

Management's Discussion and Analysis

Mission and Organizational Structure

Our Mission

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

History. 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.

Our Public Benefit. The Department is committed to ensuring that students throughout the nation develop the skills they need to succeed in school, college, and the workforce, while recognizing the primary role of states and school districts in providing a high-quality education, employing highly qualified teachers and administrators, establishing challenging content and achievement standards, and monitoring students' progress against those standards. The Department is also [setting high expectations](#) for its own employees and working to improve management practices, ensure fiscal integrity, and develop a culture of high performance.

What We Do. The [Department](#) engages in four major types of activities: establishing policies related to federal education funding, including the distribution of funds and monitoring their use; 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.

Who We Serve. [During school year \(SY\) 2012–13](#), America's schools and colleges are serving larger numbers of students as the population increases and enrollment rates rise. As of the fall of 2012, more than 49.8 million students attend public elementary and secondary schools. In fall 2012, a record 21.6 million students are expected to attend the nation's 2-year and 4-year colleges and universities.

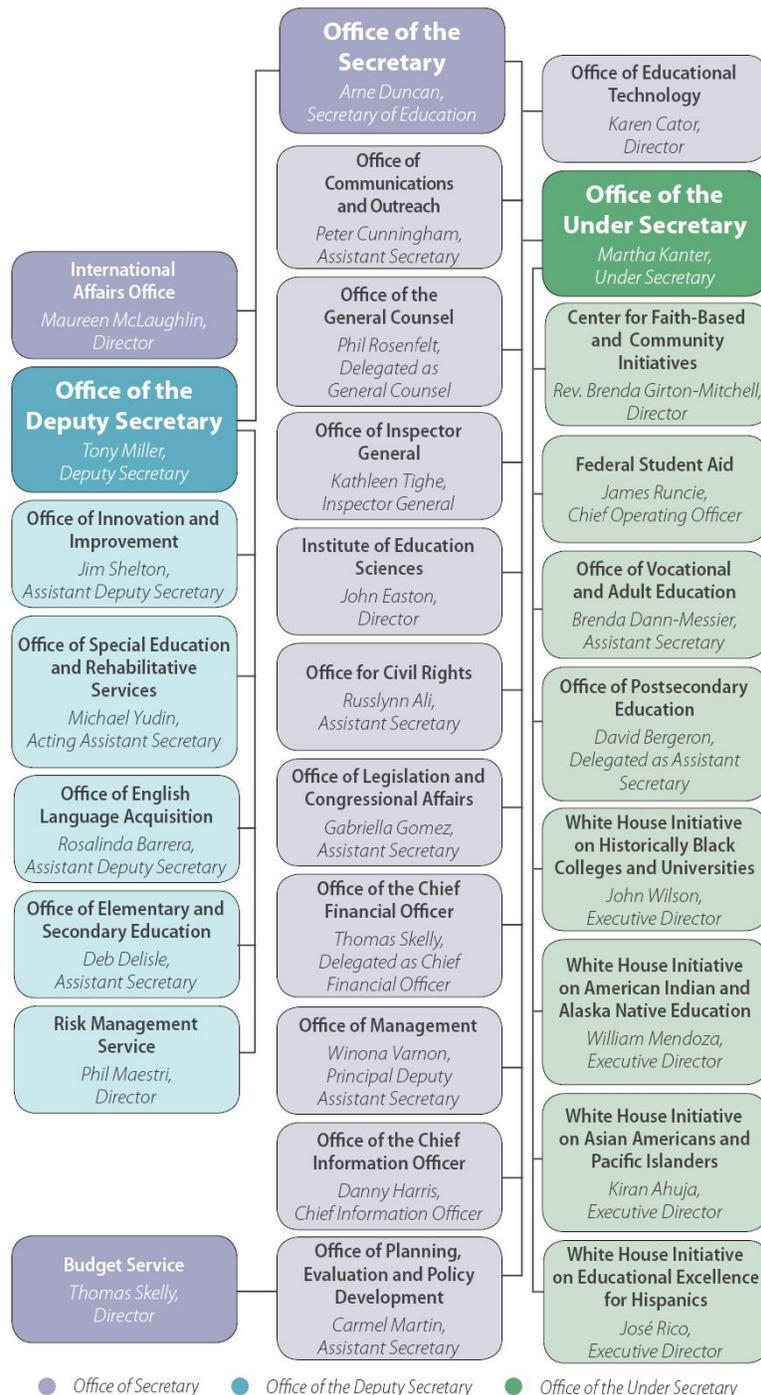
Organizational Structure. To achieve our Strategic Goals, our staff is organized as shown in the organizational chart. The Department's program offices support aspects of external Goals 1, 2, 3, 4, and 5. Our administrative offices support external Goals 1, 2, 3, 4, and 5, as well as Goal 6, which is the Department's internal goal. Links are provided to web pages that provide a detailed [description of the principal offices](#) and [overview of the activities of the Department](#).

Regional Offices. The [Department has ten regional offices](#) that provide points of contact and assistance for schools, parents, and citizens. The primary support within the regional offices is that of communications, civil rights enforcement, and 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.

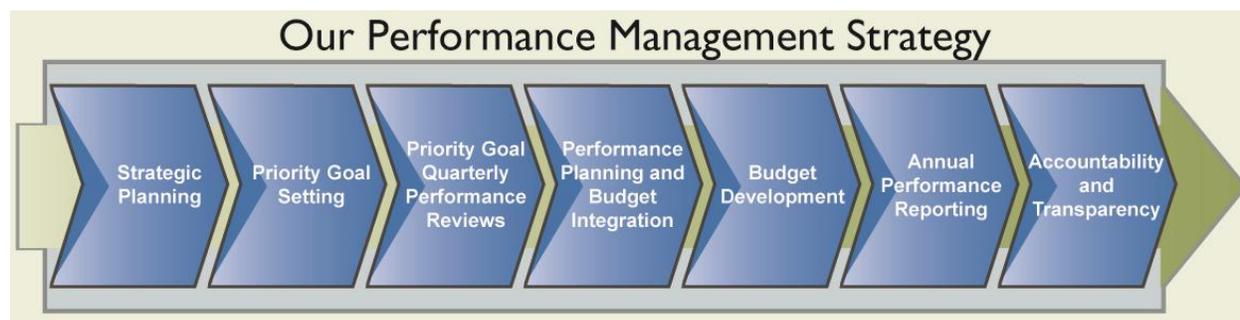
Web Presence. The Department maintains a [comprehensive website](#) that focuses on most popular searches, latest news and events, and links to social media. A partial list of Education Resources of the Department and Selected Department Web Links can be found in the appendices of this report.

Our Organization in Fiscal Year 2012

The Required Supplementary Stewardship Information section of this report contains summary information about offices within the Department. Links are provided to web pages that provide a detailed [description of the principal offices](#) of the Department and an [overview of Department activities](#). This chart reflects the Department organization as of September 30, 2012.



The Department's Approach to Performance Management



Implementing the GPRA Modernization Act of 2010

On January 4, 2011, President Obama signed into law the *GPRA Modernization Act of 2010*. The Act improves on the *Government Performance and Results Act of 1993 (GPRA)* and modernizes the federal government's performance management framework. The *GPRA Modernization Act of 2010* builds on the Department's approach to performance management to improve the effectiveness and efficiency of government by requiring that agency leaders set clear, ambitious goals for a number of outcome-focused and management priorities. Federal agencies measure, analyze, and communicate performance information to identify successful practices, and agency leaders conduct in-depth performance reviews at least quarterly to identify progress on their priorities. The *GPRA Modernization Act* serves as a foundation for engaging leaders in performance improvement and creating a culture where data and empirical information play a greater role in policy, budgetary, and management decisions.

The Department's performance management approach links strategic goals and policy priorities to program activities and outcomes. The strategic planning and performance reporting cycle results in ongoing programmatic assessment and continuous operational improvement to deliver meaningful outcomes for our nation's students.

Our National Outcome Goals

The Department has identified a select number of National Outcome Goals that focus on making improvements in student achievement needed at every level of education to achieve the President's goal that, once again, America will have the highest proportion of college graduates in the world. Achieving that outcome will require a concerted effort from all stakeholders in the education system. These goals include outcomes in the following key areas:

- postsecondary education, career and technical education, and adult education;
- elementary and secondary education;
- early learning; and
- equity.

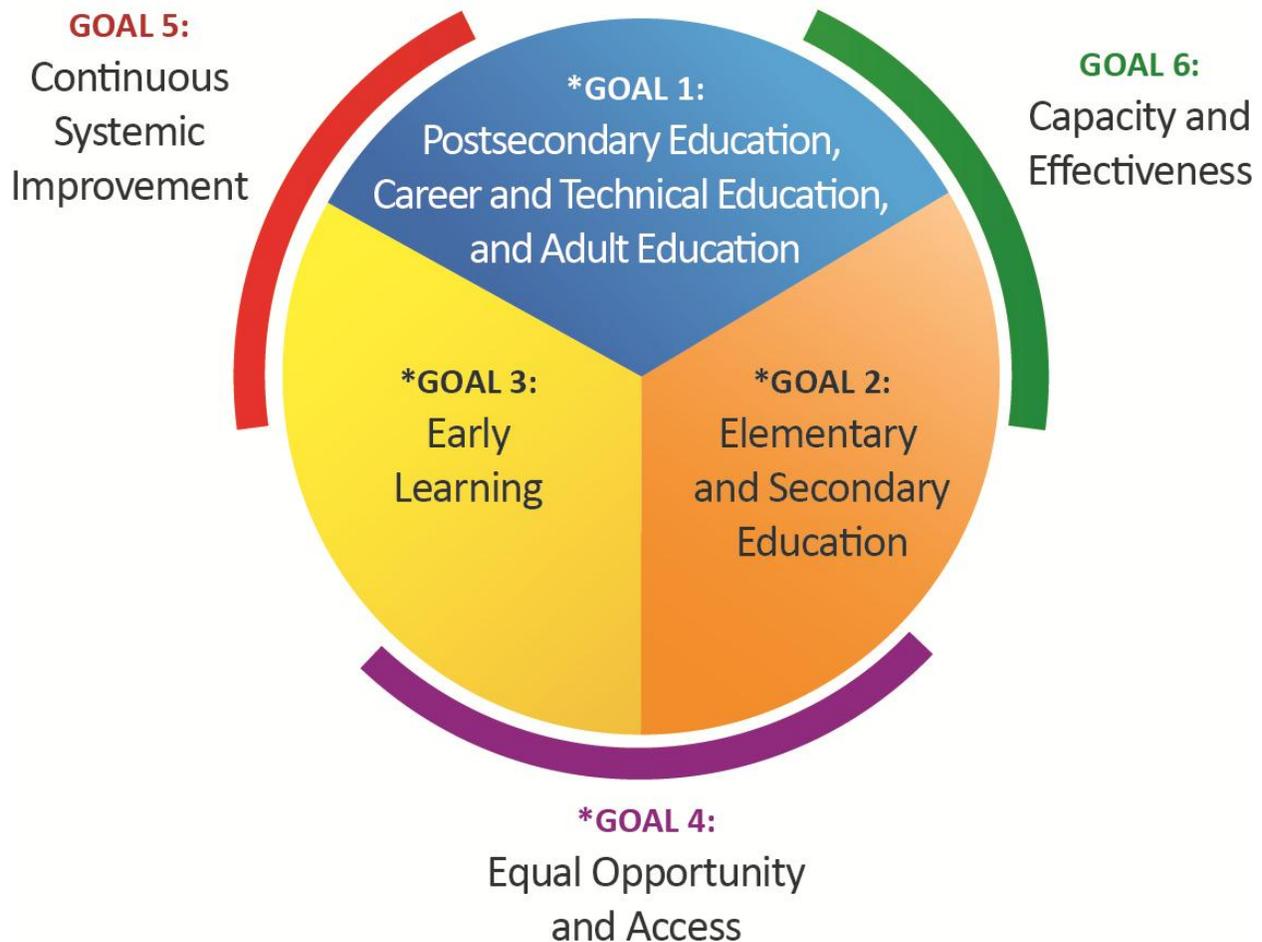
The Department's Strategic Planning Process

To meet the National Outcome Goals, changes are needed in how education is delivered. Investing in education means investing in America's future and is vital for maintaining our long-

term economic security. The nation must work to ensure that all children and adults in America receive a world-class education that will prepare them to succeed in college and careers. Strategic planning is the starting point for the work of the Department as described in its *FY 2011–2014 Strategic Plan*. Reaching this goal will require comprehensive education reforms from cradle to career, beginning with children at birth, supporting them through postsecondary education, and helping them succeed as lifelong learners who can adapt to the constant changes in the technology-driven workplaces of the global economy.

