

Report of the Independent Auditors

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**UNITED STATES DEPARTMENT OF EDUCATION
OFFICE OF INSPECTOR GENERAL**

THE INSPECTOR GENERAL

January 23, 2023

The Honorable Miguel Cardona
Secretary of Education
Washington, D.C. 20202

Dear Secretary Cardona:

The enclosed Independent Auditors' Report (report) covers the U.S. Department of Education's (Department) consolidated financial statements for fiscal years 2022 and 2021 to comply with the Chief Financial Officers Act of 1990, as amended. The report should be read in conjunction with the Department's financial statements and notes to fully understand the context of the information contained therein.

We engaged the independent certified public accounting firm KPMG LLP (KPMG) to audit the consolidated financial statements of the Department as of September 30, 2022, and 2021, 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 Presented in the Independent Auditors' Report

KPMG reports:

- A disclaimer of opinion on the fiscal year 2022 consolidated financial statements because KPMG has not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.
- The fiscal year 2021 consolidated financial statements are presented fairly, in all material respects, in accordance with U.S. generally accepted accounting principles.
- One material weakness in internal control over financial reporting:
 - Controls over the Relevance and Reliability of Underlying Data Used in Credit Reform Estimates Need Improvement.
- Two significant deficiencies in internal control over financial reporting:
 - Information Technology Controls Need Improvement, and
 - Entity Level Controls Need Improvement.

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

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

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KPMG is responsible for the auditors' report dated January 23, 2023, and the conclusions expressed therein. We do not express opinions on the Department's consolidated financial statements or internal control over financial reporting, or on whether the Department's financial management systems complied substantially with the three requirements of FFMIA, or conclusions on compliance and other matters.

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

Sincerely,



Sandra D. Bruce
Inspector General

Enclosure



KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

Independent Auditors' Report

Inspector General
United States Department of Education

Secretary
United States Department of Education:

Report on the Audit of the Consolidated Financial Statements

Disclaimer of Opinion on Fiscal Year 2022 Consolidated Financial Statements

We were engaged to audit the consolidated financial statements of the United States Department of Education (Department), which comprise the consolidated balance sheet as of September 30, 2022, and the related consolidated statements of net cost and changes in net position, and combined statement of budgetary resources for the year then ended, and the related notes to the consolidated financial statements.

We do not express an opinion on the accompanying consolidated financial statements of the Department as of and for the year ended September 30, 2022. Because of the significance of the matter described in the Basis for Disclaimer of Opinion section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the fiscal year 2022 consolidated financial statements.

Opinion on Fiscal Year 2021 Consolidated Financial Statements

We have audited the consolidated financial statements of the Department, which comprise the consolidated balance sheet as of September 30, 2021, and the related consolidated statements of net cost and changes in net position, and combined statement of budgetary resources for the year then ended, and the related notes to the consolidated financial statements.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Department as of September 30, 2021, and its net cost, changes in net position, and budgetary resources for the year then ended in accordance with U.S. generally accepted accounting principles.

Basis for Disclaimer of Opinion on Fiscal Year 2022 Consolidated Financial Statements

During fiscal year 2022, the Department announced broad-based debt relief for certain of its student loan borrowers under the Direct Loan and Federal Family Education Loan (FFEL) programs. Management estimated the subsidy costs stemming from the broad-based debt relief as of September 30, 2022. However, management was unable to provide adequate evidential matter to support certain key assumptions used to estimate the subsidy costs. As a result of this matter, we were unable to determine whether any adjustments to the balance sheet might have been necessary with respect to the fiscal year 2022 Loans Receivable, Net – Direct Loan Program; Loans Receivable, Net – FFEL Program; Subsidy Due to Treasury; Loan Guarantee Liabilities; the related balances in the consolidated statements of net cost and changes in net position; and related notes to the consolidated financial statements.

Basis for Opinion on Fiscal Year 2021 Consolidated Financial Statements

We conducted our audit of the fiscal year 2021 consolidated financial statements in accordance with auditing standards generally accepted in the United States of America (GAAS), the standards applicable to financial

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audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin No. 22-01, *Audit Requirements for Federal Financial Statements*. Our responsibilities under those standards and OMB Bulletin No. 22-01 are further described in the Auditors' Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are required to be independent of the Department and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion on the fiscal year 2021 consolidated financial statements.

