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REPORT TO THE CONGRESS

72-0050

Examination Of Financial Statements Of The Student Loan Insurance Fund Fiscal Year 1970 B-164031(1)

Office of Education
Department of Health, Education, and Welfare

BY THE COMPTROLLER GENERAL OF THE UNITED STATES

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JAN. 12, 1972

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-164031(1)

To the President of the Senate and the
Speaker of the House of Representatives

This is our report on examination of financial statements of the Student Loan Insurance Fund, administered by the Office of Education, Department of Health, Education, and Welfare, for fiscal year 1970.

Our examination was made in accordance with section 105 of the Government Corporation Control Act, as required by the Higher Education Act of 1965.

Copies of this report are being sent to the Director, Office of Management and Budget; the Secretary of the Treasury; the Secretary of Health, Education, and Welfare; and the Commissioner of Education, Department of Health, Education, and Welfare.

Elmer B. Staats

Comptroller General
of the United States

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ABBREVIATIONS

GAO General Accounting Office

HEW Department of Health, Education, and Welfare

COMPTROLLER GENERAL'S REPORT TO THE CONGRESS

EXAMINATION OF FINANCIAL STATEMENTS OF THE STUDENT LOAN INSURANCE FUND, FISCAL YEAR 1970
Office of Education
Department of Health, Education, and Welfare
B-164031(1)

D I G E S T

WHY THE EXAMINATION WAS MADE

The Guaranteed Student Loan program comprises two components: a Federal student loan insurance program and a State or private nonprofit agency student loan insurance program.

The Comptroller General is required by the Higher Education Act of 1965 to audit annually the Student Loan Insurance Fund which finances loan insurance activities under the Federal program and Federal reinsurance of loans made under the State program. The fund is administered by the Office of Education, Department of Health, Education, and Welfare (HEW).

FINDINGS AND CONCLUSIONS

Although the amounts shown for the cash and fund balance, investments, and accrued liabilities on the statement of financial condition were found to be accurate, the General Accounting Office (GAO) cannot express an opinion that the accompanying financial statements present fairly the financial position of the Student Loan Insurance Fund at June 30, 1970, and the results of its operations and the sources and application of its funds for the fiscal year then ended, in conformity with principles and standards of accounting prescribed by the Comptroller General of the United States for the following reasons.

--*Accounts receivable:* It was not practicable for GAO to confirm year-end balances with lenders or to satisfy itself as to the validity of the accounts receivable by other auditing procedures; also the accounts receivable included unpaid premiums on many loans made after the fiscal year had ended. (See p. 10.)

--*Income from insurance premiums and insurance premium income deferred:* Premiums on many loans made after the fiscal year had ended were included in the amounts shown. (See p. 10.)

--*Loans receivable:* GAO was unable to verify by direct confirmation the validity of the amounts owed by individual borrowers on their defaulted loans; also the loans receivable included amounts owed by borrowers who had been adjudicated bankrupt and who had no legal obligation to repay their loans. (See pp. 12 and 13.)

Tear Sheet

JAN. 12, 1972

--*Allowances for losses on loans receivable and accrued interest receivable:* The reasonableness of the data used to compute the loss rate was not readily determinable. (See p. 13.)

The internal controls over cash receipts for the Student Loan Insurance Fund should be improved to ensure that such receipts are recorded and deposited promptly. (See p. 16.)

GAO noted that the fund's capital for insuring loans under the Federal program was almost depleted at the end of fiscal year 1971 because the insurance premiums collected from lenders and the proceeds from the collection of defaulted loans had not been sufficient to pay lenders' claims for defaulted loans. GAO believes that additional funds will be needed to pay default claims as more loans become due for repayment. (See p. 8.)

RECOMMENDATIONS OR SUGGESTIONS

The Secretary of Health, Education, and Welfare should have the Office of Education

--improve its system for recording insurance premiums billed to and collected from lenders to ensure that year-end data is available showing actual accounts receivable and insurance premium income applicable to insured loans made during the fiscal year (see p. 11),

--record payments for loan default claims resulting from ordinary bankruptcy of the borrowers as expenses rather than as loans receivable (see p. 14), and

--strengthen the controls over cash receipts for the Student Loan Insurance Fund by preparing a listing of checks as they are received and by promptly depositing the checks in the Treasury. (See p. 16.)

AGENCY ACTIONS AND UNRESOLVED ISSUES

HEW concurred in GAO's recommendations and described actions that were taken or planned to implement them. (See pp. 11, 14, and 16.)

MATTERS FOR CONSIDERATION BY THE CONGRESS

This report, required by law, contains no recommendations or suggestions requiring action by the Congress.

CHAPTER 1

INTRODUCTION

The Office of Education administers various support and assistance programs in the field of education. One such program, commonly known as the Guaranteed Student Loan program, provides low-interest insured loans for students in institutions of higher education and vocational schools. This program, established pursuant to title IV, part B, of the Higher Education Act of 1965, as amended (20 U.S.C. 1071), comprises two components--a State or private nonprofit agency student loan insurance program and a Federal student loan insurance program.