The Department's *Strategic Plan* serves as the basis from which to align the Department's statutory requirements with the Department's operational imperatives, and is the foundation for establishing overall long-term priorities and developing performance goals and measures by which the Department can gauge achievement of its stated outcomes. The Plan was developed in collaboration with Congress, state and local partners, and other education stakeholders.

FY 2011-2014 Strategic Plan



*Aligns with National Outcome Goals.

The Department Priority Goals

The Department has identified a limited number of Agency Priority Goals for FY 2012–13 that serve as a particular focus for our activities. These Priority Goals reflect the Department's cradle-to-career education strategy, and will help concentrate efforts on the importance of teaching and learning at all levels of the education system.

Progress on the Department's FY 2012–13 Priority Goals

Priority Goal 1: Improve outcomes for all children from birth through third grade. By September 30, 2013, at least nine states will implement a high-quality plan to collect and report disaggregated data on the status of children at kindergarten entry.

The Department made a major step in FY 2012 toward reaching the Priority Goal of at least nine states implementing a high-quality plan to collect and report disaggregated data on the status of children at kindergarten entry through the awarding of Race to the Top – Early Learning Challenge (RTT-ELC) grants to nine states. The RTT-ELC states have committed to comprehensive plans for expanding access to high-quality early learning, including collecting and reporting disaggregated data on the status of children at kindergarten entry. As with many of the Department's key reform programs, Department staff are working with states to ensure that they continue to meet their commitments, through the provision of high-quality, consistent technical assistance and monitoring.

Priority Goal 2: Improve learning by ensuring that more students have an effective teacher. By September 30, 2013, at least 500 school districts will have comprehensive teacher and principal evaluation and support systems and the majority of states will have statewide requirements for comprehensive teacher and principal evaluation and support systems.

The Department has made significant progress in leveraging its programs to support state-led efforts to train, recruit, identify, and retain effective teachers, especially in areas with high needs. In particular, the Department's efforts are focused on:

- encouraging teachers to play active roles in the development of these policies (through the RESPECT project and the Teacher Incentive Fund [TIF]);
- encouraging school districts to leverage best practices to recruit and retain effective teachers (through TIF programs);
- encouraging the development and adoption of innovative strategies to transform the teaching profession that will ultimately impact student outcomes (through TIF, investing in Innovation, and other programs); and
- creating a critical mass of states that have created the conditions for education innovation and reform (through Race to the Top, ESEA Flexibility, School Improvement Grants (SIG), and other initiatives).

Priority Goal 3: Demonstrate progress in turning around the nation's lowest-performing schools. By September 30, 2013, 500 of the nation's persistently lowest-achieving schools will have demonstrated significant improvement and will have served as potential models for future turnaround efforts.

The President and Congress have made significant investments in turning around the nation's persistently lowest-achieving schools, in large part through School Improvement Grants, Race to

the Top, and through the Department's work to grant states flexibility regarding specific requirements of the *No Child Left Behind Act of 2001* (NCLB). With more than 1,300 schools now implementing one of the four SIG intervention models, schools around the country have hired new leadership, recruited effective teachers, increased learning time, changed school climate, and offered teachers data-driven professional development aimed at increasing student achievement.

Priority Goal 4: Make informed decisions and improve instruction through the use of data. By September 30, 2013, all states and territories will implement comprehensive statewide longitudinal data systems (SLDS).

Based on the five rounds of funding, 47 states, the District of Columbia, Puerto Rico, and the Virgin Islands have received at least one SLDS grant. By the end of FY 2013, we expect all states and the District of Columbia to have a functioning K-12 SLDS, 12 states to link with early childhood systems, 21 to link with postsecondary data from state institutions, and 10 to link with labor. Linkages with workforce data have presented the greatest challenge for states due to a lack of a common ID, multiple privacy laws, and insufficient multi-agency coordination so we have increased our coordination with the Department of Labor. Also, because of the paucity of early childhood data sources, the Department is creating a series of best practice materials and workshops on early childhood data sharing.

Priority Goal 5: Prepare all students for college and career. By September 30, 2013, all states will adopt internationally-benchmarked college-and career-ready standards.

Forty-five states and the District of Columbia have adopted college- and career-ready standards (CCR) through adoption of the Common Core State Standards. Through ESEA Flexibility, 44 states and the District of Columbia have submitted requests indicating that they have adopted college- and career-ready standards. The total number of states that have approved applications is significantly more than the Department initially anticipated as nearly all states have requested flexibility.

Priority Goal 6: Improve students' ability to afford and complete college. By September 30, 2013, the Department will develop a college scorecard designed to improve consumer decision-making and transparency about affordability for students and borrowers by streamlining information on all degree-granting institutions into a single, comparable, and simplified format, while also helping all states and institutions develop college completion plans.

The Department successfully reached its goal of developing a college scorecard in October 2012. Our successes to date include identifying a funding source, developing and releasing a prototype for public comment, working with software developers to ensure that colleges and universities will be able to publish scorecards quickly, and soliciting university partners to be the first group to release a scorecard. The Department has little influence over state decisions to establish college completion goals, although we continue to encourage goal setting and highlight states that have goals in speeches, editorials, and conversations. In July 2012, the Department sent to all governors a chart showing the state's current attainment rate and our estimated target to reach the President's 2020 goal and to raise awareness of progress needed and encourage goal setting.

For more information on the Department's FY 2012–13 Priority Goals, please go to <http://goals.performance.gov/agency/ed>.

In addition to the Agency Priority Goals, the Department contributes to several Cross-Agency Priority (CAP) Goals as required by the *GPRRA Modernization Act of 2010*.

Cross-Agency Priority Goal: Science, Technology, Engineering, and Math (STEM) Education

Improve the quality of science, technology, engineering, and math (STEM) education. The federal government will work with education partners to improve the quality of science, technology, engineering, and math (STEM) education at all levels, and in support of the President's goal that the U.S. have the highest proportion of college graduates in the world by 2020, help increase the number of well-prepared graduates with STEM degrees by one-third over the next 10 years, resulting in an additional 1 million graduates with degrees in STEM subjects.

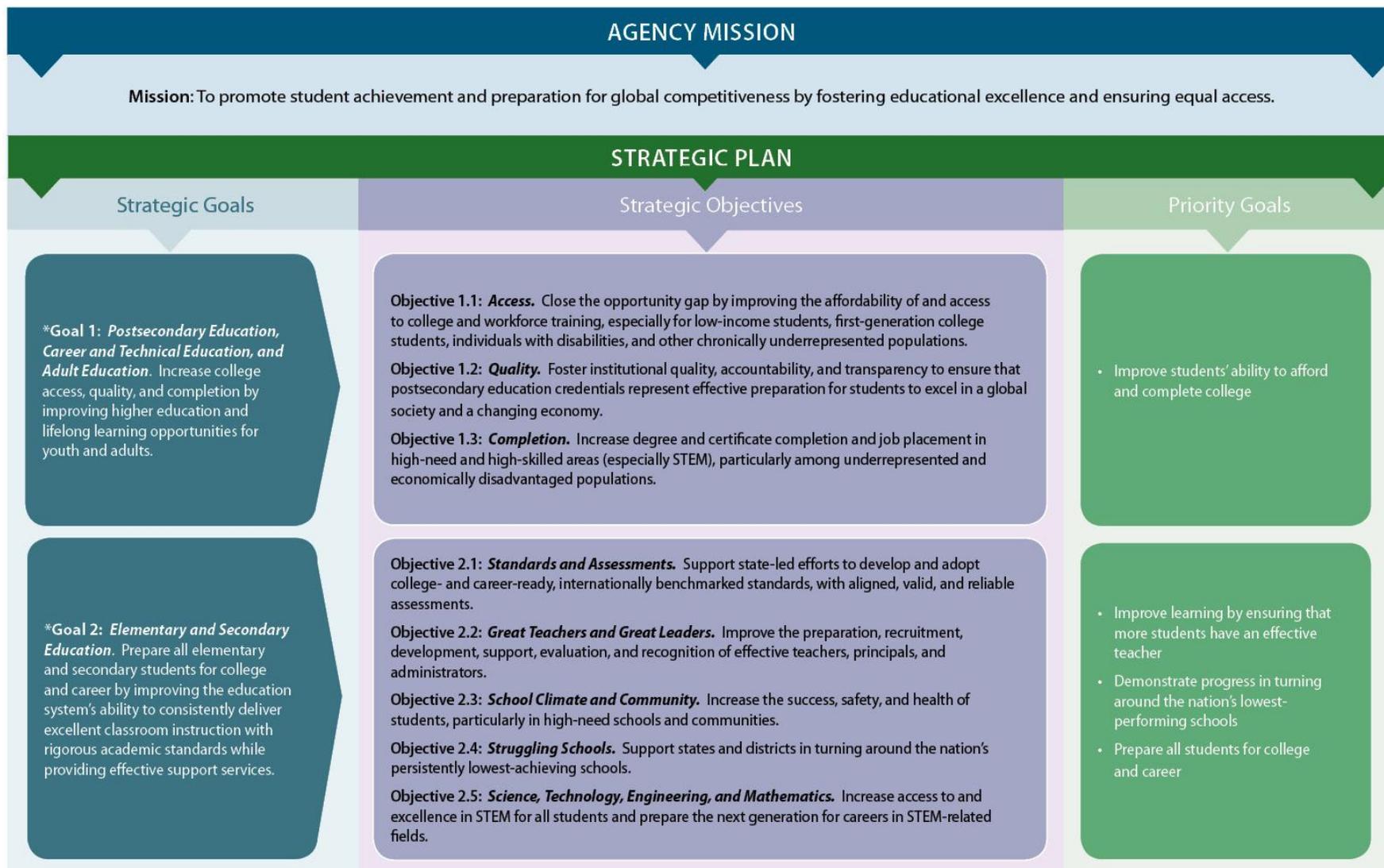
Cross-Agency Priority Goal: Veteran Career Readiness

Improve career readiness of veterans. By September 30, 2013, the federal government will help to increase the percentage of eligible service members who will be served by career readiness and preparedness programs from 50 percent to 90 percent in order to improve their competitiveness in the job market.