Other Matter - Interactive Data

Management has elected to reference to information on websites or other forms of interactive data outside the fiscal year 2022 Agency Financial Report to provide additional information for the users of its consolidated financial statements. Such information is not a required part of the consolidated financial statements or supplementary information required by the Federal Accounting Standards Advisory Board. The information on these websites or the other interactive data has not been subjected to any of our auditing procedures, and accordingly we do not express an opinion or provide any assurance on it.

Responsibilities of Management for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with U.S. generally accepted accounting principles, and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS, *Government Auditing Standards*, and OMB Bulletin No. 22-01 will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the consolidated financial statements.

Except as explained in the Basis for Disclaimer of Opinion paragraph, in performing an audit in accordance with GAAS, *Government Auditing Standards*, and OMB Bulletin No. 22-01, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Department's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the consolidated financial statements.



We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

Required Supplementary Information

U.S. generally accepted accounting principles require that the information in the Management's Discussion and Analysis and Required Supplementary Information sections be presented to supplement the basic consolidated financial statements. Such information is the responsibility of management and, although not a part of the basic consolidated financial statements, is required by the Federal Accounting Standards Advisory Board who considers it to be an essential part of financial reporting for placing the basic consolidated financial statements in an appropriate operational, economic, or historical context. We were unable to apply certain limited procedures to the required supplementary information as of and for the year ended September 30, 2022 in accordance with GAAS because of the significance of the matter described in the Basis for Disclaimer of Opinion paragraph. We do not express an opinion or provide any assurance on the information.

We have applied certain limited procedures to the required supplementary information as of and for the year ended September 30, 2021 in accordance with GAAS, 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 basic consolidated financial statements, and other knowledge we obtained during our audit of the fiscal year 2021 basic consolidated financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Report on Internal Control Over Financial Reporting

In connection with our engagement to audit the Department's consolidated financial statements as of and for the year ended September 30, 2022, we considered the Department's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing an opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*.

Our consideration of internal control was for the limited purpose described in the preceding paragraph 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. However, as described in the accompanying Exhibits, we identified certain deficiencies in internal control that we consider to be a material weakness and significant deficiencies.

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 entity's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies described in the accompanying Exhibit A, *Controls over the Relevance and Reliability of Underlying Data Used in Credit Reform Estimates Need Improvement*, to be a material weakness.

The Department management did not report the material weakness in its Statement of Assurance, included in the Management's Discussion and Analysis section of the accompanying Agency Financial Report.

A significant deficiency is a deficiency, or a 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. We consider the deficiencies described in the accompanying Exhibit B, *Information Technology Controls Need Improvement and Entity Level Controls Need Improvement*, to be significant deficiencies.



Report on Compliance and Other Matters

In connection with our engagement to audit the Department's consolidated financial statements as of and for the year ended September 30, 2022, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the consolidated financial statements. However, providing an opinion on compliance with those provisions was not an objective of our engagement, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 22-01.

We also performed tests of the Department's compliance with certain provisions referred to in Section 803(a) of the *Federal Financial Management Improvement Act of 1996* (FFMIA). Providing an opinion on compliance with FFMIA was not an objective of our engagement, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances in which the Department's financial management systems did not substantially comply with the (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the United States Government Standard General Ledger at the transaction level.

Additionally, if the scope of our work had been sufficient to enable us to express an opinion on the consolidated financial statements, instances of noncompliance or other matters may have been identified and reported herein.

Department's Response to Findings

Government Auditing Standards requires the auditor to perform limited procedures on the Department's response to the findings identified in our engagement and described in Exhibit C. The Department's response was not subjected to the other auditing procedures applied in the engagement to audit the consolidated financial statements and, accordingly, we express no opinion on the response.

Our response to the Department's response is included in Exhibit D.

Purpose of the Reporting Required by *Government Auditing Standards*

The purpose of the communication described in the Report on Internal Control Over Financial Reporting and the Report on Compliance and Other Matters sections is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Department's internal control or compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Washington, D.C.
January 23, 2023

Exhibit A

Material Weakness

Controls over the Relevance and Reliability of Underlying Data Used in Credit Reform Estimates Need Improvement**Background:**

The material weakness under this section is related to the Department's Direct and FFEL student loan portfolios.

