 30, 2014 and 2013, respectively, and comprised primarily of Pell Grant, Direct Loan, Special Education, and Education for the Disadvantaged Programs.

Note 14. Intragovernmental Cost and Exchange Revenue by Program

As required by the *GPRA Modernization Act of 2010*, each of the Department's major program offices have been aligned with the goals presented in the Department's *Strategic Plan 2014–2018*. Strategic Plan Goals 1–5 guide the Department's program offices to carry out the vision and programmatic mission, and the net cost programs can be specifically associated with these five strategic goals. The Department also has a cross-cutting Strategic Plan Goal 6, U.S. Department of Education Capacity, focusing primarily upon improving the organizational capacities of the Department to implement the Strategic Plan Goals 1–5. The costs associated with Strategic Plan Goal 6 are allocated to Goals 1–5 based on the number of full-time employee equivalents of each program. Some principal offices support more than one Departmental Strategic Goal, but have been assigned to a single net cost program for the purposes of this table based on their primary area of support. The change of $50 billion in Increase College Access, Quality, and Completion Gross Cost from FY 2013 to FY 2014 is primarily due to an upward subsidy re-estimate for the Direct Loan Program of $30 billion.

Net Cost Program	Program Office	Strategic Goal
Increase College Access, Quality, and Completion	FSA OPE OCTAE	**Goal 1: Postsecondary Education, Career and Technical Education, and Adult Education.** Increase college access, affordability, quality, and completion by improving postsecondary education and lifelong learning opportunities for youths and adults.
Improve Preparation for College and Career from Birth Through 12th Grade, Especially for Children with High Needs	OESE HR	**Goal 2: Elementary and Secondary Education.** Improve the elementary and secondary education system's ability to consistently deliver excellent instruction aligned with rigorous academic standards while providing effective support services to close achievement and opportunity gaps, and ensure all students graduate high school college- and career-ready. **Goal 3: Early Learning.** Improve the health, social-emotional, and cognitive outcomes for all children from birth through 3rd grade, so that all children, particularly those with high needs, are on track for graduating from high school college- and career-ready.
Ensure Effective Educational Opportunities for All Students	OELA OCR OSERS	**Goal 4: Equity.** Increase educational opportunities for underserved students and reduce discrimination so that all students are well-positioned to succeed.
Enhance the Education System's Ability to Continuously Improve	IES OII	**Goal 5: Continuous Improvement of the U.S. Education System.** Enhance the education system's ability to continuously improve through better and more widespread use of data, research and evaluation, evidence, transparency, innovation, and technology.

Gross Cost and Exchange Revenue by Program
(Dollars in Millions)
2014

	FSA	OESE	OSERS	Other	Total
Increase College Access, Quality, and Completion					
Gross Cost					
Intragovernmental	$ 31,267	$ -	$ -	$ 87	$31,354
With the Public	34,203	-	-	4,189	38,392
Total Gross Program Costs	**65,470**	**-**	**-**	**4,276**	**69,746**
Earned Revenue					
Intragovernmental	(4,293)	-	-	(12)	(4,305)
With the Public	(24,686)	-	-	(40)	(24,726)
Total Program Earned Revenue	**(28,979)**	**-**	**-**	**(52)**	**(29,031)**
Total Program Cost	**36,491**	**-**	**-**	**4,224**	**40,715**
Improve Preparation for College and Career from Birth Through 12th Grade, Especially for Children with High Needs					
Gross Cost					
Intragovernmental	-	202	-	-	202
With the Public	-	23,196	-	4	23,200
Total Gross Program Costs	**-**	**23,398**	**-**	**4**	**23,402**
Earned Revenue					
Intragovernmental	-	(4)	-	-	(4)
With the Public	-	(11)	-	-	(11)
Total Program Earned Revenue	**-**	**(15)**	**-**	**-**	**(15)**
Total Program Cost	**-**	**23,383**	**-**	**4**	**23,387**
Ensure Effective Educational Opportunities for All Students					
Gross Cost					
Intragovernmental	-	-	115	30	145
With the Public	-	-	16,146	810	16,956
Total Gross Program Costs	**-**	**-**	**16,261**	**840**	**17,101**
Earned Revenue					
Intragovernmental	-	-	(2)	-	(2)
With the Public	-	-	(12)	(1)	(13)
Total Program Earned Revenue	**-**	**-**	**(14)**	**(1)**	**(15)**
Total Program Cost	**-**	**-**	**16,247**	**839**	**17,086**
Enhance the Education System's Ability to Continuously Improve					
Gross Cost					
Intragovernmental	-	-	-	114	114
With the Public	-	-	-	1,932	1,932
Total Gross Program Costs	**-**	**-**	**-**	**2,046**	**2,046**
Earned Revenue					
Intragovernmental	-	-	-	(3)	(3)
With the Public	-	-	-	(61)	(61)
Total Program Earned Revenue	**-**	**-**	**-**	**(64)**	**(64)**
Total Program Cost	**-**	**-**	**-**	**1,982**	**1,982**
Net Cost of Operations	**$36,491**	**$23,383**	**$16,247**	**$7,049**	**$83,170**

Gross Cost and Exchange Revenue by Program

(Dollars in Millions)

2013

	FSA	OESE	OSERS	Other	Total
Increase College Access, Quality, and Completion					
Gross Cost					
Intragovernmental	$ 28,513	$ -	$ -	$ 85	$28,598
With the Public	(15,247)	-	-	4,255	(10,992)
Total Gross Program Costs	**13,266**	**-**	**-**	**4,340**	**17,606**
Earned Revenue					
Intragovernmental	(3,685)	-	-	(12)	(3,697)
With the Public	(23,003)	-	-	(44)	(23,047)
Total Program Earned Revenue	**(26,688)**	**-**	**-**	**(56)**	**(26,744)**
Total Program Cost	**(13,422)**	**-**	**-**	**4,284**	**(9,138)**
Improve Preparation for College and Career from Birth Through 12th Grade, Especially for Children with High Needs					
Gross Cost					
Intragovernmental	-	188	-	-	188
With the Public	-	24,676	-	7	24,683
Total Gross Program Costs	**-**	**24,864**	**-**	**7**	**24,871**
Earned Revenue					
Intragovernmental	-	(2)	-	-	(2)
With the Public	-	(23)	-	-	(23)
Total Program Earned Revenue	-	(25)	-	-	(25)
Total Program Cost	**-**	**24,839**	**-**	**7**	**24,846**
Ensure Effective Educational Opportunities for All Students					
Gross Cost					
Intragovernmental	-	-	48	30	78
With the Public	-	-	16,022	770	16,792
Total Gross Program Costs	**-**	**-**	**16,070**	**800**	**16,870**
Earned Revenue					
Intragovernmental	-	-	(1)	-	(1)
With the Public	-	-	(24)	(1)	(25)
Total Program Earned Revenue	**-**	**-**	**(25)**	**(1)**	**(26)**
Total Program Cost	**-**	**-**	**16,045**	**799**	**16,844**
Enhance the Education System's Ability to Continuously Improve					
Gross Cost					
Intragovernmental	-	-	-	62	62
With the Public	-	-	-	1,944	1,944
Total Gross Program Costs	**-**	**-**	**-**	**2,006**	**2,006**
Earned Revenue					
Intragovernmental	-	-	-	(2)	(2)
With the Public	-	-	-	(84)	(84)
Total Program Earned Revenue	**-**	**-**	**-**	**(86)**	**(86)**
Total Program Cost	**-**	**-**	**-**	**1,920**	**1,920**
Net Cost of Operations	**$(13,422)**	**$24,839**	**$16,045**	**$7,010**	**$34,472**

Note 15. Interest Expense and Interest Revenue

For FY 2014 and FY 2013, interest expense and interest revenue by program consisted of the following:

Interest Expense and Interest Revenue
(Dollars in Millions)

	2014					
	Expenses			**Revenue**		
	Federal	**Non-federal**	**Total**	**Federal**	**Non-federal**	**Total**
Direct Loan Program	$ 25,152	$ -	$25,152	$ 3,670	$ 21,482	$25,152
FFEL Program :						
Guaranteed Loan Program	2,083	(1,843)	240	240	-	240
Loan Purchase Commitment	1,163	-	1,163	64	1,099	1,163
Loan Participation Purchase	2,102	-	2,102	119	1,983	2,102
ABCP Conduit	75	-	75	14	61	75
TEACH Program	18	-	18	2	16	18
Other Programs	35	-	35	11	40	51
Total	**$ 30,628**	**$ (1,843)**	**$28,785**	**$ 4,120**	**$ 24,681**	**$28,801**

	2013					
	Expenses			**Revenue**		
	Federal	**Non-federal**	**Total**	**Federal**	**Non-federal**	**Total**
Direct Loan Program	$ 22,661	$ -	$22,661	$ 3,409	$ 19,252	$22,661
FFEL Program :						
Guaranteed Loan Program	2,083	(1,783)	300	300	-	300
Loan Purchase Commitment	1,244	-	1,244	79	1,165	1,244
Loan Participation Purchase	2,293	-	2,293	203	2,090	2,293
ABCP Conduit	124	-	124	44	80	124
TEACH Program	16	-	16	2	14	16
Other Programs	31	-	31	12	31	43
Total	**$ 28,452**	**$ (1,783)**	**$26,669**	**$ 4,049**	**$ 22,632**	**$26,681**

Federal interest expense is recognized on the Department's outstanding borrowing from Treasury (debt). The Direct Loan and FFEL Programs have $819 billion and $146 billion in debt, respectively, as of September 30, 2014. Federal Interest Revenue is earned on Fund Balance with Treasury for the Direct Loan and FFEL Programs. The interest rate set by OMB is the same for interest expense and interest revenue.

Non-federal interest expense results from the amortization of loan subsidy. Non-federal interest revenue is interest earned from the public on Credit Program Receivables held by the Department. The Credit Program Receivable net balances for the Direct Loan and FFEL Programs are $779 billion and $143 billion, respectively, as of September 30, 2014.

Note 16. Statement of Budgetary Resources

The SBR compares budgetary resources with the status of those resources. As of September 30, 2014, budgetary resources were $356 billion and net agency outlays were $180 billion. As of September 30, 2013, budgetary resources were $360 billion and net agency outlays were $189 billion.

Obligations Incurred by Apportionment Type and Category

Obligations incurred by apportionment type and category, as of September 30, 2014 and 2013, consisted of the following:

Obligations Incurred by Apportionment Type and Category

(Dollars in Millions)

	2014	2013
Direct:		
Category A	$ 1,755	$ 1,607
Category B	329,043	330,477
Exempt from Apportionment	194	280
Total Direct Apportionment	330,992	332,364
Reimbursable:		
Category A	3	4
Category B	68	49
Obligations Incurred	**$ 331,063**	**$ 332,417**

Obligations incurred can be either direct or reimbursable. Reimbursable obligations are those financed by offsetting collections received in return for goods and services provided, while all other obligations are direct. The apportionment categories are determined in accordance with the guidance provided in OMB regulations. Category A apportionments are those resources that can be obligated without restriction on the purpose of the obligation, other than to be in compliance with legislation underlying programs for which the resources were made available. Category B apportionments are restricted by purpose for which obligations can be incurred. In addition, some resources are available without apportionment by OMB.

Unused Borrowing Authority

Unused borrowing authority and related changes in available borrowing authority, as of September 30, 2014 and 2013, consisted of the following:

Unused Borrowing Authority

(Dollars in Millions)

	2014	2013
Beginning Balance, Unused Borrowing Authority	**$ 138,695**	**$ 145,532**
Current Year Borrowing Authority	182,860	195,185
Funds Drawn From Treasury	(173,451)	(180,156)
Borrowing Authority Withdrawn	(86,777)	(21,866)
Ending Balance, Unused Borrowing Authority	**$ 61,327**	**$ 138,695**

The Department is given authority to draw funds from Treasury to finance the Direct Loan, FFEL, TEACH, and other loan programs. Unused Borrowing Authority is a budgetary resource and is available to support obligations for these programs. The Department periodically reviews its borrowing authority balances in relation to its obligations and may cancel unused amounts.

Undelivered Orders at the End of the Period

Undelivered orders, as of September 30, 2014 and 2013, consisted of the following:

Undelivered Orders
(Dollars in Millions)

	2014	2013
Budgetary	$ 53,332	$ 56,901
Non-Budgetary	76,889	158,703
Undelivered Orders (Unpaid)	**$ 130,221**	**$ 215,604**

Undelivered orders at the end of the period, as presented above, will differ from the undelivered orders included in Unexpended Appropriations. Undelivered orders represent the amount of goods and/or services ordered which have not been actually or constructively received. This amount includes any orders which may have been prepaid or advanced but for which delivery or performance has not yet occurred. Undelivered orders for trust funds, reimbursable agreements, and federal financing and liquidating funds are not funded through appropriations and are not included in Unexpended Appropriations. (See Note 13)

Distributed Offsetting Receipts

The majority of the Distributed Offsetting Receipts line item on the SBR represents amounts paid from the Direct Loan Program and FFEL Program Financing Accounts to general fund receipt accounts for downward current fiscal year executed subsidy re-estimates and negative subsidies. Distributed Offsetting Receipts, for the years ended September 30, 2014 and 2013, consisted of the following:

Distributed Offsetting Receipts
(Dollars in Millions)

	2014	2013
Negative Subsidies and Downward Re-estimates:		
FFEL Program	$ 7,945	$ 9,946
Direct Loan Program	31,551	38,436
Facilities Loan Programs	24	198
TEACH Program	13	17
Total Negative Subsidies and Downward Re-estimates	39,533	48,597
Other	119	128
Distributed Offsetting Receipts	**$ 39,652**	**$ 48,725**

Explanation of Differences Between the Statement of Budgetary Resources and the *Budget of the United States Government*

The FY *2016 Budget of the United States Government* (President's Budget), which presents the actual amounts for the year ended September 30, 2014, has not been published as of the issue date of these financial statements. The FY 2016 President's Budget is scheduled for release in February 2015.

A reconciliation of the FY 2013 SBR to the FY 2015 President's Budget (FY 2013 actual amounts) for budgetary resources, obligations incurred, distributed offsetting receipts, and net agency outlays is presented below.

SBR to *Budget of the United States Government*

(Dollars in Millions)

	Budgetary Resources	Obligations Incurred	Distributed Offsetting Receipts	Net Outlays
Combined Statement of Budgetary Resources	**$ 359,939**	**$ 332,417**	**$ 48,725**	**$ 189,379**
Expired Funds	(1,473)	(575)	-	-
Amounts Included in the President's Budget	14,097	14,091	-	-
Amounts Excluded from President's Budget and Rounding	(4)	(1)	(9)	-
Distributed Offsetting Receipts	-	-	-	48,725
***Budget of the United States Government*[1]**	**$ 372,559**	**$ 345,932**	**$ 48,716**	**$ 238,104**

[1]Amounts obtained from the Appendix, *Budget of the United States Government*, FY 2015.

The President's Budget includes a public enterprise fund that reflects the gross obligations by the FFEL Program for the estimated activity of the consolidated Federal Fund of the guaranty agencies. Reconciling differences are caused by the presentation style of the President's Budget, which excludes Budgetary Resources, Obligations Incurred and Unobligated Balances in expired annual funds, as well as offsetting collections, which are required for reporting on the SBR. Ownership by the federal government is independent of the actual control of the assets. Since the actual operation of the Federal Fund is independent from the Department's direct control, budgetary resources and obligations are estimated and disclosed in the President's Budget to approximate the gross activities of the combined Federal Fund. Amounts reported on the FY 2013 SBR for the Federal Fund are compiled through combining all guaranty agencies' annual reports to determine a net valuation amount for the Federal Fund.

Note 17. Reconciliation of Net Cost of Operations to Budget

The Reconciliation of Net Cost of Operations to Budget reconciles the resources used to finance activities, both those received through budgetary resources and those received through other means, with the Net Cost of Operations on the Statement of Net Cost. This reconciliation provides an explanation of the differences between budgetary and financial (proprietary) accounting, as required by FASAB Standard No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*.

Resources Used to Finance Activities (section one) are reconciled with the net cost of operations by: (a) excluding Resources Used or Generated for Items Not Part of the Net Cost of Operations (section two); and (b) including Components of the Net Cost of Operations That Will Not Require or Generate Resources in the Current Period (section three). The primary resources used to finance activities that do not fund the net cost of operations include the acquisition of net credit program assets, the liquidation of liabilities for loan guarantees, and subsidy re-estimates accrued in the prior period. Significant components of the net cost of operations that will not generate or use resources in the current period include subsidy amortization, interest on the liability for loan guarantees, and increases in exchange revenue receivable from the public.

The Reconciliation of Net Cost of Operations to Budget, as of September 30, 2014 and 2013, are presented below:

Reconciliation of Net Cost of Operations to Budget

(Dollars in Millions)

	2014	2013
Resources Used to Finance Activities:		
Obligations Incurred	$ 331,063	$ 332,417
Spending Authority from Offsetting Collections and Recoveries	(196,485)	(110,224)
Offsetting Receipts	(39,652)	(48,725)
Net Budgetary Resources Obligated	**94,926**	**173,468**
Imputed Financing from Costs Absorbed by Others	36	34
Other Financing Sources	(36,767)	(51,054)
Net Other Resources	**(36,731)**	**(51,020)**
Net Resources Used to Finance Activities	**58,195**	**122,448**
Resources Used or Generated for Items Not Part of the Net Cost of Operations:		
(Increase)/Decrease in Budgetary Resources Obligated but Not Yet Provided	85,345	14,721
Resources that Fund Subsidy Re-estimates Accrued in Prior Period	2,383	(3,922)
Credit Program Collections	80,365	58,352
Acquisition of Fixed Assets	(4)	(1)
Acquisition of Net Credit Program Assets or Liquidation of Liabilities for Loan Guarantees	(186,999)	(191,789)
Resources from Non-Entity Activity	36,787	51,229
Net Resources That Do Not Finance the Net Cost of Operations	**17,877**	**(71,410)**
Net Resources Used to Finance the Net Cost of Operations	**76,072**	**51,038**
Components of the Net Cost of Operations That Will Not Require or Generate Resources in the Current Period:		
Change in Depreciation	(1)	6
Subsidy Amortization and Interest on the Liability for Loan Guarantees	11,615	8,109
Other	581	27
Total Components Not Requiring or Generating Resources	**12,195**	**8,142**
Increase/(Decrease) in Annual Leave Liability	2	(1)
Accrued Re-estimates of Credit Subsidy Expense	20,130	(2,382)
Increase in Exchange Revenue Receivable from the Public	(25,233)	(22,288)
Change in Accrued Interest with Treasury	2	2
Other	2	(39)
Total Components Requiring or Generating Resources in Future Periods	**(5,097)**	**(24,708)**
Total Components That Will Not Require or Generate Resources in the Current Period	**7,098**	**(16,566)**
Net Cost of Operations	**$ 83,170**	**$ 34,472**

Note 18. Incidental Custodial Collections

The Department administers certain activities associated with the collection of non-exchange revenues. The Department collects these amounts in a custodial capacity and transfers the amounts collected to the General Fund of the Treasury at the end of each fiscal year. These collections primarily consist of penalties on accounts receivable and are considered incidental to the primary mission of the Department. During FY 2014 and FY 2013, the Department collected $2.0 million and $0.1 million, respectively, in custodial revenues.