The purposes of the Guaranteed Student Loan program are to:

1. Encourage States and private nonprofit institutions and organizations to establish adequate loan insurance programs for students in institutions of higher education and vocational schools.

2. Provide a Federal program of student loan insurance for students or lenders who do not have reasonable access to a State or private nonprofit program of student loan insurance.

3. Pay, on behalf of qualified students, a part of the interest charged by lending institutions on loans which are insured under either the Federal program or an eligible loan insurance program established by a State or private nonprofit institution.

4. Guarantee a part of loans insured under an eligible loan insurance program established by a State or private nonprofit institution.

A student qualifies for interest benefits--payment by the Government of part of the interest on his loan--if the combined adjusted gross income of the student (and his parents and spouse, if applicable), as reported for Federal tax purposes for the preceding year, less 10 percent and amounts allowable for exemptions, was less than $15,000. From inception of the program in 1965 through June 30, 1970, the Office of Education expended about $160 million for interest benefits, including $85 million in fiscal year 1970.

The Congress, through fiscal year 1970, had appropriated $31,875,000 to the Office of Education for making advances to help establish or strengthen the student loan insurance programs operated by States or private nonprofit agencies, hereinafter referred to as the State program. A State or private guaranty agency provides the loan insurance through a student loan insurance fund which it administers by utilizing the Federal funds advanced by the Office of Education. As of June 30, 1970, the Office of Education had advanced $18,689,063 to State and private guaranty agencies for this purpose. Of this amount, $68,580 was advanced during fiscal year 1970.

During August 1967 the Office of Education initiated the Federal Insured Student Loan program, hereinafter referred to as the Federal program, because the demand for student loans exceeded the amount of State and/or Federal funds available for insuring loans at the State level. As of June 30, 1970, 27 States and Puerto Rico were participating in the Federal program under the provisions of the Higher Education Act of 1965, as amended. (See app. I.) Loans made under the Federal program are insured by the Student Loan Insurance Fund, which is administered by the Office of Education.

During 1968 legislation was enacted which affected the operation of the Student Loan Insurance Fund beginning in fiscal year 1969. Public Law 90-460, approved August 3, 1968, amended section 428 of the Higher Education Act of 1965 (20 U.S.C. 1078) to provide for Federal reinsurance of loans guaranteed by State or private guaranty agencies. This was done to promote the continuation of existing State or private guaranty agencies and to encourage the development of adequate State programs where none existed. Reinsurance has the effect of increasing the guaranty capacity of State or private agencies because these agencies will be reimbursed by the Office of Education for a large percentage of their losses. As of June 30, 1970, 23 States and the District of Columbia were participating under the reinsurance provision of the act. (See app. II.)

GAO is required by the Higher Education Act of 1965, as amended, to examine only those transactions affecting the Student Loan Insurance Fund under which Federal program insurance activities and reinsurance activities authorized by the act are financed. This report covers the operation of the fund for the fiscal year ended June 30, 1970.

CHAPTER 2

OPERATION AND FINANCING

OPERATION

The Guaranteed Student Loan program enables students to borrow funds from participating lending institutions to help pay for their educational costs while attending vocational, technical, or degree-granting institutions. Under the Federal program, these loans are insured by the Government and, in the event of a student's death, total and permanent disability, or failure to pay, the lender is reimbursed for 100 percent of the unpaid principal balance of the loan.

Under Federal reinsurance of loans made under the State program, the Office of Education is authorized to enter into agreements with State or private guaranty agencies whereby such an agency will be reimbursed for 80 percent of its loss resulting from a student's default of a loan or from the nonpayment of a loan made prior to December 15, 1968, due to death or disability of a student borrower.

The loss resulting from the death or disability of a student borrower on a loan made on or after December 15, 1968, is not covered by reinsurance. The legislation provides that, for such a loan, the Office of Education pay the entire amount owed on a loan by a student borrower who dies or who is totally and permanently disabled, regardless of the source of guaranty (State or private) and regardless of whether the guaranty agency has signed a reinsurance agreement.

Upon payment of a lender's claim under the Federal program, the Government acquires title to the borrower's note on which the claim is filed. The Government then attempts to collect the loan, except on a claim resulting from the death or disability of a student borrower. In the event the borrower dies or becomes totally and permanently disabled, the obligation to make any further payment of principal and interest is canceled.

Under Federal reinsurance of a loan made under the State program, the Office of Education does not acquire title to the borrower's note on any claim that is paid. After a payment has been made by the Office of Education to a guaranty agency for a default claim, that agency has full collection responsibility and is required to return to the Office of Education 80 percent of any amount it subsequently recovers from a borrower. As under the Federal program, in the event the borrower dies or becomes totally and permanently disabled, the obligation to make further payment is canceled.