The Department is required to perform interest rate and technical re-estimates (commonly referred to as estimates) of the subsidy costs of its direct loan and guaranty programs as of September 30 every year.

During fiscal year 2022, the Department announced changes to its student loan programs, including broad-based debt relief for borrowers meeting certain criteria (eligible borrowers). Management estimated the subsidy costs stemming from the broad-based debt relief as of September 30, 2022. Management's estimate used data and assumptions related to a take-up rate, among other assumptions. The take-up rate assumption represents how many eligible borrowers are expected to apply for debt-relief, hence considered a key assumption for estimating the impact of broad-based debt relief on the financial statements. This assumption is used as an input in the Income Driven Repayment (IDR), Collections, and Death, Disability & Bankruptcy (DD&B) assumptions.

These assumptions are included in the estimates calculated using the Department's internally developed cash flow model, the Student Loan Model (SLM). The SLM utilizes assumptions based on internally sourced data elements from Information Technology systems to generate future cash flows. These future cash flows are then input into the format required by the Office of Management and Budget (OMB) Credit Subsidy Calculator (CSC), a required present value discount tool for agencies with credit reform programs, to produce the subsidy cost estimate.

Condition:

Management's internal controls were not properly designed at an appropriate level of precision to address the relevance and reliability of the underlying data used to develop the take-up rate assumption used in the various loan program estimates. In addition, management did not design sufficiently precise controls over the relevance and reliability of certain data used in other key assumptions for the SLM cash flow model to develop the subsidy cost estimates.

Cause/Effect:

Management's risk assessment process was not sufficient to identify the relevance and reliability of the underlying data used in significant assumptions for the estimates, including the take-up rate assumption, as a risk that required additional controls. As a result, the documentation over the subsidy cost estimates in the financial statements was not supportive to evidence the estimate calculations. Inadequate controls over the relevance and reliability of the underlying data used to develop the estimate calculations increases the risk that the financial statements could be materially misstated.

Criteria:

The following criteria were considered in the evaluation of the material weakness presented in this exhibit:

- The Standards for Internal Control in the Federal Government issued by the Comptroller General of the United States (the Green Book), Principle No. 6, *Management should define objectives clearly to enable the identification of risks and define risk tolerances*; Principle No. 10, *Design Control Activities*; Principle No. 13, *Use Quality Information*.
- FASAB Technical Release No. 6, *Preparing Estimates for Direct Loan and Loan Guarantee Subsidies under the Federal Credit Reform Act – Amendments to Technical Release No. 3 Preparing and Auditing Direct Loan and Loan Guarantee Subsidies under the Federal Credit Reforms Act*, Paragraph 20.

Recommendation:

We recommend that management:

1. Design and implement controls that require the validation of the relevance and reliability of underlying data used in developing the assumptions related to the subsidy cost estimates. Such review should be documented and maintained.

Exhibit B

Significant Deficiencies

A. Information Technology Controls Need Improvement

The following control deficiencies in the areas of Information Technology (IT) logical access, security management, segregation of IT duties, application change management, and computer operations are related to both the Department and Federal Student Aid (FSA) systems.

Conditions:

In prior years, we reported a significant deficiency related to the Department and FSA's IT controls due to persistent unmitigated IT control deficiencies. During FY 2022, the FSA management demonstrated progress implementing corrective actions to remediate some prior-year deficiencies, such as oversight of service organization controls. However, the Department management and FSA management have not fully remediated prior-year deficiencies related to logical access administration, separated and transferred user access removal, user access reviews and recertification, and configuration management. New and existing IT control deficiencies related to security management, access controls, segregation of IT duties, application change management, and computer operations for the Department's core financial management system, three of FSA's financial and mixed systems, and two access management support systems are as follows:

Department:

1. Weakness in IT logical access controls: New and separated contractors were not consistently and accurately tracked including inconsistent reporting of start and termination dates. Further, the account controls were not consistently followed for the Department's core financial management system. Specifically:
 - a. documentation supporting the completed security awareness training for new and modified users could not be provided;
 - b. evidence supporting complete and accurate access reviews and recertifications was not provided or retained;
 - c. password controls were not designed to meet the Department's requirements; and
 - d. the Department's requirement for the use and monitoring of generic and shared accounts was not met for all accounts.
2. Weakness in IT application change management and patch management controls: The application change management and patch management policies and processes were not consistently followed for the Department's core financial management system in accordance with Department policy. The Department was unable to provide sufficient evidence supporting tracking, security assessment, and approval for certain application changes and patches.
3. Weakness in IT computer operations controls: Changes to the job processing tool and schedules were not centrally tracked and were made directly in production. Finally, the use and monitoring of generic and shared accounts for the job scheduling tool did not follow the Department's requirements.

