MANAGEMENT’S DISCUSSION AND ANALYSIS
ABOUT THE MANAGEMENT’S DISCUSSION AND ANALYSIS

The U.S. Department of Education (Department) continued to enhance the content quality, report layout, and public accessibility of the fiscal year (FY) 2020 Agency Financial Report (AFR) by refining graphics and providing more useful, balanced, and easily understood information about the Coronavirus Aid, Relief, and Economic Security Act, also known as the CARES Act, and about the Department’s loan programs, including additional cost and risk information. Additionally, we chose relevant web content to provide users with additional information about the Department’s operations and performance. To take advantage of the hyperlinks embedded in the report, the Department recommends reading it on the Internet. To help us continue to improve the quality and usefulness of information provided in our AFR, we encourage our public and other stakeholders to provide feedback and suggestions at AFRComments@ed.gov.

This section highlights information on the Department’s performance, financial statements, systems and controls, compliance with laws and regulations, and actions taken or planned to address select challenges.

MISSION AND ORGANIZATIONAL STRUCTURE

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

THE DEPARTMENT’S APPROACH TO PERFORMANCE

This section provides a brief summary of the Department’s performance goals and results for FY 2020. Since the Department has chosen to produce separate financial and performance reports, a detailed discussion of performance information for FY 2020 will be provided in the Department’s FY 2020 Annual Performance Report and FY 2022 Annual Performance Plan to be released online at the same time as the President’s FY 2022 Budget in February 2021. For more information, prior year performance reports can be found on the Department’s website. We also urge readers to seek programmatic data as it is reported in the Congressional Budget Justification, as well as on the web pages of individual programs. Any questions or comments about the Department’s performance reporting should be e-mailed to PIO@ed.gov. For more details on performance, please refer to the Department’s budget and performance web page at www.Performance.gov.

FINANCIAL HIGHLIGHTS

The Department expends a substantial portion of its budgetary resources and cash on multiple loan and grant programs intended to support state and local efforts to improve learning outcomes for all prekindergarten through 12th grade (P–12) students in every community and to expand postsecondary education options and improve outcomes to foster economic opportunity and informed, thoughtful, and productive citizens. Accordingly, the Department has included more high-level details about sources and uses of the federal funds received and net costs by program.

ANALYSIS OF SYSTEMS, CONTROLS, AND LEGAL COMPLIANCE

The Department’s internal control framework and its assessment of controls, in accordance with Office of Management and Budget (OMB) Circular A-123, Management’s Responsibility for Enterprise Risk Management and Internal Control, provide assurance to Department leadership and external stakeholders that financial data produced by the Department’s business and financial processes and systems are complete, accurate, and reliable.

FORWARD-LOOKING INFORMATION

The Forward-Looking Information section describes the challenges that the Department aims to address to achieve progress on Enterprise Risk Management, Direct Loans, Next Gen Federal Student Aid (Next Gen FSA), Leveraging Data as a Strategic Asset, and Technology Business Management Solutions (TBMS).
ABOUT THE DEPARTMENT

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

Who We Are. In 1867, the federal government recognized that furthering education was a national priority and created a federal education agency to collect and report statistical data. The Department was established as a cabinet-level agency in 1980. Today, the Department supports programs in every area and level of education from preschool through postdoctoral research.

The Department makes funds and information available to individuals pursuing an education, colleges and universities, state education agencies, and school districts by engaging in four major categories of activities:

- Establishing policies related to federal education funding, including distributing funds, collecting on student loans, and using data to monitor the use of funds.
- Supporting data collection and research on America’s schools.
- Identifying major issues in education and focusing national attention on them.
- Enforcing federal laws promoting equal access and prohibiting discrimination in programs that receive federal funds.

Our Public Benefit. The Department executes the laws passed by Congress to promote student academic achievement and preparation for global competitiveness. The Department works with students, parents, educational institutions, school districts, and states to foster educational excellence and to ensure equal access to a high quality education for all students. While recognizing the primary role of states and school districts in providing high quality education, the Department is committed to helping ensure students throughout the nation develop skills to succeed in school, pursue postsecondary options, and transition to the workforce. The Department’s vision is to improve educational outcomes for all students.

Many of the Department’s programs involve awarding grants to state and local educational agencies and providing grants and loans to postsecondary students. The Department’s largest outlays are for its portfolio of student loans (see the Financial Highlights and Notes sections). Grant programs constitute the second-largest driver of outlays. The grant programs include: student aid to help pay for college through Pell Grants, Work Study, and other campus-based programs; grants awarded based on statutory formulas mostly for elementary and secondary education; and competitive grant programs to promote innovation. The Department also supports research, collects education statistics, and enforces civil rights statutes. We manage and spend financial resources on programs designed to support parents, teachers, principals, school leadership, institutions, and states in the pursuit of instilling knowledge and transferring skills to students.
OUR ORGANIZATION IN FISCAL YEAR 2020

This chart reflects the coordinating structure of the U.S. Department of Education. A text version of the FY 2020 coordinating structure of the Department is available.

PERFORMANCE MANAGEMENT FRAMEWORK

In accordance with the GPRA Modernization Act of 2010, the Department’s framework for performance management starts with the four-year Strategic Plan, including its two-year Agency Priority Goals (APGs), which serve as the foundation for establishing and implementing long-term priorities and performance goals, objectives, and measures by which the Department can gauge achievement of its stated outcomes. Progress towards the Department’s strategic goals and its APGs is measured using data-driven review and analysis. Additional information on performance management is available in the Annual Performance Plans and Annual Performance Reports.

The FY 2018–22 Strategic Plan is comprised of four strategic goals and five FY 2019-20 APGs. The Strategic Plan aims to align the Administration’s yearly budget requests and the Department’s legislative agenda, supported by the considerable experience and resources available from its staff. The Department continues to welcome input from Congress, state and local partners, and other education stakeholders about the Strategic Plan. Questions or comments about the Strategic Plan should be emailed to PIO@ed.gov.

FY 2018–22 Strategic Goals and Strategic Objectives

<table>
<thead>
<tr>
<th>Strategic Goal 1:</th>
<th>Support state and local efforts to improve learning outcomes for all prekindergarten–grade 12 students in every community.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strategic Objective 1.1</td>
<td>Increase high-quality educational options and empower students and parents to choose an education that meets their needs.</td>
</tr>
<tr>
<td>Strategic Objective 1.2</td>
<td>Provide all prekindergarten - grade 12 students with equal access to high-quality educational opportunities.</td>
</tr>
<tr>
<td>Strategic Objective 1.3</td>
<td>Prepare all students for successful transitions to college and careers by supporting access to dual enrollment, job skills development and high-quality science, technology, engineering and mathematics (STEM).</td>
</tr>
<tr>
<td>Strategic Objective 1.4</td>
<td>Support agencies and institutions in the implementation of evidence-based strategies and practices that build the capacity of school staff and families to support students’ academic performance.</td>
</tr>
</tbody>
</table>

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<thead>
<tr>
<th>Strategic Goal 2:</th>
<th>Expand postsecondary educational opportunities, improve outcomes to foster economic opportunity and promote an informed, thoughtful and productive citizenry.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strategic Objective 2.1</td>
<td>Support educational institutions, students, parents and communities to increase access and completion of college, lifelong learning and career, technical and adult education.</td>
</tr>
<tr>
<td>Strategic Objective 2.2</td>
<td>Support agencies and educational institutions in identifying and using evidence-based strategies or other promising practices to improve educational opportunities and successfully prepare individuals to compete in the global economy.</td>
</tr>
<tr>
<td>Strategic Objective 2.3</td>
<td>Support agencies and educational institutions as they create or expand innovative and affordable paths to relevant careers by providing postsecondary credentials or job-ready skills.</td>
</tr>
<tr>
<td>Strategic Objective 2.4</td>
<td>Improve quality of service for customers across the entire student aid life cycle.</td>
</tr>
<tr>
<td>Strategic Objective 2.5</td>
<td>Enhance students’ and parents’ ability to repay their federal student loans by providing accurate and timely information, relevant tools and manageable repayment options.</td>
</tr>
</tbody>
</table>

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<thead>
<tr>
<th>Strategic Goal 3:</th>
<th>Strengthen the quality, accessibility and use of education data through better management, increased privacy protections and transparency.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strategic Objective 3.1</td>
<td>Improve the Department’s data governance, data life cycle management and the capacity to support education data.</td>
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<tr>
<td>Strategic Objective 3.2</td>
<td>Improve privacy protections for, and transparency of, education data both at the Department and in the education community.</td>
</tr>
<tr>
<td>Strategic Objective 3.3</td>
<td>Increase access to, and use of, education data to make informed decisions both at the Department and in the education community.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Strategic Goal 4:</th>
<th>Reform the effectiveness, efficiency and accountability of the Department.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strategic Objective 4.1</td>
<td>Provide regulatory relief to educational institutions and reduce burden by identifying time-consuming regulations, processes and policies and working to improve or eliminate them, while continuing to protect taxpayers from waste and abuse.</td>
</tr>
<tr>
<td>Strategic Objective 4.2</td>
<td>Identify, assess, monitor and manage enterprise risks.</td>
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<tr>
<td>Strategic Objective 4.3</td>
<td>Strengthen the Department’s cybersecurity by enhancing protections for its information technology infrastructure, systems and data.</td>
</tr>
<tr>
<td>Strategic Objective 4.4</td>
<td>Improve the engagement and preparation of the Department’s workforce using professional development and accountability measures.</td>
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</tbody>
</table>

2 The FY 2020 Statement of Net Cost and related notes align with the FY 2018–22 Strategic Plan.
THE DEPARTMENT’S AGENCY PRIORITY GOALS (APGs)

The Department identified five APGs for FY 2020-2021. Improving education starts with allowing greater decision-making authority at the state and local levels and empowering parents and students with educational options. These goals seek to increase education choices, enhance multiple pathways for student success in career and job ready skills, improve the Department's Federal Student Aid customer service, improve student privacy protection and cybersecurity at institutions of higher education (IHEs), and provide regulatory relief and burden reduction to stakeholders. The effective implementation of the Department's APGs will depend, in part, on the effective use of high-quality and timely data, including evaluations and performance measures. The Goal Action Plans and quarterly updates for the APGs are available on www.Performance.gov/education/education.html.