Any student, regardless of residence or family income, who is a citizen or national of the United States or who is in the United States for other than a temporary purpose and who is enrolled as at least a half-time student at an eligible institution, can apply for a loan. The maximum loan that can be insured for each academic year is $1,500, and the total amount of loans to any one student that can be insured is $7,500.

FINANCING

The Higher Education Act of 1965 established the Student Loan Insurance Fund. Prior to December 15, 1968, all moneys in this fund were to be used for making payments in connection with losses incurred under the Federal program. Effective December 15, 1968, the fund was to be used also for making payments in connection with losses on defaulted loans covered under the reinsurance provision of the act.

The Student Loan Insurance Fund is a revolving fund which is financed by direct appropriations from the Congress, by insurance premiums collected from participating lenders on loans made under the Federal program, and by proceeds from the collection of defaulted loans. The Office of Education is authorized to issue notes or other obligations to the Secretary of the Treasury if additional funds are required. If available funds exceed current operating needs, such excess funds may be invested by the Office of Education in bonds or other obligations guaranteed by the United States.

Federal funds provided as capital for the Student Loan Insurance Fund consist of $3,750,000 for the insurance of loans made under the Federal program and of $10,826,000 for the reinsurance of loans made under the State program.

The Higher Education Act of 1965 requires the Office of Education to charge lenders participating in the Federal program a premium on each insured loan in an amount not to exceed one fourth of 1 percent a year of the unpaid principal amount of such loan, payable in advance, at such times and in such manner as may be prescribed by the Commissioner of Education. The lenders may pass the charges on to the students borrowing the funds. The Office of Education has the option of either collecting the premiums or offsetting them against amounts payable to the lenders for interest on student loans. Since the inception of the Federal program, the Office of Education has billed participating lenders for the premiums due.

As of June 30, 1970, the Student Loan Insurance Fund's capital for insuring loans made under the Federal program was $3,372,698. HEW's accounting records for the fund showed that this balance had been reduced to $104,149 at June 30, 1971, as a result of claims paid from capital during fiscal year 1971.

We believe that, because the insurance premium income and proceeds from the collection of defaulted loans have not been sufficient to pay lenders' claims for defaulted loans, additional funds will be needed for this purpose as more loans become due for repayment. HEW officials informed us that HEW was planning either to request additional appropriations from the Congress or to borrow funds from the Treasury to meet its needs for payment of claims under the Federal program in fiscal year 1972.

During fiscal year 1970 insurance premiums charged lenders were computed at the rate of one fourth of 1 percent a year of the amounts of the loans from the dates of disbursement of the loans to the student borrowers to the anticipated dates of their graduation plus 12 months. An Office of Education official informed us that the Office of Education had elected to compute the premium over this period, rather than over the full life of the loan, to avoid the administrative work and cost (both to the Office of Education and to the lender) that would be involved in recomputing the premium each time the principal balance changed during the repayment period or for every change in the student's status (such as leaving school or entering military service).

The Office of Education does not refund or adjust a premium as a result of (1) a student's leaving school or repaying the loan prior to the date used in computing the premium or (2) the extension of a student's educational program.

Precise estimates were not readily available to show the period in which students would actually repay their loans. Usually the amount of premiums charged would be greater if the premiums were computed over the full life of the loan rather than over the shorter period used under the present method. The maximum repayment period for an insured loan generally is 10 years, beginning 9 to 12 months after the student graduates or ceases to carry an acceptable academic work load. The repayment period is extended for service in the armed services, Peace Corps, or Volunteers In Service To America.

Under Federal reinsurance of loans made under the State program, no insurance premiums are charged the State or private agencies even though some of these agencies collect premiums from the lenders. The conference report on the Higher Education Amendments of 1968 (H. Rept. 1919, dated Sept. 25, 1968) stated that it was the intent of the Congress that payments under the reinsurance provision with respect to default claims be made from appropriated funds and that collections on defaulted loans and premium income under the Federal program be used only for making payments under that program.

CHAPTER 3

COMMENTS ON FINANCIAL STATEMENTS

ACCOUNTS RECEIVABLE

Generally accepted accounting principles and techniques require that all transactions affecting accounts receivable and income be properly recorded during the accounting period and that subsidiary account balances be maintained for each debtor. We noted, however, that the amount of $1,199,255 shown in the Student Loan Insurance Fund's statement of financial condition at June 30, 1970 (sch. 1), as accounts receivable included many insurance premiums applicable to loans made by lenders after the fiscal year had ended.

The Office of Education's operating procedures require lenders to report loans within 31 days after the date of the loan disbursements. This data is processed by the Office of Education through its computer system which prints the loan transaction statements that are used to bill lenders for insurance premiums. These statements show the individual amounts of insured loans as reported by each lender and the premiums applicable to the loans. Those loans disbursed during the fiscal year and those disbursed after the end of the year, however, are not shown separately on the billings. The Office of Education does not maintain accounts receivable records showing the amounts owed by individual lenders.