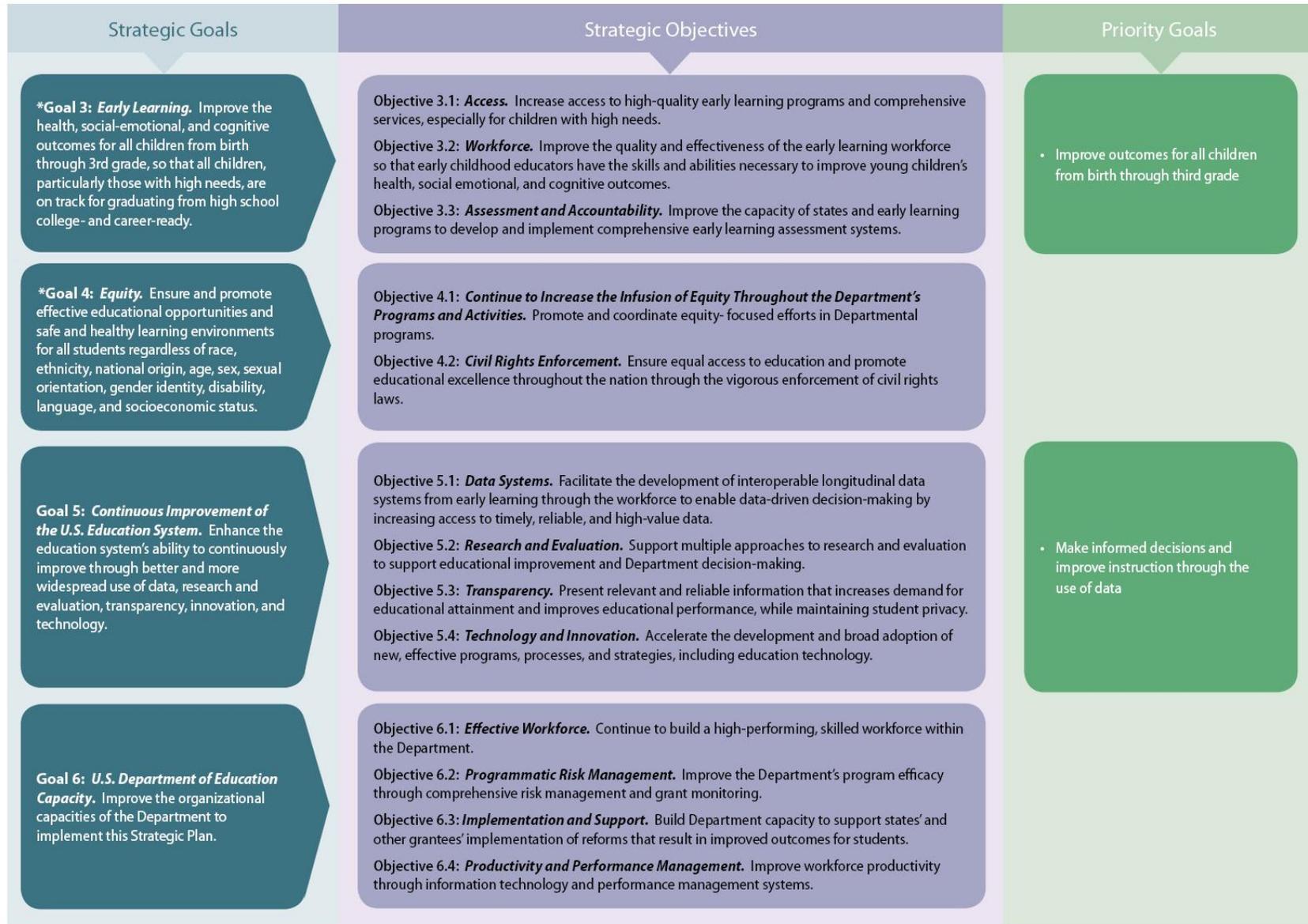
Cross-Agency Priority Goal: Job Training

Ensure our country has one of the most skilled workforces in the world. Federal agencies will prepare 2 million workers with skills training by 2015 and improve the coordination and delivery of job training services.

For additional information on the Cross-Agency Priority Goals, please go to http://goals.performance.gov/goals_2013.



*Aligns with National Outcome Goals.



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The Department's Organizational Performance Review Process

To manage agency performance, the Department has established quarterly performance reviews to assess and improve agencywide performance with a focus on the Department's Agency Priority Goals and other key policy priorities. At these reviews, senior leaders conduct real-time data-driven decision making, identify issues and best practices with significant inter-office implications, and ensure that the Department maintains a consistent focus on strategic priorities.

The Department engages individual principal operating components in organizational performance reviews to promote and focus on continuous operational improvement and capacity-building in key priority areas, including their core processes, people/organizational development, administrative management, and contributions to the department above and beyond expectations. The organizational reviews also provide a mechanism for identifying promising practices that can be applied to other areas of the agency to continuously improve and leverage the Department's internal capacity to deliver on its mission.

Challenges Linking Performance to Resources

Linking performance results, expenditures, and budget for Department programs is complicated. Most of the Department's funding is disbursed through grants and loans. Only a portion of a given fiscal year's appropriation is available to state, school, organization, or student recipients during the fiscal year in which the funds are appropriated. The remainder is available at or near the end of the appropriation year or in a subsequent year.

Funds for competitive grant programs are generally available when appropriations are passed by Congress. However, the processes required for conducting grant competitions often result in the award of grants near the end of the fiscal year, with funding available to grantees for future fiscal years.

Therefore, program results cannot be attributed solely to the actions taken related to FY 2012 funds but to a combination of funds from across several fiscal years, as well as state and local investments, and to many external factors, including economic conditions. Furthermore, the results of some education programs may not be apparent for many years after the funds are expended. In addition, results may be due to the effects of multiple programs.

Assessing the Completeness, Reliability, and Quality of Our Data

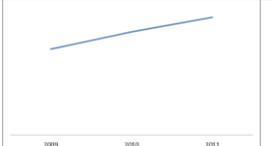
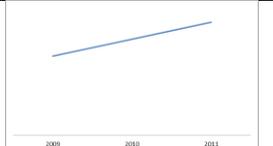
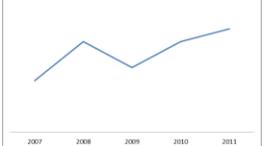
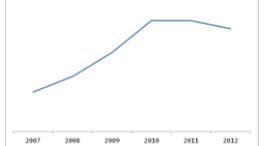
Ensuring that accurate and complete data are reported is critical in supporting transparency of management and budgetary decisions. The Department has established controls to ensure that data used by the Department to make funding decisions, evaluate program performance, and support a number of management and budgetary decisions are as accurate as possible. The Department has designed a procedure for ensuring that the best quality data are available for its planning and reporting purposes. The Department has developed guidance and a framework for principal offices to identify issues in data validation and verification for its strategic and program performance goals and measures prior to data reporting. In addition, limitations of data collected by the Department are noted and actions are planned to correct shortfalls in data completeness, accuracy, and reliability.

Selected Outcome Measures for FY 2012

In support of the FY 2011–14 Strategic Goals, the table below presents trend information for selected performance measures for FY 2007–12.

Performance Results Summary		FY 2007	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	Trend*
Student Achievement								
Increase in the percentage of parents and teachers who believe that the effective implementation of technology within instruction is important to student success**	Parents	NA	78%	91%	89%	87%	Target: 89%	
	Teachers	NA	70%	80%	78%	79%	Target: 81%	
Increase the percentage of adult education students obtaining a high school credential***,†		61.5%	64.1%	52.4%††	60.2%	Target 56.0%‡	Target: 57.0%	
Increase the percentage of public high school students who graduate four years after starting 9th grade (Averaged Freshman Graduation Rate)***		74%	75%	76%	Target: 76%‡	Target: 76%‡	Target: 77%	
Increase the percentage of 4th-grade students at or above proficient on the NAEP in reading****,‡‡		32%	NA	32%	NA	32%	NA	
Increase the percentage of 8th-grade students at or above proficient on the NAEP in reading****,‡‡		29%	NA	30%	NA	32%	NA	

Performance Results Summary	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	Trend*
Increase the percentage of 4th-grade students at or above proficient on the NAEP in mathematics****#	39%	NA	38%	NA	40%	NA	
Increase the percentage of 8th-grade students at or above proficient on the NAEP in mathematics****#	31%	NA	33%	NA	34%	NA	
Postsecondary							
Increase in the percentage of individuals completing and filing the FAFSA who are non-traditional students (25 years and above with no college degree)	NA	2.2%	2.9%	3.9%	3.8%	Target: 3.6%	
Increase in the number of undergraduate credentials/degrees (in millions)	2.3	2.3	2.4	2.5	2.7	Target: 2.7	
Increase in the number of STEM undergraduate degrees awarded***	NA	313,911	297,555	337,946	Target: 344,705 ‡	Target: 351,599	
Increase the percentage of 25- to 34-year-olds who attain an associate's or higher degree***	40.4%	41.6%	41.1%	42.3%	43.1%	Target: 44%	
Increase the percentage of students who complete a bachelor's degree within 6 years from their initial institution***	57%	57%	57%	58%	Target: 61% ‡	Target: 63%	

Performance Results Summary		FY 2007	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	Trend*
State Activities								
Increase in the number of states implementing comprehensive statewide longitudinal data systems***	Link students with teachers	NA	NA	30	36	41	Target: 47	
	Link P-12 with college	NA	NA	28	34	40	Target: 46	
Department Management								
Increase in the Department's rank in the report on the Best Places to Work (BPTW) in the Federal Government	28 out of 30	NA	27 out of 30	30 out of 32	29 out of 33	Target: 27	No trend displayed due to differences in the numbers of agencies ranked in FY 2007–11.	
Increase in the percentage of Department's positive responses that the Department receives on the Talent Management measure in the Federal Viewpoint Survey	NA	58%	54%	54%	58%	Target: 62%		
Increase in the percentage of positive responses that the Department receives on the Performance Culture measure in the Federal Viewpoint Survey	49%	52%	50%	52%	53%	Target: 58%		
Increase in the Department's American Customer Satisfaction Index rating and states and other grantees reporting satisfaction with support provided by the Department	63	65	68	72	72	71		

* Trend lines display only years with actual data available. ** Data are a sum of "Important" and "Very Important" responses to the Project Tomorrow Teacher Survey. In the FY 2011 AFR, only "Important" responses were included. *** National Outcome Goal. † Data were recalculated and corrected from previous reporting year. †† The percentage of adults who earned a high school diploma was down in program year 2009–10 due to a reporting anomaly in one large state that resulted from an issue with goal setting in some of its programs. The state has provided technical assistance to these programs. An adjustment that omits this state's data from the two most recent years indicates that the national performance on the high school completion remains relatively the same at approximately 65 percent. ‡ Data not yet available for this fiscal year. ‡‡ NAEP data are collected biennially. Data reported for the NAEP measures in the FY 2012 AFR reflect public school students only. In previous AFRs, national totals that included both public and private school data were reported. ‡‡‡ Data from National Center for Education Statistics, Integrated Postsecondary Education Data System. For the FY 2011 AFR, National Science Foundation, National Center for Science and Engineering Statistics data were reported.