<table>
<thead>
<tr>
<th>APG</th>
<th>Related Strategic Objective</th>
</tr>
</thead>
<tbody>
<tr>
<td>Education Freedom: Improve awareness of and access to high-quality K-12 education opportunities for students and families. By September 30, 2021, the Department will increase both the number and percentage of total charter school students and total scholarship students nationwide. • Charter school enrollment will increase from 3.29 million to 3.51 million (6.90 percent of all students in public schools). • The number of scholarship students, including participants in state-based vouchers, tax-credit scholarship, and education savings account program, will increase from 482,000 to 579,250 (1.10 percent of the total school age population). • The number of parents who receive support and engagement through technical assistance and other resources will increase by 5 percent per year.</td>
<td>Strategic Objective 1.1: Increase high-quality educational options and empower students and parents to choose an education that meets their needs.</td>
</tr>
<tr>
<td>Multiple Pathways to Success: Improve nationwide awareness of and access to career pathways that support job skills development and career readiness. By September 30, 2021, the Department will, through programs such as the Career and Technical Education and Adult Education State Grants: • Support the creation and expansion of integrated education and training (IET) programs in all 50 states, Puerto Rico, and the District of Columbia. • Increase enrollment of participants in IET programs to 56,000. • Support the enrollment of Career and Technical Education concentrators in science, technology, engineering, and mathematics (STEM) fields. • Increase by 25,000 the number of federal financial aid recipients who earn a postsecondary credential in STEM.</td>
<td>Strategic Objective 1.3: Prepare all students for successful transitions to college and careers by supporting access to dual enrollment, job skills development and high-quality science, technology, engineering and mathematics (STEM). Strategic Objective 2.3: Support agencies and educational institutions as they create or expand innovative and affordable paths to relevant careers by providing postsecondary credentials or job-ready skills.</td>
</tr>
<tr>
<td>FSA Customer Service: Leverage the Next Generation Financial Services Environment (Next Gen FSA) to improve and personalize customers’ experience with Federal Student Aid (FSA). By September 30, 2021, FSA will transform its relationship with prospective and current customers through deployment of significant components of the Next Gen FSA that result in a personalized experience: • The number of individuals submitting a Free Application for Federal Student Aid® (FAFSA®) through a mobile device will increase to 2.6 million. • The overall customer satisfaction level throughout the student aid life cycle, as measured by the FSA Customer Satisfaction score1, will increase.</td>
<td>Strategic Objective 2.4: Improve quality of service for customers across the entire student aid life cycle.</td>
</tr>
<tr>
<td>Student Privacy and Cybersecurity: Improve student privacy and cybersecurity at institutions of higher education (IHEs) through outreach and compliance efforts. By September 30, 2021, the Department will participate in 12 engagements with sector-related non-governmental organizations to inform the development of five best practice programmatic improvements.</td>
<td>Strategic Objective 3.2: Improve privacy protections for, and transparency of, education data both at the Department and in the education community.</td>
</tr>
<tr>
<td>Regulatory Reform: Provide regulatory relief to education stakeholders as necessary and appropriate. (Related Strategic Objective: 4.1) By September 30, 2021, the Department will provide regulatory relief for education stakeholders by taking no fewer than eight deregulatory actions, which includes reduction in paperwork burden.</td>
<td>Strategic Objective 4.1: Provide regulatory relief to educational institutions and reduce burden by identifying time-consuming regulations, processes and policies and working to improve or eliminate them, while continuing to protect taxpayers from waste and abuse.</td>
</tr>
</tbody>
</table>

1 The Federal Student Aid Customer Satisfaction Score is an annual composite metric that measures the overall customer satisfaction level throughout the student aid life cycle for Free Application for Federal Student Aid® (FAFSA®) applicants (mobile and FAFSA.gov), Title IV aid recipients in school, and borrowers in repayment. The score is based on the American Customer Satisfaction Index surveys.
Goal 1. Support state and local efforts to improve learning outcomes for all P–12 students in every community.

Strategic Goal 1 focuses on outcomes related to the transition from the No Child Left Behind Act to implementation of the Every Student Succeeds Act (ESSA), which reauthorized the Elementary and Secondary Education Act in December 2015. The hallmark of the ESSA is the flexibility it provides for states to do what is best for children while preserving important protections for economically disadvantaged students, children with disabilities, English learners, and other vulnerable students. The law requires that states take steps to ensure all students have access to excellent teachers and positive, safe learning environments that equip them for college and career success. The Department supports improved learning outcomes by awarding approximately $40 billion to states, school districts, and nonprofit organizations.

The Department encourages families to be aware of educational opportunities and choices available so that they can make the best choice for their student’s needs. Access to high-quality educational opportunities should be afforded to all students. In FY 2020, the Department conducted outreach to states, schools, and other educational organizations to promote school choice. As learning outcomes are not just affected in the classrooms, the Department launched a state information sharing tool on schoolsafety.gov which allows schools to share safety plans, compare policies, and learn from each other in an effort to create safe learning environments.

In response to the COVID-19 pandemic, the Equity Assistance Centers funded by the Department developed a set of resources to facilitate equitable learning opportunities in virtual educational environments. In FY 2020, the Department supported P–12 schools impacted by COVID-19 with more than $13.3 billion in funding. Funding included Elementary and Secondary School Emergency Relief Fund grants and the Education Stabilization Fund-Rethink K-12 Education Models Grants.

Goal 2. Expand postsecondary educational opportunities, improve outcomes to foster economic opportunity and promote an informed, thoughtful and productive citizenry.

Strategic Goal 2 focuses on expanding the Department’s efforts to support innovative and accessible paths to postsecondary credentials and job-ready skills training. In addition to supporting expanded postsecondary opportunities, the Department has a number of initiatives focused on affordability. These initiatives ensure borrowers have the best information available to make postsecondary program selection and associated borrowing decisions. The Department also continues to help students understand their financial aid options and repayment obligations. In FY 2020, $31.6 billion was appropriated to the Department in support of this Strategic Goal 2. More than 5,000 grants were awarded to support colleges and universities in their efforts to promote and expand access and improvements to post-secondary education that will contribute to the global success of our nation. In addition, funding for Strategic Goal 2 also supports the Department’s enhancements to customer service for customers and stakeholders of Federal Student Aid.

The Department continues efforts to help prepare the nation’s workforce of tomorrow with the right skills and credentials of today. In FY 2020, the Department conducted a Teaching Skills that Matter symposium with more than 1,000 teachers to help adult education instructors integrate employability skills development with academic instruction. In addition, the Department continued to prioritize workforce preparation during the COVID-19 pandemic through various virtual and technical outreach activities.

In FY 2020, the Department had much success in implementing CARES Act provisions. Approximately $14 billion in funding was appropriated for the CARES Act Higher Education Emergency Relief Fund Programs. The Department succeeded in distributing 90 percent of the funding to IHEs within 30 days of authorization. The additional 10 percent was distributed within the following
than 750 technical assistance inquiries. The Department was also proactive in its approach to cybersecurity by conducting outreach and meeting with IHEs.

**Goal 4. Reform the effectiveness, efficiency and accountability of the Department.**

Strategic Goal 4 focuses in general on protecting taxpayers from fraud, waste, and abuse. This involves improving internal decision-making and reducing regulatory burden on external stakeholders. In FY 2020, $623 million was appropriated to support Goal 4.

The Department continually performs comprehensive reviews of the Department’s regulations, guidance, and information collections to identify and take appropriate action with regard to those that are overly burdensome, inconsistent with Administration priorities, unnecessary, outdated, or ineffective. In FY 2020, there was savings from burden reduction of $113.5 million (annualized) and $1.622 billion (present value), both over a perpetual time horizon.

Strategic Goal 4 also includes the responsibility of the Department to implement Enterprise Risk Management (ERM). The Department uses a coordinated approach to identify, measure, and assess challenges related to mission delivery and resource management. In FY 2020, the Department joined an Office of Management and Budget pilot to test, assess, and validate sections or components of ERM. The Department continues to assess ERM maturity and identify likelihoods and impacts to Department operations and mission.

Strategic Goal 4 also includes the responsibility to ensure the Department’s workforce is properly trained and accountable. In FY 2020, the Department implemented a strategy focused on improving employee engagement, performance, and competency development. The Department continues its efforts to provide professional development where gaps in competency have been identified. During the COVID-19 pandemic, the Department continues to foster employee engagement through virtual platforms as most employees telework.
FINANCIAL HIGHLIGHTS

INTRODUCTION

This section provides summarized information and analyses about the Department’s assets, liabilities, net position, sources and uses of funds, program costs, and related trend data. It also provides a high-level perspective of the detailed information contained in the financial statements and related notes.

The Department consistently produces complete, accurate, and timely financial information. The Department’s financial statements and notes are prepared in accordance with accounting principles generally accepted in the United States for federal agencies issued by the Federal Accounting Standards Advisory Board and the format and content specified by OMB Circular No. A-136, *Financial Reporting Requirements*. The financial statements, notes, and underlying business processes, systems, and controls are audited by an independent accounting firm with audit oversight provided by the Office of Inspector General (OIG). For 19 consecutive years, the Department has earned an unmodified (or “clean”) audit opinion. The financial statements and notes for FY 2020 are on pages 40–85 and the Independent Auditors’ Report begins on page 90.

The principal financial statements are prepared to report the financial position and results of operations of the reporting entity, pursuant to the requirements of 31 U.S.C. § 3515(b). The statements are prepared from the Department’s books and records in accordance with generally accepted accounting principles for federal entities and the formats prescribed by OMB. Reports used to monitor and control budgetary resources are prepared from the same books and records. The financial statements should be read with the realization that they are for a component of the U.S. Government.

FINANCIAL STATEMENT IMPACTS OF COVID-19 ACTIVITIES

Most of the significant changes to the Department’s financial statements resulted from the impacts due to COVID-19 activities. The *CARES Act* totaled roughly $2 trillion dollars and included almost $31 billion of direct appropriations to the Department for educational purposes. The largest component of this funding established a $30.8 billion Education Stabilization Fund for K-12 and higher education. This fund is comprised of categories including: (1) the Elementary and Secondary School Emergency Relief Fund; (2) the Higher Education Emergency Relief Fund; (3) the Governor’s Emergency Education Relief Fund; and (4) funds provided for outlying areas and discretionary grants. The *CARES Act* also provided other direct appropriations – primarily to

<table>
<thead>
<tr>
<th>Table 1. Key Financial Statement Changes (Dollars in Billions)</th>
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<td>Financial Statement Lines with Significant Changes</td>
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<tr>
<td>Balance Sheets</td>
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<tr>
<td>Fund Balance with Treasury</td>
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<tr>
<td>Statements of Net Cost</td>
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<tr>
<td>Expand Postsecondary Opportunities, Improve Outcomes to</td>
</tr>
<tr>
<td>Foster Economic Opportunity, and Promote Productive Citizenry</td>
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<tr>
<td>Statements of Budgetary Resources</td>
</tr>
<tr>
<td>Appropriations (Discretionary and Mandatory)</td>
</tr>
<tr>
<td>New Obligations and Upward Adjustments (Total)</td>
</tr>
<tr>
<td>Unobligated Balance, End of Year (Total)</td>
</tr>
<tr>
<td>Outlays, Net</td>
</tr>
<tr>
<td>Disbursements, Net</td>
</tr>
</tbody>
</table>
The direct and indirect funding stemming from the CARES Act and the Presidential Memorandum is reflected in Figure 1.

**Elementary and Secondary School Emergency Relief (ESSER) Fund**—$13.2 billion provided for state education agencies (SEAs) and local educational agencies (LEAs) to support continued learning for K-12 students whose educations have been disrupted by COVID-19.

**Higher Education Emergency Relief (HEER) Fund**—$14.0 billion provided for IHEs to address needs directly related to COVID-19, including transitioning courses to distance education and granting aid to students for educational costs such as food, housing, course materials, health care, and child care.

**Governor’s Emergency Education Relief (GEER) Fund**—$3.0 billion provided to state governors to ensure education continues for students of all ages impacted by the COVID-19 national emergency.

**Outlying Areas, Bureau of Indian Education (BIE), and Discretionary Grants**—$0.6 billion provided for outlying areas and discretionary grants to states with the highest COVID-19 burdens.
BALANCE SHEETS

The consolidated balance sheets present, as of a specific point in time (the end of the fiscal year), the Department’s total assets, total liabilities, and net position.

The Department’s assets totaled $1,309.4 billion as of September 30, 2020. As shown in Figure 2, the vast majority of the assets relate to credit program receivables, $1,171.0 billion, which comprised 89.4 percent of all assets. Direct Loans comprise the largest share of these receivables. All other assets totaled $138.4 billion, most of which was Fund Balance with Treasury.

The Department’s liabilities totaled $1,264.5 billion as of September 30, 2020. As shown in Figure 3, the vast majority of the Department’s liabilities are also associated with credit programs, primarily amounts borrowed from the U.S. Department of the Treasury (Treasury) to fund student loans. Debt associated with Direct Loans totaled $1,160.1 billion as of September 30, 2020.

Figure 4 shows the changes in the Direct Loan receivables components over the past five years. The principal amount has continued to grow as the Direct Loan program has originated all new federal loans since July 2010, when originations of new FFEL loans ended. However, the rate of increase in principal has slowed, as the Direct Loan program has disbursed decreased amounts of new loans each year since FY 2016 as a result of stagnant and in some cases declining enrollment, while accrued interest amounts have increased as more loans have moved into active repayment statuses. Even so, new loan disbursements continue to exceed overall loan principal repayments—student loan borrowers have many options to stretch out their repayment terms and reduce their monthly payments.