The accounts receivable at June 30, 1970, comprised (1) the unpaid balance of premiums billed to lenders through September 19, 1970, on insured loans and (2) estimated premiums on loans made during the year that had not been billed to lenders due to a need for clarification of the data they had submitted to the Office of Education. An adjustment was not made, however, to eliminate from the amount of the accounts receivable the premiums included in the September billing on loans which were disbursed after June 30, 1970. This billing totaled about $208,000 and included premiums on many loans that were disbursed in July and August 1970.

Since the Office of Education did not have data available showing the actual amount of accounts receivable at year-end or the amounts owed by individual lenders, it was not feasible for us to follow the normal auditing procedure of confirming accounts receivable with lenders or to satisfy ourselves as to the validity of the accounts receivable by other auditing procedures. We are therefore unable to express an opinion regarding the reasonableness of the amount of accounts receivable as shown on the financial statements.

Because the premium billings also affected income, we cannot express an opinion regarding the amounts shown on schedule 3 of the financial statements for insurance premium income earned during the year ($553,121) and on schedule 1 for insurance premium income deferred ($2,730,141).

We believe that the Office of Education should strengthen its accounting procedures for the Student Loan Insurance Fund to ensure that amounts shown on the financial statements for accounts receivable and insurance premium income are derived from reasonable and sound bases.

Recommendation to the Secretary of Health, Education, and Welfare

We recommend that the Office of Education improve its system for recording insurance premiums billed to and collected from lenders to ensure that year-end data is available showing actual accounts receivable and insurance premium income applicable to insured loans made during the fiscal year.

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HEW commented on a draft of this report by letter dated October 20, 1971. (See app. III.) HEW stated that the computer system had been programmed to make available the amount billed by fiscal year to each lender and that backup procedures had been devised to obtain lenders' reports on loans disbursed through the end of the fiscal year in the event the computer system did not function properly.

HEW advised us that these actions would help to ensure that actual year-end data is available showing accounts receivable and that the related premium income is properly recorded.

Although year-end computer data on amounts billed to lenders would help in determining the accounts receivable balance, such data must be considered with collections received from lenders if a meaningful balance is to be obtained. We therefore believe that the computer system should be programmed to make available an accounts receivable balance at year-end.

LOANS RECEIVABLE AND ALLOWANCES FOR LOSSES

The Office of Education pays lenders and State or private guaranty agencies for claims made for defaulted insured loans. If a loan is in default due to the death or disability of the borrower, the amount of the unpaid loan is charged to an expense account; otherwise, it is recorded as a loan receivable, and, except in instances of certain bankruptcies, further attempts are made to collect the amount from the borrower.

The Student Loan Insurance Fund's statement of financial condition at June 30, 1970 (sch. 1), included loans receivable of $1,764,743 and $2,567,795 for the Federal program and for the Federal reinsurance, respectively. In accordance with generally accepted auditing standards, we attempted to determine the reasonableness of these amounts by direct confirmation with the debtors. We selected a statistical sample of 200 of the approximately 5,200 borrowers who had defaulted on their loans and requested them to confirm the balances of their indebtedness, as recorded on Office of Education records.

Sixty, or 30 percent, of the borrowers responded to our confirmation requests. Forty-eight stated that the amounts of their unpaid loans were accurate, and 12 either disagreed with the amounts or did not indicate agreement or disagreement. Of the remaining 140 confirmation requests, 64, or 32 percent, were returned by the Post Office as undeliverable and 76, or 38 percent, were not returned by the borrowers even though we sent follow-up requests to them.

Because of the limited responses to our confirmation requests, we are unable to express an opinion as to the reasonableness of the loans receivable balances as shown on the fund's statement of financial condition at June 30, 1970.

The Office of Education used a rate of 55 percent to compute the allowances for losses on accrued interest receivable and on default claims paid and charged to loans receivable during fiscal year 1970. This rate is the same as that used in establishing allowances shown on the fiscal year 1969 financial statements and was based on the experience of the Federal Housing Administration's Title I Housing Insurance Fund for the period July 1934 through June 1967. It was used because of similar factors involved in the operations of the two funds and because of the lack of experience to date under the Student Loan Insurance Fund.

We are unable to readily determine the propriety of this loss rate with respect to the Federal program or the Federal reinsurance of loans under the State program and therefore cannot express an opinion on the reasonableness of the allowances for losses on loans receivable and on accrued interest receivable.

Treatment of bankruptcy claims

Approximately $360,000, or 8.4 percent of the loans receivable at June 30, 1970, represented loans that were defaulted because the borrowers had been adjudicated bankrupt. Most of these bankruptcy claims involved ordinary bankruptcies which relieved the borrowers from the legal obligation of repaying their debts. The few remaining claims involved bankruptcies that had been filed under the provisions of chapter 13 of the Bankruptcy Act of 1898, as amended (11 U.S.C. 1001), which provides for debtors to make arrangements for paying their debts from their future earnings.