Note 19. Contingencies

The Department discloses contingencies where any of the conditions for liability recognition are not met and there is at least a reasonable possibility that a loss or an additional loss may have been incurred in accordance with FASAB Standard No. 5, *Accounting for Liabilities of the Federal Government*. The following commitments are amounts for contractual arrangements that may require future financial obligations.

Guaranty Agencies

The Department may assist guaranty agencies experiencing financial difficulties. No provision has been made in the financial statements for potential liabilities. The Department has not done so in fiscal years 2014 or 2013 and does not expect to in future years.

Federal Perkins Loan Program

The Federal Perkins Loan Program provides financial assistance to eligible postsecondary school students. In FY 2014, the Department provided funding of 82.8 percent of the capital used to make loans to eligible students through participating schools at 5 percent interest. The schools provided the remaining 17.2 percent of program funding. For the latest academic year that ended June 30, 2014, approximately 538 thousand loans were made totaling $1.2 billion at 1,486 institutions, making an average of $2,170 per loan. The Department's equity interest was approximately $6.7 billion as of September 30, 2014.

Federal Perkins Loan Program borrowers who meet statutory eligibility requirements—such as those who provide service as teachers in low-income areas or as Peace Corps or AmeriCorps VISTA volunteers, as well as those who serve in the military, law enforcement, nursing, or family services—may receive partial loan forgiveness for each year of qualifying service.

Litigation and Other Claims

The Department is involved in various lawsuits incidental to its operations. In the opinion of management, the ultimate resolution of pending litigation will not have a material effect on the Department's financial position.

Other Matters

Some portion of the current-year financial assistance expenses (grants) may include funded recipient expenditures that are subsequently disallowed through program review or audit processes. In the opinion of management, the ultimate disposition of these matters will not have a material effect on the Department's financial position.

United States Department of Education
Combining Statement of Budgetary Resources
For the Year Ended September 30, 2014

(Dollars in Millions)

	Combined		Federal Student Aid		Office of Elementary and Secondary Education	Office of Special Education and Rehabilitative Services	Other	
	Budgetary	Non-Budgetary Credit Reform Financing Accounts	Budgetary	Non-Budgetary Credit Reform Financing Accounts	Budgetary	Budgetary	Budgetary	Non-Budgetary Credit Reform Financing Accounts
Budgetary Resources:								
Unobligated Balance, Brought Forward, October 1	$ 16,207	$ 11,315	$ 13,950	$ 11,072	$ 793	$ 335	$ 1,129	$ 243
Recoveries of Prior Year Unpaid Obligations	1,131	97,274	464	97,274	433	138	96	-
Other Changes in Unobligated Balance (+ or -)	(372)	(99,811)	(148)	(99,806)	(99)	(43)	(82)	(5)
Unobligated Balance from Prior Year Budget Authority, Net	$ 16,966	$ 8,778	$ 14,266	$ 8,540	$ 1,127	$ 430	$ 1,143	$ 238
Appropriations (Discretionary and Mandatory)	95,004	581	49,854	581	21,634	16,150	7,366	-
Borrowing Authority (Discretionary and Mandatory) (Note 16)	-	182,860	-	182,749	-	-	-	111
Spending Authority from Offsetting Collections (Discretionary and Mandatory)	473	51,347	411	51,281	-	2	60	66
Total Budgetary Resources (Note 16)	**$ 112,443**	**$ 243,566**	**$ 64,531**	**$ 243,151**	**$ 22,761**	**$ 16,582**	**$ 8,569**	**$ 415**
Status of Budgetary Resources:								
Obligations Incurred (Note 16)	$ 97,606	$ 233,457	$ 51,889	$ 233,294	$ 21,925	$ 16,273	$ 7,519	$ 163
Unobligated Balance, End of Year:								
Apportioned	12,125	69	10,617	69	686	49	773	-
Unapportioned	2,712	10,040	2,025	9,788	150	260	277	252
Total Unobligated Balance, End of Year	$ 14,837	$ 10,109	$ 12,642	$ 9,857	$ 836	$ 309	$ 1,050	$ 252
Total Status of Budgetary Resources (Note 16)	**$ 112,443**	**$ 243,566**	**$ 64,531**	**$ 243,151**	**$ 22,761**	**$ 16,582**	**$ 8,569**	**$ 415**
Change in Obligated Balance:								
Unpaid Obligations								
Unpaid Obligations, Brought Forward, October 1	$ 59,630	$ 161,747	$ 23,380	$ 161,488	$ 17,557	$ 8,858	$ 9,835	$ 259
Obligations Incurred	97,606	233,457	51,889	233,294	21,925	16,273	7,519	163
Outlays (Gross) (-)	(99,886)	(217,614)	(53,339)	(217,404)	(23,101)	(16,072)	(7,374)	(210)
Recoveries of Prior Year Unpaid Obligations (-)	(1,131)	(97,274)	(464)	(97,274)	(433)	(138)	(96)	-
Unpaid Obligations, End of Year	**$ 56,219**	**$ 80,316**	**$ 21,466**	**$ 80,104**	**$ 15,948**	**$ 8,921**	**$ 9,884**	**$ 212**
Uncollected Payments								
Uncollected Payments, Federal Sources, Brought Forward, October 1 (-)	$ (3)	$ (25)	$ -	$ (3)	$ -	$ -	$ (3)	$ (22)
Change in Uncollected Payments, Federal Sources (+ or -)	2	(1)	-	(1)	-	-	2	-
Uncollected Payments, Federal Sources, End of Year (-)	$ (1)	$ (26)	$ -	$ (4)	$ -	$ -	$ (1)	$ (22)
Memorandum (Non-add) Entries								
Obligated Balance, Start of Year (+ or -)	**$ 59,627**	**$ 161,722**	**$ 23,380**	**$ 161,485**	**$ 17,557**	**$ 8,858**	**$ 9,832**	**$ 237**
Obligated Balance, End of Year (+ or -)	**$ 56,218**	**$ 80,290**	**$ 21,466**	**$ 80,100**	**$ 15,948**	**$ 8,921**	**$ 9,883**	**$ 190**
Budget Authority and Outlays, Net:								
Budget Authority, Gross (Discretionary and Mandatory)	$ 95,477	$ 234,788	$ 50,265	$ 234,611	$ 21,634	$ 16,152	$ 7,426	$ 177
Actual Offsetting Collections (Discretionary and Mandatory) (-)	(624)	(97,463)	(542)	(97,375)	-	(2)	(80)	(88)
Change in Uncollected Customer Payments from Federal Sources (Discretionary and Mandatory) (+ or -)	2	(1)	-	(1)	-	-	2	-
Budget Authority, Net (Discretionary and Mandatory)	**$ 94,855**	**$ 137,324**	**$ 49,723**	**$ 137,235**	**$ 21,634**	**$ 16,150**	**$ 7,348**	**$ 89**
Outlays, Gross (Discretionary and Mandatory)	$ 99,886	$ 217,614	$ 53,339	$ 217,404	$ 23,101	$ 16,072	$ 7,374	$ 210
Actual Offsetting Collections (Discretionary and Mandatory) (-)	(624)	(97,463)	(542)	(97,375)	-	(2)	(80)	(88)
Outlays, Net (Discretionary and Mandatory)	99,262	120,151	52,797	120,029	23,101	16,070	7,294	122
Distributed Offsetting Receipts (-) (Note 16)	(39,652)	-	(39,559)	-	-	-	(93)	-
Agency Outlays, Net (Discretionary and Mandatory) (Note 16)	**$ 59,610**	**$ 120,151**	**$ 13,238**	**$ 120,029**	**$ 23,101**	**$ 16,070**	**$ 7,201**	**$ 122**

United States Department of Education
Combining Statement of Budgetary Resources
For the Year Ended September 30, 2013

(Dollars in Millions)

	Combined		Federal Student Aid		Office of Elementary and Secondary Education	Office of Special Education and Rehabilitative Services	American Recovery and Reinvestment Act and Education Jobs Fund	Other	
	Budgetary	Non-Budgetary Credit Reform Financing Accounts	Budgetary	Non-Budgetary Credit Reform Financing Accounts	Budgetary	Budgetary	Budgetary	Budgetary	Non-Budgetary Credit Reform Financing Accounts
Budgetary Resources:									
Unobligated Balance, Brought Forward, October 1	$ 12,622	$ 18,993	$ 10,366	$ 18,579	$ 802	$ 314	$ 30	$ 1,110	$ 414
Recoveries of Prior Year Unpaid Obligations	1,191	35,425	358	35,425	556	110	56	111	-
Other Changes in Unobligated Balance (+ or -)	(428)	(39,189)	(266)	(39,189)	(72)	(33)	-	(57)	-
Unobligated Balance from Prior Year Budget Authority, Net	$ 13,385	$ 15,229	$ 10,458	$ 14,815	$ 1,286	$ 391	$ 86	$ 1,164	$ 414
Appropriations (Discretionary and Mandatory)	88,380	5	44,578	-	20,819	15,622	-	7,361	5
Borrowing Authority (Discretionary and Mandatory) (Note 16)	-	195,185	-	194,970	-	-	-	-	215
Spending Authority from Offsetting Collections (Discretionary and Mandatory)	779	46,976	711	46,926	-	2	-	66	50
Total Budgetary Resources (Note 16)	**$ 102,544**	**$ 257,395**	**$ 55,747**	**$ 256,711**	**$ 22,105**	**$ 16,015**	**$ 86**	**$ 8,591**	**$ 684**
Status of Budgetary Resources:									
Obligations Incurred (Note 16)	$ 86,337	$ 246,080	$ 41,797	$ 245,639	$ 21,314	$ 15,730	$ 2	$ 7,494	$ 441
Unobligated Balance, End of Year:									
Apportioned	13,700	-	11,952	-	665	154	-	929	-
Unapportioned	2,507	11,315	1,998	11,072	126	131	84	168	243
Total Unobligated Balance, End of Year	$ 16,207	$ 11,315	$ 13,950	$ 11,072	$ 791	$ 285	$ 84	$ 1,097	$ 243
Total Status of Budgetary Resources (Note 16)	**$ 102,544**	**$ 257,395**	**$ 55,747**	**$ 256,711**	**$ 22,105**	**$ 16,015**	**$ 86**	**$ 8,591**	**$ 684**
Change in Obligated Balance:									
Unpaid Obligations									
Unpaid Obligations, Brought Forward, October 1	$ 65,057	$ 172,230	$ 24,093	$ 171,959	$ 15,902	$ 9,248	$ 6,115	$ 9,699	$ 271
Obligation Incurred	86,337	246,080	41,797	245,639	21,314	15,730	2	7,494	441
Outlays (Gross) (-)	(90,573)	(221,138)	(42,153)	(220,685)	(22,389)	(16,032)	(2,612)	(7,387)	(453)
Recoveries of Prior Year Unpaid Obligations (-)	(1,191)	(35,425)	(358)	(35,425)	(556)	(110)	(56)	(111)	-
Unpaid Obligations, End of Year	**$ 59,630**	**$ 161,747**	**$ 23,379**	**$ 161,488**	**$ 14,271**	**$ 8,836**	**$ 3,449**	**$ 9,695**	**$ 259**
Uncollected Payments									
Uncollected Payments, Federal Sources, Brought Forward, October 1 (-)	$ (2)	$ (26)	$ -	$ (4)	$ -	$ -	$ -	$ (2)	$ (22)
Change in Uncollected Payments, Federal Sources (+ or -)	(1)	1	-	1	-	-	-	(1)	-
Uncollected Payments, Federal Sources, End of Year (-)	$ (3)	$ (25)	$ -	$ (3)	$ -	$ -	$ -	$ (3)	$ (22)
Memorandum (Non-add) Entries									
Obligated Balance, Start of Year (+ or -)	**$ 65,055**	**$ 172,204**	**$ 24,093**	**$ 171,955**	**$ 15,902**	**$ 9,248**	**$ 6,115**	**$ 9,697**	**$ 249**
Obligated Balance, End of Year (+ or -)	**$ 59,627**	**$ 161,722**	**$ 23,379**	**$ 161,485**	**$ 14,271**	**$ 8,836**	**$ 3,449**	**$ 9,692**	**$ 237**
Budget Authority and Outlays, Net:									
Budget Authority, Gross (Discretionary and Mandatory)	$ 89,159	$ 242,166	$ 45,289	$ 241,896	$ 20,819	$ 15,624	$ -	$ 7,427	$ 270
Actual Offsetting Collections (Discretionary and Mandatory) (-)	(935)	(72,672)	(844)	(72,601)	-	(2)	-	(89)	(71)
Change in Uncollected Customer Payments from Federal Sources (Discretionary and Mandatory) (+ or -)	(1)	1	-	1	-	-	-	(1)	-
Budget Authority, Net (Discretionary and Mandatory)	**$ 88,223**	**$ 169,495**	**$ 44,445**	**$ 169,296**	**$ 20,819**	**$ 15,622**	**$ -**	**$ 7,337**	**$ 199**
Outlays, Gross (Discretionary and Mandatory)	$ 90,573	$ 221,138	$ 42,153	$ 220,685	$ 22,389	$ 16,032	$ 2,612	$ 7,387	$ 453
Actual Offsetting Collections (Discretionary and Mandatory) (-)	(935)	(72,672)	(844)	(72,601)	-	(2)	-	(89)	(71)
Outlays, Net (Discretionary and Mandatory)	89,638	148,466	41,309	148,084	22,389	16,030	2,612	7,298	382
Distributed Offsetting Receipts (-) (Note 16)	(48,725)	-	(48,445)	-	-	-	-	(280)	-
Agency Outlays, Net (Discretionary and Mandatory) (Note 16)	**$ 40,913**	**$ 148,466**	**$ (7,136)**	**$ 148,084**	**$ 22,389**	**$ 16,030**	**$ 2,612**	**$ 7,018**	**$ 382**

Required Supplementary Stewardship Information

Required Supplementary Stewardship Information (RSSI), per OMB Circular A-136 guidance, requires disclosure of investments in human capital and the related program outcomes resulting from stewardship expense outlays.

Stewardship Expenses

Stewardship expenses are substantial investments by the federal government for the long-term benefit of the nation. Because costs of stewardship resources are treated as expenses in the financial statements in the year the costs are incurred, they are reported as RSSI to highlight the benefit nature of the costs and to demonstrate accountability.

Within the United States, state, local, and private sources are responsible for the majority of the estimated $1 trillion spent nationwide on all levels of education. Funding from non-federal sources provides a large portion of K-12 education, according to the National Center for Education Statistics. Public and private organizations of all kinds establish schools and colleges, develop curricula, and determine requirements for enrollment and graduation. The Department's elementary and secondary programs annually serve approximately 50 million students in 16,900 school districts.

Within federal funding, the Department provides grant, loan, loan forgiveness, and work-study assistance to more than 13 million postsecondary students. Today, the Department operates programs that encompass every area and level of education, with discretionary spending constituting the majority of the Department's budget and programs. Loan disbursements represented the bulk of the Department's $317.5 billion in gross outlays for FY 2014. However, grant making overall represented 24.7 percent of those outlays, consisting of discretionary (total $78.4 billion), formula, and needs-based grants. For a detailed breakdown of these components and of the Budget as a whole, please refer to the FY 2015 Budget Summary, as well as the Summary of Human Capital Expenses table in the next section below.

Discretionary grants, such as TRIO, Race to the Top, and the Teacher Incentive Fund, are awarded on a competitive basis. When funds for these grants are exhausted, they will cease to be funded. The Department reviews discretionary grant applications using:

- a formal review process for selection,
- both legislative and regulatory requirements,
- published selection criteria established for individual programs, and
- discretion to determine which applications best address the program requirements and selection criteria and are, therefore, most worthy of funding.

Alternatively, formula grants, such as Title I and Title III of the *Elementary and Secondary Education Act* (ESEA), are not competitive. The majority go to school districts on a formula basis and:

- provide funds as dictated by a law,
- allocate to districts on a per-student basis, and
- schools may apply for and receive formula grants annually.

Lastly, need-based grants, including the Federal Pell grant, Federal Work Study, and the Federal Supplemental Educational Opportunity Grant (FSEOG), are based on family income and economic eligibility. While there are many state, institution (college or school), and privately sourced need-based grants, most need-based grants are funded by the federal government where the financial aid formula is determined by a combination of factors, including:

- family income,
- expected contribution of a family,
- number of dependent family members, and
- student status.

Investment in Human Capital

Human capital investments are defined similarly by the OMB Circular A-136 and the Statement of Federal Financial Accounting Standards (SFFAS) No. 8, *Supplementary Stewardship Reporting,* as expenses for education and training programs intended to:

- increase or maintain national economic productive capacity, and
- produce effective outputs and outcomes that provide evidence of increasing or maintaining national productive capacity.

The amounts reported as investments in the Summary of Human Capital Expenses table below represent the majority of costs on the Statement of Net Cost. These are the costs of the Department representing human investments by their nature.