In accordance with the Federal Credit Reform Act of 1990, the Department’s financial statements report the value of direct loans (credit program receivables) at the net present value of their future cash flows, discounted at a fixed rate established based on Treasury securities. The difference between the recorded principal and interest balance and the net present value of the loans is referred to as the “allowance for subsidy,” which can be positive or negative.

Figure 2. Assets by Type

Figure 3. Liabilities by Type
the main cause being high participation in income-driven repayment (IDR) plans. As of FY 2017, the allowance for subsidy changed to a negative balance. In practical terms, this means that the present value of funds expected to be recovered is now less than the principal outstanding.

Participation in IDR plans has increased as (a) new plans have become available that are more advantageous to borrowers, (b) new plans have become available that expand the potential pool of borrowers, and (c) the Department has conducted targeted outreach to borrowers to make them aware of their potential eligibility for these plans.

In addition to the impact of the IDR plans, the negative subsidy allowance also increased in FY 2020 due to actions taken to defer student loans in response to COVID-1 (see discussion in the Analysis of Direct Loan Program Subsidy Expense section on page 16).

Table 2 shows the payment status of the Direct Loan principal and interest balances outstanding over the past five years. The Current Repayment category consists of loans that are being paid back on time, including the current portion of loans being repaid pursuant to IDR plans. The balances reported for “Current Repayment” and “Delinquent” are significantly lower than prior years, primarily due to the COVID-19 student loan deferrals that placed loans in forbearance and subsequently cured delinquencies.

Loans in the Delinquent category are past due anywhere from 31 to 360 days. Default/Bankruptcy/Other includes loans that are more than 360 days delinquent (default status); loans in a nondefaulted bankruptcy status; and loans in disability status. While technical default is 271 days delinquent, default is defined as 361 days delinquent for reporting purposes. The percentage of loans in default continues to grow, even as delinquencies and new defaults have declined, because defaulted loans can be difficult to collect or rehabilitate.

The FY 2020 delinquent balance is zero due to the ongoing deferral of all student loans through December 31, 2020.
Table 2. Payment Status of Direct Loan Principal and Interest Balance
(Dollars in Billions)

<table>
<thead>
<tr>
<th>Loan Status</th>
<th>Fiscal Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total No. of Direct Loan Recipients (in Millions)</td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td>31.5</td>
</tr>
<tr>
<td>2017</td>
<td>33.0</td>
</tr>
<tr>
<td>2018</td>
<td>34.2</td>
</tr>
<tr>
<td>2019</td>
<td>35.1</td>
</tr>
<tr>
<td>2020</td>
<td>35.9</td>
</tr>
<tr>
<td>Total Dollar Amount of Direct Loans Outstanding</td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td>953.6</td>
</tr>
<tr>
<td>2017</td>
<td>1,058.4</td>
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<tr>
<td>2018</td>
<td>1,155.7</td>
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<tr>
<td>2019</td>
<td>1,248.1</td>
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<tr>
<td>2020</td>
<td>1,316.9</td>
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<tr>
<td>Current Repayment</td>
<td></td>
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<tr>
<td>Percentage</td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td>42.6%</td>
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<tr>
<td>2017</td>
<td>44.2%</td>
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<td>2018</td>
<td>46.0%</td>
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<tr>
<td>2019</td>
<td>47.6%</td>
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<tr>
<td>2020</td>
<td>1.1%</td>
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<tr>
<td>In School, Grace Period, and Education Deferments</td>
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<tr>
<td>Percentage</td>
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<tr>
<td>2016</td>
<td>30.4%</td>
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<td>2017</td>
<td>27.6%</td>
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<td>2018</td>
<td>25.6%</td>
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<td>2019</td>
<td>23.6%</td>
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<td>2020</td>
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<td>Forbearance and Noneducation Deferments</td>
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<tr>
<td>Percentage</td>
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</tr>
<tr>
<td>2016</td>
<td>10.6%</td>
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<tr>
<td>2017</td>
<td>12.5%</td>
</tr>
<tr>
<td>2018</td>
<td>12.5%</td>
</tr>
<tr>
<td>2019</td>
<td>13.2%</td>
</tr>
<tr>
<td>2020</td>
<td>88.7%</td>
</tr>
<tr>
<td>Delinquent (Past Due 31-360 Days)</td>
<td></td>
</tr>
<tr>
<td>Percentage</td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td>71.9%</td>
</tr>
<tr>
<td>2017</td>
<td>79.7%</td>
</tr>
<tr>
<td>2018</td>
<td>92.5%</td>
</tr>
<tr>
<td>2019</td>
<td>90.8%</td>
</tr>
<tr>
<td>2020</td>
<td>0.0%</td>
</tr>
<tr>
<td>Default/ Bankruptcy/ Other*</td>
<td></td>
</tr>
<tr>
<td>Percentage</td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td>7.5%</td>
</tr>
<tr>
<td>2017</td>
<td>7.5%</td>
</tr>
<tr>
<td>2018</td>
<td>8.0%</td>
</tr>
<tr>
<td>2019</td>
<td>7.3%</td>
</tr>
<tr>
<td>2020</td>
<td>0.0%</td>
</tr>
</tbody>
</table>

Figure 5. Direct Loan Program Cumulative Financing Activity
(Dollars in Billions)

The Department borrows funds to disburse new loans and pay credit program outlays and related costs. The Department repays Treasury after consideration of cash position and the liability for future cash outflows. Figure 5 shows the Direct Loan program cumulative borrowing and repayment activity that resulted in the debt amount on the balance sheet. A diagram depicting the Direct Loan program financing process is displayed with related trend data as Figure 6 on page 14 of this report.
Figure 6. William D. Ford Federal Direct Loan Program: Following the Funding

Positive Subsidy
When estimated program cash outflows are expected to exceed inflows, the Department requests additional subsidy funding.

Negative Subsidy
When estimated program cash outflows are expected to be less than inflows, the Department returns surplus subsidy funds back to Treasury via negative subsidy transfers.

FEDERAL BORROWING
The Department borrows money from Treasury at interest rates established by OMB.

INTEREST EARNINGS
The Department earns interest from the Treasury on uninvested cash balances each year.

LOAN DISBURSEMENTS
The Department disburses loans to borrowers attending qualified institutions, at interest rates established through legislation.

PRINCIPAL DEBT REPAYMENTS & INTEREST PAYMENTS ON DEBT

Department of Treasury

Department of Education

Borrowers

Aggregate Program Cost Increases

Aggregate Program Cost Decreases

TREASURY FINANCING AND SUBSIDY COST OF DIRECT LOANS (Dollars in Billions)*

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
<th>2019</th>
<th>2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Borrowing</td>
<td>84.4</td>
<td>67.3</td>
<td>89.1</td>
<td>41.5</td>
<td>(32.0)</td>
</tr>
<tr>
<td>Borrowing from Treasury</td>
<td>147.0</td>
<td>160.5</td>
<td>155.3</td>
<td>137.6</td>
<td>116.9</td>
</tr>
<tr>
<td>Debt Repayments to Treasury</td>
<td>(62.6)</td>
<td>(93.2)</td>
<td>(66.2)</td>
<td>(96.1)</td>
<td>(148.9)</td>
</tr>
<tr>
<td>Interest Expense to Treasury</td>
<td>(30.5)</td>
<td>(31.3)</td>
<td>(32.3)</td>
<td>(33.8)</td>
<td>(34.7)</td>
</tr>
<tr>
<td>Interest Earned from Treasury</td>
<td>3.9</td>
<td>4.3</td>
<td>3.9</td>
<td>4.1</td>
<td>4.8</td>
</tr>
<tr>
<td>Cumulative Taxpayer Cost / (Savings)</td>
<td>(5.3)</td>
<td>16.8</td>
<td>40.7</td>
<td>124.4</td>
<td>216.4</td>
</tr>
<tr>
<td>Current Subsidy Expense (Revenue)</td>
<td>16.1</td>
<td>5.3</td>
<td>4.4</td>
<td>61.5</td>
<td>100.9</td>
</tr>
</tbody>
</table>

DIRECT LOAN PROGRAM CASH TRANSACTIONS WITH BORROWERS (Dollars in Billions)*

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
<th>2019</th>
<th>2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan Disbursements</td>
<td>140.5</td>
<td>142.5</td>
<td>134.1</td>
<td>130.7</td>
<td>117.4</td>
</tr>
<tr>
<td>Stafford Subsidized</td>
<td>23.8</td>
<td>23.4</td>
<td>20.3</td>
<td>20.0</td>
<td>19.1</td>
</tr>
<tr>
<td>Stafford Unsubsidized</td>
<td>52.3</td>
<td>51.4</td>
<td>49.0</td>
<td>48.1</td>
<td>46.1</td>
</tr>
<tr>
<td>PLUS</td>
<td>19.0</td>
<td>18.7</td>
<td>23.1</td>
<td>22.7</td>
<td>21.7</td>
</tr>
<tr>
<td>Consolidation¹</td>
<td>45.5</td>
<td>49.0</td>
<td>41.6</td>
<td>39.8</td>
<td>30.4</td>
</tr>
<tr>
<td>Loan Collections²</td>
<td>73.2</td>
<td>82.0</td>
<td>84.9</td>
<td>91.3</td>
<td>69.9</td>
</tr>
<tr>
<td>Principal</td>
<td>55.9</td>
<td>62.6</td>
<td>63.5</td>
<td>67.0</td>
<td>55.3</td>
</tr>
<tr>
<td>Interest</td>
<td>15.5</td>
<td>17.6</td>
<td>19.5</td>
<td>22.4</td>
<td>12.9</td>
</tr>
<tr>
<td>Fees</td>
<td>1.8</td>
<td>1.9</td>
<td>1.9</td>
<td>1.9</td>
<td>1.7</td>
</tr>
</tbody>
</table>

* Numbers may not add up due to rounding.

¹ Consolidation amounts stem from a number of loan programs, including most notably the FFEL program, in addition to Direct Loans.

² Loan collections include prepayments, including prepayments in full due to consolidation of underlying Direct Loans.
STATEMENTS OF NET COST

The consolidated statements of net cost report the Department’s components of the net cost of operations for a given fiscal year. Net cost of operations consists of the gross costs incurred less any exchange (i.e., earned) revenue from activities. Gross costs are composed of the cost of credit and grant programs, and operating costs. Exchange revenue is primarily interest earned on credit program loans. Figure 7 shows the Department’s gross costs and earned revenue over the past five years.

GROSS COSTS AND EXCHANGE REVENUE BY TYPE

As shown in Figure 8, the Department’s gross costs and earned revenue include three primary components:

- Credit program interest expense offset by credit program interest revenue and administrative fees as the result of subsidy amortization;

- Credit program subsidy expense (see Analysis of Direct Loan Program Subsidy Expense below); and

- Grant expenses (see Figure 10).

Figure 7. Gross Costs & Earned Revenue (Dollars in Billions)

Figure 8. Primary Components of Gross Costs and Earned Revenue (Dollars in Billions)
ANALYSIS OF DIRECT LOAN PROGRAM SUBSIDY EXPENSE

The Department’s gross costs can fluctuate significantly each year as a result of changes in the estimated subsidy expense. The increase in the Department’s gross costs from FY 2019 is primarily the result of an increase in the subsidy expense for Direct Loans in FY 2020, the primary components of which included year-end subsidy re-estimates and loan modifications.

Subsidy expense is an estimate of the present value cost of providing direct loans, but excludes the administrative costs of issuing and servicing the loans. The Department estimates subsidy expense using a set of econometric and financial models, as well as cash flow models.