Since borrowers who have been relieved of their debts through ordinary bankruptcy do not have a legal obligation to repay their loans, there appears to be little likelihood that the Office of Education will collect any significant amounts of loans receivable in such cases. We therefore believe that payments made by the Office of Education for default claims resulting from ordinary bankruptcy should be recorded as expenses rather than loans receivable.

Recommendation to the Secretary
of Health, Education, and Welfare

We recommend that the Office of Education record payments for loan default claims resulting from ordinary bankruptcy of the borrowers as expenses.

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HEW concurred in our recommendation but stated that such payments would be recorded as expenses within 12 months from the date that the borrower was declared bankrupt rather than upon payment of the lender's claim for the defaulted loan.

HEW pointed out that the Office of Education's experience had shown that collections sometimes were made within a year from a small percentage of bankrupt borrowers who possessed assets for distribution to creditors and from some bankrupt borrowers who reassumed their debts. HEW stated that to record ordinary bankruptcy claims as expenses when the claims were paid would require additional accounting for those claims on which recoveries were made.

CONTINGENT LIABILITIES

The Office of Education furnished to the Treasury Department a schedule with its financial statements for the Student Loan Insurance Fund for fiscal year 1970 showing contingent liabilities of $465 million for loans insured under the Federal program and of $1.13 billion for reinsured loans made under the State program as of June 30, 1970. These amounts represented the net contingent liabilities of the fund as determined by the Office of Education after considering the amount of claims paid on defaulted loans and an estimated amount for repayments made by student borrowers. (See GAO note 3 to the financial statements on page 23.)

Although lenders participating in the Guaranteed Student Loan program had been requested to report the unpaid balances of federally insured and reinsured loans at June 30, 1970, many lenders did not furnish such data in time to be of use to the Office of Education in the preparation of the financial statements of the fund. Consequently the Office of Education estimated the amount of repayments by student borrowers in determining the fund's contingent liabilities for insured and reinsured loans.

An Office of Education official stated that much of the data that was subsequently provided by lenders was considered unreliable because it did not always indicate whether the unpaid principal balances of loans made by branch banks were included. We were informed that lenders would be requested to provide more timely and accurate information so that the contingent liabilities would represent the actual outstanding principal balances of federally insured and reinsured loans. We intend to stay abreast of the agency's progress in obtaining such information in our future audits of the Student Loan Insurance Fund.

CHAPTER 4

IMPROVEMENT NEEDED IN

INTERNAL CONTROLS FOR CASH RECEIPTS

Internal controls over cash receipts for the Student Loan Insurance Fund should be improved to ensure that such receipts are recorded and deposited promptly.

Checks received from lenders in payment of insurance premiums were forwarded from the point of receipt to employees responsible for maintaining records of billings and collections without preparing any control listing. Also these checks were not deposited in the U.S. Treasury until they were reconciled with the premiums that had been billed to lenders. No listing of checks was prepared until after they were processed for deposit in the Treasury.

Because of problems encountered with the computerized billing system, many payments were not readily reconcilable and therefore were not deposited timely--in some cases not for several weeks or even months after they were received. Also payments received from student borrowers on defaulted loans were not recorded and deposited promptly.

The weaknesses in these procedures increase the possibility that checks might be misplaced or lost and might not be recorded in the records. Also they result in delays in making the funds available to the U.S. Treasury for Government needs.

RECOMMENDATION TO THE SECRETARY OF HEALTH, EDUCATION, AND WELFARE

We recommend that, to strengthen the controls over cash receipts for the Student Loan Insurance Fund, the Office of Education prepare a control listing of checks as they are received and promptly deposit the checks in the Treasury.

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HEW stated that it concurred in our recommendation and that action was being taken to implement it.

CHAPTER 5

SCOPE OF EXAMINATION

We have examined the financial statements of the Student Loan Insurance Fund administered by the Office of Education, HEW, for the fiscal year ended June 30, 1970, included herein. Our examination was made in accordance with generally accepted auditing standards and included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances, except as stated in the following paragraph.

The year-end accounts receivable included unpaid insurance premiums for many loans that were made after the end of fiscal year 1970 and estimated premiums that had not been billed to lenders for many insured loans that were made during the fiscal year. Also the Office of Education did not maintain accounts receivable balances for individual lenders. Therefore it was not feasible for us to follow the normal auditing procedure of confirming year-end balances of insurance premiums due from lenders or to satisfy ourselves as to the reasonableness of the amount of the year-end accounts receivable through other means.

Our examination included a review of the laws authorizing the Student Loan Insurance Fund and of the Office of Education's policies and procedures for implementing the legislation. Also we corresponded directly with borrowers on a test basis in an attempt to confirm the outstanding amounts of loans on which they had defaulted.

CHAPTER 6

OPINION OF FINANCIAL STATEMENTS

The financial statements accompanying this report (schs. 1 through 4) were prepared by HEW, and modifications were made by GAO to improve their clarity.