FY 2012 Goals, Objectives, and Selected Programs

In FY 2012, the Department continued a number of programs and initiatives designed to focus on meeting the President's cradle-to-career priority to support states and districts as they reform their schools and make college more affordable for students. For FY 2012, these priorities focused on:

- granting flexibility to states under ESEA,
- reforming the teaching profession,
- reducing college costs and improving college access,
- achieving equity in education, and
- improving student achievement.

A summary of major Department programs, organized by Strategic Goal, follows.

Goal 1: Postsecondary Education, Career and Technical Education, and Adult Education

Increase college access, quality, and completion by improving higher education and lifelong learning opportunities for youth and adults.

Objective 1.1: Access. Close the opportunity gap by improving the affordability of and access to college and workforce training, especially for low-income students, first-generation college students, individuals with disabilities, and other chronically underrepresented populations.

Objective 1.2: Quality. Foster institutional quality, accountability, and transparency to ensure that postsecondary education credentials represent effective preparation for students to excel in a global society and a changing economy.

Objective 1.3: Completion. Increase degree and certificate completion and job placement in high-need and high-skilled areas (especially STEM), particularly among underrepresented and economically disadvantaged populations.

In 2012, the Department continued to support President Obama's three-prong strategy (access, quality, and completion) for achieving the 2020 goal of America once again having the highest proportion of college graduates in the world.

The William D. Ford Federal Direct Loan Program (Direct Loan)

The [Direct Loan Program](#) lends funds directly to students and parents through participating schools. Created in 1993, this program is funded by borrowings from the U.S. Department of the Treasury, as well as an appropriation for subsidy costs.

The Federal Pell Grant Program (Pell Grant)

The [Pell Grant Program](#) helps ensure financial access to postsecondary education by providing grant aid to low-income and middle-income undergraduate students. Pell Grants vary according to the financial circumstances of students and their families. The maximum Federal Pell Grant award is \$5,550 for the 2012–13 award year (July 1, 2012, to June 30, 2013). However, the

amount a student receives will depend on their financial need, cost of attendance, status as a full-time or part-time student, and plans to attend school for a full academic year or less. Students eligible for a Pell Grant will receive the full amount they qualify for—each school participating in the program receives enough funds each year from the Department to pay the Federal Pell Grant amounts for all its eligible students. The amount of any other student aid for which they might qualify does not affect the amount of the Pell Grant.

Effective with the 2012–13 award year, there was a reduction in the duration of a student's eligibility to receive a Pell Grant from 18 semesters (or its equivalent) to 12 semesters (or its equivalent). The calculation includes all earlier years of the student's receipt of Pell Grants.

The Federal TRIO Programs (TRIO)

TRIO provides federal outreach and student services programs designed to identify and provide services for individuals from disadvantaged backgrounds. TRIO includes [eight programs](#) targeted to serve and [assist low-income individuals](#), first-generation college students, and individuals with disabilities to progress through the academic pipeline from middle school to postbaccalaureate programs. TRIO also includes a [training program](#) for TRIO programs and is designed to assist TRIO personnel in improving the operation and success of the TRIO projects. In FY 2012, \$840.0 million was available for TRIO programs.

Career and Technical Education

[Career and Technical Education programs](#) (CTE) provide academic, technical, and employability skills to enable secondary students to graduate from high school and transition into postsecondary education, training, and employment in in-demand occupations in high-growth industry sectors. These programs also enable postsecondary students and adults to obtain industry-recognized credentials (in sectors where they exist and are appropriate) and postsecondary certificates or degrees that lead to employment in those sectors.

Under the *Carl D. Perkins Career and Technical Education Act of 2006*, the Department provides formula grants to eligible states and outlying areas to fund programs that assist secondary and postsecondary students to acquire academic and technical skills and to prepare for high-skill, high-wage, or high-demand occupations in the global economy.

The Perkins Act of 2006 also authorizes the Department to award discretionary grants to help improve CTE for Native Americans and Native Hawaiians, for CTE students at Tribally Controlled CTE Institutions, and for grants to organizations, institutions, and agencies for CTE research, evaluation, capacity building, dissemination, technical assistance, and promising practices. In addition, the Department supports a [collaborative resources network](#), as well as [statistics collection and reporting](#).

Adult Education Programs. In addition, the Department administers formula grant funds to states for adult education and literacy programs. States distribute funds to local eligible entities to provide adult education and literacy services that provide educational opportunities below the postsecondary level for young people and adults, 16 years of age and older, who are not currently enrolled in school, and who lack a high school diploma or the basic skills to function effectively in the workplace and in their daily lives, or are unable to speak, read, or write the English language. A weekly electronic newsletter, [OVAE Connection](#), published by the Office of Vocational and Adult Education, provides information to state officials involved in adult education, CTE, and community colleges, as well as to practitioners, researchers, education groups, and others interested in community colleges, CTE, and adult education.

Goal 2: Elementary and Secondary Education

Prepare all elementary and secondary students for college and career by improving the education system's ability to consistently deliver excellent classroom instruction with rigorous academic standards while providing effective support services.

Objective 2.1: Standards and Assessments. Support state-led efforts to develop and adopt college- and career-ready, internationally benchmarked standards, with aligned, valid, and reliable assessments.

Objective 2.2: Great Teachers and Great Leaders. Improve the preparation, recruitment, development, support, evaluation, and recognition of effective teachers, principals, and administrators.

Objective 2.3: School Climate and Community. Increase the success, safety, and health of students, particularly in high-need schools and communities.

Objective 2.4: Struggling Schools. Support states and districts in turning around the nation's persistently lowest-achieving schools.

Objective 2.5: Science, Technology, Engineering, and Mathematics. Increase access to and excellence in STEM for all students and prepare the next generation for careers in STEM-related fields.

In FY 2012, the Department continued to support programs to help states to prepare students for college and careers, by consistently providing students with the education necessary to achieve that goal.

Race to the Top

On August 12, 2012, the Department published the final application for the 2012 Race to the Top—District competition, which will provide support to school districts in implementing local education reforms that personalize instruction, close achievement gaps, and take full advantage of 21st century tools that prepare each student for college and careers.

The [Race to the Top](#) state competition provided support to states to strengthen standards and assessments, increase teacher and principal quality, turn around the lowest-performing schools, and improve the use of education data. In addition, the Department awarded [state grants](#) to develop a new generation of tests that assess students' knowledge of mathematics and English language arts from third grade through high school. The early childhood component is discussed in Goal 3.

Race to the Top requires that reform occur as part of a comprehensive approach but acknowledges that there is no one path to reform. The [Race to the Top Annual Performance Report](#) is a tool that permits the Department, grantees, and the public to follow grantees' progress in implementing comprehensive education reform plans and meeting ambitious goals for student outcomes, including increasing student achievement and closing achievement gaps.

Teacher Incentive Fund

The Department's [Teacher Incentive Fund](#) (TIF) has provided grants to states, rural and urban school districts, and nonprofit organizations to develop and implement performance-based teacher and principal compensation systems in high-need schools. The Department conducted

[a new competition](#) in FY 2012 that seeks to strengthen the education profession by rewarding excellence, attracting teachers and principals to high-need schools, and providing all teachers and principals with the feedback and support they need to succeed.

ESEA Flexibility

The Department has invited each state educational agency (SEA) to [request flexibility](#) from certain requirements of the *Elementary and Secondary Education Act of 1965*, as reauthorized by the *No Child Left Behind Act of 2001*, on behalf of itself, its local educational agencies, and schools, in order to better focus on improving student learning and increasing the quality of instruction. During 2012, the Secretary approved requests from states and the District of Columbia to provide educators and state and local leaders with flexibility regarding specific requirements in exchange for rigorous and comprehensive state-developed plans designed to improve educational outcomes for all students, close achievement gaps, increase equity, and improve the quality of instruction.

School Improvement Grants

[School Improvement Grants](#) (SIG) are used to improve student achievement in three tiers of schools: (1) Tier I schools, which are generally the lowest-achieving five percent of Title I schools identified for improvement, corrective action, or restructuring; (2) Tier II schools, which are generally the lowest-achieving five-percent of secondary schools that are eligible for, but do not receive, Title I funds; and (3) Tier III schools, which are all other Title I schools identified for improvement, corrective action, or restructuring. Under the School Improvement Grants program, SEAs give priority to awarding funds to enable Tier I and Tier II schools to implement dramatic interventions to help turn around their academic performance.

In August 2012, the White House welcomed state, district, and school leaders and educators for panel discussions on the transformative efforts underway in low-performing schools through the SIG program, including efforts to turnaround schools characterized by years of low attendance rates, low student achievement, and low graduation rates, as well as high rates of student disciplinary action and staff turnover.

Investing in Innovation Fund

In FY 2012, the Department invited pre-applicants to submit an application for the FY 2012 Full Application Development Competition under the [Investing in Innovation](#) (i3) grant competition. The grants continue support for evidence-based practices in education. The purpose of this program is to provide competitive grants to applicants with a record of improving student achievement and attainment in order to expand the implementation of, and investment in, innovative practices that are demonstrated to have an impact on improving student achievement or student growth, closing achievement gaps, decreasing dropout rates, increasing high school graduation rates, or increasing college enrollment and completion rates.

Promise Neighborhoods

[Promise Neighborhoods](#), established under the legislative authority of the Fund for the Improvement of Education, provides funding to support eligible entities, including nonprofit organizations, which may include faith-based nonprofit organizations, institutions of higher education, and Indian tribes. In FY 2012, the Department received applications and awards are expected no later than December 31, 2012.

The purpose of Promise Neighborhoods is to significantly improve the educational and developmental outcomes of children and youth in the nation's most distressed communities, and to transform those communities by: identifying and increasing the capacity of eligible entities that are focused on achieving results for children and youth throughout an entire neighborhood; building a complete continuum of cradle-to-career solutions of both educational programs and family and community supports, with great schools at the center; integrating programs and breaking down agency "silos" so that solutions are implemented effectively and efficiently across agencies; developing the local infrastructure of systems and resources needed to sustain and scale up proven, effective solutions across the broader region beyond the initial neighborhood; and learning about the overall impact of the Promise Neighborhoods program and about the relationship between particular strategies in Promise Neighborhoods and student outcomes.

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. Increase access to high-quality early learning programs and comprehensive services, especially for children with high needs.

