FORWARD-LOOKING INFORMATION

This section summarizes information pertinent to the Department's future progress and success.

Enterprise Risk Management

The Department is focused on improving enterprise risk management (ERM) to maximize the Department's value to students and taxpayers through achievement of the Department's strategic goals and objectives. The Department's implementation of ERM includes three critical strategies that are more fully described under Strategic Objective 4.2, *Identify, assess, monitor and manage enterprise risks*:

1. Creating a risk-aware culture that includes transparent discussions of risks.
2. Implementing an ERM framework and capability that leverages existing risk management activities and governance bodies.
3. Managing risks in a more coordinated and strategic manner.

Beginning in FY 2019, when the ERM framework is fully implemented, the Department plans to include risk information as a central consideration in all critical day-to-day and strategic decision-making activities, including resource allocations. In FY 2018, the Department established a new governance structure for ERM and focused on building a top-down understanding of and commitment to managing risk more effectively across the organization. Under the new governance structure, senior leaders from all offices will participate in establishing and implementing enterprise-wide risk management strategies to promote strategic risk-taking and coordinated approaches to managing cross-cutting management challenges.

While the Department continues working to mature its ERM capability and develop a more complete portfolio of risks to inform decision-making at all levels of the organization, the Senior Management Council has focused on providing strategic direction to effectively manage its most significant risks. The risks summarized below are several of the most significant challenges and opportunities facing the Department that will continue to receive management priority in FY 2019 and beyond.

DIRECT LOAN PROGRAM

The Department's largest program, the William D. Ford Federal Direct Loan (Direct Loan) program, provides students and their families with funds to help pay for their postsecondary education costs. The following is a discussion of (1) the steps the Department has taken to help make student debt more manageable and (2) the risks inherent in estimating the cost of the program.

Managing Student Loan Debt

Each year, federal student loans help millions of Americans obtain a college education—an investment that, on average, has high returns. While the average return to a college degree remains high, some students leave school poorly equipped to manage their debt.

Traditionally, federal loans of this type have had flat 10-year repayment schedules, making it difficult for borrowers to pay at the start of their career when their salaries are lower. The recent expansion of income-driven repayment plans grants students the opportunity for greater financial flexibility as it pertains to their monthly payment. For more details on these plans, visit FSA's **How to Repay Your Loans Portal**.

Recent trends in student loan repayment data show that:

- More than 80 percent of Direct Loan recipients with loans actively in repayment are current on their loans.
- As of June 2018, nearly 7.1 million Direct Loan recipients were enrolled in income-driven repayment plans, representing a 13 percent increase from June 2017 and a 34 percent increase from June 2016.

The Department continues to work relentlessly to make student debt more manageable. Looking to the future, the Department will:

- Continue conducting outreach efforts to inform student loan borrowers of their repayment options.
- Work to improve customer service and student aid systems and processes by implementing FSA's Next Generation Financial Services Environment (Next Gen FSA).

- Continue to support additional tools like the College Scorecard and Financial Aid Shopping Sheet to increase transparency around higher education costs and outcomes, in an effort to help students and families make informed decisions before college enrollment.

Managing Risks and Uncertainty Facing the Direct Loan Program's Cost Estimates

Direct Loan program costs are estimated consistent with the requirements of the *Federal Credit Reform Act of 1990*. Under the Act, the future costs and revenues associated with a loan are estimated for the entire life of the loan, up to 40 years in this case. The actual performance of a loan cohort tends to deviate from the estimated performance during that time, which is not unexpected given the inherent uncertainty involved in developing estimates. There are four types of inherent risk that make estimating lifetime program costs a difficult task.

Legislative, Regulatory, and Policy Risk

There are inherent risks from the possibility that the cost structure of the Direct Loan program may be altered through legislative, regulatory, or administrative action. In addition, recent legislative, regulatory, and policy action may be difficult to interpret with regard to effects on financial modeling and estimation, given the lack of actual trend data availability. Some examples of current risks include the following:

Income-Driven Repayment Plans: Several new income-driven repayment (IDR) plans have been introduced in recent years, including Income-Based Repayment, Pay as You Earn (PAYE), and Revised Pay As You Earn. IDR plans tend to be more costly to the government than non-IDR plans; for the 2018 loan cohort, it is estimated that the government will recover 29 percent less for loans in income-driven repayment plans as compared to loans in standard plans. It is important to be careful in making such comparisons, however, as the underlying characteristics of borrowers selecting plans (and the corresponding dynamics of behavior driving selection in plans) also plays a role in driving the cost of loans enrolled in specific plans. In general, the proliferation of IDR plans has made income-driven repayment terms more generous (and more costly to the government) and made the plans available to a greater number of borrowers. Having more plans complicates repayment plan selection, since the tradeoffs between available plans vary by borrower and may not always be entirely clear. Selected comparisons between projected originations and borrower repayments under the different income-driven repayment plans are available on the **Department's website**. Future commitment to market and increased participation in these plans are areas of uncertainty.

Public Service Loan Forgiveness: Enacted in 2007, the Public Service Loan Forgiveness (PSLF) program allows a Direct student loan borrower to have the balance of their Direct student loans forgiven after having made 120 qualifying monthly payments under a qualifying repayment plan, while working full time for a qualifying public service employer (such as government or certain types of nonprofit organizations). In general, forgiveness provided via PSLF raises the cost of the Direct Loan program; however, there is still uncertainty as to how many borrowers will take advantage of the program. Much of this uncertainty arises because borrowers do not need to apply for the program until after having made the 120 qualifying monthly payments.

Data on approved PSLF applications first became available in FY 2018, since borrowers first became eligible for PSLF starting October 1, 2017. As of September 30, 2018, the total number of borrowers who received forgiveness totaled 206. The value of this forgiveness totaled $12.32 million. Despite the relatively modest figures of approved applications to date, the number of borrowers who have certified their employment in a public service organization continues to increase. As of September 30, 2018, the number of borrowers with certified employment totaled 936,029. The low number of approved PSLF applications in relation to employment certifications may be partially due to the complicated nature of the program, in particular the determination of what constitutes a qualifying payment. Many borrowers who file employment certification forms early in their careers may also move into private sector employment before reaching the 10 years and thus may (a) never apply for forgiveness or (b) apply for forgiveness much later, after returning to public service work. In the *Consolidated Appropriations Act*, FY 2018, Congress provided $350 million in funding to forgive up to $500 million in loan balances which were ineligible for immediate PSLF solely due to having made a payment under a nonqualifying repayment plan. Future congressional action that may affect eligibility for PSLF will continue to be an area of uncertainty. Lastly, the Department continues to remain informed on, and manage the risk that may arise in relation to, the uncertainty about the effect of further borrower outreach on boosting participation in the PSLF program.

Total and Permanent Disability: The *Tax Cut and Jobs Act of 2017*, signed into law on December 22, 2017, exempted the discharge of student loans due to total and permanent disability (TPD) from taxable income. TPD discharges had previously been considered taxable income. However, loan amounts discharged due to TPD may continue to be considered taxable income for state tax purposes. On April 16, 2018, the Department of Education announced that it would start matching records from the Department's National Student Loan Data System with Department of Veterans Affairs systems, in order to expedite the processing of total and permanent disability discharges. Borrowers matched through this process will be mailed a customized letter that will explain eligibility for loan discharge and include a TPD application. The borrower can sign and return the application to complete the process of applying for a TPD discharge. The individual effects of each of these changes, as well as the potential interaction between them, will remain an area of uncertainty until enough actual data can be observed to analyze their impact.

Estimation Risk

Actual student loan outcomes may deviate from estimated student loan outcomes, which is not unexpected given the long projection window of up to 40 years. The Direct Loan program is subject to a large number of future borrower-level events and economic factors that heavily impact the ultimate cost of issued loans. For example, estimates that need to be made for loans originating in FY 2017 include how long students will remain in school; what repayment plan will be chosen; whether the loan will be consolidated; whether the borrower will die, become disabled, bankrupt, or have another claim for discharge or forgiveness (closed school, borrower defense, etc.); if the loan will go into deferment or forbearance; if the loan will go into default and, if so, what collections will be received on the defaulted loan; and, if the loan is in income-driven repayment, what the borrower's employment (public sector or not) and income and family status will be over the next 25 years. These types of projections are not only extremely difficult to make but also are subject to change if future student behaviors deviate from past experience. Changes in private student loan markets, such as the recent increase in refinancing of federal student loans into private student loans, also add a layer of uncertainty to student loan estimates. Lastly, the Direct student loan portfolio has grown from approximately $382 billion in FY 2011 to around $1.2 trillion as of the end of FY 2018. This growth naturally results in larger re-estimates, since a re-estimate worth 1 percent of the portfolio today would be more than three times as large as a similar re-estimate in FY 2011 ($11.2 billion vs. $3.8 billion).