The amounts shown for the cash and fund balance, investments, and accrued liabilities on the statement of financial condition were found to be accurate. We cannot express an opinion regarding the reasonableness of the amounts shown on the financial statements for:

--Accounts receivable, because it was not practicable for us to confirm year-end balances with lenders or to satisfy ourselves as to the validity of the accounts receivable by other auditing procedures; also the accounts receivable included unpaid premiums on many loans made after the fiscal year had ended.

--Income from insurance premiums and insurance premium income deferred, because premiums on many loans made after the fiscal year had ended were included in the amounts shown.

--Loans receivable, because we were unable to verify by direct confirmation the validity of the amounts owed by individual borrowers on their defaulted loans; also the loans receivable included amounts owed by borrowers who had been adjudicated bankrupt and who had no legal obligation to repay their loans.

--Allowances for losses on loans receivable and accrued interest receivable, because the reasonableness of the data used to compute the loss rate was not readily determinable.

For the reasons set forth in the preceding paragraph, we cannot express an opinion that the accompanying financial statements present fairly the financial position of the Student Loan Insurance Fund at June 30, 1970, and the results of its operations and the sources and application of its funds for the fiscal year then ended, in conformity with principles and standards of accounting prescribed by the Comptroller General of the United States.

SCHEDULE 1

OFFICE OF EDUCATION

STUDENT LOAN INSURANCE FUND

STATEMENT OF FINANCIAL CONDITION

AS OF JUNE 30, 1970

A S S E T S

	Insured	Reinsured		
CASH AND FUND BALANCE:				
Cash on hand and in transit			$ 32,017	
Fund balance with U.S. Treasury			12,077,536	
Total cash and fund balance				$12,109,553
INVESTMENTS--PUBLIC DEBT SECURITIES AT PAR VALUE (cost $893,328, market value $898,687)				900,000
ACCOUNTS RECEIVABLE				1,199,255
ACCRUED INTEREST RECEIVABLE:				
Public debt securities				17,031
Accrued interest on loans receivable	$ 28,294	$ 47,684		
Less allowance for losses	15,562	26,226		
	12,732	21,458		34,190
LOANS RECEIVABLE (note 1)	1,764,743	2,567,795		
Less allowance for losses	970,609	1,412,287		
Net loans receivable	794,134	1,155,508		1,949,642
DEFERRED CHARGES--PREMIUM ON INVESTMENTS				2,481
Total assets				$16,212,152

L I A B I L I T I E S

ACCRUED LIABILITIES (note 2)				$ 1,151,311
DEFERRED CREDITS:				
Discount on investment--public debt securities			$ 4,526	
Insurance premium income			2,730,141	
Total deferred credits				2,734,668
Total liabilities				3,885,979

I N V E S T M E N T O F U. S. G O V E R N M E N T

	Insured	Reinsured		
CAPITAL APPROPRIATED	$3,750,000	$10,826,000		
Less excess of accumulated insurance costs over income received	-377,302	-1,872,525		
Balance (note 3)	3,372,698	8,953,475		12,326,173
Total liabilities and investment				$16,212,152

The opinion of the General Accounting Office on these financial statements appears on page 18 of this report.

The notes on page 23, which were prepared by the General Accounting Office, should be considered when reading the statement of financial condition.

SCHEDULE 2

OFFICE OF EDUCATION

STUDENT LOAN INSURANCE FUND

STATEMENT OF CHANGES IN INVESTMENT

OF THE U.S. GOVERNMENT

FOR THE FISCAL YEAR ENDED JUNE 30, 1970

	Insured	Reinsured	Total
Balance at beginning of period	$3,600,917	$ 166,974	$ 3,767,891
Funds appropriated for reinsured claims	-	10,826,000	10,826,000
Adjustment for fiscal year 1969 reinsured claims paid from insured loan funds	262,325	-262,325	-
Net income or deficit (-) for year ended June 30, 1970 (see schedule 3)	-490,545	-1,777,173	-2,267,718
Balance at end of period	$3,372,697	$ 8,953,476	$12,326,173

The opinion of the General Accounting Office on these financial statements appears on page 18 of this report.

OFFICE OF EDUCATION

STUDENT LOAN INSURANCE FUND

STATEMENT OF INCOME AND EXPENSE

FOR THE FISCAL YEAR ENDED JUNE 30, 1970

	Insured	Reinsured	Total
INCOME:			
Insurance premiums	$ 553,121		$ 553,121
Interest on public debt securities	48,194		48,194
Interest on loans receivable	27,276	$ 47,470	74,746
Total income	628,591	47,470	676,061
EXPENSE (note a):			
Loss on loans--deaths and disabilities	169,874	397,851	567,725
Estimated losses on accrued interest receivable	14,984	26,108	41,092
Estimated losses on loans receivable	934,278	1,400,684	2,334,962
Total expense	1,119,136	1,824,643	2,943,779
Net income or deficit (–)	–$ 490,545	$1,777,173	–$2,267,718

[a]Under Section 437 of the Act, losses by death or disability on loans made after December 15, 1968, will be paid from the higher education activities appropriation (75X0293) and are therefore excluded from these statements. Cumulative through June 30, 1970, claims of $305,000 have been received, $200,000 for insured and $105,000 for reinsured.