The 2015 Budget request for the Department focuses on six priorities:

(1) increasing equity and opportunity for all students,
(2) strengthening support for teachers and school leaders,
(3) expanding high-quality preschool programs,
(4) augmenting affordability and quality in postsecondary education,
(5) promoting educational innovation and improvement, and
(6) improving school safety and climate.

Summary of Human Capital Expenses
(Dollars in Millions)

	2014	2013	2012	2011	2010
Federal Student Aid Expense					
Direct Loan Subsidy	$ 8,126	$ (39,557)	$ (10,720)	$ (28,630)	$ (1,567)
Federal Family Education Loan Program Subsidy	(6,585)	(8,753)	(14,381)	(16,126)	(14,344)
Perkins Loans, Pell and Other Grants	33,098	33,542	34,310	39,008	26,799
Salaries and Administrative	206	222	192	193	208
Subtotal	**34,845**	**(14,546)**	**9,401**	**(5,555)**	**11,096**
Other Departmental					
Elementary and Secondary Education	22,832	22,221	22,137	21,195	21,608
Special Education and Rehabilitative Services	15,948	15,919	16,139	15,357	15,227
American Recovery and Reinvestment Act and Education Jobs Fund	-	2,623	7,651	27,945	44,019
Other Departmental Programs	6,938	6,175	6,211	7,341	7,067
Salaries and Administrative	667	703	481	504	502
Subtotal	**46,385**	**47,641**	**52,619**	**72,342**	**88,423**
Grand Total	**$ 81,230**	**$ 33,095**	**$ 62,020**	**$ 66,787**	**$ 99,519**

The Department's annual appropriations and outlays supplement state and local government funding and help build human capital in the nation by supporting cradle-to-career education programs. The Department invests in human capital through its grant and loan programs, research, leadership, and technical assistance. These activities are supported across the Department, primarily through expenditures to assist students who attend institutions of higher education and receive grants and support for state and local educational agencies.

Primary support is offered by the Office of Federal Student Aid, which administers need-based financial assistance programs for students pursuing postsecondary education and makes available federal grants, direct loans, guaranteed loans, and work-study funding to eligible undergraduate and graduate students.

The offices of Elementary and Secondary Education; Special Education and Rehabilitative Services; Innovation and Improvement; English Language Acquisition; Career, Technical, and Adult Education; and Postsecondary Education provide leadership, technical assistance, and financial support to state and local educational agencies, institutions of higher education, and not-for-profit organizations for reform, strategic investment, and innovation.

Institute of Education Sciences is the internal research arm of the Department. Its goal is the transformation of education into an evidence-based field where decision makers routinely seek out the best available research and data before adopting programs or practices that will affect significant numbers of students. The Department's organizational listing of offices is available on the Department's website.

Program Outcomes

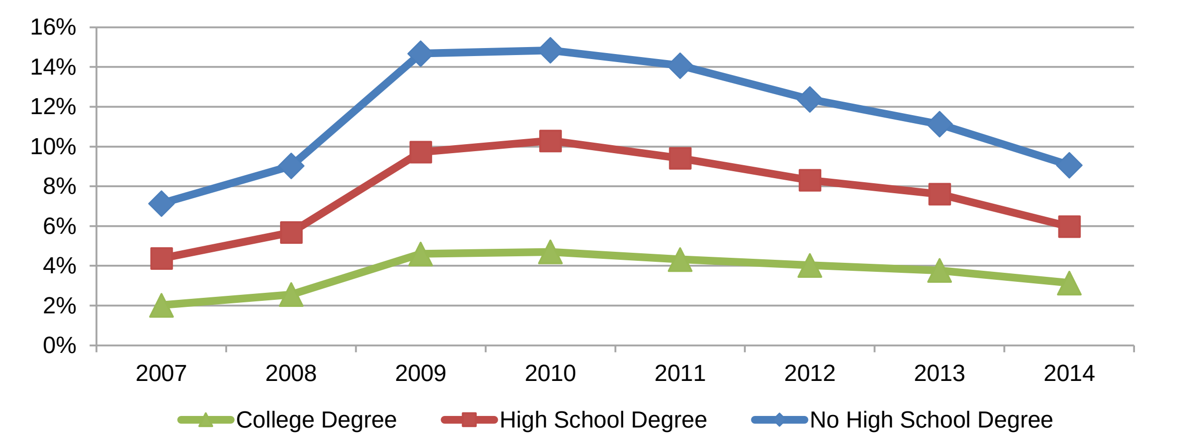
Dramatically boosting completion rates for bachelor's and associate degrees is essential for Americans to compete in a global economy. Education is the stepping stone to higher living standards for American citizens and is vital to national economic growth and security. Economic outcomes, such as wage and salary levels, have historically correlated with individuals' educational attainments and the high level skills employers expect of those entering the labor force. Like all investments, developing higher-level skills involves costs and benefits. Other potential returns may include: increased job opportunities; jobs that are less sensitive to general economic conditions; improved employability of a person over one's lifetime; and economic well-being of the nation through increased national productivity.

Improving education increases the equity of opportunity for every child to succeed. As a nation, we are making progress: High school graduation rates are at their highest ever (80 percent), dropout rates have gone down sharply, NAEP is at its highest ever for 4th/8th grade reading/math, and college enrollment has gone up. Our greatest progress has been in places with the boldest and most sustained commitment to reform.

The Department administers federal investments, including Titles I, II, and III of the *Elementary and Secondary Education Act* (ESEA), as well as the *Individuals with Disabilities Education Act* (IDEA), and provides guidance and technical assistance to states to ensure that teachers and principals are well prepared and students have the resources and support needed to graduate from high school ready for college and careers.

Unemployment Rate. As depicted in the graph below, individuals with lower levels of educational attainment are more likely to be unemployed than those individuals with higher levels of educational attainment. The September 2014 Department of Labor unemployment rate for adults (25 years old and over) who had not completed high school was 9.1 percent, compared with 6.2 percent for those with four years of high school and 3.2 percent for those with a bachelor's degree or higher. Younger people with only high school diplomas tended to have higher unemployment rates than adults 25 and over with similar levels of education.

Unemployment Rate by Educational Level

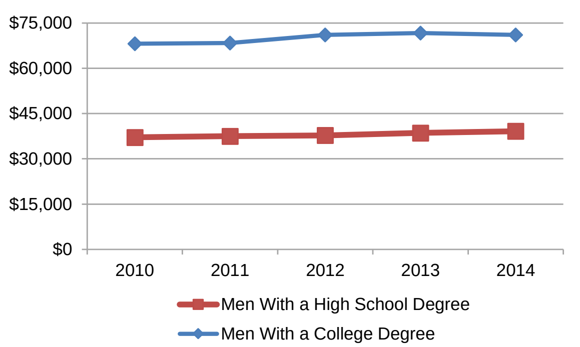


Source: Bureau of Labor Statistics (Department of Labor) Economic News Release, Table A-4: http://www.bls.gov/news.release/empsit.t04.htm

Annual Income. As depicted in the two graphs below, according to the September 2014 Department of Labor data, annualized median income for adults (25 years old and over) varied considerably by education level as follows:

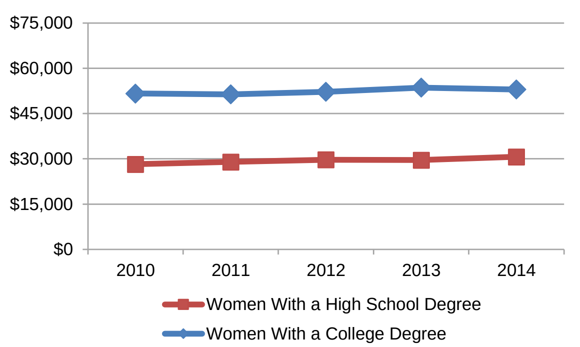
- Men with a high school diploma earned $38,324, compared with $71,604 for men with a college degree.
- Women with a high school diploma earned $30,368, compared with $54,548 for women with a college degree.
- Men and women with college degrees earned 80 percent more than men and women with high school diplomas.
- These returns on investment in education directly translate into the advancement of the American economy as a whole.

Annualized Median Income for Men (25 Years Old and Over), 2010–2014*



* The 2011–2014 data are annualized as of September of each year; the 2010 data are annualized as of July of that year.

Annualized Median Income for Women (25 Years Old and Over), 2010–2014*



* The 2011–2014 data are annualized as of September of each year; the 2010 data are annualized as of July of that year.

Source: Bureau of Labor Statistics (Department of Labor) Economic News Release, Table A-4: http://www.bls.gov/news.release/empsit.t04.htm

UNITED STATES DEPARTMENT OF EDUCATION
OFFICE OF INSPECTOR GENERAL

THE INSPECTOR GENERAL

November 14, 2014

The Honorable Arne Duncan
Secretary of Education
Washington, D.C. 20202

Dear Secretary Duncan:

The enclosed reports present the results of the audit of the U.S. Department of Education's (Department) financial statements for fiscal years 2014 and 2013 to comply with the Chief Financial Officers Act of 1990, as amended. The reports should be read in conjunction with the Department's financial statements and notes to fully understand the context of the information contained therein.

We contracted with the independent certified public accounting firm of CliftonLarsonAllen, LLP (CliftonLarsonAllen) to audit the financial statements of the Department as of September 30, 2014 and 2013, and for the years then ended. The contract requires that the audit be performed in accordance with U.S. generally accepted government auditing standards and Office of Management and Budget bulletin, *Audit Requirements for Federal Financial Statements.*

Results of the Independent Audit

CliftonLarsonAllen found:

- The fiscal years 2014 and 2013 financial statements are presented fairly, in all material respects, in accordance with accounting principles generally accepted in the United States of America;
- One significant deficiency in internal control over financial reporting; and
- One instance of reportable noncompliance with certain provisions of the Debt Collection Improvement Act of 1996, as amended.

Evaluation and Monitoring of Audit Performance

The Inspector General Act of 1978 requires that the Inspector General take appropriate steps to assure that any work performed by non-Federal auditors complies with the audit standards established by the Comptroller General. In that regard, we evaluated the independence, objectivity, and qualifications of the auditors and specialists; reviewed the plan and approach of the audit; monitored the performance of the audit; reviewed CliftonLarsonAllen's reports and related audit documentation; and inquired of its representatives.

400 MARYLAND AVENUE, S.W., WASHINGTON, DC 20202-1510

Promoting the efficiency, effectiveness, and integrity of the Department's programs and operations.

Page 2 – The Honorable Arne Duncan

Our review was not intended to enable us to express, and we do not express, an opinion on the Department's financial statements, or conclusions about the effectiveness of internal control, whether the Department's financial management systems substantially complied with the Federal Financial Management Improvement Act of 1996, or on compliance with laws and regulations.

CliftonLarsonAllen is responsible for the enclosed auditors' report and the conclusions expressed in the related reports on internal control and compliance with laws and regulations. Our review disclosed no instances where CliftonLarsonAllen did not comply, in all material respects, with U.S. generally accepted government auditing standards.

We appreciate the cooperation given CliftonLarsonAllen and my office during the audit. If you have any questions or would like to discuss the reports, please contact me at (202) 245-6900.

Sincerely,

Kathleen S. Tighe

Kathleen S. Tighe
Inspector General

Enclosure

CliftonLarsonAllen

CliftonLarsonAllen LLP

www.cliftonlarsonallen.com

INDEPENDENT AUDITORS' REPORT

Inspector General
United States Department of Education

Secretary
United States Department of Education

Report on the Financial Statements

We have audited the accompanying financial statements of the United States Department of Education (Department), which comprise the consolidated balance sheets as of September 30, 2014 and 2013, and the related consolidated statements of net cost and changes in net position, and the combined statements of budgetary resources for the years then ended, and the related notes to the financial statements (financial statements).

Management's Responsibility for the Financial Statements

The Department's management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America (U.S.) and the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the U.S.; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 14-02, *Audit Requirements for Federal Financial Statements* (OMB Bulletin 14-02). Those standards and OMB Bulletin 14-02 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of

INDEPENDENT AUDITORS' REPORT (Continued)

significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

We are also responsible for applying certain limited procedures with respect to the Required Supplementary Information and Other Information included with the financial statements.

Opinion on the Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the United States Department of Education as of September 30, 2014 and 2013, and its net costs, changes in net position, and budgetary resources for the years then ended, in accordance with accounting principles generally accepted in the U.S.

Other Matters

Required Supplementary Information
Accounting principles generally accepted in the U.S. issued by the Federal Accounting Standards Advisory Board (FASAB) require that the Department's Management Discussion and Analysis (MD&A), other Required Supplementary Information (RSI), and Required Supplementary Stewardship Information (RSSI) on pages 1 through 48 and 95 through 101 of the United States Department of Education's FY 2014 Agency Financial Report, be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by FASAB, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the MD&A, other RSI, and RSSI in accordance with auditing standards generally accepted in the U.S., which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on this information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information
The Message from the Secretary, Message from the Chief Financial Officer, and the Other Information on pages iii and iv, 50 and 51, and 119 through 150, of the United States Department of Education's FY2014 Agency Financial Report, respectively, contain a wide range of information, some of which is not directly related to the financial statements. This information is presented for purposes of additional analysis and is not a required part of the financial statements or RSI. This information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

INDEPENDENT AUDITORS' REPORT (Continued)

Report on Internal Control over Financial Reporting and Report on Compliance Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Report on Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Department's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control or on management's assertion on internal control included in the MD&A. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control or on management's assertion on internal control included in the MD&A.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Department's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described below and in more detail in Exhibit A, which we consider to be a significant deficiency.

<u>Department and Federal Student Aid Management Need to Mitigate Persistent Information Technology Control Deficiencies</u>

Due to the unique requirements of the Department's grant, loan and administrative business activities, the Department manages its general support system and core financial management system and oversees a large portfolio of Federal Student Aid (FSA) or contractor owned information systems. The third party servicers who manage FSA's general support systems and contractor-owned and contractor operated financial systems are monitored by FSA management through the use of Service Level Agreements and third party independent reviews. We continued to identify control deficiencies in the areas of security management, personnel security, access controls, and configuration management across these systems. These deficiencies can increase the risk of unauthorized access to the Department's systems used to capture, process, and report financial transactions and balances, affecting the reliability and security of the data and information.

INDEPENDENT AUDITORS' REPORT (Continued)

Report on Compliance

As part of obtaining reasonable assurance about whether the Department's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements consistent with our professional responsibilities discussed below.

The results of our tests, exclusive of those required by the Federal Financial Management Improvement Act of 1996 (FFMIA) as discussed below, disclosed one instance of noncompliance with respect to a certain aspect of the Department's debt collection activities, described in Exhibit B, that is required to be reported in accordance with *Government Auditing Standards* and OMB Bulletin No. 14-02.

Compliance with FFMIA Requirements

Under FFMIA, we are required to report whether the financial management systems used by the Department substantially comply with the FFMIA Section 803(a) requirements. To meet this requirement, we performed tests of compliance with (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the United States Standard General Ledger (USSGL) at the transaction level. However, providing an opinion on compliance with FFMIA was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests of FFMIA Section 803(a) requirements disclosed no instances in which the Department's financial management systems did not substantially comply with (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, or (3) the USSGL at the transaction level.

Management's Responsibility for Internal Control and Compliance

Management is responsible for (1) evaluating the effectiveness of internal control over financial reporting based on criteria established under the Federal Managers' Financial Integrity Act (FMFIA), (2) providing a statement of assurance on the overall effectiveness on internal control over financial reporting, (3) ensuring the Department's financial management systems are in substantial compliance with FFMIA requirements, and (4) complying with other applicable laws, regulations, contracts, and grant agreements.

Auditors' Responsibilities

We are responsible for: (1) obtaining a sufficient understanding of internal control over financial reporting to plan the audit, (2) testing whether the Department's financial management systems substantially comply with the FFMIA requirements referred to above, and (3) testing compliance with certain provisions of laws, regulations, contracts and grant agreements that have a direct and material effect on the determination of the financial statement amounts and applicable laws and regulations for which OMB Bulletin 14-02 requires testing.

We did not evaluate all internal controls relevant to operating objectives as broadly established by the FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to testing controls over financial reporting. Because of inherent limitations in internal control, misstatements due to error or fraud, losses or noncompliance may nevertheless occur and not be detected. We also caution that projecting our audit results to future periods is subject to risk that controls may become inadequate because of changes in conditions or that the degree of compliance with controls

INDEPENDENT AUDITORS' REPORT (Continued)

may deteriorate. In addition, we caution that our internal control testing may not be sufficient for other purposes.

We did not test compliance with all laws, regulations, contracts and grant agreements applicable to the Department. We limited our tests of compliance to certain provisions of laws, regulations, contracts and grant agreements that have a direct and material effect on the determination of financial statement amounts and applicable laws and regulations for which OMB Bulletin 14-02 requires testing. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes. Also, our work on FFMIA would not necessarily disclose all instances of noncompliance with FFMIA requirements.

Management's Response to Findings

Management's response to the findings identified in our report is presented in Exhibit C. We did not audit the Department's response and, accordingly, we express no opinion on it.

Status of Prior Year's Control Deficiencies and Noncompliance Issues

We have reviewed the status of the Department's corrective actions with respect to the findings included in the prior year's Independent Auditors' Report, dated December 11, 2013. The status of prior year findings is presented in Exhibit D.

Purpose of the Report on Internal Control over Financial Reporting and the Report on Compliance

The purpose of the Report on Internal Control over Financial Reporting and the Report on Compliance sections of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the Department's internal control or on compliance. These reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Department's internal control and compliance. Accordingly, these reports are not suitable for any other purpose.