Macroeconomic Risk

The ultimate amount, timing and value of future borrower repayments under the Direct Loan program are heavily affected by certain economic factors, especially since the introduction of income-based repayment plans. Some examples include the following:

Interest Rates: Direct Loan subsidy estimates are very sensitive to changes in interest rates. Under the current program terms, the fixed borrower rates for direct loans are established in advance of the upcoming school year, while the Treasury fixed interest rate on borrowings to fund those loans is not set until after those awards are fully disbursed, which can be as much as 18 months later. Unexpected changes in interest rates during this time can significantly impact the subsidy cost of these loans.

Unemployment: The financial crisis of 2008 and ensuing spike in unemployment rates had a dramatic effect on both student loan volume and student loan performance. Student loan volume peaked along with unemployment, as many displaced workers sought higher education opportunities. Student loan performance suffered as many borrowers repaying their loans were left with much less disposable income with which to make their loan payments. For example, the cohort default rate for students was at a high of 14.7 percent for loans entering repayment in 2010, while the most recent rate is 10.8 percent for loans entering repayment in 2015. While recessions and economic downturns are cyclical phenomena, their exact timing and impact on the cost estimates remain an area of uncertainty.

Wage Growth: The estimated costs of income-driven repayment plans are largely dependent on trends in observed wage growth. To the extent that future wage growth deviates significantly from prior wage growth, actual costs of income-driven repayment plans may deviate from projected estimated costs. The Department continues to manage risks in this area by continuing to learn about its borrower base and remain informed on such labor market statistics.

Operational Risk

Unforeseen issues in administering and servicing student loans may impact the cost estimates. For example, in March 2017, a tool used to transfer automatically a family's tax information to both student aid applications and IDR plan applications was taken down due to security concerns. Although usage of the tool for IDR recertification has since been brought back up, it is yet uncertain what, if any, impact this outage may have had on student loan cost estimates. However, this example highlights that there is an inherent risk that future, unpredictable disruptions in the administrative status quo may impact student loan cost estimates.

NEXT GEN FSA

About FSA

As the nation's largest provider of financial aid for education beyond high school, FSA delivers more than $120 billion in aid each year to students and their families. Through programs authorized under the *Higher Education Act of 1965*, as amended, FSA provides grants, loans, and work-study funds for college or career school. FSA also oversees the approximately 6,000 postsecondary institutions that participate in the federal student aid programs. In every interaction with students and their families, FSA strives to be the most trusted and reliable source of student financial aid information and services in the nation.

The Vision

FSA has one of the largest consumer loan portfolios in the country at $1.4 trillion.[1] It is critical that we provide a customer experience that is on par with world-class financial services firms and to establish our organization as one of the most trusted brands in the student aid industry. The Next Generation Financial Services Environment (Next Gen FSA) will enable FSA to realize this vision by modernizing the way we connect with our customers, while streamlining our student aid systems and processes. This broad effort will deliver an exceptional customer experience for millions of Americans across the entire student aid life cycle, from fostering greater awareness about the availability of financial aid, to applying for aid, to repaying loans.

Today's Environment

In the current federal financial aid process, students and families must negotiate a complex and fragmented landscape, interacting with multiple systems, vendors, processes, and interfaces across a multitude of brands and user experiences. Too often, this poor customer experience creates confusion, resulting in borrowers failing to understand their repayment options and the financial implications of their student debt, borrower indifference, and, ultimately, higher loan delinquency and default rates. Additionally, operational complexities and inefficiencies result in higher administrative costs and hinder effective oversight.

Next Gen FSA Environment

Multiple websites, mobile applications, contact centers, and other customer interfaces will be combined into a simplified, consistent, and engaging experience, which will be enhanced by standardized training and tools across vendors and partners. With a focus on mobile engagement, Next Gen FSA will meet customers where they are, letting them connect with FSA on the device of their choice. Customers will access a modernized, online portal with personalized information that helps them quickly understand their options and make informed decisions throughout the financial aid life cycle, including borrowing and loan repayment. While Next Gen FSA will cut through the information clutter and provide robust self-service, it also will seamlessly connect customers with additional support when needed.