Objective 3.2: Workforce. Improve the quality and effectiveness of the early learning workforce so that early childhood educators have the skills and abilities necessary to improve young children's health, social-emotional, and cognitive outcomes.

Objective 3.3: Assessment and Accountability. Improve the capacity of states and early learning programs to develop and implement comprehensive early learning assessment systems.

In FY 2012, the Department continued funding and assistance to help state education systems to prepare students for college and careers, by encouraging and creating incentives for states and local educational agencies to offer high-quality early learning programs, especially for children with high needs.

Inter-Governmental Cooperation

The Department prioritizes improving the health, social, emotional, and educational outcomes for young children from birth through third grade by enhancing the quality of early learning programs, and increasing the access to [high-quality early learning programs](#)—especially for young children at risk for school failure. The Department's role in promoting early learning is significant and includes: administering several early learning programs; collaborating and coordinating early learning programs, research, and technical assistance with the U.S. Department of Health and Human Services; encouraging states and local districts to target resources for early learning; promoting state and local educational agency partnerships with other early learning agencies and programs in the state or community; conducting research on early learning through the Institute of Education Sciences (IES); funding technical assistance on early learning topics, including early literacy and social and emotional development; and supporting the development of state longitudinal data systems that include early learning programs.

Race to the Top-Early Learning Challenge

[The Race to the Top-Early Learning Challenge](#) (RTT-ELC) provides state competitive grants to improve early learning and development programs. The goal of the RTT-ELC is to better prepare more children with high needs for kindergarten, because children from birth to age five, including those from low-income families, need a strong foundation for success.

RTT-ELC focuses on five key areas of reform:

- *Establishing Successful State Systems* by building on states' existing strengths, ambitiously moving forward states' early learning and development agendas, and carefully coordinating programs across agencies to ensure consistency and sustainability beyond the grant;
- *Defining High-Quality, Accountable Programs* by creating a quality rating and improvement system that is used across the state to evaluate and improve program performance and to inform families about program quality;
- *Promoting Early Learning and Development Outcomes for Children* by developing common standards within a state and assessments that measure child outcomes, address behavioral and health needs, as well as inform, engage, and support families;
- *Supporting a Great Early Childhood Education Workforce* by providing professional development, career advancement opportunities, appropriate compensation, and a common set of standards for workforce knowledge and competencies; and
- *Measuring Outcomes and Progress* so that data can be used to inform early learning instruction and services and to assess whether children are entering kindergarten ready to succeed in elementary school.

The RTT-ELC program is jointly administered with the Department of Health and Human Services.

Goal 4: Equity

Ensure and promote effective educational opportunities and safe and healthy learning environments for all students regardless of race, ethnicity, national origin, age, sex, sexual orientation, gender identity, disability, language, and socioeconomic status.

Objective 4.1: Continue to Increase the Infusion of Equity Throughout the Department's Programs and Activities. Promote and coordinate equity-focused efforts in Departmental programs.

Objective 4.2: Civil Rights Enforcement. Ensure equal access to education and promote educational excellence throughout the nation through the vigorous enforcement of civil rights laws.

In FY 2012, the Department continued to support programs to help the education system, with a focus on technical assistance, data collection, and enforcement activities on critical issues including: school culture, by working to ensure students are free from harassment and sexual violence; issues of access, by ensuring equitable distribution of resources; ensuring that English learners get the services they need; ensuring that schools, including charter schools, do not engage in discriminatory recruitment practices or segregate students; and disparate discipline rates.

Under the *FY 2011–2014 Strategic Plan*, the Department focused on the pursuit of equity in two primary ways: (1) by increasing the infusion of equity throughout the Department's programs and activities and (2) by ensuring equal access to education and promoting educational excellence throughout the nation through the vigorous enforcement of civil rights laws.

For example, the Department worked to provide a greater focus on equity throughout its initiatives and programs, including in the awarding of competitive grants like Race to the Top—District and the Charter School Program; working to preserve accountability for subgroup performance while offering flexibility for states under the ESEA; improving the affordability of postsecondary education; ensuring a safe learning environment where students are free from bullying and harassment; ensuring the equitable distribution of effective teachers and resources in low-performing, high-poverty, and high-minority schools; increasing traditionally underrepresented students' access to college- and career-ready curricula such as STEM classes, advanced placement, and other high-level courses; and increasing access to high-quality early learning programs for high-need children.

Increasing the Infusion of Equity Throughout Department Programs and Activities

In general, the Department's work includes major activities in the area of early education, elementary and secondary education, postsecondary education, and career and technical education. The Department supports White House initiatives; economically disadvantaged students; English learners; students with disabilities; women and girls; and lesbian, gay, bisexual, and transgender students. The Department continues to host and staff the ongoing work of the Equity and Excellence Commission, a group of 27 national education experts assembled to discuss ways to improve educational equity and excellence, which is expected to develop policy recommendations.

During FY 2012, senior leaders from across the Department met throughout the year to assess how equity is being pursued through current activities and what priorities or activities might be warranted, including how the Department could better promote equitable access to high quality teachers. The Office for Civil Rights (OCR), Office of English Language Acquisition, Office of Vocational and Adult Education, and Office of Special Education and Rehabilitative Services, play a leading role in planning how to increase the infusion of equity throughout the Department.

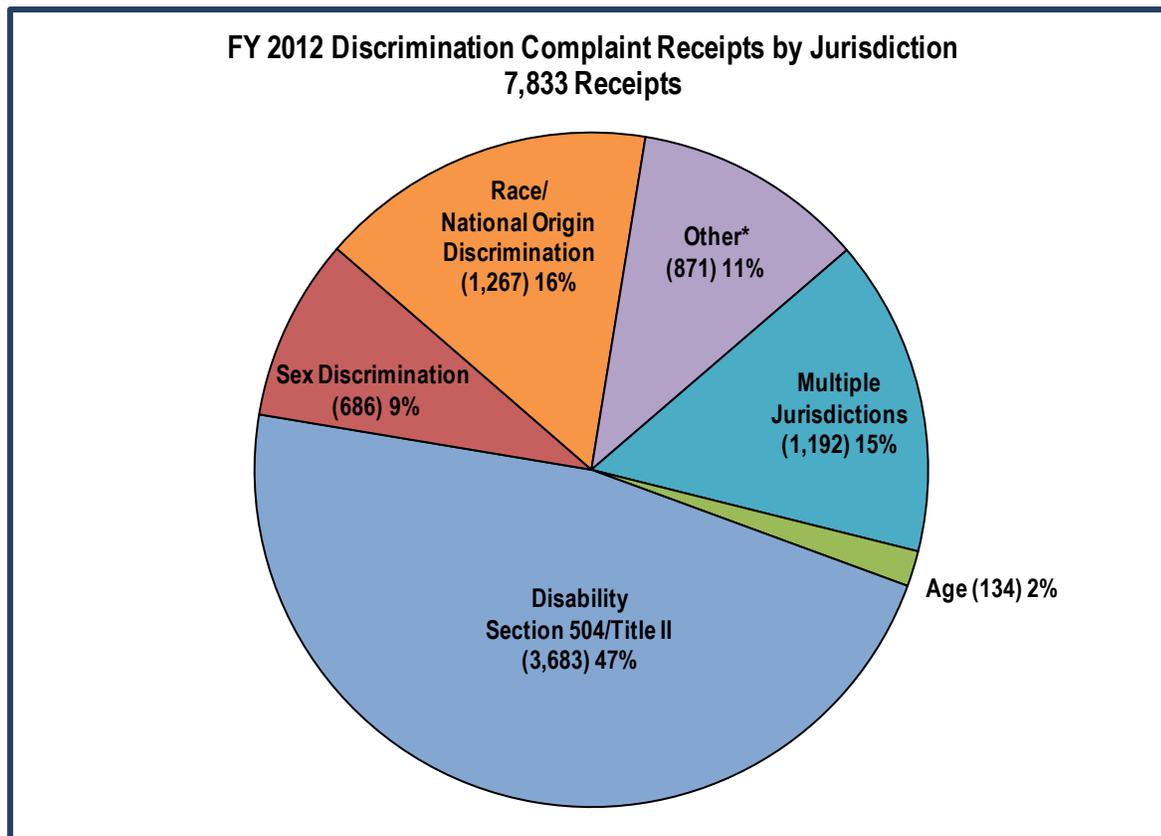
During FY 2012, the Department [launched a new website](#) and an enhanced set of data indicators for the Civil Rights Data Collection, a biannual survey. Data are disaggregated in most instances by race/ethnicity, sex, disability, and limited English proficient status. The data provided through the survey help tell the "equity story" about the nation's educational system. The data are fully accessible to the public through the website, so parents, educators, and advocates can compare and analyze schools and districts. This year, the data covered 85 percent of the nation's students and more than 70,000 public schools nationwide. Schools are now reporting more detailed and useful information related to incidents of school discipline, access to college preparatory math and science courses, bullying and harassment, restraint and seclusion, school finance, and other areas.

Ensuring Equal Access

The Department enforces federal civil rights laws that prohibit discrimination on the basis of race, color, national origin, sex, disability, and age in our nation's schools, primarily in educational institutions that receive federal funds from the Department. OCR, a law enforcement agency within the Department, performs the Department's civil rights enforcement responsibilities in a variety of ways, including: investigating complaints alleging discrimination;

conducting proactive and systemic investigations in educational institutions to determine if they are in compliance with the laws; and providing technical assistance to educational institutions on how to comply with the law and to parents and students on their rights under the law. The Department also issues regulations on civil rights laws, develops policy guidance interpreting the laws, and distributes the information broadly.

In FY 2012, OCR received a total of 7,833 complaints alleging discrimination, comparable to FY 2011's all-time high of 7,841, and resolved 8,161 complaints, some of which were received the previous year. As shown in the chart below, close to half of the complaints received by the Department allege discrimination due to disability. In addition to the issues addressed through complaint processing, OCR resolved or negotiated the settlement of 32 proactive compliance reviews, which are among the most significant public statements that OCR makes concerning civil rights compliance. OCR also initiated 6 proactive compliance reviews, and conducted 42 proactive technical assistance activities. In addition, OCR developed policy guidance to address discrimination against students on the basis of race, color, national origin, sex, and disability. OCR's law enforcement work supports progress on the Department's efforts to address equity.



* This category reflects new complaint receipts for which jurisdiction has not yet been determined. It also includes complaint receipts under the *Boy Scouts of America Equal Access Act* and those with issues over which OCR has no jurisdiction.

Source: Office for Civil Rights Case Management System

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, transparency, innovation, and technology.

Objective 5.1: Data Systems. Facilitate the development of interoperable longitudinal data systems from early learning through the workforce to enable data-driven decision-making by increasing access to timely, reliable, and high-value data.

Objective 5.2: Research and Evaluation. Support multiple approaches to research and evaluation to support educational improvement and Department decision-making.

Objective 5.3: Transparency. Present relevant and reliable information that increases demand for educational attainment and improves educational performance, while maintaining student privacy.

Objective 5.4: Technology and Innovation. Accelerate the development and broad adoption of new, effective programs, processes, and strategies, including education technology.