CliftonLarsonAllen LLP

CliftonLarsonAllen LLP

Arlington, Virginia
November 14, 2014

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT A
Significant Deficiency

Department and Federal Student Aid Management Need to Mitigate Persistent Information Technology Control Deficiencies

Due to the unique requirements of the Department's grant, loan and administrative business activities, the Department oversees a large portfolio of government owned and operated, government owned and contractor operated, and contractor owned and operated information systems. Four Federal Student Aid (FSA) systems and one Department system comprise the key financial systems. The third party servicers who manage the Department and FSA's general support systems and contractor owned and operated financial systems are monitored by the Department and FSA management through the use of Service Level Agreements and independent reviews. Managing the information and system security across the Department is the responsibility of the Department's Chief Information Security Officer (CISO), in conjunction with FSA's CISO. For several years, financial and other audits have identified numerous system deficiencies that affect the security and reliability of the information within these systems. Last year, we noted information technology (IT) control deficiencies in the areas of security management, personnel security, access controls, incident response, configuration management, and contingency planning in one or more systems. In addition, last year we noted application-level control issues for four of the seven independent reviews of FSA's contractor owned and operated systems. Based on testing performed this year, we noted no control deficiencies in the areas of incident response and contingency planning. During fiscal year (FY) 2014, FSA implemented an oversight function involving FSA's Business Operations and Finance offices to closely monitor completion of corrective action plans for the noted control deficiencies. This year, none of the independent reviews identified significant system control deficiencies. Despite these improvements, our audit continued to identify control deficiencies in the following areas:

Security management

- The Department's IT policies and procedures and certain system security plans were outdated or did not fully address specific controls required by the National Institute of Standards and Technology (NIST)
- Annual security control assessments were not completed
- Security assessments and authorization of certain systems did not comply with NIST requirements
- System risk assessments were not kept current
- System vulnerabilities were not being formally tracked through remediation
- Mitigation strategies for corrective actions related to IT control weaknesses were missing and corrective action deadlines were missed
- Security awareness training for new system users was not always completed
- Role based security awareness training for users with significant system security responsibilities was not always completed

Personnel security

- Background reinvestigations were not completed timely by the Department
- Position sensitivity levels for some users were incorrect based on their job function

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT A
Significant Deficiency

Access controls

- User access was not always granted in accordance with the principle of least privilege
- Termination of system access for separated employees and contractors was not always completed timely
- Inactive accounts were not always disabled
- Certain users had access to application development and production environments
- User access was not always recertified

Configuration management

- System configuration settings were not always in compliance with FSA policy
- System change testing was not always documented

These deficiencies can increase the risk of unauthorized access to the Department and FSA's systems used to capture, process, and report financial transactions and balances, affecting the reliability and security of the data and information. These findings are discussed in further detail below and in a Limited Distribution Report provided to the Department and FSA management.

Security management
An effective information security management program should have a framework and process for assessing risk, effective security procedures, and processes for monitoring and reporting the effectiveness of these procedures. We noted the Department's information security policies were outdated or did not fully address specific controls required by NIST Special Publication (SP) 800-53, Revision 4, *Recommended Security and Privacy Controls for Federal Information Systems and Organizations*.[1] For two systems, we noted their System Security Plans' control baselines were based on NIST SP 800-53, Revision 3. NIST SP 800-53, Revision 4 was published in 2013 with an April 1, 2014 implementation deadline for executive agencies.

Additionally, two systems were given Authority to Operate (ATO) memoranda prior to the completion of security assessment and authorization (SA&A) activities. Although an assessment of the design of controls was conducted in 2013, the last security control assessment that determined the extent to which the controls were implemented and operating as intended was completed in 2010. As such, the most recent system risk assessment was completed in 2010. Therefore, the ATOs were issued without the review of a complete and timely security assessment and authorization package as required by NIST SP 800-37, Revision 1 *Guide for Applying the Risk Management Framework to Federal Information Systems*, resulting in an

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[1] NIST SP 800-53 revision 4 was issued in April 2013. According to the Office of Management and Budget (OMB) memorandum M-10-15, *FY 2010 Reporting Instructions for the Federal Information Security Management Act and Agency Privacy Management* requires that for non-national security programs and information systems, agencies must follow NIST standards and guidelines. For legacy information systems, agencies are expected to be in compliance with NIST standards and guidelines within one year of the publication date unless otherwise directed by OMB. The one year compliance date for revisions to NIST publications applies only to the new and/or updated material in the publications.

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT A
Significant Deficiency

increased risk that the Authorizing Official, Information System Security Officers (ISSOs), and system owners were not informed of the ongoing security issues and risks to these systems.

With regard to corrective action of system control weaknesses, we noted that the Plans of Action and Milestones (POA&Ms) for one system had passed their scheduled dates of completion without documented justification for missed completion dates or adjusted expected completion dates. Additionally, we noted POA&Ms that did not have a documented mitigation strategy. We also noted that the corrective action of certain control weaknesses discovered through vulnerability scanning of another system was not being formally tracked through its remediation. Without formally documenting each remediation plan, along with the estimated dates of completion and status of corrective actions, management cannot ensure weaknesses are remediated effectively or timely.

Finally, for two of the five systems tested, we noted system users did not always complete the required security awareness training. Also, individuals with significant system security responsibilities had not always completed role based training for these systems.

Personnel Security
Personnel security involves screening individuals before granting them access to computer resources commensurate with the risk and magnitude of the harm the individual could cause. We found background reinvestigations were not being tracked effectively and position sensitivity levels were not always commensurate with the users' current job duties. Specifically, we noted the following for a sample of individuals with significant system security responsibilities:

- Lack of evidence of an investigation or users with overdue reinvestigations
- Investigation levels lower than the level required by the users' access requirements and responsibilities
- Lack of sensitivity level documentation for users or sensitivity level documentation lower than the level required for a users' access requirements and responsibilities

Access Controls
Access controls limit or detect inappropriate access to systems, protecting the data within them from unauthorized modification, loss or disclosure. Agencies should have formal policies and procedures for controlling access to information systems and related control activities should be properly implemented and monitored. One key element of access control is *boundary protection*. Properly managed interfaces between FSA systems and external parties help reduce the risk of unauthorized access. NIST SP 800-47, *Security Guide for Interconnecting Information Technology Systems,* specifies that an agreement should be documented for the interconnection between organizations. A Memorandum of Understanding (MOU) documents the terms and conditions for sharing data and information resources in a secure method. An Interconnection Security Agreement (ISA) identifies the technical and security requirements for establishing, operating, and maintaining the interconnection and supports the MOU. We identified expired MOUs and instances in which interconnections were not detailed in the System Security Plan for one system.

User authorization refers to the documentation of the granting of user access to only the elements of a system the user needs to perform his or her duties. To be an effective control, user access should be documented, approved and periodically reviewed. Accounts for users

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT A
Significant Deficiency

should be terminated when the user no longer needs access to the system. Based on our work, we noted:

- Accounts for terminated employees and contractors were not disabled for three of the four systems tested
- Inactive accounts were not disabled for two systems
- For one system, an individual was granted an inappropriate level of system access
- User access recertification was not fully completed for three systems
- Certain users had inappropriate access to one system's development and production environments

Configuration Management
Configuration management ensures changes to systems are tested and approved, and systems are configured securely in accordance with policy. In our audit, we found two systems with configuration settings that were not in compliance with FSA's policy and one system with configuration settings that were not in compliance with Department's policy. Additionally, we could not obtain evidence of testing related to a sample of changes for one system. This was primarily due to testing documentation not being maintained in the change management ticketing system.

The Department's Chief Information Officer FY2014 Federal Managers' Financial Integrity Act of 1982 (FMFIA) Assurance Letter reported control deficiencies related to access controls and contingency planning. In addition, FSA's FY2014 FMFIA Assurance Letter reported control deficiencies related to access controls and configuration management. Also, the Department's FY2014 Federal Information Security Management Act (FISMA) review identified control deficiencies in six of eleven reporting metrics related to the following areas: configuration management, identity and access management, incident response and reporting, risk management, remote access management, and contingency planning. In addition, five of the 11 reporting metrics contained repeat or modified repeat findings from reports issued from the last three years.

These deficiencies can increase the risk of unauthorized access to the Department's systems used to capture, process, and report financial transactions and balances.

NIST Special Publication 800-39, *Managing Information Security Risk - Organization, Mission, and Information System View*, states:

> "The complex relationships among missions, mission/business processes, and the information systems supporting those missions/processes require an integrated, organization-wide view for managing risk. Unless otherwise stated, references to risk in this publication refer to information security risk from the operation and use of organizational information systems including the processes, procedures, and structures within organizations that influence or affect the design, development, implementation, and ongoing operation of those systems. The role of information security in managing risk from the operation and use of information systems is also critical to the success of organizations in achieving their strategic goals and objectives. Historically, senior leaders/executives have had a very narrow view of information security either as a technical matter or in a stovepipe that was independent of organizational risk and the traditional management and life cycle processes. This extremely limited perspective

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT A
Significant Deficiency

often resulted in inadequate consideration of how information security risk, like other organizational risks, affects the likelihood of organizations successfully carrying out their missions and business functions. This publication places information security into the broader organizational context of achieving mission/business success. The objective is to:

- Ensure that senior leaders/executives recognize the importance of managing information security risk and establish appropriate governance structures for managing such risk;
- Ensure that the organization's risk management process is being effectively conducted across the three tiers of organization, mission/business processes, and information systems;
- Foster an organizational climate where information security risk is considered within the context of the design of mission/business processes, the definition of an overarching enterprise architecture, and system development life cycle processes; and
- Help individuals with responsibilities for information system implementation or operation better understand how information security risk associated with their systems translates into organization-wide risk that may ultimately affect the mission/business success.

To successfully execute organizational missions and business functions with information system-dependent processes, senior leaders/executives must be committed to making risk management a fundamental mission/business requirement. This top-level, executive commitment ensures that sufficient resources are available to develop and implement effective, organization-wide risk management programs. Understanding and addressing risk is a strategic capability and an enabler of missions and business functions across organizations. Effectively managing information security risk organization-wide requires the following key elements:

- Assignment of risk management responsibilities to senior leaders/executives;
- Ongoing recognition and understanding by senior leaders/executives of the information security risks to organizational operations and assets, individuals, other organizations, and the Nation arising from the operation and use of information systems;
- Establishing the organizational tolerance for risk and communicating the risk tolerance throughout the organization including guidance on how risk tolerance impacts ongoing decision-making activities; and
- Accountability by senior leaders/executives for their risk management decisions and for the implementation of effective, organization-wide risk management programs."

The ineffective and untimely remediation of application control weaknesses and repeat deficiencies identified across multiple applications indicates the need for improved strategic IT management.

In recognition of the need to improve internal control related to information security, the Department and FSA CISOs continue to work together to put a framework in place for more effectively managing system security risk by reviewing control weaknesses across the organization, determining their root cause, and tracking remediation activities. The security

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT A
Significant Deficiency

posture of the systems is reviewed on a monthly basis by reviewing control weaknesses noted from audits, self assessments, vulnerability scans, and associated POA&Ms. In addition, the Department updated and approved OCIO-1, *Information Assurance/Cybersecurity Policy,* which provides policy guidance from the OCIO for all IT assets and services operated within or on behalf of the Department. Underlying security procedures and guidance documentation is in the process of being updated. The Department also completed the implementation of a Security Operations Center allowing for security issues to be centrally tracked and managed for the Department and FSA. The Department has continued to make progress on implementing a risk management framework for applying continuous system monitoring based on NIST SP 800-37 with a scheduled completion date of FY2015. Furthermore, the Department refined the service-level agreements for the IT general support system contract to increase accountability of the service provider for remediating system control issues. FSA is working on a plan to review selected IT security controls at all Guaranty Agencies (GAs) within a two year period. FSA has already been assessing the IT security controls at the Title IV Additional Servicers (TIVAS) and Private Collection Agencies (PCAs) in order for the CISO to issue an ATO. These activities show progress and commitment from the Department and FSA senior managers to strengthen system security controls across the Department and FSA.

In order to fully implement an agency-level program for monitoring compliance with the information security program, the procedures and guidance supporting the Information Assurance/Cybersecurity Policy need to be completed, approved and disseminated in order to define the agency-wide information security program and practices. Without comprehensive current information security policies and procedures, there is an increased likelihood that information security may not be addressed throughout the lifecycle of the Department and FSA's information systems. Moreover, employees and contractors may be performing tasks without clear direction or training. Due to the continuance of persistent IT control deficiencies across multiple systems, the CISOs need to continue to refine the process for ensuring accountability of the Department and FSA system owners, ISSOs, contractors, and FSA's Technology Office and Business Operations responsible for the security, operation and maintenance of the Department and FSA systems to remediate control deficiencies.

<u>Recommendations:</u>

We recommend the Department CISO work with the FSA CISO to:

1a. Refine and fully implement FSA's system security program to monitor compliance with NIST requirements, in coordination with the Department's organization wide information security program, at both the agency and system level.

1b. Implement a process to ensure accountability for individuals responsible for remediating the identified control deficiencies in the Department and FSA's systems, including cooperation between the Technology Office and Business Operations.

1c. Implement a process for holding contractors accountable for remediation of control deficiencies in the Department and FSA's systems.

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT B
Instance of Noncompliance

Noncompliance with Title 31 United States Code (U.S.C.) Section 3716(c)(6)

Title 31 U.S.C. Section 3716(c)(6) states that any Federal agency that is owed by a person a past due, legally enforceable nontax debt that is over 180 days delinquent, including nontax debt administered by a third party acting as an agent for the Federal Government, shall notify the Secretary of the Treasury of all such nontax debts for purposes of administrative offset under this subsection.

The Digital Accountability and Transparency Act (DATA Act), Public Law 113-101, was signed into law on May 9, 2014. Section 5 of the DATA Act amends Title 31 U.S.C. Section 3716(c)(6) and now requires agencies to notify the Secretary of the Treasury of valid, delinquent nontax debts that are over 120 days delinquent – 60 days earlier than the previous 180 days requirement – for the purpose of administrative offset. Section 5 of the DATA Act also added a new requirement, according to which "the Secretary of the Treasury shall notify Congress of any instance in which an agency fails to notify the Secretary [of the Treasury] as required" by 31 U.S.C. Section 3716(c)(6)(A).[2]

The Department and FSA have not changed their loan servicing procedures and internal processes to comply with the new 120 days requirement. Further, the existing loan servicing procedures and internal processes do not notify the Secretary of the Treasury of past due, legally enforceable nontax debts once they become over 180 days past due. Instead, notification is performed once a year when most past due, legally enforceable nontax debts are significantly older than 180 days delinquent. Therefore, the Department and FSA are noncompliant with the timing requirement of 31 U.S.C. Section 3716(c)(6) as of September 30, 2014.

<u>Recommendation:</u>

We recommend that the Secretary of Education and FSA Chief Operating Officer:

2. Revise their loan servicing procedures and internal processes to comply with the timing requirement of Title 31 U.S.C. Section 3716(c)(6), as amended by the DATA Act.

[2] The official U.S.C has not yet been amended to reflect the statutory change due to the passage of the DATA Act.

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT C
Management's Response

UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF THE CHIEF FINANCIAL OFFICER

MEMORANDUM

NOV - 7 2014

TO: Kathleen S. Tighe
Inspector General

FROM: Thomas P. Skelly
Delegated to Perform the Functions
and Duties of the Chief Financial Officer

Danny A. Harris, Ph.D.
Chief Information Officer

SUBJECT: DRAFT AUDIT REPORTS
Fiscal Years 2014 and 2013 Financial Statements
U.S. Department of Education
ED-OIG/A17O0001

Please convey our sincere thanks and appreciation to everyone on your staff who worked diligently on this financial statement audit. The Department reviewed the draft Fiscal Years 2014 and 2013 Financial Statement Audit Report. We concur and agree with the Independent Auditors' Report.

We will share the final audit results with responsible senior officials, other interested program managers, and staff. At that time, we will also request the preparation of corrective action plans to be used in the resolution process.

Again, please convey our appreciation to everyone on your staff whose efforts permitted the Department to complete the audit within the established timeframe.

Please contact Gary Wood, Director, Financial Management Operations, at (202) 245-8118 with any questions or comments.

550 12th St. S.W., WASHINGTON, DC 20202
www.ed.gov

The Department of Education's mission is to promote student achievement and preparation for global competitiveness by fostering educational excellence and ensuring equal access.

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT D
Status of Prior Year Recommendations

Our assessment of the current status of the recommendations related to findings identified in the prior year audit is presented below:

Fiscal Year 2013 Recommendation	Fiscal Year 2014 Status
Significant Deficiency 1- *Functionality and Internal Controls over Some Loan Servicing Systems Need Improvement*	
CLA recommended that the Chief Operating Officer of FSA:	
1a. Ensure all servicing application functionality is corrected to meet the Department's requirements for servicing loans and reporting financial activity and balances timely and accurately.	One of the systems was decommissioned. Significant functionality issues for the other system were addressed. Minor remaining and new issues reported in the management letter.
1b. Continue to monitor the scheduled transfers of defaulted loans to DMCS and ensure that all new loan servicers are fully set up to transfer defaulted loans to the defaulted loan servicer.	Significant functionality issues relating to transfers addressed and the transfer backlog was significantly reduced. Minor remaining and new issues reported in the management letter.
1c. Continue to correct loan balances affected by the functionality issues and properly inform the impacted borrowers of the corrected account balances.	Corrective action to adjust immaterial errors in account balances will continue into FY2015. Remaining issues reported in the management letter.
1d. Continue to monitor servicers' efforts to reduce the balance of unposted cash transactions, unrecorded borrower transactions, and general ledger posting differences, including the posting of transfer transactions in and out of DMCS.	One of the systems was decommissioned. The effect of the remaining issues in the other system was immaterial throughout FY2014. Recommendation made in the management letter.
1e. Establish protocols for management approval for write-offs and manual adjustments of unresolved differences once corrective actions are no longer cost effective.	Management implemented a protocol to approve write-offs and manual adjustments arising from the corrective actions that address the system functionality issues. Resolved.
1f. Continue to monitor the timeliness and accuracy of account reconciliations prepared by the servicers.	Improvement noted during FY2014. Recommendation to continue monitoring new contractor noted in management letter.

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT D
Status of Prior Year Recommendations

Significant Deficiency 2 - *Department and FSA Management Need to Mitigate Persistent Information Technology (IT) Control Deficiencies*	
CLA recommended that the Department and FSA CISOs:	
2a. Refine and fully implement the program to monitor compliance with the Department's organization-wide information security program and NIST requirements at the Department and system level.	Progress was made, however corrective action is still in process; see Significant Deficiency
2b. Implement a process ensuring accountability for individuals responsible for remediating the identified control deficiencies in the Department and FSA's systems, including cooperation between the Technology Office and Business Operations.	Progress was made, however corrective action is still in process; see Significant Deficiency
2c. Implement a process for holding contractors accountable for remediation of control deficiencies in the Department and FSA systems.	Progress was made, however corrective action is still in process; see Significant Deficiency
2d. Implement a process for holding third party service providers accountable for the remediation of control deficiencies associated with their information systems.	Resolved
Noncompliance with Laws and Regulations	
The Department's Financial Management Systems Do Not Meet Federal Financial Management Systems Requirements	Resolved, as the key system contributing to noncompliance was decommissioned and the other system was significantly improved.