The opinion of the General Accounting Office on these financial statements appears on page 18 of this report.

SCHEDULE 4

OFFICE OF EDUCATION

STUDENT LOAN INSURANCE FUND

STATEMENT OF SOURCES AND APPLICATION OF FUNDS

FOR THE FISCAL YEAR ENDED JUNE 30, 1970

FUNDS PROVIDED BY:	
Appropriations	$10,826,000
Loan repayments	84,426
Interest on loans receivable	74,746
Insurance premiums	553,121
Interest on public debt securities	48,194
Total funds provided	$11,586,487
FUNDS APPLIED TO:	
Purchase of investment--public debt securities	$ 488,000
Increase in loans receivable	4,162,832
Death and disability claims paid	567,725
Increase in working capital (see subschedule below)	6,367,930
Total funds applied	$11,586,487

SUBSCHEDULE

INCREASE IN WORKING CAPITAL

INCREASES IN WORKING CAPITAL:		
Cash on hand and in transit	$ 25,140	
Operating fund balance with U.S. Treasury	7,981,996	
Accounts receivable	713,449	
Accrued interest receivable	91,744	
Decrease in discount on investment	3,510	
Increase in premium on investment	2,481	$ 8,818,320
DECREASES IN WORKING CAPITAL:		
Accrued liabilities	908,468	
Deferred insurance premiums	1,541,922	2,450,390
Increase in working capital		$ 6,367,930

The opinion of the General Accounting Office on these financial statements appears on page 18 of this report.

GENERAL ACCOUNTING OFFICE

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 1970

1. Loans receivable represented the amounts paid to lenders for federally insured defaulted loans--the notes are assigned to the Office of Education--and the amounts paid to State and private guaranty agencies for federally reinsured defaulted loans--the notes are retained by those agencies. Loans receivable also included amounts for loan default claims on hand but not paid as of June 30, 1970.

2. Accrued liabilities represented claims payable to lenders and State or private guaranty agencies and consisted of:

Insured loan claims due lenders	$ 536,620
Reinsured loan claims due State and private guaranty agencies	614,691
Total	$1,151,311

3. The financial statements which the Office of Education submitted to the Treasury included a schedule showing the fund's estimated net contingent liability of $465 million for federally insured loans and $1.13 billion for reinsured loans that had been disbursed as of June 30, 1970. The Office of Education determined these amounts after considering the amount of claims paid on defaulted loans and an estimated amount for repayments made by student borrowers. Additional amounts of $173 million for federally insured loans and $132 million for reinsured loans were shown on the schedule as the potential contingent liabilities for loans that had been approved but had not been disbursed as of June 30, 1970.

STUDENT LOAN INSURANCE FUND

VOLUME OF COMMITMENTS FOR FEDERALLY INSURED LOANS

FROM INCEPTION THROUGH JUNE 30, 1970

Location	Date Federal program was implemented	Commitments Number	Commitments Amount (note a)
Alabama	5-68	23,721	$ 20,522,013
Arizona	12-67	18,896	14,446,769
California	12-67	181,243	166,997,791
Colorado	8-67	32,629	33,537,552
Florida	2-68	30,249	30,186,736
Hawaii	8-67	5,031	5,404,935
Idaho	2-68	8,811	7,748,986
Indiana	9-67	41,363	39,205,965
Iowa	1-69	23,576	23,209,369
Kansas	9-67	18,711	16,277,056
Kentucky	12-68	11,694	10,288,065
Minnesota	9-67	61,531	55,478,233
Mississippi	12-68	13,689	11,311,645
Montana	10-67	14,086	12,287,425
Nebraska	11-67	13,967	13,044,615
New Jersey	10-67	13,512	12,317,236
New Mexico	8-68	5,218	4,032,510
North Dakota	8-67	29,294	25,196,334
South Dakota	8-68	12,747	10,889,431
Tennessee	10-68	394	377,964
Texas	12-68	31,598	31,180,530
Utah	9-67	18,043	16,227,149
Vermont	9-67	5,111	4,710,854
Virginia	9-68	3,879	3,898,578
Washington	11-67	20,240	16,797,980
West Virginia	10-67	14,592	13,031,019
Wyoming	11-67	1,987	1,911,794
Puerto Rico	8-68	10,492	8,140,911
Total		666,304	$608,659,445

[a] Amount the Office of Education agreed to insure, not the actual amount of loans disbursed.