FSA:

1. Weakness in IT security management controls: Plan of Action and Milestone (POA&M) closure documentation for FSA systems did not always address the root cause of the deficiencies, thereby increasing the potential of IT control deficiencies reoccurring in the future.

2. Weakness in IT logical access controls: The access control processes were not consistently followed for three FSA systems and two access control support systems. Evidence supporting complete and accurate access listings and evidence supporting new, modified, or separated users could not be provided or was provided with missing required information and/or approvals; evidence supporting complete and accurate access reviews and recertifications was not provided or retained; and the Department's requirement for two-factor authentication was not met for all internal system users.
3. Weaknesses in IT controls related to the segregation of IT duties: For one FSA system, users with developer access had access greater than read-only to the system's production environment or update access to the production and development environments.
4. Weakness in IT application change management controls: The application change management process was not consistently followed for one FSA system. FSA was unable to provide a complete and accurate population of application changes. Also, documentation for a selection of changes contained inaccuracies in recorded testing and migration dates.

Cause/Effect:

There was a lack of effective monitoring controls by the Department and FSA to ensure:

1. Corrective actions to remediate prior-year conditions and associated causes are fully implemented, as well as verifying and validating that these corrective actions were effectively addressing the weakness with adequately documented supporting evidence.
2. Systems and support processes consistently adhered to documented agency-wide policies and procedures for the financial and mixed systems hosted and managed by FSA and the Department.
3. The established logical access control process is followed and requests and related evidence for new, modified, or separated users were retained, documented completely and accurately, and approved.
4. Complete and accurate access reviews are performed to detect and mitigate the risk of unauthorized accounts, access that is not commensurate with job responsibilities or least privilege, and access permissions not being revoked timely.
5. Password controls are designed to meet the Department's requirements.
6. The requirements for the use and monitoring of generic and shared accounts controls are followed and enforced.
7. Segregation of duties and least privilege principles are followed and enforced.
8. The established change process and patch management process are followed.
9. The established process for job processing changes is followed and the requirements for the use and monitoring of generic/shared accounts controls for the job scheduling tool are followed and enforced.
10. The established computer operations process detects and/or prevents unauthorized changes to the job processing tool and schedules within the core financial system environment.

Ineffective IT controls increases the risk of unauthorized use, disclosure, disruption, modification, or destruction of information, and information systems that could impact the integrity and reliability of information processed in the associated applications which may lead to misstatements of the financial statements.

Criteria:

The following criteria were considered in the evaluation of the significant deficiency presented in this exhibit:

- The Departmental Directive OCIO 3-112, *Cybersecurity Policy*.
- Department Information Technology (IT) System Access Control Standard.
- EDCAPS System Security Plan (SSP) control requirements.
- EDCAPS Configuration Management Plan (CMP).
- Department Information Technology System and Information Integrity (SI) standard policy section 2.2 control SI-2, *Flaw Remediation*.
- EDCAPS Patch Management Plan, section 4.7 *Patch Maintenance*.
- Department Baseline Cybersecurity Standard, OCIO-STND-01, dated September 23, 2021, Section 3.15, *Acceptable Use*.
- The Standards for Internal Control in the Federal Government issued by the Comptroller General of the United States (the Green Book), Principle No. 3.08 *Assignment of Responsibility and Delegation of Authority*, Principle No. 4, *Demonstrate Commitment to Competence*, Principle No. 7, *Identify, Analyze, and Respond to Risks*, Principle No. 8.07 *Response to Fraud Risks*, Principle No.10.03, *Design of Appropriate Types of Control Activities*, Principle No.10.12 *Segregation of Duties*, Principle No. 10.3 *Design of Appropriate Types of Control Activities*, Principle No. 11, *Design Activities for the Information System*, Principle No. 13, *Use Quality Information*, Principle No.16, *Perform Monitoring Activities*.
- Federal Information Processing Standards (FIPS) 200, *Minimum Security Requirements for Federal Information and Information Systems*.
- National Institute of Standards and Technology Special Publication 800-53, *Security and Privacy Controls for Federal Information Systems and Organizations*, Revision 5, specifically security control requirements PM-4 *Plan of Action and Milestone*, AC-2 *Account Management*, AC-5 *Separation of Duties*, AC-6 *Least Privilege*, AT-3 *Role-based Training*, AT-4 *Training records*, CM-3 *Configuration Change Control*, and SI-2 *Flaw Remediation*.