The Department estimates subsidy costs annually for new loans disbursed in the current year; updates the previous cost estimates for outstanding loans disbursed in prior years (subsidy re-estimates); and updates previous cost estimates based on changes to terms of existing loans (subsidy modifications). Figure 9 shows three components of the Direct Loan program subsidy expense for the past five years.

Factors such as interest rates charged to the borrower, interest rates on Treasury debt, default rates, fees and other costs, and assumptions concerning borrowers’ selection of repayment plans impact the estimated cost calculation and determine whether the overall subsidy expense is positive or negative. Subsidy expense for new loans disbursed in the current year has been negative in recent years primarily because lending interest rates charged were greater than the historically low rates at which the Department borrowed from Treasury. In practical terms, a negative subsidy occurs when the interest and/or fees charged to the borrower are more than sufficient to cover the interest on Treasury borrowings and the costs of borrower default. Subsidy expense for new loans disbursed in the current year was positive in FY 2020 due to rising enrollment in IDR plans and a reduction in projected future income of borrowers in IDR plans.

The Direct Loan program subsidy re-estimate for FY 2020 totaled $56.1 billion. In addition to the major assumption updates described below, the re-estimate reflects several other assumption updates, including interest rates provided by OMB, loan volume, and contract collection costs.

- **IDR Model Changes (including Public Service Loan Forgiveness (PSLF)).** The Department completed a standard IDR data update to reflect the immediate prior cycle for defaults, prepayments and Death, Disability, and Bankruptcy (DDB). The DDB update includes adjustments for the Total Permanent Disability for Veterans regulation. In addition, an existing borrower income file was calibrated using an additional year of IDR application data through 2018. The additional year of borrower income data taken from IDR applications has been substantially lower than projected. As such, the Department reduced its projections of future borrower income by 35%, increasing costs associated with IDR. The Department also analyzed the actual PSLF approval rates and supplementary data. As a result of that analysis, the PSLF approval rate was adjusted downward for initial cohorts to better reflect the actual data. Trends indicate that there has been some improvement in PSLF approval rates over time as borrowers better understand the application process. PSLF estimates were revised to reflect the most recent borrower behavior and adjust the temporal element to ramp up PSLF forgiveness over time. The combined effect of these updates led to a net upward re-estimate of $35.5 billion.
**Repayment Plans.** The Department updated the data and made an adjustment to exclude special consolidation of FFEL loans in FY 2012 and FY 2013 from the model. These loans are modeled separately and were less likely to enroll in income dependent repayment plans than typical consolidation loans. The combined effect of these changes led to a net upward re-estimate of $6.5 billion.

**Default.** In addition to the adjustments for the *CARES Act*, the Department updated the data and incorporated actual unemployment rates from the Bureau of Labor Statistics through June 2020. The combined effect of these changes led to a net upward re-estimate of $1.8 billion.

**2019 Cohort Assumption Changes.** The technical re-estimate cannot reflect the impacts of certain assumption changes applicable to the current year loan cohort until the following fiscal year per OMB guidance. The current year’s re-estimate includes a net upward adjustment of $4.8 billion for these current year assumption changes attributable to the FY 2019 cohort.

**Interest on the Re-estimate.** Interest on re-estimates is the amount of interest that would have been earned or paid by each cohort on the subsidy re-estimate, if the re-estimated subsidy had been included as part of the original subsidy estimate. The interest on the re-estimate calculated on the overall subsidy re-estimate resulted in a net upward re-estimate of $5.9 billion.

**Interactive Effects.** The re-estimate includes a net upward re-estimate of $1.5 billion attributed to the interactive effects of the assumption changes described above. Each assumption described above is run independently. The interactive effect is a result of combining all assumptions together to calculate the final re-estimate.

The Direct Loan program modifications were primarily the result of student loan deferral actions provided by Congress and the Administration in response to COVID-19. The student loan deferrals increased the government’s cost of student loans and were recognized as loan modifications for FY 2020. These modifications included the following:

**CARES Act.** The *CARES Act* automatically suspended principal and interest payments and set interest rates to 0 percent on federally held student loans starting in March through September 30, 2020. The relief for borrowers resulted in an upward modification cost of $24.6 billion, with an additional $459 million for cancelled loans for students that did not complete the semester due to a qualifying emergency. There was a net positive $82 million modification adjustment transfer associated with this modification, bringing the total to $25.0 billion.

**Presidential Memorandum.** On August 8, 2020, the President signed a Presidential Memorandum that continued the temporary suspension of payments and the waiver of all interest on federally held student loans through December 31, 2020. The relief for borrowers resulted in an upward modification cost of $13.5 billion. There was a net negative $66 million modification adjustment transfer associated with this modification, bringing the total to $13.6 billion.

**Total and Permanent Disability.** The Department recorded an upward modification for costs associated with the regulatory action to provide proactive discharge (unless the borrower elects to reject the discharge) to borrowers for whom the Department of Veterans Affairs provides information showing the borrower has a total and permanent disability. These discharges resulted in an upward modification cost of $1.0 billion. There was a net negative $98 million modification adjustment transfer associated with this modification, bringing the total to $1.1 billion.

---

**GRANT EXPENSES**

**Figure 10. Grant Expenses by Program Areas**

<table>
<thead>
<tr>
<th>Program Area</th>
<th>FY 2020</th>
<th>FY 2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>CARES Act Grants</td>
<td>$11.2</td>
<td></td>
</tr>
<tr>
<td>Pell Grants</td>
<td></td>
<td>$25.9</td>
</tr>
<tr>
<td>Education for the Disadvantaged</td>
<td>$15.8</td>
<td>$16.3</td>
</tr>
<tr>
<td>Special Education</td>
<td>$12.7</td>
<td></td>
</tr>
<tr>
<td>All Other Grants</td>
<td>$18.9</td>
<td>$18.3</td>
</tr>
</tbody>
</table>

(Dollars in Billions)
As shown in Figure 10, overall grant expenses increased primarily as a result of the CARES Act—primarily the Education Stabilization Fund grants described on pages 76–77.

In addition to the CARES Act funded grants, the Department has more than 100 other grant and loan programs. The three largest of these grant program areas are:

- **Pell Grants**—provides need-based grants to students to promote access to postsecondary education. Grant amounts are dependent on: the student’s expected family contribution; the cost of attendance (as determined by the institution); the student’s enrollment status (full-time or part-time); and whether the student attends for a full academic year or less. Pell grants are the single largest source of grant aid for postsecondary education.

- **Education for the Disadvantaged**—primarily consists of grants that provide financial assistance through SEAs to LEAs and public schools with high numbers or percentages of poor children to help ensure that all children meet challenging state academic content and student academic achievement standards. Also provides funds to states to support educational services to children of migratory farmworkers and fishers, and to neglected or delinquent children and youth in State-run institutions, attending community day programs, and correctional facilities.

- **Special Education**—primarily consists of Individuals with Disabilities Education Act (IDEA) grants that provide funds by formula to states to assist them in providing a free appropriate public education in the least restrictive environment for children with disabilities ages 3 through 21 and assists states in providing early intervention services for infants and toddlers from birth through age two and their families. Also provides discretionary grants to IHEs and other nonprofit organizations to support research, demonstrations, technical assistance and dissemination, technology, personnel development and parent-training, and information centers.

In addition to student loans and grants, the Department offers other discretionary grants under a variety of authorizing legislation, with approximately 90 percent of non-student aid funds awarded by formula and 10 percent through competitive processes.

### STATEMENTS OF CHANGES IN NET POSITION

The consolidated statements of changes in net position report the beginning net position, the summary effect of transactions that affect net position during the fiscal year, and the ending net position. Net position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations include undelivered orders and unobligated balances for grant and administrative operations. Cumulative results of operations represent the net difference since inception between (1) expenses and (2) revenues and financing sources.

### STATEMENTS OF BUDGETARY RESOURCES

The combined statements of budgetary resources present information on how budgetary resources were made available and their status at the end of the fiscal year. Information in the statements is based on budgetary transactions as prescribed by OMB and Treasury.

Figure 11 shows the components of the Department’s budgetary resources which totaled $473.4 billion for the year ended September 30, 2020, increasing from $358.2 billion, or approximately 32.2 percent from the prior year. This increase was primarily due to increases in appropriations received totaling $126.5 billion, of which $73.2 billion was for direct and indirect appropriations for COVID-19 activity. An increase of $45.5 billion in appropriations received for executed re-estimates in FY 2020 versus FY 2019 also contributed to this overall increase (see the following outlay discussion).
New obligations incurred increased by $107.7 billion, or approximately 33.3 percent, due primarily to grants funded by the CARES Act and loan modifications for COVID-19 student loan deferrals.

The combined statements of budgetary resources also present the Department’s summary disbursement and collection amounts for which Table 3 provides additional detail.

| Table 3. Outlays, Distributed Offsetting Receipts, and Disbursements, Net  |
|--------------------------|-------|-------|
|                         | FY 2020 | FY 2019 |
| Outlays, Net            |        |        |
| Credit Programs         | $129.8 | $36.8  |
| Grants                  | 85.5   | 76.9   |
| Contractual Services    | 2.0    | 2.2    |
| Personnel Compensation and Benefits | 0.7 | 0.6 |
| Other                   | -      | 0.1    |
| Total Outlays, Net      | $218.0 | $116.6 |
| Distributed Offsetting Receipts |       |        |
| Negative Subsidies and Downward Reestimates of Subsidies | (12.3) | (12.1) |
| Repayment of Perkins Loans and Capital Contributions | (1.3) | (0.1) |
| Other                   | -      | (0.1)  |
| Total Distributed Offsetting Receipts | $ (13.6) | $ (12.3) |
| Disbursements, Net      |        |        |
| Direct Loan Program     |        |        |
| Gross Disbursements     | $158.2 | $175.5 |
|Offsetting Collections   | (188.1) | (128.7) |
| Total Direct Loan Program Disbursements, Net | (29.9) | 46.8 |
| FEEL Program            |        |        |
| Gross Disbursements     | 17.5   | 14.7   |
|Offsetting Collections   | (30.6) | (21.5) |
| Total FEEL Program Disbursements, Net | (13.1) | (6.8) |
| Other Loan Programs     |        |        |
| Gross Disbursements     | 0.5    | 0.3    |
|Offsetting Collections   | (0.4)  | (0.2)  |
| Total Other Loan Program Disbursements, Net | 0.1 | 0.1 |
| Total Disbursements, Net | $ (42.9) | $ 40.1 |

Outlays, net is comprised of gross outlays and offsetting collections in the Department’s budgetary funds. Outlays, net increased $101.4 billion (87.0 percent) due primarily to transfers from the Department’s credit program budgetary funds to its credit program non-budgetary financing funds for (1) increased executed re-estimates in FY 2020 versus FY 2019 ($45.5 billion), and (2) COVID-19 related loan modifications recognized in FY 2020 ($42.2 billion).

Disbursements, net is comprised of gross outlays and offsetting collections in the Department’s credit program non-budgetary financing funds. Disbursements, net decreased $83.0 billion, primarily due to the transfers to the Department’s credit program non-budgetary financing funds from its credit program budgetary funds for the aforementioned executed re-estimate and COVID-19 loan modifications.
MANAGEMENT ASSURANCES

The Secretary of the Department of Education’s Fiscal Year 2020 Statement of Assurance provided below is the final report produced by the Department’s annual assurance process.

STATEMENT OF ASSURANCE
FISCAL YEAR 2020
November 16, 2020

The Department of Education’s (the Department) management is responsible for managing risks and maintaining effective internal control to meet the objectives of the Federal Managers’ Financial Integrity Act of 1982 (FMFIA).

In accordance with Section 2 of FMFIA and Office of Management and Budget (OMB) Circular A-123, Management’s Responsibility for Enterprise Risk Management and Internal Control, management assessed risk and evaluated the effectiveness of the Department’s internal controls to support effective and efficient operations, reliable reporting, and compliance with applicable laws and regulations.