STUDENT LOAN INSURANCE FUND

OUTSTANDING PRINCIPAL BALANCES

SUBJECT TO REINSURANCE PROVISION

AS OF JUNE 30, 1970

Location	Effective date of reinsurance agreement	Balance (note a)
Arkansas	9-68	$ 6,418,824
Connecticut	12-68	77,129,579
District of Columbia	9-68	3,208,676
Georgia	12-68	27,892,743
Illinois	9-69	113,565,841
Louisiana	7-69	14,784,449
Maine	8-69	14,823,779
Maryland	8-69	11,367,729
Massachusetts	9-68	62,759,449
Michigan	2-69	29,589,720
Missouri	8-69	9,433,542
Nevada	10-69	483,487
New Hampshire	9-68	6,831,570
New Jersey	12-68	98,788,673
New York	9-68	419,306,083
North Carolina	8-69	6,980,555
Ohio	6-69	40,209,763
Oklahoma	9-68	9,762,733
Oregon	9-68	16,221,946
Pennsylvania	9-68	168,653,514
Rhode Island	2-69	11,176,559
Tennessee	9-68	17,910,549
Vermont	5-69	2,325,777
Wisconsin	9-68	16,654,670
Total		$1,186,280,210

[a]Balances were estimated by the Office of Education.

DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE
WASHINGTON, D.C. 20201

OFFICE OF THE SECRETARY

OCT 20 1971

Mr. Henry Eschwege
Associate Director
U.S. General Accounting Office
Washington, D.C.

Dear Mr. Eschwege:

The Secretary has asked me to reply to your letter dated August 25, 1971, pertaining to the General Accounting Office draft report to the Congress entitled "Examination of Financial Statements of the Student Loan Insurance Fund, Fiscal Year 1970." The enclosed comments set forth the actions taken or planned on the matters discussed in the report.

Sincerely yours,

James B. Cardwell
Assistant Secretary, Comptroller

Enclosure

Department of Health, Education and Welfare Comments Pertinent to the Draft of Report to the Congress of the United States by the Comptroller General of the United States on the Examination of Financial Statements of the Student Loan Insurance Fund, Fiscal Year 1970 B-164031(1)

OVERVIEW OF GAO REPORT

GAO's report indicates that they believe that the Department needs to improve and strengthen (i) its system for recording insurance premiums billed to and collected from lenders, (ii) the recording of payments for loan default claims resulting from ordinary bankruptcy, and (iii) controls over cash receipts for the Student Loan Insurance Fund.

Our specific comments on each of GAO's recommendations follow:

GAO RECOMMENDATIONS

1. The Office of Education should improve its system for recording insurance premiums billed to lenders and collected from lenders to ensure that actual year-end data is available showing accounts receivable and insurance premium income applicable to insured loans made during the fiscal year.

DEPARTMENT COMMENTS

Our computer system is now programmed to make available, upon request, the amount billed (by Fiscal Year) to each lender for that particular year.

However, as a back-up in case the system is unable to function properly, we plan to ask each lender to submit separate Lenders Manifest, OE FORM 1151, for all disbursements up to June 30. Uniquely identified, the 1151 will be requested by July 15 and will be processed separately to reflect the end of the fiscal year disbursements.

These actions, we believe, will ensure that actual year-end data is available showing accounts receivable - and by the same token - will help assure that related premium income is properly recorded.

2. Record payments for loan default claims resulting from ordinary bankruptcy of the borrowers as an expense rather than loans receivable.

DEPARTMENT COMMENTS

We concur that ordinary bankrupts should be expensed or charged off. We plan to do so within 12 months of the date of the bankrupt's discharge, however, rather than to expense them upon payment of loan default claims. To do otherwise, additional accounting would be required for each account on which recoveries are made. These recoveries occur because a small percentage of bankrupts possess assets for distribution to creditors. Some reassume their obligations after bankruptcy discharge, particularly those students who have need of student loans to complete their education. Therefore, since our experience has shown that these recoveries and reassumptions normally take place within 12 months of the student borrower's discharge in bankruptcy, it appears reasonable to expense them after this time period has elapsed.

3. Strengthen the controls over cash receipts for the Student Loan Insurance Fund by preparing a listing of checks as they are received and promptly depositing the checks with Treasury.

DEPARTMENT COMMENTS

We concur with this recommendation. Action has been taken to obtain the staff required for its implementation. The necessary procedures are also being developed.

PRINCIPAL OFFICIALS OF THE DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE HAVING RESPONSIBILITY FOR THE ACTIVITIES DISCUSSED IN THIS REPORT

	Tenure of office	
	From	To
SECRETARY OF HEALTH, EDUCATION, AND WELFARE:		
Elliot L. Richardson	June 1970	Present
Robert H. Finch	Jan. 1969	June 1970
COMMISSIONER OF EDUCATION		
Sidney P. Marland, Jr.	Dec. 1970	Present
Terrel H. Bell (acting)	June 1970	Dec. 1970
James E. Allen, Jr.	May 1969	June 1970

U.S. GAO, Wash., D.C.

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