Recommendations:

We recommend that the Department:

1. Evaluate, develop, and implement a formal process to track and report all new and separated contractors.
2. Ensure separated contractors are off-boarded and system personnel are notified in a timely manner to disable or remove access to IT resources.
3. Provide training and oversight to the Department's personnel with on/off-boarding responsibilities to help ensure new/separated contractors are properly tracked.
4. Update access review procedures to require the reviewers to verify the access lists received to be used in the performance of the access reviews is complete and accurate and not modified prior to commencing the access reviews.
5. Identify and implement a process for the reviewer to validate the population generated for review is complete and accurate.
6. Enforce established access authorization controls and ensure all requirements are met prior to granting system access.

7. Formally perform and document the periodic reviews of all database user accounts in accordance with Department policy to confirm access is current, authorized, and commensurate with job responsibilities.
8. Ensure the application and database server access reviews include the verification of access privileges assigned to the user accounts are commensurate with job responsibilities and follow the concept of least privilege.
9. Ensure the database and server layers comply with the disabling of inactive accounts and account lockout duration password setting requirements, as required by Department policy.
10. Adhere to the SSP control requirements and avoid the use of generic and shared accounts. If generic and shared accounts are required, obtain a formal risk acceptance and develop a policy and procedure to:
 - Authorize the use of these accounts by approved personnel,
 - Control who can access the generic/shared accounts and those sensitive actions performed by the accounts are logged and reviewed every time the accounts are used, and
 - Require that generic/shared accounts' passwords are changed each time approved personnel separate or transfer from the Department.

We recommend that FSA:

11. Implement a process to evaluate the magnitude of impact, likelihood of occurrence, and nature of the deficiency in order to tailor the corrective actions to remediate the risk and address the root cause. Further, update guidance to ensure that quality reviews over the POA&M closure documentation are conducted to confirm the noted deficiencies are fully addressed to help prevent future reoccurrences.
12. Formally develop and implement a quality control review process to ensure that logical access control processes are followed completely and accurately to validate logical access requests, reviews, and recertifications.
13. Ensure segregation of duties and least privilege principles are adhered to when granting user access to prevent users from having the ability to develop and/or change application code and having update access to the environment where the final tested and approved changes are staged prior to migration to the production environment; and prevent users with access to develop code from having update access to the production environment.
14. Evaluate and update the access review control process based on risk and enforce segregation of duties.
15. Reconcile the list of users' roles and responsibilities per the identity and access software tools to the lists that reside in each system accessed by such users.
16. Update access review procedures to require the reviewer to verify the access list, received to be used in the performance of the access reviews, is complete and accurate and not modified prior to commencing the access reviews.
17. Enforce established access authorization controls and ensure all requirements are met prior to granting access to systems.
18. Ensure a complete and accurate population of application changes is provided. Formally develop and implement a quality control review process to ensure that the application change control process is followed and consistently and accurately documented.

B. Entity Level Controls Need Improvement

The Department and FSA are continually seeking ways to improve accountability in achieving the entity's mission. A key factor in improving accountability in achieving an entity's mission is to implement an effective internal control system. The control environment sets the tone of an organization by influencing the control consciousness of its personnel. It is also the foundation for all components of internal control, providing discipline and structure. The Department and FSA need to address weaknesses in its entity-wide control environment as we have observed, through our procedures, two entity-wide control environment conditions in the areas of risk assessment and monitoring activities that have a pervasive influence on the effectiveness of controls.