Section 4 of FMFIA and the Federal Financial Management Improvement Act of 1996 (FFMIA) require management to ensure the Department’s financial management systems provide reliable, consistent disclosure of financial data. Management evaluated the Department’s financial management systems for substantial compliance with FFMIA requirements. The Department also conducted a separate assessment of the effectiveness of its internal control over reporting with consideration of its Data Quality Plan in accordance with Appendix A of OMB Circular A-123.

With the exception of a material weakness in financial reporting reported in the Independent Auditors’ Report, the Department has not identified any material weaknesses in operations, reporting, or compliance with applicable laws and regulations.

Based on the results of the Department’s assessments described above, our system of internal controls provides the Department’s management with reasonable assurance that the objectives of Sections 2 and 4 of the FMFIA were achieved as of September 30, 2020.

Betsy DeVos

Betsy DeVos
INTRODUCTION

Strong risk management practices and internal control help the Department run its operations efficiently and effectively, report reliable information about its operations and financial position, and comply with applicable laws and regulations. The FMFIA requires federal agencies to establish internal controls that provide reasonable assurance that agency objectives will be achieved. OMB Circular A-123, Management’s Responsibility for Enterprise Risk Management (ERM) and Internal Control implements FMFIA and defines management’s responsibilities for ERM and internal control. The Circular provides guidance to federal managers to improve accountability and effectiveness of federal programs as well as mission support operations through implementation of ERM practices and by establishing, maintaining, and assessing internal control effectiveness. The guidance requires federal agencies to provide reasonable assurance that it has met the three objectives of internal control:

- **Operations**—Effectiveness and efficiency of operations.
- **Reporting**—Reliability of reporting for internal and external use.
- **Compliance**—Compliance with applicable laws and regulations.

This section describes the Department’s internal control framework, offers an analysis of the effectiveness of its internal controls, and explains assurances provided by the Department’s leadership that internal controls were in place and working as intended during FY 2020 to meet the three objectives.

**Internal Control Framework**

The Department’s internal control framework helps to ensure that the Department achieves its strategic goals and objectives related to delivering education services effectively and efficiently, complies with applicable laws and regulations, and prepares accurate reports. The Department maintains a comprehensive internal control framework and assurance process as depicted in the following diagram.

![Diagram of Department of Education Internal Control Framework](image)

- **LEGISLATIVE REQUIREMENTS AND GUIDANCE**
- **FEDERAL STUDENT AID METHODOLOGY**
  - Plan
  - Document
  - Assess
  - Report
- **DEPARTMENT METHODOLOGY**
  - Plan
  - Document
  - Assess
  - Report
- **OUTPUTS**
  - FSA Annual Report
  - Congressional Reporting
  - FMFIA Assurance Letters
  - Corrective Action Plans
  - Department AFR
- **OUTCOMES**
  - BETTER INTERNAL CONTROL SYSTEM
    - Effective & efficient operations
    - Reliable financial and operational reporting
    - Compliance with applicable laws and regulations
  - REDUCED RISK
    - Safeguarding of assets
    - Protecting Department reputation
    - Proactive risk mitigation

Governance—Department Senior Management Council
The Department continues to focus on streamlining and coordinating internal control activities to ensure efficiency of operations, recognizing the connection points across areas, and enabling transparency of information across the Department. This framework enables increased visibility across compliance processes to allow for greater oversight and more informed monitoring of activities related to internal controls and risk management by all offices and governance bodies, including the Department’s Senior Management Council (SMC). This framework also allows for the Department to obtain the outcomes of a better control system and a reduced risk landscape. Furthermore, this streamlined approach helps the Department provide reasonable assurance to internal and external stakeholders that the data produced by the Department is complete, accurate, and reliable, that internal controls are in place and working as intended, and that operations are efficient and effective.

**ANALYSIS OF CONTROLS**

Overall, the Department relies on annual assurances provided by the heads of its principal offices, supported by risk-based internal control evaluations and testing as well as annual internal control training for all employees, to provide reasonable, but not absolute, assurance that its internal controls are well designed, in place, and working as intended. The Department’s annual assurance process conforms to the requirements contained in the revised U.S. Government Accountability Office (GAO) publication, *Standards for Internal Control in the Federal Government* (commonly referred to as the “Green Book”) and OMB Circular A-123, *Management’s Responsibility for Enterprise Risk Management and Internal Control*.

In FY 2020, the Department identified no material weaknesses related to effective, efficient program operations and no areas of noncompliance with laws and regulations other than those noted in the Analysis of Legal Compliance section below. The Department acknowledges that it has areas of control that need further strengthening, such as those identified elsewhere in this report, as well as the major challenges identified by the Department’s OIG in its FY 2021 Management Challenges report. As an example, data quality and reporting are a challenge identified by OIG. The Department, its grantees, and its subrecipients must have effective controls to ensure that reported data are accurate and complete. The Department relies on program data to evaluate program performance and inform management decisions. The establishment of a Data Quality Plan integrated into testing of controls is helping to address this challenge identified by the OIG.

In accordance with OMB Circular A-123, the Department also conducted a separate assessment of the effectiveness of the Department’s internal control over reporting and compliance with key financial management laws and regulations, as described below.

**Internal Control over Reporting**

The Department maintains processes and procedures to identify, document, and assess internal control over reporting. Key activities include:

- Maintaining process documentation for the Department’s significant business processes and subprocesses.
- Maintaining an extensive library of key financial, operations, and Information Technology (IT) controls.
- Providing technical assistance to principal offices to help them understand and monitor key controls.
- Refining the Data Quality Plan to improve reporting controls and data quality.
- Implementing a risk-based control testing strategy.
- Developing corrective action plans when internal control deficiencies are found and tracking progress against those plans.

In FY 2020, the Department tested 86 key financial controls for both grants and non-grants areas. The internal controls assessment detected some control deficiencies, but none that would rise to the level of material weakness. Corrective actions have been initiated for the deficiencies identified. In addition, numerous recommendations have been provided to process owners to strengthen internal controls in their processes, such as verifying immaterial differences, obtaining electronic signatures, and updating policies and procedures.

Further, operational internal controls have been formally aligned with the agency’s overall ERM strategy and assessed accordingly. No control deficiencies have been reported for FY 2020 related to this assessment.
ANALYSIS OF FINANCIAL MANAGEMENT SYSTEMS

The Federal Financial Management Improvement Act of 1996 (FFMIA) requires management to ensure that the Department's financial management systems consistently provide reliable data that comply with federal financial management system requirements, applicable federal accounting standards, and the U.S. Standard General Ledger at the transaction level. Appendix D to OMB Circular A-123, Compliance with the Federal Financial Management Improvement Act of 1996, and OMB Circular A-130, Managing Federal Information as a Strategic Resource, provide specific guidance to agency managers when assessing conformance to FFMIA requirements.

The Department's vision for its financial management systems is to provide objective financial information to stakeholders to support data-driven decision-making, promote sound financial management, and enhance financial reporting and compliance activities. The Department's core financial applications are together under common management control as part of the Education Central Automated Processing System (EDCAPS). EDCAPS is a suite of financial applications (subsystems), including commercial off-the-shelf, custom code, and interfaces that encompass the Department's core financial management processes. Specifically, EDCAPS provides the following functions:
- General ledger—Preparation of financial statements and reconciliation of general ledger balances with subsystems maintained in program areas and Treasury.
- Funds management—Budget formulation, budget execution, and funds control.
- Grants pre- and post-award processing, including grant payment processing.
- Contract pre- and post-award processing.
- Receivable management.
- Cost management.
- Recipient management.
- Administrative processes (e.g., purchasing, travel, and miscellaneous payments).

EDCAPS is composed of four main integrated components:
- Contracts and Purchasing Support System (CPSS).
- Grants Management System (G5).
- E2 Travel System.

Across all its components, EDCAPS is serving approximately 2,800 Departmental internal users in Washington, D.C. and 10 regional offices throughout the United States and territories. EDCAPS is serving approximately 40,500 external users, mostly users of the G5. In FY 2020, the Department conducted an annual risk assessment of EDCAPS and tested 82 IT security controls out of a baseline of 630 IT security controls. No significant deficiencies or material weaknesses were identified.

The Department designated the FMSS as a mission-critical system that provides core financial management services and focused its system strategy on the following areas during FY 2020:
- Managing and implementing cross-validation rules throughout the fiscal year to prevent invalid accounting transactions from being processed.
- Transmitting the Department's spending data related to contracts, grants, loans, and other financial assistance awards for the USA Spending.gov initiative as part of the Federal Funding Accountability and Transparency Act of 2006 (FFATA) and Digital Accountability and Transparency Act of 2014 (DATA Act).
- Transmitting the entire Department's payments through the Department of Treasury Secure Payment System.

The FMSS Oracle E-Business Suite application is behind the Department firewall and not external-facing. FMSS includes the following interfaces to multiple applications which are either not part of the Oracle suite of applications in the Enterprise Resource Plan or are outside the financial management segment:
- Hyperion Budget Planning module—currently only the license fees are included in FMSS investment.
- ED Facilities Loan System (Nortridge)—currently only the license fees are included in FMSS investment.
- The Invoice Processing Platform (IPP).
- FSA-Financial Management System financial data.
MANAGEMENT’S DISCUSSION AND ANALYSIS

- Lockbox.
- Department of the Treasury systems.
- Department of Interior systems.

The Department’s financial management systems are designed to support effective internal control and produce accurate, reliable, and timely financial data and information. Based on self-assessments, system-level general controls tests, and the results of internal and external audits, the Department has not identified any material weaknesses in controls over these systems. The Department has also determined that its financial management systems substantially comply with FFMIA requirements. However, as noted below in the Analysis of Legal Compliance section, the Department continues to address issues and improve its controls over systems.

ANALYSIS OF LEGAL COMPLIANCE

The Department is committed to maintaining compliance with applicable laws and regulations. Below are some examples:

**Debt Collection Improvement Act of 1996**

The Debt Collection Improvement Act of 1996 (DCIA), Pub. L. 104-134, 110 Stat. 1321-358, was enacted into law as part of the Omnibus Consolidated Rescissions and Appropriations Act of 1996, Pub. L. 104-134, 110 Stat. 1321. The primary purpose of the DCIA is to increase the collection of nontax debts owed to the federal government. Additionally, the DATA Act, Pub. L. 113-101, 128 Stat. 1146, amended Section 3716(c)(6) of the DCIA to require referral of delinquent debt to Treasury’s Offset Program within 120 days.

Due to unique program requirements of the Higher Education Act of 1965 (HEA), the Department requested guidance from the Chief Counsel of the Department of the Treasury’s Bureau of the Fiscal Service to interpret the impact of this revised DATA Act’s delinquent debt referral requirement on Title IV debt. In July 2015, the Fiscal Service’s Chief Counsel determined compliance for Title IV debt requires that the Title IV debt be: 1) in technical default (i.e., 271 days delinquent per Title IV aging) and 2) a receivable of the federal government. Therefore, the DCIA Treasury Offset Program (TOP) referral requirement for Title IV debt owned by FSA at the time of delinquency is 271 days delinquent, and the requirement for debt acquired via a FFEL guarantee default claim or default Perkins Loan assignment is 120 days delinquent (per DCIA aging, which begins upon acceptance of a defaulted debt). As of September 30, 2020, the Department and FSA were not in compliance with the DCIA TOP referral requirement for Title IV debt as interpreted by Treasury because FSA had not yet revised its loan servicing systems, procedures, and internal processes in response to this interpretation. During FY 2020, FSA continued to implement changes to its default loan servicing systems, procedures, and internal business process for referring eligible debts to the Treasury Offset Program sooner. FSA will build DCIA requirements into the NextGen FSA servicing platform. This area of noncompliance is noted in the independent auditors’ report, Exhibit C.

This determination of noncompliance with the DCIA does not represent a material weakness in the Department’s internal controls.

