



NOV - 8 2017

Honorable Gene Dodaro
Comptroller General
Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Mr. Dodaro:

I am pleased to write on behalf of the Secretary in response to the statements and recommendations made in the U.S. Government Accountability Office (GAO) report, "Higher Education: Education Should Address Oversight and Communication Gaps in Its Monitoring of the Financial Condition of Schools" (GAO-17-555).

The Department's regulations require that audited financial statements be prepared in accordance with generally accepted accounting principles, and audited in accordance with generally accepted government auditing standards (34 C.F.R. § 668.23(d)). The Financial Accounting Standards Board updates the accounting standards to improve the information reported about an entity in an audited financial statement. Changes made to the accounting standards become an integral part of the audited financial statements that are submitted annually to the Department by institutions. The Department monitors changes to the accounting standards to ensure the financial analysis staff is consistently determining the composite scores for institutions. The Department will continue to work with individual schools to take into consideration additional information that may have an impact on a school's composite score calculation.

As noted by the GAO and by the Department's Office of Inspector General, the Department has taken steps to increase its oversight of certain schools. In December 2014, Federal Student Aid (FSA) created an office that is responsible for monitoring large school groups and currently monitors 47 companies, including major publicly-traded companies, private equity firms, and privately-held companies, which collectively own 330 schools. FSA has implemented significant new tools and processes to identify at-risk schools and mitigate potential student and taxpayer harm, that include requiring more frequent financial and enrollment reporting requirements for at-risk schools, subscribing to in-depth industry analyses for fiscal information about publicly-traded schools, and enhancing the FSA annual risk model used to select schools for program reviews.

We generally concur with the report's recommendations and provide a response to each as follows:

Recommendation 1: Update the composite score formula to better measure schools' financial conditions and capture financial risks.

Federal Student Aid
An OFFICE of the U.S. DEPARTMENT of EDUCATION

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Response: GAO states that the Department does not have reasonable assurance that the composite score is a reliable indicator of financial health but has not shown how any changes in the accounting standards have made the Department's composite score calculations any less reliable. Given that the regulations provide for audited financial statements to be prepared in accordance with generally accepted accounting principles, changes to those accounting standards are reflected in the audited financial statement submissions to FSA. The potential for a component of the financial measure to be manipulated is a factor to consider and address but does not in itself undermine the benefits of using the composite score calculation.

On August 30, 2017, the Department published a Federal Register Notice, 82 Fed. Reg. 41,194, announcing its intent to establish two negotiated rulemaking committees. The committee on Borrower Defense and Financial Responsibility Issues will include a Financial Responsibility Subcommittee to consider and report to the full committee whether or how the Financial Accounting Standards Board's (FASB's) recent changes to the accounting standards for financial reporting necessitate modifications to the Department's financial responsibility regulations with respect to the calculation of the Primary Reserve Ratio, the Equity Ratio, and the Net Income Ratio that are used to calculate an institution's composite score, as well as whether clarifications in terms used in the Primary Reserve, Equity, and Net Income ratio calculations are needed as a result of changes in the financial accounting standards. These accounting changes overlap with a number of accounting changes cited in the GAO report, and, as such, the Department may address those matters as part of the negotiated rulemaking process.

Additionally, as stated in the Department's response to GAO's draft report, the Department will provide more guidance as discussed in Recommendation 2 to mitigate any disagreements with the community that are related to Recommendation 1.

In regard to a school potentially manipulating information that is used to calculate the school's composite score, the Department is conducting a study to determine if manipulation of composite scores is a widespread issue. Based on the results of that study, a determination will be made as to whether additional procedures need to be put in place when reviewing a school's financial statements, including identifying when additional information should be requested to obtain an accurate calculation of a school's composite score.

Recommendation 2: Improve guidance to schools about how the financial composite score is calculated, for example, by updating current guidance to include explanations about common areas of confusion and misinterpretation for schools.

Response: The Department agrees that additional general guidance on how it calculates the composite score would be useful to schools. The Department will update its current guidance to schools in the Federal Student Aid Handbook to include a description of its general calculation methodology and may post additional guidance online with answers to frequently asked questions.

Recommendation 3: Increase the transparency of public data on schools' financial health by publicly listing the final composite score for each school.

Response: The Department already posts composite scores annually for institutions, but the list does not include institutions where the composite score is under appeal and does not show the composite scores for all schools in a school group. Going forward, the Department agrees to update the annual list of composite scores to include the revised composite scores for schools that appealed their original composite score. The Department will also include composite scores for all schools in a school group on the Department's Federal Student Aid Data Center, School Data website.

We appreciate the opportunity to respond to the final recommendations outlined in the GAO report.

Sincerely,

A black rectangular redaction box covering the signature of A. Wayne Johnson.

A. Wayne Johnson
Chief Operating Officer