Other Information

About the Other Information Section

This section includes improper payments reporting details, the schedule of spending, summary of assurances, a summary of the Office of Inspector General management and performance challenges for FY 2015, and Freeze the Footprint information. Additional information is available at the links provided. The Department welcomes comments from readers to improve the report.

Improper Payments Reporting Details

The Improper Payments Reporting Details summarizes the Department's efforts to identify, recover, and prevent improper payments. It includes the data required to be reported annually to the President and Congress on assessments of risk, estimates of improper payments, actions to mitigate improper payments, and recoveries of improper payments.

Schedule of Spending

The Schedule of Spending (SOS) presents total amounts to be spent by the Department broken out by (a) what money was available to spend, (b) how the money was spent, and (c) who the money went to. For information on spending, USASpending.gov is a searchable website provided by the Office of Management and Budget (OMB) that provides information on federal awards and is accessible to the public at no cost.

Summary of Financial Statement Audit and Management Assurances

This summary table provides information on any material weaknesses reported by the agency or through the audit process.

Office of Inspector General's Management and Performance Challenges

The Office of Inspector General's Management and Performance Challenges for Fiscal Year 2015 report is summarized in this section. The FY 2015 management challenges are: (1) Improper Payments, (2) Information Technology Security, (3) Oversight and Monitoring, (4) Data Quality and Reporting, and (5) Information Technology System Development and Implementation. These challenges reflect continuing vulnerabilities and emerging issues faced by the Department as identified through the OIG's recent audit, inspection, and investigative work. For the full report, including the Department's response, visit the OIG website.

Freeze the Footprint

The Freeze the Footprint summarizes the Department's efforts in promoting efficient spending to support the agency's operations in accordance with OMB Management Procedures Memorandum 2013-02, the *Freeze the Footprint policy* implementing guidance, which states that all CFO Act departments and agencies shall not increase the total square footage of their domestic office and warehouse inventory compared to an FY 2012 baseline. OMB is working in partnership with the General Services Administration to better align the size of the federal real property inventory.

Improper Payments Reporting Details

The Department is committed to preventing improper payments with front-end controls, and detecting and recovering them if they occur. In FY 2014, the Department continued efforts to: 1) assess the risk of improper payments, 2) estimate improper payments, 3) address root causes of improper payments, and 4) recover improper payments. These four efforts are described in more detail below.

The Department implemented actions that meet the requirements of the *Improper Payments Elimination and Recovery Improvement Act of 2012* (IPERIA) (Public Law 112-248) and the *Improper Payments Elimination and Recovery Act of 2010* (IPERA) (Public Law 111-204), both of which amend the *Improper Payments Information Act of 2002* (IPIA) (Public Law 107-300), as well as the Office of Management and Budget's (OMB) Circular A-123, Appendix C, *Requirements for Effective Measurement and Remediation of Improper Payments*. Agencies are required to review and assess all programs and activities to identify those susceptible to significant improper payments. The OMB guidance defines significant improper payments as those in any particular program that exceed both 1.5 percent of program payments and $10 million annually or that exceed $100 million. 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.

Internal Controls and Accountability

The Department maintains the internal controls, human capital, information systems, and other infrastructure necessary to minimize improper payments. As detailed in the *Analysis of Controls, Systems, and Legal Compliance* portion of this AFR, the Department's internal control framework is robust. It includes important controls at many levels of the payment process designed to help prevent and detect improper payments. These controls are periodically assessed for design and operating effectiveness as part of Department self-assessments of internal controls. For example:

- Schools are responsible and held accountable for recipient verification for need-based aid. FSA certifies a school's eligibility for participation in Title IV programs, conducts periodic Program Reviews of schools to verify compliance, and evaluates school financial statement and compliance audits to ensure any potential compliance issues or control weaknesses are resolved.
- FSA offices, managers, and staff responsible for these programs are accountable for establishing and maintaining sufficient internal controls, including a control environment that prevents improper payments from being made, and promptly detects and recovers any improper payments that may occur. Offices and managers are held accountable through a variety of mechanisms and controls, including annual performance measures aligned to the strategic plan, organizational performance review criteria, and individual annual performance appraisal criteria.
- Department and FSA contractors are held accountable through various contract management and oversight activities and functions, control assessments, and audits.
- Department program staff work with the Department's Risk Management Service (RMS) to use the Decision Support System (DSS) Entity Risk Reviews (ERR) to assess

grantee risk and assist in the determination of special conditions for grant awards. In FY 2014, RMS produced 112 reports assessing risk for 1,214 grant applicants to new discretionary grant awards, and 141 reports assessing risk for 2,984 discretionary grantees. These reports were used to review 95 new award competitions, and 84 non-competitive continuations (NCCs).

- The Department coordinates and manages the resolution of internal and external audits, which includes working with program managers, the Office of General Counsel, and impacted parties to collect debt associated with improper payments.
- The Department leverages a continuous controls monitoring process to help detect anomalies and potential issues in agency payment-related data, including Department and FSA payments made through the core financial system.

Risk Assessments

As required by the OMB Circular A-123, Appendix C, the Department conducts an assessment of the risk of improper payments in each program at least once every three years. Below is a summary of these assessments.

Risk Assessment Results		
Program	**Last Risk Assessment**	**Risk-Susceptible?**
FSA Managed Programs		
Federal Pell Grants	FY 2014	Yes
The Teacher Education Assistance for College and Higher Education Grant	FY 2014	No
Federal Supplemental Educational Opportunity Grant	FY 2014	No
Iraq and Afghanistan Service Grant	FY 2014	No
Federal Perkins Loan Program	FY 2014	No
Federal Direct Loan Program	FY 2014	Yes
Federal Family Education Loan Program	FY 2014	Yes(1)
Federal Work-Study Program	FY 2014	No
Other Department Programs		
Title I	FY 2013	No(2)
Other Grant Programs	FY 2013	No
Contract Payments	FY 2013	No
Administrative Payments	FY 2014	No

(1) FFEL, as a program that had previously been determined to be risk-susceptible, must first report improper payment estimates that are less than the stated thresholds for a minimum of two consecutive years before formally reclassifying the program's risk categorization. FFEL was estimated below the threshold for high-risk programs in FY 2013 and FY 2014.
(2) Title I is included in the table because it is a Section 57 program.

FSA-Managed Programs

The Department performed a risk assessment for all FSA-managed programs during FY 2014 and determined that the Pell Grant and Direct Loan programs were susceptible to risk of significant improper payments. For each program, risk assessment meetings were held with program owners, key personnel, and other designees to discuss the inherent risk of improper payments as it relates to the following ten risk factors:

- Newness of Program or Transactions;
- Complexity of Program or Transactions;
- Volume of Payments;
- Level of Manual Intervention;
- Changes in Program Funding Authorities, Practices, and Procedures;
- History of Audit Issues;
- Prior Improper Payments Reporting Results;
- Human Capital Management;
- Nature of Program Recipients; and
- Management Oversight.

A risk rating was assigned to each factor based on established criteria. Weighted percentages were assigned to each risk factor rating based on the probability of occurrence of an improper payment. An overall risk score was then computed for each program, calculated by the average of the sum of the weighted scores for each risk factor and overall rating scale.

The risk assessment results found that, in FY 2014, the FFEL program is low risk (i.e., not risk susceptible to significant improper payments). This determination is corroborated by the prior year (FY 2013) estimate of 0 percent, which is well below the risk-susceptible thresholds of 1.5 percent and $10 million in estimated error or $100 million in estimated error as defined in OMB Circular A-123, Appendix C. While FFEL has been assessed as low risk this year, a FFEL estimate was still performed and is presented here. Consistent with OMB guidance, any program that has previously been determined to be risk-susceptible must first report improper payment estimates that are less than the stated thresholds for a minimum of two consecutive years before formally reclassifying the program's risk categorization. We will coordinate with OMB in FY 2015 to formally change this risk categorization and, in so doing, remove the requirement for future annual reporting of FFEL estimates.

Other Department Programs

The Department performed a risk assessment for all non-FSA grant programs during FY 2013 using the methodology described in the FY 2011 AFR. This methodology relies on an examination of the total questioned costs for each program that result from required OMB Circular A-133 Single Audits. The Department's FY 2013 assessment determined that none of these non-FSA grant programs were susceptible to significant improper payments. The specific grant programs reviewed are provided on the Department's website.

During FY 2013, the Department completed a risk assessment of all contract payments, including those for FSA. The risk assessment was based on the results of an ongoing FY 2013 contingency-based contract to review FY 2007 through FY 2012 contract payments as well as cyclical A-123 risk assessments. Based on an evaluation of the risk assessments and results of the recapture audit, the Department determined that contract payments are not susceptible to significant improper payments.

In 2014, the Department also completed risk assessments on administrative payments to employees in accordance with IPERIA. Five areas of administrative payments were examined: Salary, Locality Pay, Travel, Purchase Card, and Transit Benefits. The Department determined it was not susceptible to significant improper administrative payments to employees. This analysis was based on a review of actual recaptured payments and the likelihood of payment errors. Each respective administrative payment area noted above was below the risk threshold designated for susceptibility.

Improper Payment Estimate Methodologies

FSA-Managed Programs

After refining the FY 2013 alternative estimation methodology, the Department obtained approval from OMB to use an alternative methodology for estimating improper payments for the FSA programs for FY 2014 and forward. This alternative methodology, as contemplated in OMB Circular A-123, Appendix C (A-123C), leverages data collected through FSA Program Reviews, which include procedures such as verifying student-reported income levels, student academic performance, and eligibility on the disbursed funds for a sample of students in each review. The methodologies for all three programs are described on the Department's improper payment website.

In addition to the rate that resulted from the OMB-approved methodology, the Department has, consistent with prior years, estimated an improper payment rate for the Pell program using Internal Revenue Service (IRS) data. This estimate is provided as a supplemental data point for comparison to prior year estimates calculated under that methodology.

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

The Department estimates improper payments for this program using questioned cost data in audit reports. This methodology is described in the FY 2012 AFR. No reduction targets are proposed since the Department's risk assessments have not identified Title I as a program susceptible to significant improper payments; Title I is included in the table because it is a Section 57 program.

Improper Payment Estimates (Dollars in Millions)

Program or Activity	FY 2013			FY 2014			FY 2015			FY 2016			FY 2017		
	Outlays $[2]	IP %	IP $	Outlays $[3]	IP %	IP $	Outlays $[4]	IP %	IP $	Outlays $[4]	IP %	IP $	Outlays $[4]	IP %	IP $
Pell Grants[1]	32,338	2.26	731	31,554	2.16	682	32,456	2.15	698	33,135	2.14	709	34,767	2.13	740
Direct Loan	102,497	1.03	1,056	102,140	1.50	1,532	100,936	1.49	1,504	106,057	1.48	1,570	111,473	1.46	1,628
FFEL	10,817	0.00	0	10,016	0.00	0	8,004	0.00	0	7,458	0.00	0	7,101	0.00	0
Title I	14,724	.385	56.7	16,372	.214	35.0	16,062	.214	34.4	15,394	.214	32.9	15,442	.214	33.0

(1) The Pell estimate for FY 2013 was reported using the previously developed methodology that relies on a comparison of student data with IRS data. In FY 2014, OMB approved the alternative methodology relying on FSA Program Reviews, and the Pell estimates are reported using the updated methodology. As a point of comparison, the FY 2014 preliminary estimate for Pell using the previous methodology that relies on data from comparing student data with IRS data is 1.94 percent or $612 million.

(2) The source of FY 2013 outlays for all programs is FMS as presented in the FY 2013 AFR.

(3) The source of FY 2014 outlays for all program amounts is FMS.

(4) The source of FY 2015–2017 Pell outlay amounts is the supporting documentation for the FY 2014 President's Budget request at the Mid-Session Review. The source of FY 2015–2017 Direct Loan and FFEL outlay amounts is the supporting documentation for the FY 2014 President's Budget request.

NOTE: The FY 2014 Pell overpayment improper payment rate estimate is 2.11 percent or $666 million and the underpayment improper payment rate estimate is 0.05 percent or $16 million. The FY 2014 Direct Loan overpayment improper payment rate estimate is 1.46 percent or $1,491 million and the underpayment improper payment rate estimate is 0.04 percent or $41 million. The FY 2014 FFEL overpayment and underpayment improper payment rate estimates round down to 0.000 percent or $0 million.

Root Causes and Corrective Actions

This section summarizes the root causes of improper payments and the Department's strategies to mitigate improper payments.

FSA-Managed Programs

FSA continues to utilize the Internal Revenue Service Data Retrieval Tool (IRS DRT), which enables Title IV student aid applicants and, as needed, parents of applicants, to transfer certain tax return information from an IRS website directly to their online Free Application for Federal Student Aid (FAFSA). In addition, FSA continues to enhance verification procedures and require selected schools to verify specific information reported on the FAFSA by student aid applicants. These and other ongoing corrective actions, such as system edits, Program Reviews, and compliance audits, are described in the FY 2012 AFR.

In the charts that follow for each risk-susceptible program, the root causes presented were identified through improper payment testing and categorized using categories of error as defined in the March 2010 update to OMB Circular A-123, Appendix C (OMB Memorandum M-10-13). The corrective actions presented are recommendations to the schools (for Pell Grants and Direct Loans) and financial institutions (for FFEL) for findings that resulted from FSA Program Reviews.

Pell Grant Program. The Pell Grant Program includes the drawdown of funds by schools and the disbursement of aid from the school to the student; year-end closeout and the return of unsubstantiated funds; return of undisbursed funds to Title IV collections from schools; and collections by the school on overpayments from recipients.

Direct Loan Program. The Direct Loan Program includes the drawdown of funds by schools, the origination of a loan and disbursement of funds from the school to the student (or their account); consolidations; servicing of the loan and collections from loan holders; and return of Title IV collections (undisbursed funds or overpayments) from schools.

Root Causes and Corrective Actions for the Pell Grant and Direct Loan Programs

IPIA Error Category	Root Cause
Documentation and Administrative Errors	Incorrect awards based on Expected Family Contribution (EFC)
	Incorrect processing of student data during normal operations
	Student account data changes not applied or processed correctly
Verification Errors	Ineligibility for a Pell Grant/Direct Loan (e.g., validity of high school attended, history of degrees obtained)
	Satisfactory academic progress not achieved
	Incorrectly calculated return period

Improper payment findings are detailed within the FSA Program Reviews, which also include the corrective actions taken by the schools or financial institutions to either resolve the finding or finding(s) that contain liabilities or detail their ongoing corrective actions. Overall, FSA necessitates that all findings identified during the FSA Program Reviews are tracked through resolution via the Postsecondary Education Participants System (PEPS). This corrective action process is further described in the FY 2012 AFR.

Root Causes and Corrective Actions for the Direct Loan Consolidation Program

IPIA Error Category	Root Cause
Documentation and Administrative Errors	Incorrect processing of Loan Verification Certificate (LVC)
	Processing of duplicate LVCs
	Loan not intended for consolidation was processed
	Incorrect information submitted on the LVC and processed

The underlying root cause of improper payments identified for Direct Loan Consolidations in the table above is due to processing errors at the servicer level. However, the legacy servicer's contract is ending and the day-to-day servicing of newly made traditional Direct Loan Consolidations has been transferred to the Title IV Additional Servicers' (TIVAS) platforms. FSA will continue to monitor the full transition of the consolidation function to these servicers.

Improper payments identified through testing of Direct Loan Consolidations for FY 2014 were remediated or are in the process of being remediated.

FFEL Program. During FY 2014, the FFEL Program made no new loan originations. FY 2014 payment types and cash flows associated with the guarantees on loans originated in prior years (i.e., the existing FFEL portfolio) include: Special Allowance Payments (SAP), Interest Benefits, Lender Fees, Origination Fees, Consolidation Loan Rebate Fees, Reinsurance, and Account Maintenance Fees.

Root Causes and Corrective Actions for the FFEL Program

Most of the reporting errors observed during FY 2014 were the result of smaller lenders using software systems that were not updated or were processed on bank systems not designed for processing the reporting of FFEL program loans.

IPIA Error Category	Root Cause
Documentation and Administrative Errors	Manual entries processed erroneously (e.g., using only one payment code during the billing quarter when an activity occurred that required the use of two billing codes)
	Incorrect calculation of the average daily balance due to software formula errors

Corrective actions include recommendations to the financial institutions for findings that resulted from FSA Program Reviews, which include, but are not limited to: regularly conduct staff training courses designed to prevent incorrect usage of payment codes, including SAP codes, and incorrect calculation of average daily balances; establish procedures that eliminate reporting errors related to manual entries processed erroneously; hire sufficient staff/employees who are knowledgeable of the FFEL program; and obtain and install any necessary updates to their systems to certify software formulas are accurate.

If unable to perform servicing requirements, lenders are required to seek the services of other individuals or firms to reduce and eliminate reporting errors due to manual processing.

Root Cause Summary

Consistent with FY 2013, the results of the root cause analysis across all risk-susceptible FSA programs for FY 2014 highlighted that the underlying root cause of improper payments was due to processing errors that occur at the institution level.

Further analysis of the improper payment findings and associated root causes identified for FSA programs were attributed to Documentation and Administrative Errors and Verification Errors (as defined by IPIA) by the following percentages, calculated by dollar amount (i.e., the absolute dollar amount of improper payments identified within the category proportional to the total dollar amount of error in the sample reviewed):

IPIA Error Category	Pell Grants	Direct Loans	Direct Loan Consolidations	FFEL
Documentation and Administrative Errors	15%	19%	100%	100%
Verification Errors	85%	81%	0%	0%

Other Department Programs

Risk Management. The Department continues to take measures to prevent improper payments through the application of the Entity Risk Review (ERR) report by grants officers and awarding officials in the preaward stage of the grants process. Using data drawn from the Federal Audit Clearinghouse, Dun & Bradstreet, the Department's grants system, and Institutes of Higher Education (IHE) accreditation reporting, this report identifies financial, programmatic, and controls risks posed by award to the prospective grantee. Program staff apply this report in devising special conditions of award, as well as monitoring plans for the life of the grant, strengthening them as the Department's first line of defense against improper payments by grantees.