**Federal Information Security Modernization Act of 2014**

The Federal Information Security Modernization Act of 2014 (FISMA) requires federal agencies to develop, document, and implement an agency-wide program to provide security for the information and information systems that support the operations and assets of the agency and ensure the confidentiality, integrity, and availability of system-related information.

The Department’s and FSA’s information security programs completed several significant activities in FY 2020 to improve cybersecurity capabilities and functions, some of which included:

- Office of the Chief Information Officer (OCIO) established the Department’s cybersecurity risk tolerance and appetite which integrates with the Department’s overall Enterprise Risk Management (ERM) program. Key Performance Indicators (KPIs) and Key Risk Indicators (KRIs) have been established to support tracking and reporting progress made towards the Department’s OCIO ERM target profile.

- OCIO publishes monthly Department Cyber Security Framework (CSF) Risk Scorecards as part of the Department’s Information Security Continuous Monitoring efforts to identify cybersecurity risks, issues, and opportunities for improvements in our cybersecurity protections. The Department CSF Risk Scorecard provides a detailed analysis tool for Authorizing Officials, Information System Owners, and Information System Security Officers to prioritize and mitigate risks to the Department’s information systems.
In FY 2020, the CSF Risk Scorecard was enhanced to include risk scoring and reporting for privacy controls as well as additional reporting views for the recently released security authorization documentation and incident response plan testing status scoring risk factors. These enhancements further enable the Department’s stakeholders to effectively manage system level security and privacy risks while ensuring authorization documentation and processes are continuously monitored for effectiveness. CSF Risk Scorecard visualizations were also expanded upon to include specific views for FSA servicers and pertinent investment review board reporting to streamline communication of risk to appropriate stakeholders. These recent CSF Risk Scorecard enhancements have provided the Department’s executives with new capabilities to identify trends, patterns, and opportunities for improvement across the organization. Additionally, the scorecard is now updated daily for a timely view of risk.

- OCIO disseminated monthly ‘State of IT’ principal office-level reports for continued outreach to executive stakeholders to take the appropriate actions as necessary based on cyber data, trends, metrics, and key insights specific to their organization offered through cybersecurity data visualizations.

- The average time to close a Plan of Action and Milestones (POA&M) was reduced from 167 days in 2019 to 47 days in 2020. The number of accepted POA&Ms also dropped from 53 to 29 during the same time period. At the closing of FY 2020, the Department achieved a 68 percent net reduction in past due POA&Ms since starting the reporting period on October 1, 2019. These positive metrics are direct indicators of the progress achieved in maturing risk management capabilities and reduction capabilities.

- OCIO authorized the FedRAMP compliant Splunk Cloud as the Department’s cybersecurity data lake and began initial configuration for ingestion of Continuous Diagnostics and Mitigation and continuous monitoring data. Currently, ten data sources have been identified for initial operational capabilities. These enhancements allow for better cyber risk visibility and monitoring of Department information systems to enable prompt data driven decisions.

- To mitigate operational impacts of the COVID-19 pandemic, OCIO delivered Personal Identity Verification authentication (PIV-A) as alternative multi-factor authentication solution providing continuity of critical business functions. Additionally, OCIO identified, analyzed, and recommended a cloud-based solution to provide rapid expansion of the Department’s VPN capacity supporting the workforce during COVID-19 telework phase. OCIO also performed outreach for increased vigilance during the COVID-19 telework phase. OCIO implemented proactive security monitoring of PIV-A VPN connections by utilizing new data-lake-based Security Information and Event Management (SIEM) software solution. Department employees have also been educated regarding increased phishing and other cybercriminal scams targeting a largely at-home workforce (stimulus checks, spoofing legitimate Government Health organizations, etc.).

- OCIO completed the enhancement of the Department’s Network Access Control (NAC) capability for non-government furnished equipment (GFE) within the Department’s new IT environment that is superior to capabilities that existed prior to the FY 2019 transition. This provides a foundation to further implement the Department’s zero-trust architecture.

- To bolster the Department’s email security, OCIO fully deployed and monitored the Office 365 (O365) email Data Loss Prevention (DLP) capability. This capability enhances the Department’s overall DLP capabilities and works in concert with network and desktop DLP solutions. OCIO also deployed DLP desktop agents on nearly 100 percent of Department endpoint devices to further enhance the identification of personally identifiable information such as Social Security and credit card numbers. In FY 2020, the Department’s DLP solution identified and blocked 9,809 emails which prevented potential sensitive personally identifiable information security incidents.

- Through enhanced reporting of email and web security posture, the Department was able to significantly increase U.S. Department of Homeland Security (DHS) Binding Operational Directive (BOD) 18-01 compliance from 54 percent to 100 percent for email security and 87 percent to 96 percent for Hypertext Transfer Protocol Secure (HTTPS) tracking. Additionally, there were no overdue critical or high vulnerabilities in FY 2020 for ED’s public facing assets reported in accordance with DHS BOD 19-02 Cyber Hygiene.
Cybersecurity and personnel security requirements were incorporated into the Department’s acquisition regulations in December 2019. The Office of Acquisition Management issued Acquisition Alert 2020-01, “Education Acquisition Regulation Class Deviation: Cyber and Personnel Security Requirements for Contractors”. This deviation ensures active contracts, solicitations, and future contracts communicate the Department’s cybersecurity and personnel security requirements to contractors and prospective contractors.

The Department deployed a “Report Phishing” button on March 25, 2020, to all Department email clients, allowing users to directly report suspicious emails to ED’s Security Operations Center (EDSOC) with a single click of a button. Prior to deployment, the average reporting rate for simulated exercises in FY 2019 was 15.21 percent (the highest reporting rate was 27.82 percent in March 2019). A phishing exercise conducted in the third quarter of FY 2020 resulted in a 41 percent reporting rate, with 91 percent of those who reported using the new “Report Phishing” button. The highest reporting rate noted in FY 2020 was 52.5 percent in August 2020 in response to an exercise which appeared to contain an attachment. This was the highest reporting rate since the launch of the phishing program in FY 2014. The Department also improved its overall response time in reporting. During FY 2018 and FY 2019 exercises, the first report from an end user was within an average of two minutes of the exercise launch. In FY 2020, the first report was received within an average of one minute of the exercise launch. In the event the email was an actual attack, early notification would enable the Department to block the internet addresses or domains associated with the email and reduce the potential impact and risk.

OCIO continued conducting quarterly Department-level system-tailored Incident Response and Contingency Plan testing tabletop exercises virtually, which focused on system contingency planning in the event of a cyber incident and how the Department would respond to such an incident. As of July 2020, 100 percent of the Department’s FISMA reportable systems had a valid contingency plan test. Feedback reports were provided to system stakeholders on weaknesses and opportunities for improvement to their contingency plans:

- Quarterly Risk Management Assessment score.
- Department Cyber Risk score.
- Previous year IG FISMA maturity score.
- DHS Cyber Hygiene Scorecard.

OCIO continued supporting the Scholarship for Service (SFS) program which is managed by the National Science Foundation in collaboration with the U.S. Office of Personnel Management (OPM) and DHS. This initiative reflects the critical need for IT professionals, industrial control system security professionals, and security managers in federal, state, local, and tribal governments. Upon graduation, scholarship recipients are required to work for a federal, state, local, or tribal government organization in a position related to cybersecurity. The Department spoke to students from SFS about the Department’s internship and upcoming employment opportunities. Over 100 students stopped by to learn about the Department’s cybersecurity initiatives and how their interests, knowledge, skills, and abilities aligned with future employment opportunities. OCIO continued to support the SFS program during COVID-19 by virtually onboarding a student internship team of eight students who performed a gap analysis, provided recommendations, and aided with next steps for adopting a Zero Trust Architecture environment at the Department.

OCIO removed and blocked the Zoom video teleconferencing software across the enterprise after increased reports of security vulnerabilities. After thorough review of the risks associated with Zoom to Department users, updated guidance and notifications were communicated, allowing the use of Zoom for external hosted meetings with the understanding that there was no expectation of privacy, and meeting contents could be made public.

OCIO nominated Subject Matter Experts (SMEs) to support the DHS Supply Chain Risk Management initiative, C-SCRM Cybersecurity Standards Innovation Group (CyberSIG). The SMEs contribute as key members of the CyberSIG under the sponsorship of the General Services Administration and OMB. The CyberSIG provides input into
OCIO completed an engagement with the National Institute of Standards and Technology’s (NIST) Security and Privacy Implementation Collaboration Tiger Team to integrate cybersecurity and privacy more effectively across government and to promote collaborative working relationships between cybersecurity and privacy, regardless of organizational structure/reporting. As a result of this engagement, NIST determined they will not include the collaboration index in revision 5 but will instead develop a template of the index as a supplemental resource for individualized agency use.

- OCIO established initial operating capabilities in support of standing-up the Department’s Information and Communications Technology SCRM program. An inter-agency agreement with the Department of Energy was established to use their operationalized enterprise SCRM program to help identify and reduce potential risks associated with third party vendor relationships. Through this shared service, the Department will receive vendor-specific risk assessment services for our information systems and our vendors.

- OCIO established initial operating capabilities that will be used for C-SCRM government wide shared services.

- OCIO completed an engagement with the National Institute of Standards and Technology’s (NIST) Security and Privacy Implementation Collaboration Tiger Team to integrate cybersecurity and privacy more effectively across government and to promote collaborative working relationships between cybersecurity and privacy, regardless of organizational structure/reporting. As a result of this engagement, NIST determined they will not include the collaboration index in revision 5 but will instead develop a template of the index as a supplemental resource for individualized agency use.
This section summarizes information pertinent to the Department’s future progress and success.

**ENTERPRISE RISK MANAGEMENT**

The Department’s Enterprise Risk Management (ERM) program supports agency-wide efforts to maximize the Department’s value to students and taxpayers through achievement of strategic goals and objectives. The Department’s ERM program strategically focuses on the complete spectrum of the organization’s significant risks and the combined impact of those risks as an interrelated portfolio rather than simply addressing risks within silos. This coordinated approach leverages data and analytical solutions to identify, measure, and assess challenges related to mission delivery and resource management. Through ERM, the Department seeks to embed a systematic and deliberate view of risk into key management practices, ultimately yielding more effective performance and operational outcomes. The Department’s implementation of ERM includes three critical strategies that are more fully described under Strategic Objective 4.2, **Identify, assess, monitor and manage enterprise risks**:

1. Creating a risk-aware culture that includes transparent discussions of risks.

2. Implementing an ERM framework and capability that leverages existing risk management activities and governance bodies.

3. Managing risks in a more coordinated and strategic manner.

In FY 2020, the Department took significant steps to further develop the ERM program by establishing the Office of Enterprise Data Analytics and Risk Management (OEDARM), within the Office of Finance and Operations (OFO), to direct the agency’s overall ERM strategy and formally align ERM and internal controls processes. OEDARM leadership established a formal Enterprise Risk Management Working Group (ERMWG) with senior representation across the agency to further solidify the Department’s ERM governance structure. The ERMWG helped to conduct coordinated risk assessments and incorporated the risks highlighted or exacerbated by the COVID-19 pandemic into short- and long-term risk planning. OEDARM leveraged partnerships with agency leaders to identify, measure, and assess challenges related to mission delivery and develop coordinated, actionable response plans.

OEDARM leadership actively sought to enhance strategic partnerships with ERM colleagues across the government as well as with Department's own Office of Inspector General. To better understand how the Department’s ERM program has evolved over time, the Department enrolled in the Office of Management and Budget’s Pilot to validate the Federal ERM Maturity Model V1.0, a pilot that will extend through FY 2021. Through the pilot, the Department seeks to 1) test, assess, and validate sections or components of the Model for its iterative refinement; and 2) assess the maturity of the Department’s own ERM program. Evaluation will focus on an assessment of the Model’s operational viability and the influence of the Model on the Department’s risk-informed culture—including executive engagement and resourcing processes—with a goal of identifying potential improvements to the Model.