Conditions:

1. Risk Assessment- The Department and FSA's entity level controls were not designed and implemented appropriately in order to define objectives related to the financial reporting process to enable the identification of risks, define risk tolerances and identified processes and controls responsive to those risks.
2. Monitoring Activities- The Department and FSA's entity level controls were not designed and implemented appropriately in order to remediate identified internal control deficiencies in a timely manner.

Cause/Effect:

- 1) Risk assessment considerations address the risks facing the entity as it seeks to achieve its objectives. This assessment provides the basis for developing appropriate risk responses. Specifically, inadequate risk assessment throughout the Department and FSA, prevented the proper identification and analysis of certain risks related to the financial reporting process at the Department and FSA, and from designing appropriate risk responses.
- 2) Monitoring activities considerations address management's processes to establish and implement operations that assess the quality of performance over time and promptly resolve the findings of audits and other reviews. Specifically, insufficient monitoring has prevented the Department and FSA from ensuring that corrective action plans are implemented, and control deficiencies are remediated timely.

The conditions noted above contributed to the control deficiencies described earlier in the report and could lead to other weaknesses in internal control over financial reporting.

Criteria:

The following criteria were considered in the evaluation of the significant deficiency presented in this Exhibit:

- GAO Standards for Internal Control in the Federal Government (Green Book) Principle 6, *Management should define objectives clearly to enable the identification of risks and define risk tolerances.*
- GAO Standards for Internal Control in the Federal Government (Green Book) Principle 17, *Management should remediate identified internal control deficiencies on a timely basis.*

Recommendations:

We recommend that management implement the following to improve the effectiveness of entity-level controls:

1. Improve the risk assessment process at the financial statement assertion level and at the process level to ensure the department is appropriately defining objectives to enable the identification of risks and define risk tolerances.
2. Implement key monitoring controls to ensure that corrective action plans are implemented to timely remediate control deficiencies identified. In addition, increase oversight, review, and accountability over the process among various offices and directorates within the Department and FSA.

Exhibit C

Management's Response



UNITED STATES DEPARTMENT OF EDUCATION
WASHINGTON, D.C. 20202

MEMORANDUM

DATE: January 20, 2023

TO: Bryon S. Gordon
Assistant Inspector General for Audit

FROM: Denise L. Carter Denise Carter Digitally signed by Denise Carter
Date: 2023.01.20 10:10:44 -0500
Delegated the authority to perform the functions and duties of the position of Chief Financial Officer

Luis Lopez LUIS LOPEZ Digitally signed by LUIS LOPEZ
Date: 2023.01.20 10:11:02 -0500
Chief Information Officer

SUBJECT: DRAFT INDEPENDENT AUDITORS' REPORT
Fiscal Years 2022 and 2021 Financial Statements
U.S. Department of Education
(ED-OIG/A22FS0064)

We appreciate the opportunity to provide input on the draft audit report and would like to thank the Office of Inspector General audit team for their partnership and support during the annual audit of the Department's financial statements.

The Department concurs with the two significant deficiencies and partially concurs with the material weakness and will take appropriate action to address the audit recommendations. The agency takes its fiscal responsibilities seriously and we continue to have a high degree of confidence in the integrity of our programs and financial operations.

At the end of the fiscal year, the Department took on the challenge of integrating a brand-new program into its financial portfolio. Notwithstanding the inherent risks and challenges that come with implementing a new program of this scope and magnitude, we believe we did so carefully and thoughtfully with strong and supported financial analysis. We will make it a priority to address the items raised in the audit feedback as we strive to return to an unmodified opinion in the future.

Please find attached management's response to the FY 2022 Independent Auditors' Draft Report of the Department of Education's Consolidated Financial Statements.

Please contact Gary Wood, Deputy Assistant Secretary, Office of Financial Management, Office of Finance and Operations, and Acting Deputy Chief Financial Officer, at (202) 453-7631 with any questions or comments.

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.

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C-1

Material WeaknessControls over the Relevance and Reliability of Underlying Data Used in Credit Reform Estimates Need Improvement

Sound financial management is an integral part of the Department's efforts to deliver services and administer programs. We are confident in the integrity of our programs and financial operations and their ability to ensure that taxpayer funds are spent appropriately and effectively. These efforts include ensuring that effective internal controls are in place for the underlying data that is relied upon in financial analyses.