Do Not Pay. The Department continues to mitigate risk of improper payments by leveraging available data to detect and prevent payments before they occur. These data are collected through the Continuous Control Monitoring System (CCMS), which applies seven integrity checks that are used as systemic preventive and predictive analytic tools to mitigate risks related to improper payments. Two additional integrity checks were implemented in FY 2014 that increased the reliability of transactional controls and the effectiveness of antifraud controls. The Department also participates in the Department of Treasury Do Not Pay System initiative. Both of these preventive processes allow the Department to conduct research and investigation of any findings in order to initiate proper actions.

Implementation of the Do Not Pay Initiative to Prevent Improper Payments						
	Number (#) of payments reviewed for improper payments	Dollars ($) of payments reviewed for improper payments	Number (#) of payments stopped	Dollars ($) of payments stopped	Number (#) of improper payments reviewed and not stopped	Dollars ($) of improper payments reviewed and not stopped
Reviews with the Death Master File (DMF) only	998,447	$138,196,388,434	0	0	0	0
Reviews with System for Award Management (SAM) databases	1,005,029	$140,864,372,529	0	0	0	0

Data Analytics. The Department leverages data analytics techniques to help reduce the risk of improper payments and to better identify and address root causes of error. The Department gathers and manages thousands of records on audits of grantees in an Audit Accountability and Resolution Tracking System (AARTS). The Department is analyzing the audit data to determine trends in findings and resolution throughout the Department; these data enable the Department to search for and better understand commonalities in findings as well as grantees with repeat findings. This analytics effort is helping the Department reduce improper payments by strengthening audit resolution and grants management.

Recovery Auditing

Agencies are required to conduct recovery audits for contract payments and programs that expend one million dollars or more annually if conducting such audits would be cost effective. The following table presents a summary of the Department's cost-benefit analysis.

Additional Recovery Auditing Cost Effectiveness	
Recovery Audit Program Area	Cost Effective
Non-FSA Grant Programs	No
FSA Programs	No
Contracts	No

A comprehensive report on the cost effectiveness of the various recapture audit programs can be found in the Department's FY 2012 Report on the Department of Education's Payment Recapture Audits.

Contract Payment Recapture Audits. Although the Department has not found prior contract recovery audits to be cost effective, the Department issued a contingency-based contract during FY 2013 to audit all FY 2007 through FY 2012 contract payments for possible errors and recapture. This contract was awarded with the expectation that advances in data mining techniques might be able to detect payment errors that were previously undetected.

The audit ended in January 2014 and did not uncover any improper payments. In addition to the audit, as part of its A-123 review, the Department reviewed a random sample of contract payments made in FY 2014 and similarly did not uncover any improper payments subject to recovery. As a result of these efforts, the Department plans no further efforts to conduct recapture audits.

The following chart presents the results of previous recapture efforts:

Contract Payment Recapture Audit Reporting ($ in millions)	
Amount Subject to Review for Current Year (2014) Reporting*	$10,027
Actual Amount Reviewed and Reported (2014)*	$10,027
Amounts Identified for Recovery (2014)	$0
Amounts Recovered (2014)	$0
% of Amount Recovered out of Amount Identified (2014)	NA
Amount Outstanding (2014)	$0
% Amount Outstanding out of Amount Identified (2014)	NA
Amount Determined Not to be Collectable (2014)	$0
% Amount Determined Not to be Collectable out of Amount Identified (2014)	NA
Amounts Identified for Recovery Prior Years (2005–14)	$0
Amounts Recovered (2005–14)	$0
Cumulative Amounts Identified for Recovery (2005–14)	$0
Cumulative Amounts Recovered (2005–14)	$0
Cumulative Amounts Outstanding (2005–14)	$0
Cumulative Amounts Determined Not to be Collectable (2005–14)	$0

*Includes FY 2007 through FY 2012 contract payments subject to the FY 2013–2014 recapture audit contract.

The Department has not established formal recovery targets for contract payments given the consistently insignificant findings. Since FY 2004, the Department's audits have found no improper payments for recovery, and there are no outstanding overpayments to report. Should future contract payments be identified for recovery, the Department will establish recovery targets, taking into consideration the nature of the overpayments and any potential barriers to recovering funds.

Recoveries of Improper Payments. The Department works with grantees and Title IV (FSA) program participants to resolve and recover amounts identified in Compliance Audits, OIG Audits, and Department-conducted program reviews as potential improper payments. Accounts receivable are established for amounts determined to be due to the Department and collection actions are pursued. Recipients of Department funds can appeal the management decisions regarding funds to be returned to the Department, thereby delaying or decreasing the amounts the Department is able to collect. The following chart provides estimates of the amounts identified and recovered through all Compliance Audits, OIG Audits, and Program Reviews for FY 2012 through FY 2014. The Department anticipates recovering similar amounts in FY 2015.

Overpayments Recaptured Outside of Payment Recapture Audits ($ in millions)

Agency Source	Amount Identified (FY 2014)	Amount Recovered (FY 2014)[1]	Amount Identified (FY 2013)	Amount Recovered (FY 2013)[1]	Cumulative Amount Identified (FY 2012–14)	Cumulative Amount Recovered (FY 2012–14)
Compliance Audit Reports	26.3	14.6	19.8	7.7	67.8	26.6
OIG Audit Reports	0.4	0.7	22.1	5.2	25.2	6.1
Program Reviews	47.7	18.5	38.9	8.0	117.3	33.2

[1] Includes all amounts recovered during the year, not just the recoveries of amounts identified during the year.

In addition to the amounts above, for the Pell Grant Program, recoveries also occur when overpayments to students are assigned to FSA for collection. Pell amounts recovered through student debt collection were approximately $13.7 million in FY 2014, $13.0 million in FY 2013, and $113.7 million cumulative from FY 2004 to FY 2014. While all programs may have student debts transferred to debt collection, the categorization of resulting collections as an improper payment recovery is unique to Pell. Unlike loans, Pell Grant payments transferred to debt collection commonly indicate a potential improper payment at time of disbursement.

Statutory and Regulatory Barriers

The Department believes that there are high burden of proof requirements in the *General Education Provisions Act* (GEPA), which are a significant reason why the Department recovers only a small percentage of the original questioned costs in non-FSA grant program audits. The GEPA, 20 U.S.C. 31 Subchapter IV § 1234a, requires the Department to establish a prima facie case for the recovery of funds, including an analysis reflecting the value of services obtained. In accordance with 20 U.S.C. 31 Subchapter IV § 1234b, any amount returned must be proportionate to the extent of harm the violation caused to an identifiable federal interest. A detailed discussion of program-specific barriers can be found in the FY 2012 Report on the Department of Education’s Payment Recapture Audits.

Accountable Official’s Report on High-Priority Programs

OMB issued an overhauled version of Appendix C to Circular A-123 on October 20, 2014. Included among the changes is the elimination of a separate report on high-priority programs as mandated by Executive Order 13520, *Reducing Improper Payments* (November 30, 2009), and previous OMB Appendix C guidance. To eliminate duplicate reporting, the new version of Appendix C to Circular A-123 states that agencies should include the accountable official’s report on high-priority programs in their AFRs or PARs beginning with FY 2014 reporting.

An agency's accountable official's report is required to include:

(i) the agency's methodology for identifying and measuring improper payments by the agency's high-priority programs;

(ii) the agency's plans, together with supporting analysis, for meeting the reduction targets for improper payments in the agency's high-priority programs; and

(iii) the agency's plan, together with supporting analysis, for ensuring that initiatives undertaken pursuant to this order do not unduly burden program access and participation by eligible beneficiaries.

In FY 2010, OMB designated the Pell Grant Program a high-priority program because estimated FY 2010 Pell improper payments of $1,005 million exceeded the OMB FY 2010 high-priority program threshold of $750 million. Since then, the Department has worked with OMB to implement all applicable high-priority program requirements. In order to avoid duplicate reporting on the Department's high-priority programs, certain requirements already reported in preceding sections of this AFR will be referenced in this section instead.

Estimation Methodology and Reduction Targets. Please see the Improper Payment Estimate Methodologies section for additional information on the new alternative estimation methodology, this year's estimate, and reduction targets for the Pell Grant Program. This alternative methodology, which leverages FSA Program Reviews, is described on the Department's improper payment website.

Root Causes and Internal Controls. Root causes and internal controls for improper payments in the Pell Grant Program are discussed in the previous sections of this AFR. Additional controls for the Pell Grant Program are presented in this section.

Front-end System Edits. The Department continues to take steps to implement or improve preventative controls, such as front-end edits in eligibility and payment systems. Recent examples include the following.

As reported in the FY 2012 Accountable Official's Report, the Department implemented two new controls related to the Pell Grant Program (Pell Grant Lifetime Eligibility Used (LEU) and Unusual Enrollment History (UEH)).

- **Pell LEU.** The *Consolidated Appropriations Act of 2012,* Public Law 112-74, amended the *Higher Education Act* (HEA) of 1965, as amended, section 401(c)(5), to reduce the duration of a student's eligibility to receive a Federal Pell Grant from 18 semesters (or its equivalent) to 12 semesters (or its equivalent). This provision applies to all Federal Pell Grant eligible students effective with the 2012–13 award year. The calculation of the duration of a student's eligibility will include all years of the student's receipt of Federal Pell Grant funding. This change in the duration of students' Federal Pell Grant eligibility is not limited only to students who received their first Federal Pell Grant on or after the 2008–09 award year, as the HEA previously provided when the duration of eligibility was 18 semesters. Beginning with the 2013–14 award year, Pell Grant LEU percentages are provided by National Student Loan Data System (NSLDS) and are included along with the Pell Lifetime Limit Flag values on the Institutional Student Information Record (ISIR).

- **Pell UEH Flag.** The UEH Flag serves the purpose of indicating whether the student has an unusual enrollment history with regard to the receipt of Federal Pell Grant funds. When a student's records indicate that the student's enrollment history falls significantly outside the norm, the student's records must be reviewed by the institution. Based upon academic transcripts it may already possess, or by obtaining academic transcripts or grade reports, the institution must determine, for each of the previously attended institutions, whether academic credit was earned during the relevant award year. Academic credit is considered to have been earned if the academic transcript shows that the student completed any number of credits or clock hours.

  If the institution makes a determination of continued eligibility, the financial aid administrator may choose to require the student to establish an academic plan, similar to the type of plan used to resolve satisfactory academic progress appeals. It may also be necessary to counsel the student about the Pell Grant duration of eligibility provisions—and the impact of the student's attendance pattern on the future Pell Grant eligibility. It is also recommended that the student be counseled on the impact of loan eligibility under the new 150 percent subsidized loan limitation.

  If a student who did not earn academic credit at the relevant institutions does not provide, to the financial aid administrator's satisfaction, an explanation and documentation for each of those failures, the institution must deny the student additional Title IV, HEA program assistance, not just Pell Grant eligibility.

In FY 2013, a new Central Processing System (CPS) edit was added: the NSLDS Fraud Loan Flag. Previously, a warning was indicated for situations where a guaranty agency, a Perkins school, or the Department (e.g., OIG) had determined that a loan was obtained fraudulently. This new control alerts both the institution and the FAFSA applicant that the NSLDS indicates that the student has one or more student loans that may have been obtained fraudulently and is not eligible to receive any federal student aid until this issue is resolved. In these rare cases, the loan is listed under the perpetrator's identifiers and thus he or she cannot get further Title IV federal student aid, including a Pell Grant.

In addition, in FY 2014, two new IRS Display Flags were added to CPS and included in FAFSA reports sent to schools and students: the Student IRS Display Flag and the Parent IRS Display Flag. The new IRS Display Flags inform schools whether the IRS DRT was displayed to the student or parent, and, if not, the reason the IRS DRT was not displayed. The IRS Display Flags are used in addition to the Student IRS Request Flag and Parent IRS Request Flag, which describe the student or parent's use of the IRS DRT. The IRS Request Flags inform schools whether tax information was requested from the IRS and whether the student or parent changed the requested data after it was transferred. These flags aid schools in their verification requests to students.

IRS Data Retrieval Tool. The IRS DRT is a joint effort by the Department and the IRS which enables Title IV student aid applicants and, as needed, parents of applicants to transfer certain tax information from an IRS website directly to their online FAFSA. For the 2014–15 FAFSA processing cycle, 5.6 million students and parents have transferred their tax data from the IRS to the FAFSA using the IRS DRT. This usage represents approximately 31.7 percent of the 17.7 million FAFSAs submitted for the 2014–15 academic year between January 1, 2014, and September 28, 2014. Recent functionality changes to the IRS DRT include redesigned filtering questions to require yes or no responses instead of check-the-box responses and improved instructions for using the IRS

DRT, including enhanced help text to aid users in determining who might be able to use the tool and how it should be used.

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 by using web-based “smart logic” and promoting the real-time use of the IRS DRT. For example, compared to the 2009–10 FAFSA processing cycle, the estimated time to complete the FAFSA application online has decreased from approximately 60 minutes to less than 30 minutes. These enhancements, coupled with improved error detection, should allow FSA to further reduce improper payments.

High-priority programs are required to develop a supplemental measure (or measures) to help gauge progress in reduction efforts and to augment the annual measure. In coordination with OMB, the Department developed a supplemental measure around IRS DRT usage. The most current supplemental measure for the Pell Grant Program is the total number of Pell-eligible applicants who transferred tax data from the IRS as a percent of the total number of Pell-eligible applicants who were determined to be eligible to use the IRS DRT to transfer tax data. As of September 28, 2014, this measure is estimated at 66.5 percent for the 2014–15 FAFSA processing year. Upon OMB approval, the Department will begin to post IRS DRT usage status using this measure to PaymentAccuracy.gov.

School Verification. FSA continues to utilize the verification process as a key action in addressing the inaccuracies on the FAFSA by enhancing verification regulations which are published in the Federal Register annually. Verification is the process required by the Department that schools conduct to confirm specific information reported on the FAFSA by the applicant. The Department requires schools to have written verification policies and procedures to include deadlines for students to submit documentation and consequences of not meeting the deadlines; method of notifying students of award changes due to verification; correction procedures; and procedures for referring overpayment cases to the Department. Schools are required to give each applicant selected for verification a written statement explaining the student’s responsibilities and the school’s method of notification during the process.

The Department continues to refine the verification process and to conduct statistical analysis to establish the most effective and efficient criteria for selecting applicants with the highest probability of error on their FAFSA submissions for verification. Changes to the verification process for the 2014–15 award year included adding other untaxed income to the FAFSA items selected for verification, adding identity verification result functionality to financial aid administrator access and making adjustments to the verification tracking groups as discussed below.

As with 2014–15 award year verification, the Department will continue to use data-based statistical analysis to select applicants for verification. A Verification Tracking Flag will be set on the applicant’s Institutional Student Information Record (ISIR) to indicate placement into one of the 2015–16 Verification Tracking Groups. An applicant will remain in the original 2015–16 Verification Tracking Group for the entire 2015–16 award year regardless of subsequent corrections to the applicant’s record. Although 2015–16 applicants will not be assigned to Verification Tracking Group V2 (formerly Supplemental Nutrition Assistance Program (SNAP) Verification Group), SNAP must be verified for applicants placed in

Verification Tracking Groups V1, V4, V5, and V6, if the receipt of SNAP is indicated on the ISIR. The individual verification items from the 2015–16 Federal Register notice that an applicant must verify are based upon the Verification Tracking Group to which the applicant is assigned. The complete chart of the 2015–16 Verification Tracking Groups is found in the Department's Dear Colleague Letter, GEN-14-11, issued on June 30, 2014.

Annually, the Department analyzes grant recipients and the verification selection system, and informs the financial aid community of what FAFSA items are subject to verification for the upcoming award year. This annual analysis is performed to enhance verification methodology and to meet the goal of selecting the applicants who are most likely to have incorrect information on their FAFSA.

The anticipated costs to the Department related to improving the IRS DRT so that more FAFSA applicants use the tool is, in relation to projected savings and simplicity, marginal. More significant, but not able to be estimated, are the increased costs to the schools and colleges that must perform verification. However, to the extent that applicants use the IRS DRT, schools' verification efforts are reduced.

Measures to Ensure Program Access. FSA is committed to ensuring program access and providing federal student aid, such as the Pell Grant, to all eligible students pursuing postsecondary education. The IRS DRT supports access to aid programs through the financial aid application process by allowing students to transfer tax data directly from the IRS to the online FAFSA and lessens the burden of income verification. Thus, FSA continuously promotes use of the IRS DRT. In addition, FSA recognizes the importance of an application process that can accurately determine eligibility without causing undue burden on students and their families. For example, while we recognize an increased and well adopted move towards online FAFSA completion, we continue to offer additional application methods to individuals to ensure that applicants can take advantage of an application option that best suits their personal needs. Furthermore, improvements in the last few years to the FAFSA and IRS DRT have resulted in a decrease in the average time it takes a student to complete the online FAFSA.

On February 4, 2013, FSA's Customer Experience group announced a new partnership alliance between FSA and the IRS. This partnership is a result of ongoing IRS DRT agreement between the two organizations. The new partnership will focus on reaching more individuals in low- to moderate-income communities with the goal of providing them with information, assistance, and access to relevant IRS and FSA services. The partnership is expected to contribute to increased awareness of FSA programs, such as the Pell Grant Program, and create opportunities for increased access to the FAFSA, which determines student aid eligibility.

In addition, as indicated in Dear Colleague Letter GEN-13-16 issued on June 13, 2013, and referred to in GEN-14-05, the Department encouraged all FAFSA applicants to use IRS DRT to transfer official IRS tax return information into their FAFSA application, either when initially completing the FAFSA or during the corrections process. The Department also noted in GEN-13-16 that acceptable documentation for verification of IRS tax return information is generally limited to the IRS DRT or an IRS Tax Return Transcript.