Throughout FY 2021, the Department plans to further integrate ERM with key management processes to ensure risk indicators and considerations inform budget formulation, strategic planning, and performance management. OEDARM seeks to support a culture of continuous improvement within the Department—where data and awareness of enterprise risk are used to objectively inform strategic and operational decisions and optimize agency performance. To that end, in FY 2021, OEDARM plans to develop and implement a comprehensive ERM training program for all levels of the organization as well as to enhance digital tools for collecting, analyzing, and reporting risk data to promote transparency and accountability across the Department. In light of the current COVID-19 pandemic, the Department has intentionally shifted to an even more comprehensive, strategic approach to risk management—one that seamlessly considers national health emergencies or other significant crises that could adversely impact continuity of operations.
DIRECT LOAN PROGRAM
The Department’s largest program, the William D. Ford Federal Direct Loan (Direct Loan) program, provides students and their families with funds to help pay for their postsecondary education costs. The following describes (1) the steps the Department has taken to help make student debt more manageable and (2) the risks inherent in estimating the cost of the program.

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

Traditionally, federal student loans had fixed-payment 10-year repayment schedules, making it difficult for borrowers to begin repaying at the start of their career when their salaries are low. The recent expansion of income-driven repayment (IDR) plans allows students the opportunity for greater financial flexibility as it pertains to their monthly repayment. For more details on these plans, visit FSA’s How to Repay Your Loans Portal.

Recent trends in student loan repayment data show that:

- Nearly 70 percent of the Direct Loan portfolio is in administrative forbearance, the suspended payment status provided to students through the CARES Act.

- As of June 2020, nearly 8.2 million Direct Loan recipients were enrolled in IDR plans, representing a 7 percent increase from June 2019 and a 16 percent increase from June 2018. Overall, more than 50 percent of Direct Loan dollars and 32 percent of borrowers in repayment are enrolled in an IDR plan.

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

- Continue conducting outreach efforts to inform student loan borrowers of their repayment options before the emergency loan relief measures expire on December 31, 2020.

- Work to improve customer service and student aid systems and processes by implementing FSA’s Next Generation Federal Student Aid (Next Gen FSA), see page 33.

Continue to support the development of additional tools, such as the College Scorecard and Financial Aid Shopping Sheet, to increase transparency around higher education costs and outcomes that may help students and families make informed decisions before college enrollment.

Managing Risks and Uncertainty Facing the Direct Loan Program’s Cost Estimates
Direct Loan program costs are estimated consistent with the requirements of the Federal Credit Reform Act of 1990. Under the Act, the future disbursements and collections associated with a cohort of loans are estimated for the entire life of the loan, up to 40 years in this case. The actual performance of a loan cohort tends to deviate from the estimated performance during that time, which is not unexpected given the inherent uncertainty involved in developing estimates. There are four types of inherent risk, described below, that make estimating lifetime program costs a difficult task.

Legislative, Regulatory, and Policy Risk
There are inherent risks to estimating future lifetime disbursements and collections for a cohort stemming from legislative, regulatory, or administrative actions. For instance, the cost structure of the Direct Loan program may be significantly altered. In addition, the effects on financial modeling and estimation associated with recent legislative, regulatory, and policy action is difficult to interpret given the lack of actual trend data availability. Some examples of current risks include the following:

CARES Act and Presidential Memorandum (“Memorandum on Continued Student Loan Payment Relief During the COVID-19 Pandemic”):

The CARES Act provided emergency relief measures in the Direct Loan program, including suspending loan payments, halting collections on defaulted loans, and setting interest rates to 0 percent through September 30, 2020. On August 8, 2020, the President directed the Secretary to continue these measures through December 31, 2020. These actions have largely insulated federal student loan performance from economic disruption caused by the coronavirus pandemic, while at the same time reducing the amount of loan repayments being remitted to the Department of Education. As the pandemic is ongoing, there is great uncertainty regarding cost estimates as future legislative and administrative actions could extend these emergency relief measures past December 31, 2020.

Income-Driven Repayment Plans: Without consideration of impacts from the pandemic, IDR plans

tend to be more costly to the government than non-IDR plans. For the 2020 loan cohort, it is estimated that the government will recover 40 percent less for loans in IDR plans as compared to loans in standard plans. It is important to be careful in making such comparisons, however, as the underlying characteristics of borrowers (and the corresponding behavioral dynamics driving selection of plans) also impact the overall cost of loans under each plan. In general, the proliferation of IDR plans has made IDR terms more generous and made the plans available to a greater number of borrowers; however, these plans are traditionally more costly to the government. Also, having more repayment plan options complicates repayment plan selection, since the tradeoff decisions when selecting the plans vary by borrower and may not always be entirely clear. Selected comparisons between projected originations and borrower repayments under the different IDR plans are available on the Department's website. Future commitment to market and increased participation in these plans are areas of uncertainty. Future legislative and regulatory activity could also affect the underlying cost of IDR plans.

Public Service Loan Forgiveness: Enacted in 2007, the Public Service Loan Forgiveness (PSLF) program allows a Direct student loan borrower to have the balance of their Direct student loans forgiven after having made 120 qualifying monthly payments under a qualifying repayment plan, while working full time for a qualifying public service employer (such as government or certain types of nonprofit organizations). In general, forgiveness provided via PSLF raises the cost of the Direct Loan program; however, there is still uncertainty as to how many borrowers will take advantage of the program. Much of this uncertainty arises because borrowers are not required to apply for the program or provide any supporting documentation on their employment until after having made the 120 qualifying monthly payments, and data on actual PSLF forgiveness remains rather limited, as borrowers first became eligible in FY 2018.

Data on approved PSLF applications first became available in FY 2018 since borrowers first became eligible for PSLF loan forgiveness starting October 1, 2017, after having made 120 qualifying payments. As of September 30, 2020, the total number of borrowers who received forgiveness totaled 3,469. The value of this forgiveness totaled $260.49 million. Despite the relatively modest numbers of approved applications to date, the number of borrowers who have certified their employment in a public service organization continues to increase. As of September 30, 2020, the number of borrowers with certified employment totaled 1,357,699. The low number of approved PSLF applications in relation to employment certifications may be partially due to the complicated nature of the program, in particular the determination of what constitutes a qualifying payment. In addition, many borrowers who file employment certification forms early in their careers may also move into private sector employment before completing the 10 years of qualifying payments and thus may (a) never apply for forgiveness or (b) apply for forgiveness much later after returning to public service work. The Consolidated Appropriations Act, FY 2018, and the Department of Education Appropriations Act, FY 2019, each provided $350 million toward Temporary Expanded Public Service Loan Forgiveness (TEPSLF) for borrowers who met eligibility for public service employment but were not enrolled in a qualified repayment plan. The Consolidated Appropriations Act, FY 2020, provided $50 million for TEPSLF. Future congressional action that may affect eligibility for PSLF continues to be an area of uncertainty. Lastly, although the Department continues to remain informed on and manage the risk associated with estimating participation in this program, uncertainty remains about further borrower outreach to boost participation in the PSLF program.

Estimation Risk

Actual student loan outcomes may deviate from estimated student loan outcomes, which is not unexpected given the long projection window of up to 40 years. The Direct Loan program is subject to a significantly large number of borrower-level events and future economic factors that heavily impact the ultimate cost of student loans. For example, assumptions that need to be estimated for loans originating in FY 2020 include how long students will remain in school; what repayment plan will be chosen; whether the loan will be consolidated; whether the borrower will die, become disabled, bankrupt, or have another claim for discharge or forgiveness (closed school loan discharge, borrower defense to repayment, etc.); whether the loan will go into deferment or forbearance; whether the loan will go into default and, if so, what collections will be received on the defaulted loan; and, if the loan is in an IDR plan, what the borrower’s employment (public sector or not) and income and family status will be over the next 25 years. These projections are generally made based on historical data about borrower characteristics and behavior, which are more difficult to estimate during times of unprecedented
uncertainty facing students and borrowers in repayment plans today. Lastly, the Direct student loan portfolio has grown from approximately $356 billion in FY 2011 to more than $1.2 trillion as of the end of FY 2020. This growth naturally results in larger re-estimates, since a re-estimate worth 1 percent of the portfolio today would be more than three times as large as a similar re-estimate in FY 2011.

**Macroeconomic Risk**

The ultimate amount, timing, and total value of future borrower repayments under the Direct Loan program are heavily affected by certain economic factors, especially since the introduction of IDR plans.

In 2020, the coronavirus pandemic caused widespread disruption to the American economy. The emergency relief measures provided by Congress and the President resulted in flexibilities for federal student loan borrowers, preventing spikes in delinquency and default rates. Involuntary loan collections from wage garnishment, tax refund reductions, and reductions of federal benefits such as Social Security are also suspended. However, the ultimate impact of the pandemic on long-term Direct Loan program costs is subject to significant uncertainty and will depend on, among other things, short and long-term unemployment, economic growth trends, and potential structural changes in the overall economy and job markets. Some types of macroeconomic risk are inherent to student loan cost estimation, and the Department analyzes them regularly—though some of these risks have been exacerbated by the unprecedented worldwide pandemic. New risks have also developed due to the conditions surrounding the pandemic. Specific examples of macroeconomic risk include:

**Economic Assumptions:** As part of its technical re-estimate process for the financial statement re-estimates, the Department updates economic assumptions used to calculate forecasted borrower cash flows. The Department obtains the information used to update economic assumptions from the OMB. OMB typically provides an economic assumption package for Mid-Session Review (MSR) which updates the economic assumptions used for the President’s budget in November of the previous year. The Department historically has used the MSR assumptions for calculation of financial statement re-estimates.

OMB did not release a MSR economic assumptions package in FY 2020, and no official guidance was issued to use alternative assumptions. Consequently, the Department explored the possibility of using economic factors from other sources, including, but not limited to, the Congressional Budget Office (CBO). Ultimately, the Department made the decision after extensive consultations with Education leadership and OMB to calculate the FY 2020 financial statement re-estimate using the President’s Budget 2021 assumptions (OMB assumptions). Factors contributing to this decision include the fact that any available economic projections have a high degree of uncertainty due to the uniqueness of the potential economic conditions caused by the pandemic. In addition, there is little historical data comparable to the current crisis that can be used to extrapolate and adjust student loan assumptions. Finally, current legislation and the presidential memorandum (i.e., the CARES Act) provided temporary relief to student loan borrowers through December 31, 2020; as a result, there is no meaningful data on the impact of current economic conditions on student loan performance. Alternatively, the Department conducted targeted sensitivity analysis to address potential economic impacts of the pandemic.

The Department conducts sensitivity analyses as one way to assess the degree of uncertainty around the economic assumptions. In the analysis reported here, the Department replaced the most important inputs from the President’s Budget 2021 economic assumptions used in the models with the numbers from CBO’s July 2020 economic package. The following examples show the projections of cohorts 1994-2019, where one specific assumption is varied from the assumption used in the financial statement re-estimate.

The monthly unemployment rate is an assumption used in the default projection model. For the sensitivity analysis, the CBO projected quarterly unemployment rate assumptions were used after June of 2020. Actual data from the Bureau of Labor Statistics was available for unemployment prior to June 2020; therefore, the rates used in the financial statement re-estimate do not differ from those used in the sensitivity analysis for that timeframe. Changing this assumption resulted in a projected increase to the re-estimate of $3.7 billion. The chart below shows the changes to the default rate for a sub population of loans.
The IDR model is used to develop cash flows for Direct Loans being repaid under any of the IDR repayment plans, including the income contingent repayment (ICR) plan, the income based repayment (IBR) plan, the Pay as You Earn (PAYE) plan, and the Revised Pay as You Earn (REPAYE) plan. The IDR model also uses information from the OMB economic package on the Consumer Price Index (CPI-U) as a factor for borrower income inflation, balances, and poverty guidelines. A sensitivity analysis that replaces the CPI-U with the assumptions from the July CBO estimates resulted in a projected increase to the re-estimate of $1.7 billion.