The Department develops and maintains a Student Loan Model (SLM), which is used to produce the official estimates of the cost of federal student loan programs published in the President's Budget and the Department's Agency Financial Report. The model is revised at least two times per year using updated data and economic assumptions. It has been in use in its current form since 1998 and is based on two decades of rigorous analysis and independent validation by third party contractors as well as the Office of Management and Budget (OMB), and other parties. The model has been audited by multiple, independent financial statement auditors, undergone OMB Circular A-123 reviews, and been the focus of several GAO engagements.

For 20 consecutive years, the Department has earned an unmodified (i.e., clean) audit opinion, confirming that the Department's previous financial statements were presented fairly, in all material respects, and conform with generally accepted accounting principles. These reviews have fueled continuous improvement in the model's methodology to ensure the Department's cost estimates are as accurate as possible. Improvements to the underlying data, assumptions, and methodology are in line with best practices across the federal government, and all improvements and major assumptions are reviewed and approved by Department leadership, per its exhaustive and rigorous governance process.

Over the past three years, the Department has managed a series of vital steps to address challenges facing students and borrowers due to the Covid-19 pandemic and resulting national emergency. One of those was the new broad-based debt relief program, which required that the Department estimate the take-up of the benefit among eligible borrowers and integrate this variable into the agency loan estimates. The Department developed its estimate based upon relevant research literature, the Department's own extensive experience of take-up rates from a variety of benefit programs, take-up rates from means-tested programs operated by other federal agencies, and consultation with internal and external experts.

The Department's cost estimate was reviewed by both management at the Department and the Office of Management and Budget (OMB), consistent with existing policies and procedures for modifications. The cost estimate was approved, and appropriate budgetary resources were made available through the OMB apportionment process per OMB Circular A-11. The processes and controls used to validate assumptions were properly designed and consistent with estimates used in previous years, but the Department does acknowledge that controls may not have operated as intended due to the lack of strictly comparable other federal benefit programs.

The Department will leverage the audit feedback as input into its next round of SLM business process and internal control reviews and will implement appropriate actions to further improve the SLM process, including its methodology for assessing take-up rates. Specifically, it will assess the efficacy of controls in place and make appropriate changes as needed.

Significant DeficienciesA. Information Technology Controls Need Improvement

The security of our IT systems is critical and a high priority for the agency. The Department has taken the following actions to make improvements in this area and will leverage the audit feedback to make additional changes. The Department recently awarded our new Identity, Credential, and Access Management contract. The vendor has developed strategic solutions for our logical access control deficiencies and is responsible for optimizing our existing practices that include: single sign on capabilities, separation of duties, and privileged access management for newly

onboarded and departing users.

In fiscal year 2022 the Department achieved a cybersecurity level 4 maturity rating, managed and measurable, which is considered operating at an effective level of security by the Federal Information Security Modernization Act (FISMA) of 2014.

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The Department, through the American Rescue Plan and Technology Modernization Funds, was successfully awarded \$20 million dollars in fiscal year 2022. These funds allowed the Department to develop and incrementally implement a zero-trust architecture plan across all offices while modernizing cybersecurity technologies, ultimately helping the Department carry out its mission and provide a more secure and less burdensome user experience for employees and the public.

B. Entity Level Controls Need Improvement

The Department has taken the following actions to make improvements in this area and will leverage the audit feedback to continue in this direction.

FSA analyzed the business processes and transactions underlying material financial statement line items, performed a qualitative risk assessment of those processes including the results of the Department's risk assessment of ED's student loan model and subsidy estimation processes, and considered those results in testing internal controls. FSA also performed additional control testing over batch job processing in the system that provided key data for the loan subsidy model. In addition, FSA implemented additional monitoring and reporting processes to increase oversight and accountability for the resolution of audit and review findings, including escalation of extension requests to FSA executive management.

The Department will continue to review all processes impacting entity level controls and implement additional improvements accordingly.

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Exhibit D**Auditors' Response to Management's Response**

We acknowledge the Department's response to our Independent Auditors' Report, presented in Exhibit C and noted that the Department partially concurred with the material weakness included in our report presented in Exhibit A. We evaluated management's response and have determined that the material weakness in internal control over financial reporting is appropriate. As noted in Exhibit A, management's controls were not designed at a sufficient level of precision to address the relevance and reliability of the aforementioned data used in the subsidy cost estimates.

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