Beginning with the 2013 tax year (the 2014–15 FAFSA Processing Year), the IRS has added a new, more efficient way that tax filers can request and receive Tax Return

Transcripts. With the new IRS "Get Transcript Online" tool, the tax filer submits an online transcript request to the IRS and, if the request is authenticated, a second window displays the transcript in Portable Document Format (PDF). This new IRS tool potentially reduces the burden on FAFSA applicants who are requested to provide tax transcripts. Overall, both the Department's and FSA's strategic plans support efficient and effective access to student aid programs such as the Pell Grant Program.

In March 2014, the Department launched a new initiative, the FAFSA Completion Initiative, through which the Department is partnering with state student grant agencies to allow these agencies to provide secondary schools, school districts, and certain designated entities with limited, yet important, information on student progress in completing the FAFSA form. Because the timely completion of a FAFSA form is an essential step for many families in obtaining financial aid to pursue a postsecondary education, the FAFSA Completion Initiative will enable state student grant agencies and their school and district partners to identify those students who have not filed a FAFSA form and better target counseling, filing help, and other resources to those students. FAFSA completion is essential for receiving federal financial aid; therefore, identifying such students can promote college access and success by ensuring students, particularly low-income students, have access to financial aid to fund their education.

United States Department of Education
Schedule of Spending

For the Years Ended September 30, 2014 and 2013
(Dollars in Millions)

	FY 2014 Budgetary	FY 2014 Non-Budgetary Credit Reform Financing Accounts	FY 2013 Budgetary	FY 2013 Non-Budgetary Credit Reform Financing Accounts
Section I: What Money Is Available to Spend?				
This section presents resources that were available to spend by the Department.				
Total Resources	$ 112,443	$ 243,566	$ 102,544	$ 257,395
Amount Available but Not Agreed to be Spent	(12,125)	(69)	(13,700)	-
Amount Not Available to be Spent	(2,712)	(10,040)	(2,507)	(11,315)
Total Amounts Agreed to be Spent	**$ 97,606**	**$ 233,457**	**$ 86,337**	**$ 246,080**
Section II: How Was the Money Spent?				
This section presents services and items purchased, is grouped by major program, and is based on outlays.				
Increase College Access, Quality, and Completion				
Credit Program Loan Disbursements and Claim Payments	$ 65	$ 144,929	$ 97	$ 141,724
Credit Program Subsidy Transfers	18,570	39,534	6,405	48,598
Federal Interest Payments	3	30,620	-	28,453
Other Credit Program Payments	3	1,423	3	1,692
Federal Student Loan Reserve Fund Valuation	194	-	279	-
Grants	37,223	-	38,344	-
Personnel Compensation and Benefits	270	-	258	-
Contractual Services	1,205	1,108	1,216	671
Other [1/]	35	-	40	-
Total Program Spending	**57,568**	**217,614**	**46,642**	**221,138**
Improve Preparation for College and Career from Birth Through 12th Grade, Especially for Children with High Needs				
Grants	23,032	-	24,777	-
Personnel Compensation and Benefits	69	-	72	-
Contractual Services	96	-	100	-
Other [1/]	12	-	14	-
Total Program Spending	**23,209**	**-**	**24,963**	**-**
Ensure Effective Educational Opportunities for All Students				
Grants	16,793	-	16,728	-
Personnel Compensation and Benefits	162	-	160	-
Contractual Services	55	-	57	-
Other [1/]	23	-	24	-
Total Program Spending	**17,033**	**-**	**16,969**	**-**
Enhance the Education System's Ability to Continuously Improve				
Grants	1,519	-	1,453	-
Personnel Compensation and Benefits	91	-	82	-
Contractual Services	451	-	433	-
Other [1/]	15	-	31	-
Total Program Spending	**2,076**	**-**	**1,999**	**-**
Total Spending	**$ 99,886**	**$ 217,614**	**$ 90,573**	**$ 221,138**
Amounts Remaining to be Spent[2/]	(2,280)	15,843	(4,236)	24,942
Total Amounts Agreed to be Spent	**$ 97,606**	**$ 233,457**	**$ 86,337**	**$ 246,080**
Section III: Who Did the Money Go To?				
This section identifies with whom the Department is spending money based on obligations incurred.				
Non-Federal Obligations	$ 97,101	$ 233,457	$ 85,598	$ 246,076
Federal Obligations	505	-	739	4
Total Amounts Agreed to be Spent	**$ 97,606**	**$ 233,457**	**$ 86,337**	**$ 246,080**

[1/] Other primarily consists of payments for rent, utilities, communication, land, structures, equipment, travel, and transportation.

[2/] The "Amounts Remaining to be Spent" line is the difference between "Total Spending" and "Total Amounts Agreed to be Spent." Actual spending in the current FY may include spending associated with amounts that are agreed to be spent during previous FYs, which may result in negative amounts shown for the "Amounts Remaining to be Spent" line.

Summary of Financial Statement Audit and Management Assurances

The following tables provide a summarized report on the Department's financial statement audit and its management assurances. For more details, the auditor's report can be found beginning on page 102 and the Department's management assurances on pages 37–47.

Summary of Financial Statement Audit

Audit Opinion: Unmodified*
Restatement: No

Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Ending Balance
Total Material Weaknesses	**0**	**0**	**0**	**0**	**0**

Summary of Management Assurances

Effectiveness of Internal Control over Financial Reporting—*Federal Managers' Financial Integrity Act* (FMFIA) 2

Statement of Assurance: Unqualified*

Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Total Material Weaknesses	**0**	**0**	**0**	**0**	**0**	**0**

The Department had no material weaknesses in the design or operation of the internal control over financial reporting.

Effectiveness of Internal Control over Operations—FMFIA 2

Statement of Assurance: Unqualified*

Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Total Material Weaknesses	**0**	**0**	**0**	**0**	**0**	**0**

Conformance with Financial Management System Requirements—FMFIA 4

Statement of Assurance: The Department systems conform to financial management system requirements.

Non-Conformances	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Total Non-Conformances	**0**	**0**	**0**	**0**	**0**	**0**

Compliance with *Federal Financial Management Improvement Act (FFMIA)*

	Agency	Auditor
1. System Requirements	**No lack of substantial compliance noted**	**No lack of substantial compliance noted**
2. Federal Accounting Standards	**No lack of substantial compliance noted**	**No lack of substantial compliance noted**
3. United States Standard General Ledger at Transaction Level	**No lack of substantial compliance noted**	**No lack of substantial compliance noted**

*Table uses the term "unmodified" for financial statement audit opinions and "unqualified" for management assurances based on OMB guidance.

UNITED STATES DEPARTMENT OF EDUCATION
OFFICE OF INSPECTOR GENERAL

The Inspector General

October 9, 2014

TO: The Honorable Arne Duncan
Secretary of Education

FROM: Kathleen S. Tighe Kathleen S Tighe
Inspector General

SUBJECT: Management Challenges for Fiscal Year 2015

The Reports Consolidation Act of 2000 requires the U.S. Department of Education (Department), Office of Inspector General 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 post significant challenges because of their breadth and complexity.

Last year, we presented five management challenges: improper payments, information technology security, oversight and monitoring, data quality and reporting, and information technology system development and implementation. While the Department remains committed to addressing these areas and has taken or plans action to correct many of their underlying causes, each remains as a management challenge for fiscal year (FY) 2015.

The FY 2015 management challenges are:

(1) Improper Payments,
(2) Information Technology Security,
(3) Oversight and Monitoring,
(4) Data Quality and Reporting, and
(5) Information Technology System Development and Implementation.

We provided our draft challenges report to Department officials and considered all comments received. We look forward to working with the Department to address the FY 2015 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.

Office of Inspector General's (OIG) Management and Performance Challenges for Fiscal Year 2015 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 five management challenges: improper payments, information technology security, oversight and monitoring, data quality and reporting, and information technology system development and implementation. Although the Department made some progress in addressing these areas, each remains as a management challenge for fiscal year (FY) 2015.

The FY 2015 management challenges are:

(1) Improper Payments,

(2) Information Technology Security,

(3) Oversight and Monitoring,

(4) Data Quality and Reporting, and

(5) Information Technology System Development and Implementation.

These challenges reflect continuing vulnerabilities and emerging issues faced by the Department as identified though recent OIG audit, inspection, and investigative work. A summary of each management challenge area follows. The full FY 2105 Management Challenges Report is available at http://www2.ed.gov/about/offices/list/oig/managementchallenges.html.

Management Challenge 1—Improper Payments

Why This Is a Challenge

The Department must be able to ensure that the billions of dollars entrusted to it are reaching the intended recipients. The Department identified the Federal Pell Grant (Pell), William D. Ford Federal Direct Loan (Direct Loan), and Federal Family Education Loan (FFEL) programs as susceptible to significant improper payments.

Our recent work has demonstrated that the Department remains challenged to meet new requirements and to intensify its efforts to successfully prevent, identify, and recapture improper payments. We have identified concerns in numerous areas relating to improper payments, including calculation of the estimated improper payment rate for the Pell, FFEL, and Direct Loan programs and improper payments involving grantees and contractors. Our Semiannual Reports to Congress from April 1, 2011, through March 31, 2014, included more than $53 million in questioned or unsupported costs from audit reports and over $47 million in restitution payments from our investigative activity.

Progress in Meeting the Challenge

The Department has revised its estimation methodologies for each of its risk-susceptible programs (Pell, Direct Loan, and FFEL) and the Office of Management and Budget approved the new estimation methodologies for all three programs in September 2014. Although the Office of Management and Budget (OMB) approved the estimation methodologies, improvements are needed to ensure their completeness.

The Department has identified root causes for improper payments in its risk-susceptible programs that included documentation, administrative, and verification errors. In response, the Department planned or completed numerous corrective actions. These actions included a voluntary data exchange program with the Internal Revenue Service that is intended to improve the accuracy of financial aid applicant's income data reported on the online Free Application for Federal Student Aid (FAFSA); improved verification requirements; enhanced system edits within the Central Processing System, Common Origination and Support System, and the National Student Loan Data System; continued use of data analytics; and various internal controls to prevent and detect errors integrated into its grant and Direct Loan program-related systems and activities.

What Needs to Be Done

The Department needs to continue to explore additional opportunities for preventing, identifying, and recapturing improper payments. The Department should continue to work to develop estimation methodologies that adequately address recommendations made in our audit work.

Management Challenge 2—Information Technology Security

Why This Is a Challenge

The OIG has identified repeated problems in information technology (IT) security and noted increasing threats and vulnerabilities to Department systems and data. Department systems contain or protect an enormous amount of confidential information such as personal records, financial information, and other personally identifiable information. Without adequate management, operational, and technical security controls in place, the Department's systems and information are vulnerable to attacks. Unauthorized access could result in losing data confidentiality and integrity, limiting system availability, and reducing system reliability.

Over the last several years, IT security audits have identified controls that need improvement to adequately protect the Department's systems and data. This included weaknesses in configuration management, identity and access management, incident response and reporting, risk management, security training, plan of action and milestones, remote access management, and contingency planning. In addition, investigative work performed by the OIG has identified IT security control concerns in areas such as the Federal Student Aid (FSA) PIN system, mobile IT devices, malware, incident response, and e-mail spear phishing.

Progress in Meeting the Challenge

The Department provided corrective action plans to address the recommendations in our audits and has procured services to provide additional intrusion detection capabilities for its primary enterprise environment and related data center. The Department also awarded a contract for a continuous monitoring program of its enterprise infrastructure. It has nearly completed the requirement of implementing two-factor authentication for Government and contractor employees and is well into the process of supplying and implementing multifactor authentication for its external business partners.

The Department also stated that it is laying a foundation for increased security oversight and efficiency with an in-house Cyber Security Operations Center that is scheduled to be fully operational in the latter part of 2014.

What Needs to Be Done

The Department needs to continue its efforts to develop more effective capabilities to respond to potential IT security incidents. It also should continue its progress towards fully implementing and enforcing the use of two-factor authentication when accessing its system. The Department should strive towards a robust capability to identify and respond to malware installations.

Management Challenge 3—Oversight and Monitoring

Effective oversight and monitoring of the Department's programs and operations is 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 stakeholders. Four subareas are included in this management challenge—Student Financial Assistance (SFA) program participants, distance education, grantees, and contractors.

Oversight and Monitoring—SFA Program Participants

Why This Is a Challenge

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, and abuse. In FY 2014, the Federal Government planned to provide $161.3 billion in grants, loans, and work-study assistance to help students pay for postsecondary education. The Department's FY 2015 budget request outlines $169.8 billion in Federal student aid, including $29.2 billion in Pell Grants and more than $133.7 billion in student loans. Nearly 12.8 million students would be assisted in paying the cost of their postsecondary education at this level of available aid.

Our audits and inspections, along with work the Government Accountability Office conducted, continue to identify weaknesses in FSA's oversight and monitoring of SFA program participants. In addition, our external audits of individual SFA program participants frequently identified noncompliance, waste, and abuse of SFA program funds. OIG investigations have also identified various schemes by SFA program participants to fraudulently obtain Federal funds.

Progress in Meeting the Challenge

FSA identified numerous initiatives that were completed, in progress, or under consideration to help ensure that SFA funds are delivered accurately and efficiently. For example, FSA makes software and updates available to FSA program participants to assist them in managing Federal funds. FSA also provides training opportunities to financial aid professionals that are intended to enhance their ability to effectively implement the Department's student aid programs. Additionally, FSA reported that it has continued to develop its risk management processes by enhancing the agency's analytical capabilities and strengthening its ability to recognize and mitigate risks in its operational and credit portfolios.

What Needs to Be Done

Overall, FSA needs to continue to assess and improve its oversight and monitoring of postsecondary institutions; FFEL program guaranty agencies, lenders, and servicers; and other SFA program participants. It needs to act effectively when issues are identified in its oversight and monitoring processes. FSA also needs to evaluate the risks within its programs and develop strategies to address risks identified to ensure effective operations. It further needs to assess its control environment, using information from OIG reviews and other sources as appropriate, and implement actions for improvement.

Oversight and Monitoring—Distance Education

Why This Is a Challenge

Management of distance education programs presents a challenge for the Department and school officials because of few or no in-person interactions to verify the student's identity or attendance. In addition, laws and regulations are generally modeled after the campus-based classroom environment, which does not always fit delivering education through distance education. Distance education refers to courses or programs offered through a technology, such as the Internet, that supports regular and substantive interaction between postsecondary students and instructors. 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.

Our investigative work has noted an increasing risk of people attempting to fraudulently obtain Federal student aid through distance education programs. Our audits have identified noncompliance by distance education program participants that could be reduced through more effective oversight and monitoring.

Progress in Meeting the Challenge

The Department has taken or plans to take numerous actions in response to our work in this challenge area. For example, starting in the January 2013 FAFSA cycle (for the 2013–2014 award year), applicants selected for verification who are in a distance education program must provide a notarized copy of a government-issued identification to the school. For the same FAFSA cycle, the Department began screening applicants for unusual attendance, such as a pattern of enrolling at several schools, receiving aid, and then withdrawing. Schools will follow up with these applicants to ensure they are attending school with an educational purpose, or the Department will not disburse aid. The Department has also begun tracking applicants who use the same e-mail and IP address for multiple applications using different names.

What Needs to Be Done

FSA needs to increase its monitoring and oversight of schools providing distance education. The Department should also gather information to identify students who are receiving SFA program funds to attend distance education programs—and gather other information as needed to analyze the differences between campus-based education and distance education. Based on this analysis, the Department should develop and implement requirements to specifically address potential problems inherent in distance education.

The Department should develop regulations that require schools offering distance education to establish processes to verify the student's identity as part of the enrollment process. Once these regulations are implemented, the Department should establish requirements for independent public accountants to assess the effectiveness of schools' processes for verifying distance education student's identity. Finally, the Department should also work with Congress to amend the *Higher Education Act* to specify that a school's cost of attendance budget for a distance education student include only those costs that reflect actual educational expenses.

Oversight and Monitoring—Grantees

Why This Is a Challenge

Effective monitoring and oversight is essential for ensuring that grantees meet grant requirements and achieve program goals and objectives. The Department's early learning, elementary, and secondary education programs annually serve nearly 16,900 public school districts and 50 million students attending more than 98,000 public schools and 28,000 private schools. Key programs administered by the Department include Title I of the *Elementary and Secondary Education Act* (ESEA), which under the President's 2015 request would deliver $14.4 billion to help 23 million students in high-poverty schools make progress toward State academic standards. Another key program is the *Individuals with Disabilities Education Act,* Part B Grants to States, which would provide $11.6 billion to help States and school districts meet the special educational needs of 6.6 million students with disabilities.

OIG work has identified a number of weaknesses in grantee oversight and monitoring. These involve local educational agency (LEA) fiscal control issues, State educational agency (SEA) control issues, fraud perpetrated by LEA and charter school officials, and internal control weaknesses in the Department's oversight processes.

Progress in Meeting the Challenge

The Department has planned or completed numerous corrective actions in response to our audits. This includes enhancing guidance to applicants and reviewers, updating and clarifying internal guidance and policy, developing formal monitoring plans, and developing training to grantees and Department staff. The Department has also developed and implemented a risk analysis tool that is intended to help identify areas of potential risk in the Department's grant portfolio and develop appropriate monitoring, technical assistance, and oversight plans as a part of grants management. Finally, the Department plans to develop a working group to consider potential regulations and other measures to address SEA monitoring issues.

What Needs to Be Done

The Department should continue to improve its monitoring efforts for recipients of formula and discretionary grant funds. This includes 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 also should consider adding language to its regulations so that prime recipients are fully cognizant of their responsibilities related to minimum requirements for monitoring subrecipients. The Department should include a reporting requirement for fraud and criminal misconduct in connection with all programs authorized by the *Elementary and Secondary Education Act of 1965,* as amended, when the Education Department General Administrative Regulations are revised.

Oversight and Monitoring—Contractors

Why This Is a Challenge

The Department must effectively monitor performance to ensure that it receives the quality and quantity of products or services for which it is paying. As of May 2014, over $6.6 billion has been obligated towards the Department's active contracts. Proper oversight is necessary to ensure that contractors meet the terms and conditions of each contract; fulfill agreed-on 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, such as systems development, operation, and maintenance; loan servicing and debt collection; technical assistance for grantees; administrative and logistical support; and education research and program evaluations.