In FY 2012, the Department continued to support programs to help the education system, by facilitating the development of the infrastructure necessary to collect and disseminate high-value education information for the improvement of child and student outcomes.

Streamlining Data Content. In FY 2012, a database hosted by the Department was merged with [Data.gov](#) to save the cost of hosting and maintaining a separate data website and to benefit from greater participation in the shared services of [Data.gov/Education](#), where the growing community of developers and researchers continues to be supported by an expanding platform of tools and features.

The Data Quality Initiative. The Data Quality Initiative (DQI), begun in 2006, is designed to improve the quality of the Department's program performance data and reporting. The DQI contractor has worked with the Department's program offices and with grantees to review grantee [evaluation plans and reports](#); develop annual performance reporting methodologies; develop data collection and reporting guidance; review and analyze grantee annual performance data; and deliver grantee briefings and workshops focused on evaluation issues.

In 2009, the Department initiated a companion DQI contract to conduct data audits for selected programs to examine the quality and methods used to report program performance information. A second DQI technical assistance contract, awarded in September 2012, builds on prior work and provides direct assistance to program offices regarding the review, development, analysis, and reporting on *GPRA Modernization Act* and other measures to inform programmatic and budget decisions. This work also helps staff to identify key indicators, and guide their collection and use of data.

Consolidating Data Collection Through ED*Facts*. Complete and accurate data are essential for effective decision-making. [ED*Facts*](#) is the Department's initiative to put performance data at the center of policy, management, and budget decision-making for elementary and secondary educational programs. ED*Facts* centralizes performance data supplied by state educational agencies and enables the Department to better analyze and use data in policy development, planning, and management. The ED*Facts* system enables the consolidation of separate data collections and reduces the reporting burden for states by eliminating redundant data requests.

Data are available for both state and local educational agencies and school data include data on demographics, program participation, implementation, and outcomes.

Statewide Longitudinal Data Systems. The [Statewide Longitudinal Data Systems \(SLDS\) grant program](#), as authorized by the *Educational Technical Assistance Act of 2002*, is designed to aid state educational agencies in developing and implementing longitudinal data systems. Most statewide longitudinal data systems funds are awarded as state grants, but a portion of the funds are used for activities to improve data quality, coordination, and use. Current activities include the Education Data Technical Assistance program, the Privacy Technical Assistance Center, and work on common education data standards. These initiatives are intended to enhance the ability of states to efficiently and accurately manage, analyze, and use education data, including individual student records. The data systems developed with funds from these grants should help states, districts, schools, and teachers make data-driven decisions to improve student learning, as well as facilitate research to increase student achievement and close achievement gaps.

Data Strategy Team. The Department's Data Strategy Team (DST) develops and promotes coordinated and consistent data strategies among the various principal offices within the Department. The mission of the DST is to coordinate the Department's public-facing data initiatives by building cohesiveness in internal processes and data policies and by improving transparency in matters related to the Department's collection of data. The DST supports states' use of education data through data websites and technical assistance to grantees and identifies best practices for the use and promotion of data policy.

The Department's Evaluation Planning Initiatives

In May 2010, the Department launched a new agencywide evaluation planning process to better align its investments in knowledge building with the Department's Strategic Plan and its budget and policy priorities. This process, now in its second year, ensures that evaluation funds are used efficiently and effectively to advance the Department's goals. To determine the effectiveness of programs, policies, and strategies for improving education outcomes, funding is directed at evaluations that will yield reliable measures of effectiveness. For priority questions related to other issues, such as performance management and implementation support, the funding is directed to evaluations that use rigorous methods appropriate for answering those questions.

The evaluation planning team meets with the Department's policy and program offices and, based on their input, develops recommendations for future evaluation activities in the current fiscal year and beyond. Each office identifies its highest-priority research questions, as well as other program-specific research questions they would like addressed. The evaluation team examines the extent to which these research questions are supported by existing research or are being addressed through ongoing evaluations and then develops recommendations based on current and prospective resources. In FY 2011, the Department developed and approved a set of priority research questions to inform future investments in knowledge building. Planning for FY 2012 investments was largely completed this spring and planning for FY 2013 is underway, although final decisions are contingent on appropriations action.

Goal 6: U.S. Department of Education Capacity

Improve the organizational capacities of the Department to implement this Strategic Plan.

Objective 6.1: Effective Workforce. Continue to build a high-performing, skilled workforce within the Department.

Objective 6.2: Programmatic Risk Management. Improve the Department's program efficacy through comprehensive risk management and grant monitoring.

Objective 6.3: Implementation and Support. Build Department capacity to support states' and other grantees' implementation of reforms that result in improved outcomes for students.

Objective 6.4: Productivity and Performance Management. Improve workforce productivity through information technology and performance management systems.

Human Capital and Client Services

The Department is committed to ensuring its workforce has the skills needed to accomplish its Strategic Goals and to further develop human capital skills that will be needed for the future. In FY 2011, the Department assessed its human capital needs and focused on ways to improve workforce competencies through the delivery of training courses, leadership development programs, tuition reimbursement, career and organizational counseling, and computer learning support. In FY 2012, the Department's Office of Management (OM) set goals for closing competency gaps in mission critical occupations and leadership positions. These targeted competencies included fiscal monitoring, policy, legislation, and administrative rulemaking.

Additionally, OM has invested in the development of grants management staff to ensure that the workforce has the knowledge and skills required to oversee the department's grants-making process through the design and implementation of a grants management competency model and certificate program.

Continuous development for the Department's leaders is critical to the success of accomplishing our mission and vital to human capital management and succession planning. To strengthen the skills of our leaders, a number of programs were developed to enhance the leadership skills of those who are in leadership positions and those aspiring to become leaders. These programs include our Pathways to Leadership Program and Transition to Supervision Program, as well as participation in the Excellence in Government Fellows Program.

The Department Continues Risk-Based Grant Management Strategies

The Department continues to build its capacity to use data to continuously improve its grant management. In FY 2012, the Department advanced its use of data about grant applicants and recipients to inform its pre-award and post-award grant management decisions. The agency is developing its tools and procedures for grant risk management in a context of increasing governmentwide attention to grant risk, which includes significant attention to reducing improper payments through pre-payment screenings and the deployment of the Department of the Treasury's "Do Not Pay" system.

FY 2012 was the second year of the agency's consistent pre-award assessment of applicants' financial and grant management capacity. Because of new agency pre-award grant management procedures, 100 percent of programs conducted a risk assessment in FY 2012.

Each Department program staff employed a risk assessment rubric with indicators of an applicant's past performance with grants and potential financial and management weaknesses. The Department's Decision Support System Entity Risk Review (ERR), which was pilot tested in FY 2011, continued to provide program officers access to risk-related information from Dun & Bradstreet, the Department's grant management system, and the Federal Audit Clearinghouse of recipients' independent audit ("A-133 audit") results. Program officers use these data in conjunction with other performance information, including findings from on-site and desk monitoring of past and current awards, to review grant applicants' capability to manage federal funds. In FY 2012, the rubrics used to identify risk were refined based on last year's experiences to focus on the most useful and meaningful data.

In FY 2012, the agency substantially increased its resources for applying data analysis to its decision making. Guidance documents outline the allowable and recommended actions that program officers may take to mitigate risk when a recipient has past performance or management problems. The risk mitigation guidance emphasizes the use of special award conditions, such as extra reporting by the recipient, technical assistance, and increased oversight of a grant, as methods for promoting successful grant projects. Increased communication among programs—both in regular meetings and through web-based document sharing—is increasing the amount of information program officers have about their grantees. Program offices also used risk assessments to inform their annual grant monitoring plans. The agency is capturing information from risk assessments in order to improve the process over the next few years.

Programs requested and received 186 ERR reports during FY 2011. These reports were used during a Department pilot test of the ERR as a risk assessment tool. The total number of ERR reports requested and delivered for FY 2012 was 320. Grant officers use ERR reports for purposes in addition to discretionary grant pre-award risk reviews, such as oversight during the performance period of formula and discretionary grants. Therefore, the count of ERR reports used is not the same as the number of programs conducting pre-award risk reviews.

During FY 2011, 32 percent of Department programs making awards during the year participated in the pilot test, using an ERR report to inform risk assessments. Some programs that did not use ERRs may have used other sources of information for risk assessment.

During FY 2012, the Department implemented an internal policy that all discretionary grant programs will conduct a risk assessment of applicants prior to making awards. All programs used a risk index that included audit findings and information on the applicants' past performance prior to making awards. Most programs used ERR reports as a component of the risk assessment.

Because the Department has reached 100 percent program participation in the application of a risk index to conduct a risk assessment, a new measure and baseline of grant risk management will be established in 2013.

Customer Satisfaction with the Department of Education

In FY 2012, in response to the President's April 27, 2011, Executive Order 13571, Streamlining Service Delivery and Improving Customer Service, the Department survey included 38 programs.

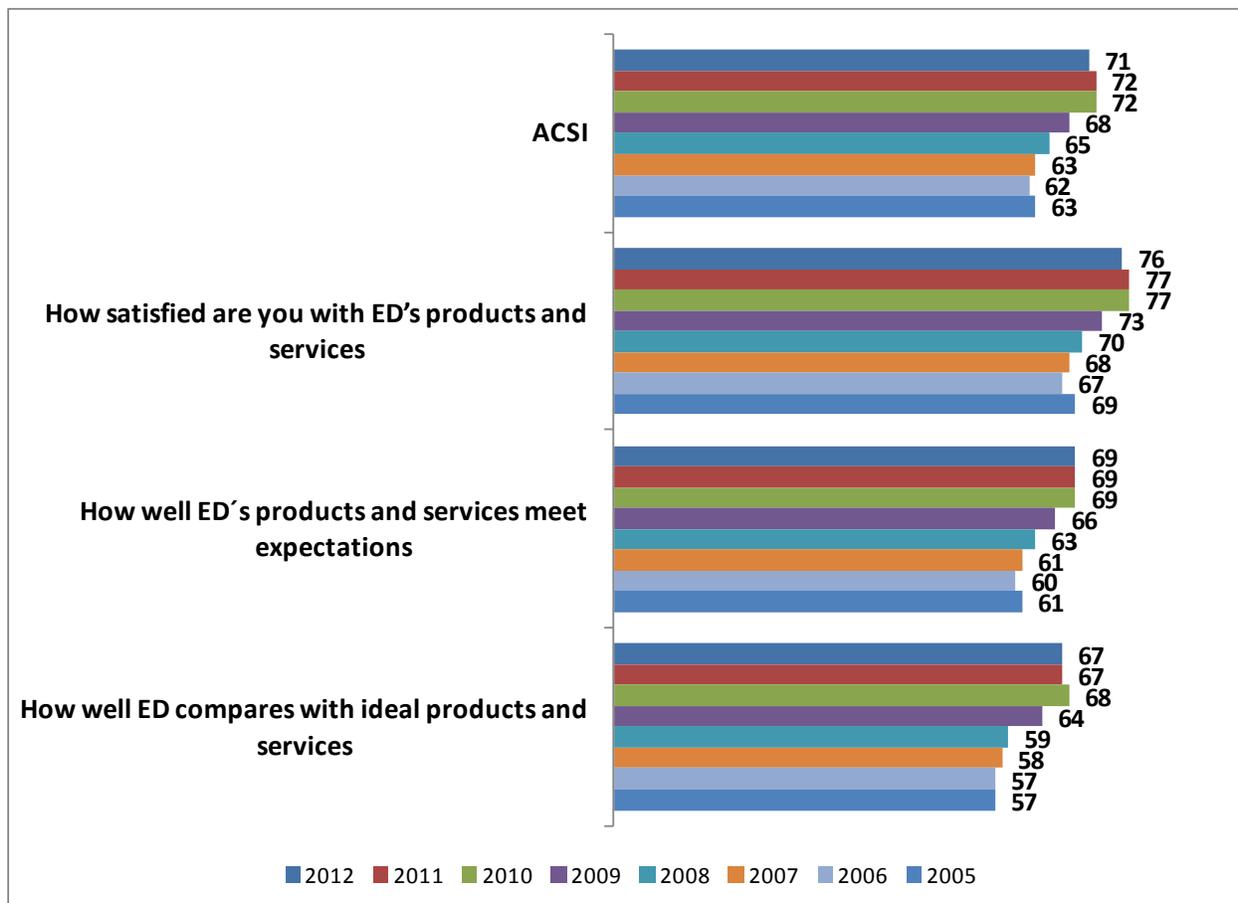
The survey uses the American Customer Satisfaction Index (ACSI). The ACSI is the national indicator of customer evaluations of the quality of goods and services. It is the only uniform benchmarking measure of customer satisfaction across agencies and private industry.