In addition to an improved customer experience, Next Gen FSA will completely modernize FSA's back-end systems and infrastructure. This transformation will pave the way for improved processing and customer management at lower costs. Vendor and partner performance standards and accountability measures will be built into Next Gen FSA to ensure customers receive world-class service while protecting taxpayer dollars. Next Gen FSA will integrate state-of-the-art cybersecurity protections across every aspect of the student aid experience. Enterprise-wide data analytics will drive improved customer service, particularly for at-risk students and borrowers, while also enhancing our oversight of participating postsecondary schools and supporting vendors.

Solicitation and Procurement Process

The Next Gen FSA implementation plan was based, in part, on extensive market research with more than 60 industry leaders. This research-based approach enabled FSA to identify best-in-industry standards and technical benchmarks that continue to inform the procurement process. On February 20, 2018, FSA initiated a multistage procurement process designed to identify the vendors most capable of supporting the implementation of Next Gen FSA; FSA intends to select a pool of vendors to deliver the Next Gen FSA environment. The Department anticipates awards will be made with the goal of new systems and processes coming online beginning in FY 2019. The current Title IV Additional Servicing (TIVAS) and Not-for-Profit (NFP) indefinite-

[1] This includes FFEL Lender held loans.

delivery, indefinite-quantity (IDIQ) contracts are set to expire in June and September 2019, respectively. Should FSA require continued servicing support beyond these dates, there are multiple options it can pursue. For example, one option would be to issue a new task order prior to the expiration of the underlying IDIQ contract to one or more of the current servicers. Another option would be to extend the underlying IDIQ contract up to 6 months in accordance with FAR 52.217-8, then issue new task orders. The appropriate contractual actions will be taken to ensure continued servicing capabilities until this portion of the Next Gen FSA vision is implemented.

CONTINUOUS IMPROVEMENT

Improving critical infrastructure, systems, and overall capacity, and ensuring sound strategic decision making regarding allocation of resources are essential to the Department's future progress and success. Implementing Technology Business Management Solutions and exploring the expanded use of Shared Services are two of the Department's key initiatives.

Technology Business Management Solutions (TBMS)

The purpose of the TBMS project is to provide an integrated solution that will support the Office of the Chief Information Officer (OCIO)'s role in implementing an Information Technology (IT) cost transparency capability. The TBMS project will also allow OCIO to communicate IT value with senior leadership, improve the efficiency and predictability of capital planning, and optimize IT costs. In the FY 2019 IT Budget-Capital Planning Guidance, the Office of Management and Budget requires agencies to begin reporting IT spending in alignment with the TBM Framework. The new requirements include using Cost Pools and IT Towers to classify IT spending. The project consists of two phases. The first phase will include OCIO's operating budget of approximately $120 million into the TBM Cost Transparency tool provided by the Department's TBM Vendor, Apptio. The second phase will incorporate the Department's entire IT budget of approximately $750 million, as well as the ability to use the Apptio Benchmarking, Business Insights, and Bill of IT modules. These modules will allow the Department to benchmark costs between the different program offices at ED, as well as between different federal agencies. The Business Insights and Bill of IT modules will offer additional details regarding total costs for IT projects at the Department as well as allow more analysis of our vendors and business practices when it comes to IT.

The objective is to implement an integrated solution that will allow OCIO to:

- Accurately account for and categorize IT spending in IT Cost Towers and Pools.
- Evaluate IT spending using a method that helps identify redundant IT assets (e.g. systems, applications, and licenses).
- Extract cost elements from disparate sources, analyze these elements, and report cost stressors and trends to stakeholders.
- Report IT spending in IT Towers and Cost Pools to OMB for capital planning. Prepare accurate pricing to client offices for the services provided.

Shared Services

The Department of Education uses shared services where feasible and practical, including payroll services with Department of the Interior and travel services with Carlson Wagonlit. The Department is exploring shared service and commercial off-the-shelf offerings to replace its G5, and its contracts and purchasing system (Comprizon). Additionally, the Department will explore migrating its financial management system to a shared service once the current upgrade from Oracle Enterprise Business Suite R11i to R12 is completed and stabilized. We will continue to explore other options to further leverage shared services for other mission support areas in the coming years.