OIG audits have identified issues relating to the lack of effective oversight and monitoring of contracts and contractor performance. This is primarily related to the appropriateness of contract payments and the effectiveness of contract management. In addition, OIG investigations have noted contractor activities, such as false claims, that resulted in improper billings and payments.

Progress in Meeting the Challenge

The Department has provided corrective action plans to address the issues noted in our audit work. It has also developed and implemented several training programs and procedures within this area.

What Needs to Be Done

The Department needs to ensure that it has an appropriately qualified staff in place and in sufficient numbers to provide effective oversight of its contracts.

Management Challenge 4—Data Quality and Reporting

Why This Is a Challenge

The Department, its grantees, and its subrecipients must have effective controls to ensure that reported data are accurate and reliable. The Department uses data to make funding decisions, evaluate program performance, and support a number of management decisions.

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. This includes weaknesses in controls over the accuracy and reliability of program performance and academic assessment data.

Progress in Meeting the Challenge

The Department has completed corrective actions to address issues with implementation of the *GPRA Modernization Act.* These include developing internal guidance related to strategic goals and plans, and the quarterly performance review process, and including disclosures related to data limitations in all applicable performance reports. The Department has also reported several planned corrective actions to address deficiencies in internal controls over assessment results, which include requiring SEAs to respond to all flagged comments related to assessments and accountability, updating its monitoring plan, and revising the peer review manual. Additionally, the Department plans to issue Dear Colleague letters to address identifying and monitoring high-risk schools, timely reporting and resolving of test irregularities, implementing of test security procedures, and strengthening of test administration practices.

To address concerns related to one program's performance data, the Department plans to provide training to staff on assessing the SEA's efforts to sufficiently test performance data and provide reasonable assurance that the data are valid and complete. It also plans to revise its site visit monitoring instrument to ensure staff sufficiently evaluates SEA monitoring activities related to the reliability of program performance data.

The Department requires management certifications regarding the accuracy of some SEA-submitted data. The Department also conducts an ongoing peer review process to evaluate State assessment systems, and it currently 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 they could take to help ensure the integrity of the data used to measure student achievement. The Department also has a contract that runs through 2015 to provide technical assistance to improve the quality and reporting of outcomes and impact data from Department grant programs.

What Needs to Be Done

While the Department has demonstrated its commitment to improving staff and internal system capabilities for analyzing data and using data to improve programs, it must work to ensure that effective controls are in place at all applicable levels of the data collection, aggregation, and analysis processes and to ensure that accurate and reliable data is reported.

Management Challenge 5—Information Technology System Development and Implementation

Why This Is a Challenge

The Department faces an ongoing challenge of efficiently providing services to growing numbers of program participants and managing additional administrative requirements with consistent staffing levels. The Department reported that its inflation adjusted administrative budget is about the same as it was 10 years ago while its full-time equivalent staffing level has declined by 9 percent. This makes effective information systems development and implementation, and the greater efficiencies such investments can provide, critical to the success of its activities and the achievement of its mission.

According to data from the Federal IT Dashboard, the Department's total IT spending for FY 2014 was $682.9 million. The Department identified 38 major IT investments, accounting for $587.9 million of its total IT spending. Our recent work has identified weaknesses in the Department's processes to oversee and monitor systems development; these weaknesses have negatively impacted operations and may have resulted in improper payments. In its *FY 2012 Agency Financial Report,* the Department self-reported two material weaknesses relating to financial reporting of Federal student aid data and operations of the Direct Loan and FFEL programs that resulted from system functionality issues occurring after large-scale system conversions in October 2011.

Progress in Meeting the Challenge

The Department reported it has taken action to correct the financial reporting deficiencies associated with the system conversions. It also reported that FSA implemented other internal control improvements that resulted in system fixes and restored system functionality.

The Department further reported that actions to correct the root causes of the internal control deficiencies impacting operation of the Direct Loan and FFEL programs are ongoing. Actions include researching borrower balances and analyzing root causes of system limitations to inform recommendations on system and process fixes. In response to issues surrounding its defaulted loan servicing system, FSA awarded an operations and maintenance contract to a new vendor.

What Needs to Be Done

The Department needs to continue to monitor contractor performance to ensure that contractors correct system deficiencies and that system performance fully supports the Department's financial reporting and operations. Further actions needed to address this challenge include improving management and oversight of system development and life cycle management (to include system modifications and enhancements) and ensuring that the Department obtains appropriate expertise to managing system contracts (including accepting deliverables).

Freeze the Footprint

This effort strives to bring a new approach to the workplace at the Department, by building greater employee performance and productivity through innovative space designs and technology enhancements, while reducing the agency's space footprint and associated out-year costs. The project will also allow the agency to meet the new federal space guidelines (150–180 usable square footage/person vs. the current usable square footage of 338).

The Department Challenges:

- Limited IT tools to support new mobile workforce
- IT infrastructure is outdated
- In some cases, telework expansion has outpaced space designs
- Agency employee recruitment efforts restricted to a limited number of states, limiting the size of the mobile workforce

The Department Strategy:

- Upgrade the IT infrastructure
- Provide mobile workers with 21st century tools
- Strengthen the Performance Management Program
- Promote cultural acceptance of a mobile workforce
- Design innovative work spaces
- Implement an Electronic Records Management System
- Reduce the space footprint

Freeze the Footprint Baseline Comparison

	FY 2012 Baseline	2013 (Current Year-1)	Change (FY 2012 Baseline–2013)
Square Footage	1,563,641	1,573,317	(9,676)

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Appendices

Appendix A: Selected Department Web Links and Education Resources

College Cost Lists

The Department provides college affordability and transparency lists under the *Higher Education Opportunity Act of 2008.* Each list is broken out into nine different sectors to allow students to compare costs at similar types of institutions, including career and technical programs. http://collegecost.ed.gov/catc/

College Navigator

The Department provides a multi-dimensional review of higher education options for students and provides links to other sites. http://nces.ed.gov/collegenavigator/

College Scorecards

College Scorecards in the Department's College Affordability and Transparency Center make it easier to find out more about a college's affordability and value.
http://www.whitehouse.gov/issues/education/higher-education/college-score-card

One-Stop Shopping for Student Loans

The Department provides a site from which students can manage their loans.
http://studentloans.gov/

College Preparation Checklist

This Departmental tool gives prospective college students step-by-step instructions on how to prepare academically and financially for education beyond high school. Each section is split into subsections for students and parents, explaining what needs to be done and which publications or websites might be useful to them. http://studentaid.ed.gov

Additional resources within the checklist assist students in finding scholarships and grants.

http://studentaid.ed.gov/students/publications/checklist/main.html

http://studentaid.ed.gov/students/publications/checklist/MoreSourcesOfStudentAid.html

College Completion Toolkit

The College Completion Toolkit provides information that governors and other state leaders can use to help colleges in their state increase student completion rates. It highlights key strategies and offers models to learn from, as well as other useful resources.
http://www.ed.gov/sites/default/files/cc-toolkit.pdf

Resources for Adult and Career and Technical Education

The Literacy Information and Communication System (LINCS) is a Department Initiative that seeks to expand evidence-based practice in the field of adult literacy. LINCS provides high-quality, on-demand educational opportunities to practitioners of adult education in order to help adult learners successfully transition to postsecondary education and employment. LINCS is comprised of three components: 1) the LINCS Resource Collection provides free online access to high-quality, evidence-based materials and self-access courses to help practitioners and state and local staff improve programs, services, instruction and teacher quality; 2) LINCS Regional Professional Development Centers work with states to offer practitioners training and professional development activities; and 3) LINCS Community provides an online social learning space (a community of practice) for networking, information sharing, and collaboration among adult education leadership, professional developers, administrative staff, and practitioners across the country. http://lincs.ed.gov/

Program Inventory

The *GPRA Modernization Act of 2010,* P.L. 111-352, requires that OMB establish a single website with a central inventory of all federal programs, including the purpose of each program and its contribution to the mission and goals of the Department. The initial Federal Program Inventory was published in May 2013. The Department described each program within 27 budgetary accounts, as well as how the programs support the Department's broader Strategic Goals and Objectives.

Since that time, Congress passed the DATA Act requiring new public reporting requirements, which impact the definition of program used in this guidance. OMB is currently working with agencies to merge the implementation of the DATA Act and the Federal Program Inventory requirements to the extent possible to avoid duplicative efforts. While OMB and agencies determine the right implementation strategy, the initial Federal Program Inventory remains available on Performance.gov or at http://www2.ed.gov/programs/inventory.pdf.

Grants Information and Resources

In addition to student loans and grants, the Department offers other discretionary grants. These are awarded using a competitive process, and formula grants, which use formulas determined by Congress with no application process. This site lists Department discretionary grant competitions previously announced, as well as those planned for later announcement, for new awards organized according to the Department's principal program offices. http://www2.ed.gov/fund/grant/find/edlite-forecast.html

For more information on the Department's programs, see http://www2.ed.gov/programs/gtep/gtep.pdf.

Federal Registry for Educational Excellence

Federal Registry for Educational Excellence (FREE) provides easily accessible resources in a wide gamut of subjects for educators. The tool breaks resources into categories ranging from art and music to science and mathematics. FREE is built on the Learning Registry, an open database for sharing educational resources. It also offers a wide variety of primary documents, photos, and videos. In addition, FREE allows educators to follow via Twitter, a social network, which facilitates the sharing of ideas. This tool acts as a library of digital resources for educators to help them enrich their lessons. http://free.ed.gov/

Practice Guides for Educators

The Department offers guides that help educators address everyday challenges faced in classrooms and schools. Developed by a panel of nationally recognized experts, practice guides consist of actionable recommendations, strategies for overcoming potential roadblocks, and an indication of the strength of evidence supporting each recommendation. The guides themselves are subjected to rigorous external peer review. Users can sort by subject area, academic level, and intended audience to find the most recent, relevant, and useful guides. http://ies.ed.gov/ncee/wwc/publications_reviews.aspx

Performance Data

EDFacts is a Department initiative to put performance data at the center of policy, management, and budget decisions for all K-12 educational programs.
http://www.ed.gov/about/inits/ed/edfacts/index.html

Condition of Education and Digest of Education Statistics

The Condition of Education is a congressionally mandated annual report that summarizes developments and trends in education using the latest available statistics. The report presents statistical indicators containing text, figures, and data from early learning through graduate-level education. http://nces.ed.gov/programs/coe/

The primary purpose of the Digest of Education Statistics is to provide a compilation of statistical information covering the broad field of American education from pre-kindergarten through graduate school. The Digest includes a selection of data from many sources, both government and private, and draws especially on the results of surveys and activities carried out by the National Center for Education Statistics.
http://nces.ed.gov/programs/digest/

Projections of Education Statistics to 2021

For the 50 states and the District of Columbia, the tables, figures, and text in this report contain data on projections of public elementary and secondary enrollment and public high school graduates to the year 2021. The report includes a methodology section that describes the models and assumptions used to develop national and state-level projections.
http://nces.ed.gov/pubsearch/pubsinfo.asp?pubid=2013008

Open Government Initiative

The Department's Open Government Initiative is designed to improve the way the Department shares information, learns from others, and collaborates to develop the best solutions for America's students. http://www2.ed.gov/about/open.html

National Assessment of Educational Progress

The National Assessment of Educational Progress (NAEP) assesses samples of students in grades 4, 8, and 12 in various academic subjects. Results of the assessments are reported for the nation and states in terms of achievement levels—basic, proficient, and advanced. http://nationsreportcard.gov/

Government Accountability Office

The Government Accountability Office supports Congress in meeting its constitutional responsibilities and helps improve the performance and accountability of the federal government for the benefit of the American people.
http://www.gao.gov/docsearch/agency.php

Office of Inspector General

The Office of Inspector General conducts independent and objective audits, investigations, inspections, and other activities to promote the efficiency, effectiveness, and integrity of the Department's programs and operations. http://www.ed.gov/about/offices/list/oig/index.html

For a list of recent reports, go to: http://www2.ed.gov/about/offices/list/oig/reports.html.

Appendix B: Glossary of Acronyms and Abbreviations

AARTS	Audit Accountability and Resolution Tracking System
ABCP	Asset-Backed Commercial Paper
AFR	*Agency Financial Report*
APG	Agency Priority Goals
APR	*Annual Performance Report*
ARRA	*American Recovery and Reinvestment Act of 2009* (Recovery Act)
CAP Goals	Cross-Agency Priority Goals
CAT	Core Assessment Team
CCMS	Continuous Control Monitoring System
CFO	Chief Financial Officer
CHAFL	College Housing and Academic Facilities Loan Program
CPSS	Contract and Purchasing Support System
CSRS	Civil Service Retirement System
DCIA	*Debt Collection Improvement Act of 1996*
DL	Direct Loan
DMF	Death Master File
DOI	U.S. Department of Interior
DOL	U.S. Department of Labor
DSS	Decision Support System
EAG	Enhanced Assesment Grants
ECASLA	*Ensuring Continued Access to Student Loans Act of 2008*
EDCAPS	Education Central Automated Processing System
ED-DRB	Education Department’s Disclosure Review Board
EDGAR	Education Department General Administrative Regulations
EFC	Expected Family Contribution
ELC TA	Early Learning Challenge Technical Assistance Center
ERIC	Education Resource Information Center

ERR	Entity Risk Reviews
ESEA	*Elementary and Secondary Education Act of 1965*
FAFSA	Free Application for Federal Student Aid
FAM	Financial Audit Manual
FASAB	Federal Accounting Standards Advisory Board
FCRA	*Federal Credit Reform Act of 1990*
FECA	*Federal Employees' Compensation Act*
FERS	Federal Employees Retirement System
FFB	Federal Financing Bank
FFEL	Federal Family Education Loan
FFMIA	*Federal Financial Management Improvement Act of 1996*
FISMA	*Federal Information Security Management Act of 2002*
FMFIA	*Federal Managers' Financial Integrity Act of 1982*
FMLoB	Financial Management Line of Business
FMSS	Financial Management Support System
FREE	Federal Registry for Educational Excellence
FSA	Federal Student Aid
FSEOG	Federal Supplemental Educational Opportunity Grant
FY	Fiscal Year
G5	Grants Management System
GAAP	Generally Accepted Accounting Principles
GAO	Government Accountability Office
GEPA	*General Education Provisions Act*
GPA	Grade Point Average
GPRA	*Government Performance and Results Act of 1993*
GPRAMA	*GPRA Modernization Act of 2010*
GSA	General Services Administration
HBCUs	Historically Black Colleges and Universities

HCERA	*Health Care and Education Reconciliation Act of 2010*
HEA	*Higher Education Act of 1965*
HEAL	Health Education Assistance Loans
HHS	U.S. Department of Health and Human Services
HR	Hurricane Education Recovery
ICOFR	Internal Control over Financial Reporting
IDEA	*Individuals with Disabilities Education Act*
IES	Institute of Education Sciences
IHE	Institutes of Higher Education
IPERA	*Improper Payments Elimination and Recovery Act of 2010*
IPERIA	*Improper Payments Elimination and Recovery Improvement Act of 2012*
IPIA	*Improper Payments Information Act of 2002*
IRS	Internal Revenue Service
IRS DRT	IRS Data Retrieval Tool
ISE	Integrated Student Experience
ISIR	Institutional Student Information Record
ISU	Implementation and Support Unit
i3	Investing in Innovation Fund
IT	Information Technology
KEA	Kindergarten Entry Assessment
LEA	Local Educational Agency
LEU	Lifetime Eligibility Used
LVC	Loan Verification Certificates
NIEER	National Institute for Early Education Research
NIST	National Institute of Standards and Technology
NLS	Nortridge Loan System
NSLDS	National Student Loan Data System
OCFO	Office of the Chief Financial Officer

OCR	Office for Civil Rights
OCTAE	Office of Career, Technical, and Adult Education
OELA	Office of English Language Acquisition
OESE	Office of Elementary and Secondary Education
OIG	Office of Inspector General
OII	Office of Innovation and Improvement
OMB	Office of Management and Budget
OPE	Office of Postsecondary Education
OPEPD	Office of Planning, Evaluation, and Policy Development
OPM	Office of Personnel Management
OSEP	Office of Special Education Programs
OSERS	Office of Special Education and Rehabilitative Services
PIC	Performance Improvement Council
QPU	Quarterly Performance Update
RELs	Regional Educational Laboratories
RMS	Risk Management Service
RSSI	Required Supplementary Stewardship Information
RTT	Race to the Top
RTTA	Race to the Top-Assessment
RTT-ELC	Race to the Top-Early Learning Challenge
SAFRA	*SAFRA Act*
SAM	System for Award Management
SAP	Special Allowance Payments
SAT	Senior Assessment Team
SBR	Statement of Budgetary Resources
SEA	State Educational Agency
SFA	Student Financial Assistance
SFFAS	Statement of Federal Financial Accounting Standards

SIG	School Improvement Grant
SMC	Senior Management Council
SOS	Schedule of Spending
SPFI	*Summary of Performance and Financial Information*
SSAE	Statements on Standards for Attestation Engagements
SSP	System Security Plan
STEM	Science, Technology, Engineering, and Mathematics
SY	School Year
TEACH	Teacher Education Assistance for College and Higher Education Grant
TIVAS	Title IV Additional Servicers
Treasury	U.S. Department of Treasury
UEH	Unusual Enrollment History
U.S.	United States

Acknowledgments

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Within the Office of the Chief Financial Officer, the office of Financial Management Operations (FMO) is responsible for certifying, processing, reconciling, evaluating, and reporting all agency financial transactions; preparing annual financial statements and related notes and schedules; and coordinating the external audit of the agency's financial statements.

Financial Improvement and Post Audit Operations (FIPAO) provides leadership and direction in the areas of internal control assessment, financial management training, post audit activities, and indirect cost determination.

Contracts and Acquisitions Management (CAM) is responsible for the solicitation, award, administration, and closeout of all contracts and other acquisition instruments for the Department.

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An electronic version is available on the World Wide Web at
http://www2.ed.gov/about/reports/annual/index.html

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