The ACSI allows benchmarking between federal agencies and provides information unique to each agency on how activities that interface with the public affect the satisfaction of its customers. The ACSI is a weighted average of three questions that measure: overall satisfaction, satisfaction compared to expectations, and satisfaction compared to an ideal organization.

Additionally, each principal office in the Department surveys their stakeholders on the effective use of technology, clarity and organization of documents, staff knowledge, responsiveness, collaboration with other Department offices, provision of technical assistance, and ease of accessing online resources.

In FY 2012, there was a slight drop in satisfaction from the previous year—from 72 to 71 points on a 100-point scale. To review the complete results of the Department’s customer satisfaction surveys: <http://www2.ed.gov/about/reports/annual/gss/index.html>.

Customer Satisfaction With the Department of Education, 2005–2012



Financial Summary

The table below summarizes trend information concerning components of the Department's financial condition. The Consolidated Balance Sheet presents a snapshot of our financial condition as of September 30, 2012, compared to fiscal year (FY) 2011, and displays assets, liabilities, and net position. Another component of the Department's financial picture is the Consolidated Statement of Net Cost. Each of these components is discussed in further detail in this section and in the Financial Details section of this report.

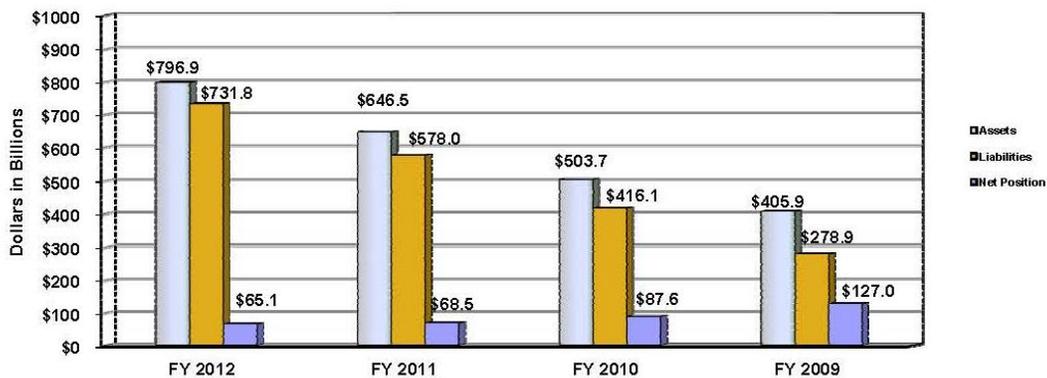
Financial Summary

Dollars in Millions

Consolidated Balance Sheet

As of September 30, 2012, 2011, 2010, 2009

	% Change 2012/2011	FY 2012	FY 2011	FY 2010	FY 2009
Fund Balance with Treasury	+7%	\$ 121,993	\$ 114,085	\$ 132,259	\$ 168,032
Credit Program Receivables, Net	+27%	673,488	530,491	367,904	234,254
Other	-26%	1,446	1,966	3,501	3,659
Total Assets	+23%	796,927	646,542	503,664	405,945
Debt	+31%	715,303	547,108	374,335	235,385
Liabilities for Loan Guarantees	-90%	1,037	10,025	14,479	20,543
Other	-26%	15,432	20,824	27,248	22,957
Total Liabilities	+27%	731,772	577,957	416,062	278,885
Unexpended Appropriations	+1%	72,686	71,729	94,371	127,269
Cumulative Results of Operations	+140%	(7,531)	(3,144)	(6,769)	(209)
Total Net Position	-5%	65,155	68,585	87,602	127,060
Total Liabilities and Net Position	+23%	\$ 796,927	\$ 646,542	\$ 503,664	\$ 405,945



Consolidated Statement of Net Cost

For the Periods Ended September 30, 2012, 2011, 2010, 2009

	% Change 2012/2011	FY 2012	FY 2011	FY 2010	FY 2009
Gross Cost	-1%	\$ 89,263	\$ 89,910	\$ 116,953	\$ 55,412
Less: Earned Revenue	+25%	(25,490)	(20,397)	(17,279)	(11,251)
Total Net Cost of Operations	-8%	\$ 63,773	\$ 69,513	\$ 99,674	\$ 44,161

Financial Highlights

The Department consistently produces accurate and timely financial information that is used by management to inform decision-making and drive results in key areas of operation. For the eleventh consecutive year, the Department achieved an unqualified (clean) opinion from independent auditors on the annual financial statements. In accordance with OMB's Circular No. A-123, *Management's Responsibility for Internal Control*, the Department continues to test and evaluate findings and risk determinations uncovered in management's internal control assessment.

Financial Position

The Department's financial statements are prepared in accordance with established federal accounting standards, as promulgated by the Federal Accounting Standards Advisory Board (FASAB), and are audited by the independent accounting firm of Ernst & Young, LLP. The Office of Inspector General (OIG) provides audit oversight. Financial statements and footnotes for FY 2012 appear on pages 41–87.

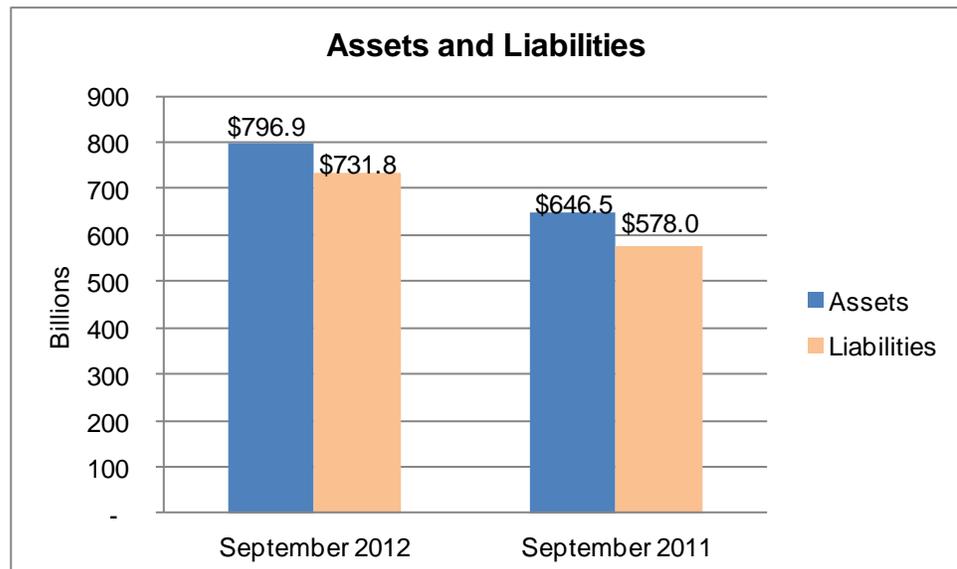
An analysis of the principal financial statements follows.

Balance Sheet.

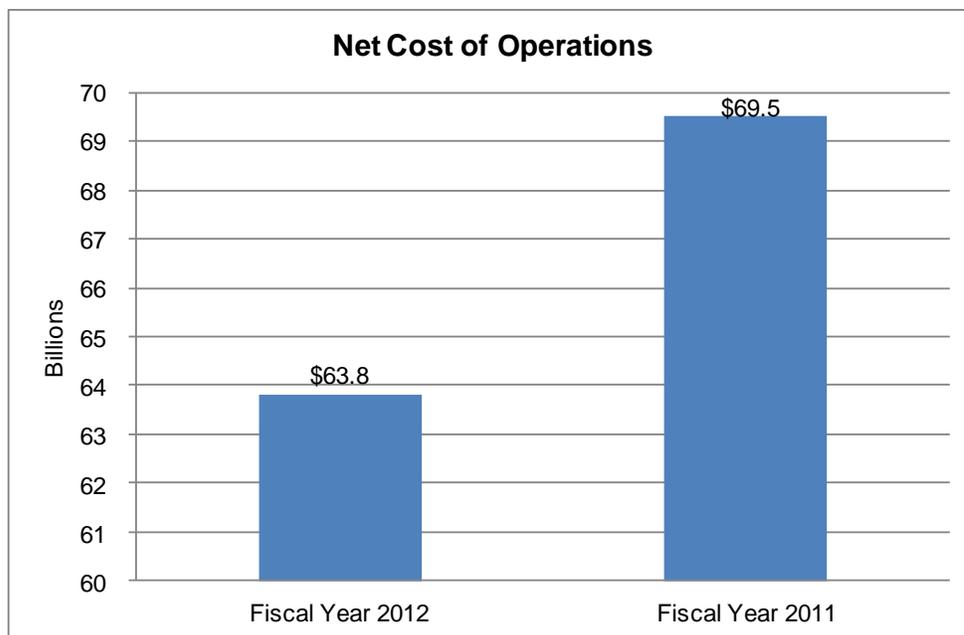
The Balance Sheet presents, as of a specific point in time, the recorded value of assets and liabilities retained or managed by the Department. The difference between assets and liabilities represents the net position of the Department.

The Balance Sheet displayed on page 41 reflects total assets of \$796.9 billion, a 23 percent increase over FY 2011. The vast majority of this increase is due to Credit Program Receivables, which increased by \$143.0 billion, a 27 percent increase over FY 2011. This increase is largely the result of Direct Loan disbursements for new loan originations and loan consolidations, net of borrower principal and interest collections, which increased the net portfolio for Direct Loans by \$144.6 billion.