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

**Unemployment:** Unemployment rates have been shown to affect both student loan volume and student loan repayment decisions and behavior. During periods of economic downturn, displaced workers have tended to pursue higher education opportunities in high numbers as a way to strengthen their credentials, change career paths, or improve future employment opportunities. While the coronavirus pandemic has been accompanied by a spike in unemployment (at least in the short term), the impact on student loan volume has been more mixed, as higher education has struggled to provide students the level of instruction they were receiving pre-pandemic. The exact impact on the cost estimates from the current recession remains a significant area of uncertainty. For instance, higher short-term unemployment rates could have an impact on future collections of already defaulted loans by increasing the risk of fewer collections from wage garnishment and tax refund reductions. A sensitivity analysis examining the impact of a 5 percent reduction in default collections for three years, starting in the second quarter of FY 2021 when the pandemic relief provisions are set to expire, resulted in a projected increase in the re-estimate of $1 billion.

**Wage Growth:** The estimated costs of IDR plans are largely dependent on trends in observed wage growth. To the extent that future wage growth deviates significantly from prior wage growth, actual costs of IDR plans may deviate from estimated costs. The Department will closely monitor impacts to wage growth as a result of the pandemic. Data is not available for the FY 2020 financial statements, and the ultimate cost may not be known for some time. The estimates are sensitive to slight changes in model assumptions. For instance, a 10 percentage point increase in borrowers reporting zero discretionary income from FY 2020 to FY 2022 and a 5 percentage point increase for FY 2023 to FY 2025 would result in a projected increase to the re-estimate of $2.9 billion. The Department continues to manage risks in this area by building its knowledge about its borrower base and remaining informed of labor market statistics.

**Operational Risk**

Unforeseen issues in administering and servicing student loans may impact the cost estimates. For example, in December 2019, the President signed the Fostering Undergraduate Talent by Unlocking Resources for Education Act (FUTURE Act), which amends Section 6103 of the Internal Revenue Code to allow the IRS to share taxpayer data directly with the Department. Once implemented, this will make it easier for borrowers to stay enrolled in an IDR plan by allowing automated data sharing between federal agencies and eliminating the need for borrowers to annually recertify their income. A timeline for implementation of the FUTURE Act is uncertain, which can make predicting the impact on student loan
cost estimates a challenge. The Department invests significant resources to ensure continuous improvements in cybersecurity defenses based on current and emerging threats. Despite this investment, security threats to operations are ongoing and incidents may happen without warning, potentially disrupting student loan administration and ultimately borrower cash flows, which can be impacted by the timing of when collections or disbursements are processed. Hence, there is an inherent risk that future, unpredictable disruptions in the administrative status quo may impact student loan cost estimates.

NEXT GEN FSA

About FSA
As the nation’s largest provider of financial aid for education beyond high school, FSA delivers more than $115 billion in aid each year to students and their families. Through programs authorized under the Higher Education Act of 1965, as amended, FSA provides grants, loans, and work-study funds for college or career school. FSA also oversees the approximately 5,600 postsecondary institutions that participate in the federal student aid programs. In every interaction with students and their families, FSA strives to be the most trusted and reliable source of student financial aid information and services in the nation.

The Vision
FSA manages one of the largest consumer loan portfolios in the country, valued at $1.6 trillion. It is critical that we provide an environment that provides customers with the services and experiences that they expect and the outcomes that they deserve. The Next Generation Federal Student Aid (Next Gen FSA) initiative is enabling FSA to realize this vision by modernizing the way we connect with our customers and streamlining our student aid systems and processes. This broad effort will deliver an improved customer experience for millions of Americans across the entire student aid life cycle, from fostering greater awareness about the availability of financial aid, to applying for aid, to repaying loans, to improving the participation experiences and oversight of our partners at postsecondary institutions.

Legacy Environment
In the current federal financial aid process, students and families must negotiate a complex and fragmented landscape, interacting with multiple systems, vendors, processes, and interfaces across a multitude of brands and user experiences. Too often, this poor customer experience creates confusion, resulting in borrowers failing to understand how to apply for and maintain their aid eligibility, which repayment options they qualify for, and the financial implications of their student debt. Additionally, operational complexities and out-of-date contracts result in higher administrative costs and hinder effective oversight of our vendors.

Next Gen FSA Environment
Multiple websites, mobile applications, contact centers, and other customer interfaces have been combined into a simplified, consistent, and engaging customer experience, which will be enhanced by standardized training and tools. Since December 2019, FSA has launched a single front door on the web, Studentaid.gov, and has launched multiple modern self-service and consumer information tools that help our customers understand the aid they have received, their remaining eligibility, and how they can manage loan repayment in a way that meets their goals. While FSA’s digital platform helps customers cut through the information clutter and access robust self-service, other components of Next Gen will bring onboard multiple contact centers that provide customers and partners with support across the entire student aid lifecycle, all under the FSA brand.

In addition to an improved customer experience, Next Gen FSA will completely modernize FSA’s back-end systems and infrastructure. This transformation will pave the way for improved application and loan processing and management of customer accounts. The contracts that bring onboard these new systems will include objective performance standards and accountability measures to ensure customers receive accurate, timely responses to their inquiries. These new technologies will also integrate modern cybersecurity protections, and a new enterprise-wide data analytics platform will drive improved data and governance standards.

Solicitation and Procurement Process
In January 2019, FSA awarded a major contract for Digital and Customer Care, which provides FSA with new digital, marketing and communications, and customer care platforms that enable the implementation of a modern StudentAid.gov and myStudentAid mobile application, as well as improved tools for customer outreach. In June 2020, FSA awarded five Business Process Operations contracts, which bring on board vendors that will eventually provide enterprise-wide contact centers and back-office processing for all of FSA’s customers and institutional partners. In October 2020, FSA released a solicitation for the Interim Servicing Solution (ISS) which will provide the core processing...
system, fulfillment, and labor servicing for the federally managed loan portfolio.

The current Title IV Additional Servicing (TIVAS) and Not-for-Profit indefinite-delivery, indefinite-quantity contracts may be extended through December 2021 and March 2022, respectively. ISS will replace the current TIVAS and Not-for-Profit relationship upon award and migration of borrowers. In the event of a delay in the ISS implementation, the appropriate contractual actions will be taken to ensure continued servicing capabilities are maintained. FSA is taking a similar approach to all legacy contracts that will be impacted by the Next Gen FSA system, fulfillment, and labor servicing for the federally managed loan portfolio.

**LEVERAGING DATA AS A STRATEGIC ASSET**

The Department is focusing on further leveraging its data as a strategic asset, in part in response to requirements in the *Foundations for Evidence-Based Policymaking Act* (Evidence Act; PL. 115-435) and the Federal Data Strategy. This section highlights three initiatives intended to help the Department realize the power of data in daily operations and national policy: (1) the development of an ED Data Strategy; (2) priorities for Open Data; and (3) a new focus for the Evidence Leadership Group in advising the Evaluation Officer and developing the Department’s learning agenda.

**Data Strategy**

The 2020 Action Plan under the Federal Data Strategy calls for agencies to “put in place a data strategy or road map.” The Agency-wide Data Governance Board (DGB) has initiated a process to develop the Department’s Data Strategy in order to realize the full potential of data to improve education outcomes and to lead the nation in a new era of evidence-based policy insights and data driven operations. This Department-wide effort will include agency-wide discussions about data priorities that will help improve data maturity and will focus on the Department’s capabilities to leverage data, operationalize and optimize data governance, and drive cultural change for the benefit of all stakeholders. It will build on strengths, weaknesses, and opportunities within the Department to 1) strengthen agency-wide data governance, 2) build human capacity to leverage data, 3) advance the strategic use of data, and 4) improve data access, transparency, and privacy.

**Open Data**

The *Evidence Act* requires agencies to make data “open by default.” The Department is planning to develop, release, and execute the Act’s required open data plan consistent with OMB guidance. The Department will balance privacy and security with the open data mandate and the priority of the Department to enable broader public use of data paid for by its citizens. The Department is also developing an Open Data Platform (ODP), a central repository for its data assets. Recently released in beta, it is a fully featured, robust, and highly scalable data repository that maintains all data assets in a fully searchable catalog.

As required by the *Evidence Act*, the Department will build towards a comprehensive data inventory by expanding on the ODP and increasing its catalogued data assets for both externally available open data and internal sources subject to open data priorities, reviewing all data assets for release consistent with *Evidence Act* mandates and exclusions, and incrementally expanding the number of Department open data assets listed in the Federal Data Catalogue.

**Evaluation Officer and Evidence Leadership Group**

The *Evidence Act* created a new role, a Department Evaluation Officer (EO), who is responsible for: (a) developing the Department’s Learning Agenda by assessing the Department’s portfolio of evaluations, policy research, and ongoing evaluation activities; (b) assessing the Department’s capacity to support the development and use of evaluation; (c) establishing and implementing the Department’s evaluation policy; and (d) coordinating a Department-wide evidence-building plan. IES’s Commissioner of the National Center for Education Evaluation and Regional Assistance is the Department’s EO.

As required by the *Evidence Act*, the Department submitted its Draft Learning Agenda to OMB at the end of fiscal year 2020. The Learning Agenda was developed in consultation with the Department’s Evidence Leadership Group (ELG). The ELG is co-chaired by the EO and the Director of the Department’s Grants Policy Office (GPO) and includes members from the Department’s primary grant-making offices as well as mission-support units, such as the Department’s Budget Service, and Office of General Counsel, and ex-officio representatives from the Office of the Chief Data Officer, the Statistical Official, and the Performance Improvement Officer.

Feedback from OMB guidance. The Department will balance privacy and security with the open data mandate and the priority of the Department to enable broader public use of data paid for by its citizens. The Department is also developing an Open Data Platform (ODP), a central repository for its data assets. Recently released in beta, it is a fully featured, robust, and highly scalable data repository that maintains all data assets in a fully searchable catalog.
Department’s Final Learning Agenda to be submitted to OMB at the end of fiscal year 2021.

In addition to advising the EO on the development of the Draft Learning Agenda, the ELG advises Department leaders on how to support the capacity of ED staff to make better use of data and evidence. GPO, led by the ELG co-chair, has spearheaded a range of internal training opportunities for Department staff to bolster the use of the Secretary’s policy priorities, including the use of evidence in program design, and to consider how the Department’s grantmaking activities can build evidence for improvement in the future. This work, done in close collaboration with partners across the Department, will be informed in fiscal year 2021 by the recently-completed Interim Capacity Assessment, which included a systematic effort to collect information about staff members’ capacity to use evidence in their day-to-day work.

CONTINUOUS IMPROVEMENT

Improving critical infrastructure, systems and overall capacity, and ensuring sound strategic decision making regarding allocation of resources are essential to the Department’s future progress and success. Implementing Technology Business Management Solutions is one of the Department’s key initiatives.

Technology Business Management Solutions (TBMS)

The purpose of the TBMS project is to provide greater cost transparency into IT spending. The TBMS project will allow OCIO to communicate the cost drivers and value of IT to senior leadership, improve the efficiency and predictability of the formulation of the IT budget, and optimize IT costs.

Beginning in 2017, OMB required agencies to begin reporting IT spending in alignment with the TBM Framework, including using Cost Pools and IT Towers to classify IT spending. The Department intends to leverage TBM beyond the minimum OMB reporting requirements to encompass the full implementation of the TBM cost accounting framework. The Department of Education is refining the TBM effort to: 1) provide accurate cost analysis and accounting of operations and services to improve tracking cost variances; 2) provide ad hoc reports to stakeholders on IT spending; and 3) contextualize ED’s internal resource costs with real world data to inform decisions. Ultimately, the goal is to provide a “bill of IT” to form the basis of a show-back model to drive more informed decision-making around IT.

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

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