Total liabilities for the Department increased by \$153.8 billion, a 27 percent increase over FY 2011. The increase is the result of current year borrowing for the Direct Loan and FFEL Programs that provided funding for Direct Loan disbursements and FFEL Program downward re-estimates. This current year borrowing, net of repayments, resulted in a \$168.2 billion increase in Debt. Liabilities for Loan Guarantees for the FFEL Program decreased by \$9.0 billion, a 90 percent decrease that is primarily due to FY 2012 subsidy re-estimates.



Statement of Net Cost. The Statement of Net Cost presents the components of the Department's net cost, which is the gross cost incurred less any revenues earned from the Department's activities. The Department's total program net costs, as reflected on the Statement of Net Cost, page 42, were \$63.8 billion during FY 2012,



an 8 percent decrease compared to total program net costs during the prior year. Significant components of this change include a \$20.3 billion decrease in Recovery Act and Education Jobs Fund disbursements and a \$17.9 billion increase in Direct Loan program subsidy related costs (negative subsidy transfers and re-estimated subsidy cost).

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 goals presented in the Department's *Strategic Plan 2011–2014*.

Net Cost Program	Reporting Group/ Program Office	Strategic Goal
Increase College Access, Quality, and Completion	Federal Student Aid Office of Postsecondary Education Office of Vocational and Adult Education	1. Increase college access, quality, and completion by improving higher education and lifelong learning opportunities for youth and adults.

Net Cost Program	Reporting Group/ Program Office	Strategic Goal
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	2. Prepare all elementary and secondary students for college and career by improving the education system's ability to consistently deliver excellent classroom instruction with rigorous academic standards while providing effective supportive services. 3. 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	Office of English Language Acquisition Office for Civil Rights Office of Special Education and Rehabilitative Services	4. Ensure and promote effective educational opportunities and safe and healthy learning environments for all students regardless of race, ethnicity, national origin, age, sex, sexual orientation, gender identity, disability, language, and socioeconomic status.
Enhance the Education System's Ability to Continuously Improve	Institute of Education Sciences Office of Innovation and Improvement	5. Enhance the education system's ability to continuously improve through better and more widespread use of data, research and evaluation, transparency, innovation and technology.
American Recovery and Reinvestment Act and Education Jobs Fund	American Recovery and Reinvestment Act Education Jobs Fund	Cuts across Strategic Goals 1–5

Strategic Plan Goals 1–5 are sharply defined directives that 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, 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.

The goals of the Recovery Act and Education Jobs Fund are consistent with the Department's current *Strategic Plan* goals and programs.

Statement of Budgetary Resources. This statement provides information about the provision of budgetary resources and their status as of the end of the reporting period. The statement displayed on page 44 shows that the Department had \$375.0 billion in total budgetary resources for the year ended September 30, 2012. These budgetary resources were composed of \$104.7 billion in appropriated budgetary resources and \$270.3 billion in non-budgetary credit reform resources that primarily consist of borrowing authority for the loan programs. Of the \$31.6 billion that remained unobligated for the year ended September 30, 2012, \$20.5 billion represents funding provided in advance for activities in future periods that were not available at year end. These funds will become available during the next, or future, fiscal years.

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 2012 and FY 2011, 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.

Management's Assurances

Federal Managers' Financial Integrity Act of 1982 (FMFIA)

FMFIA requires that agencies establish internal controls and financial systems that provide reasonable assurance that the integrity of Federal programs and operations is protected. It requires that the head of the agency provide an annual assurance statement as to whether the agency has met this requirement. Appendix A of OMB Circular A-123 provides specific requirements for conducting management's assessment of internal control over financial reporting, and also requires the agency head to provide an assurance statement on the effectiveness of internal controls over financial reporting.

The Department's rigorous FY 2012 assessment of internal controls identified two material weaknesses with Federal Student Aid servicing systems. These weaknesses reflect, in aggregate, a number of internal control deficiencies that resulted from system functionality issues occurring after large-scale system conversions in October 2011. The conversions involved extensive data transfers under two information technology system contracts. The systems—currently operated under contracts with Xerox, Inc.—help track and report on data from the Direct Loan and Federal Family Education Loan (FFEL) programs. Within the Department, these two contracts with the conversion challenges are known as: 1) ACS, Inc. Education Servicing (ACES); and 2) Debt Management Collection System (DMCS2).

Material Weakness in Internal Controls Over Financial Reporting of Federal Student Aid Data

The Department's management teams responsible for implementation and oversight of these systems identified multiple internal control deficiencies with ACES and DMCS2 as a result of the system conversions that may adversely impact the accuracy of financial reporting, to include the reporting of loan balances, fund balance with Treasury, and suspense account balances; the processing of portfolio and cash reconciliations; and qualified Service Organization Control 1 (SOC 1) Reports. As of June 30, 2012, in management's judgment these reportable conditions, in the aggregate, would result in more than a remote likelihood that a material misstatement of the Department's financial statements would not be prevented or detected—if the conditions remained uncorrected.

Since June 30, 2012, the Department has taken aggressive action to correct these financial reporting deficiencies. Federal Student Aid (FSA) management actively monitored and tracked system functionality issues and worked closely with Xerox, Inc. to fully examine root causes, impacts, and affected processes. The Department took a number of corrective actions.

To correct inaccurate loan balances, FSA implemented a number of system fixes, and researched and corrected borrower balances. FSA conducted and eliminated a backlog of portfolio and cash reconciliations, and evaluated and corrected suspense account balances by adjusting the matching process. FSA also implemented other internal control improvements that resulted in system fixes, restored system functionality, and reduced backlogs (including administrative wage garnishment and Treasury offset to improve collections, rehabilitation of loans and transfer of loans to continue servicing, and file processing).

As a result of these aggressive actions, as of September 30, 2012, the Department is confident these corrective actions have reduced the potential adverse impacts of the underlying reportable conditions such that, in the aggregate, they do not result in more than a remote

likelihood that a material misstatement of the financial statements in this report would not be prevented or detected. In management's judgment, in the aggregate these reportable conditions and the potential errors that may fail to be prevented or detected are below the level that is material. Reportable conditions remain; however, the Department continues to take these remaining reportable conditions and potential errors very seriously and continues to take aggressive corrective action to fully resolve them.

Material Weakness in Internal Controls Over Operation of Direct Loan and FFEL Programs

The internal control deficiencies related to ACES and DMCS2 impact multiple internal control objectives. In addition to internal control over financial reporting, some of these deficiencies impact internal control over the effectiveness and efficiency of operations. These include issues with the acceptance of loan assignments, transfers, and collection activities. These issues result in material weaknesses for FMFIA Section 2 reporting, for the year ended September 30, 2012.

The Department has taken similarly aggressive actions to begin to correct the root causes of these internal control deficiencies, but in management's assessment the outstanding deficiencies in this area, in the aggregate, remain significant as of September 30, 2012. These actions will continue into 2013 and include research into borrower balances and root cause analysis of system limitations to inform recommendations on system and process fixes.

Federal Financial Management Improvement Act of 1996 (FFMIA)

FFMIA requires that agencies implement and maintain financial management systems that comply substantially with the Federal financial management system requirements, applicable Federal accounting standards, and the United States Government Standard General Ledger at the transaction level. The agency head is to make an annual determination whether the financial systems substantially comply with FFMIA.

On account of the outstanding internal control deficiencies associated with the ACES and DMCS2 financial systems that affect financial reporting, the Secretary has determined the Department's financial systems do not substantially comply with all FFMIA requirements as of September 30, 2012. The previously described deficiencies that continue to impact borrower data elevate the risk of the Department's financial systems to a moderate level. In addition, the Department's assessment identified a number of system-related internal control deficiencies including: security management and user access issues (e.g., user access documentation, security awareness training, review and termination of inactive users, security documentation), application-level issues (e.g., change control, logging and monitoring, password parameters), and business process issues related to dormant data, edit checks, and transaction data processing. The Department believes the combination of these deficiencies support the non-compliance determination.

Consistent with OMB Circular A-123 requirements, the Department's plans for bringing all financial systems—namely ACES and DMCS2—into substantial compliance with FFMIA are summarized in the previous section. These efforts will increase the reliability and timeliness of financial information for managing current operations. The Department also will continue efforts to address security and control weaknesses with an emphasis on addressing their root cause uniformly across the organization. The goal of this action is to decrease the likelihood of similar weaknesses.

The Department continues to meet other key criteria for compliance with FFMA:

- Financial statements, both annual and quarterly presentations, and other required financial and budget reports are prepared using information generated by the Financial Management Support System (FMSS); and
- The FMSS operations and procedures remain consistent with Federal accounting standards and comply with the U.S. Government Standard General Ledger guidance at a transactional level.

Federal Managers' Financial Integrity Act and Federal Financial Management Improvement Act

Federal Managers' Financial Integrity Act

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). The Department conducted its assessment of the effectiveness of internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations in accordance with OMB Circular A-123, *Management's Responsibility for Internal Control*. Based on the results of this evaluation, the Department identified a material weakness in internal controls over the operation of the Direct Loan and FFEL programs. For all other program areas, the Department can provide reasonable assurance that internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations as of September 30, 2012, was operating effectively; no other material weaknesses were found in the design or operation of the internal controls.

In addition, 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. Based on the results of the evaluation, the Department identified a material weakness in internal controls over financial reporting of student loan data as of June 30, 2012. However, corrective actions were taken and, as of September 30, 2012, the Department can provide reasonable assurance that its internal controls over financial reporting were operating effectively and no material weaknesses were present in the design or operation of the internal controls.

Federal Financial Management Improvement Act

The *Federal Financial Management Improvement Act of 1996* (FFMIA) requires agencies to implement and maintain financial management systems that are substantially in compliance 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 and outstanding internal control deficiencies, the Department's financial management systems do not substantially comply with FFMIA as of September 30, 2012.

/s/

Arne Duncan
November 16, 2012

Financial Management Systems Strategy

The Department's FMSS is designated a mission-critical system of the Department that provides departmentwide core financial management services. These services include funds control, budget planning, general ledger, administrative payments, accounts receivable; financial management system and access controls; financial system reports, including financial statements, FACTS, SF224, etc. The Department expects to continue on its improvements in the following performance outcomes: continued control over and accountability of Department financial management services, including financial management system controls and practices that include cross-validation rules that prevent erroneous accounting transactions from being processed; and financial system reporting capabilities that continue the ability to respond quickly to internal and external financial information inquiries. Additional outcomes are continued tight integration and streamlining with the Office of Federal Student Aid and business processes; reduced manual reconciliation efforts for the Financial Management Operations Group within 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). The Oracle system has operated successfully for the Department since its implementation in January 2002. Since this time, the Department has met all of its financial management performance measures, which include receiving unqualified financial statement audit opinions for each year since implementation, system availability rates of better than 99 percent of the scheduled time, and closing periods within three days of the end of the month.

Oracle has recently issued Release 12 of its software. This version has passed the necessary testing and is federally compliant for financial management. The Department has completed an analysis on the change between the 11i and Release 12 versions of the software to determine the benefits and level of effort to implement the new version. Based on the outcome of this analysis and budget constraints, the Department has decided to delay migration to Release 12 until FY 2017. Migration activities will begin during FY 2015 and will be completed in October 2016. These timeframes are subject to change based on funding levels and other priorities.

