

# Session #27

## Foreign Schools Audit and Financial Statements

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# Session Agenda

- General Requirements
- Foreign Institution Compliance  
Audit Reporting Requirements
- Compliance Audit Resolution
- Audited Financial Statements and  
Standards of Financial Responsibility

# Foreign Institution Audits

- Requirements
  - Two types of audits required
    - Audited Financial Statements
    - Compliance Audits
- Type of compliance audits and financial statements based on institution type and annual Federal Student Aid funding

# Foreign Institution Audits

- *Foreign School Audit Guide*  
Published by Office of Inspector General (OIG)
  - OIG is agency watchdog
- Two types of audits
  - Financial Statement Reporting Requirements
  - Compliance Audit Reporting Requirements

FOREIGN SCHOOL AUDIT GUIDE



<http://www2.ed.gov/about/offices/list/oig/nonfed/sfa.html>

U.S. DEPARTMENT OF EDUCATION  
Office of Inspector General

# Foreign Institution Audits – The Players

- 34 C.F.R. Part § 668.23 Subpart B

Definition of an Independent Public Auditor (IPA)

*(a) For purposes of this section, the term independent auditor refers to an independent certified public accountant or a government auditor. To conduct an audit under this section, a government auditor must meet the Government Auditing Standards qualification and independence standards, including standards related to organizational independence.*



# Foreign Institution Audits – The Players

- 34 C.F.R. Part § 668.23 Subpart B  
Definition of an Institution

*(a)(2) An institution that participates in any Title IV, HEA program must at least annually have an independent auditor conduct a compliance audit of its administration of that program and an audit of the institution's general purpose financial statements.*

# Foreign Institution Audits – The players

- The Department's role is to ensure a foreign institution demonstrates that it satisfies the Department's standards of administrative capability and financial responsibility, in part, by annually submitting audited compliance reports, as required by 34 C.F.R. § 668.23.

# Audit Due Dates

- Compliance Audit **and** Audited Financial Statements are due no later than six (6) months after the last day of the institution's fiscal year

## Audit Submission Address

U.S. Department of Education  
Federal Student Aid, School Eligibility Channel  
Document Receipt and Control Center  
830 First Street, NE, Room 7111  
Washington, D.C. 20202-5340

Phone for shipping label: 1-202-377-3168



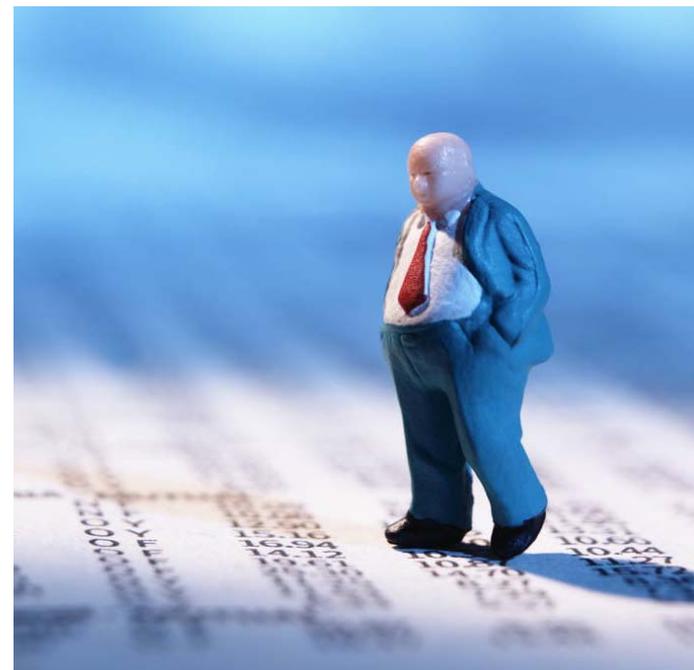
# Compliance Audits

- Compliance audits performed in accordance with ED OIG's Foreign School Audit Guide and *US Government Auditing Standards*
- Standard Compliance Engagement is an examination level engagement
- Alternative Compliance Engagement is an agreed upon procedures engagement
- Covers School Fiscal Year
- Must cover all Title IV, HEA program transactions since last audit



# Student Listing for Audit

- *Foreign School Audit Guide* requires independent public accountants to receive student listing
- Listing contains information for the IPA to conduct their audit:
  - Students with Loans Originated/Certified During Fiscal Year
  - Amount of Loan Certified
  - Total Amount of Loans Certified for All Students



# Student Listing for Audit

- The Student Listing can be requested within NSLDS, under the Report Tab
- Report name is SCHLL1 – School Loan List
- Enter the criteria for the fiscal year to be audited and submit
- The report will be available within 1-3 days in your EDConnect/TG mailbox
- For CPS/SAIG technical assistance, please call at +1-800-330-5947 or e-mail [CPSSAIG@ed.gov](mailto:CPSSAIG@ed.gov)
- For NSLDS technical assistance, please call 785-838-2141 or [nslds@ed.gov](mailto:nslds@ed.gov)



# Compliance Audits – For Audits Due On Or After 07/01/2011

Title IV Funds Received During Most Recent Fiscal Year	Public & Private Non-Profit	For-Profit
\$500,000 +	Standard Compliance Audit Submit Annually	
Less than \$500,000	Alternative Compliance Audit Submit Annually	Standard Compliance Audit  Submit Annually
	Alternative Compliance Audit may cover up to 3 fiscal years <b>IF</b> <ul style="list-style-type: none"> <li>• Receive &lt; \$500,000 in most recent FY period</li> <li>• Fully Certified</li> <li>• Has submitted timely acceptable compliance audits for two consecutive years and has no history of late submissions since then</li> <li>• Notified by ED</li> </ul>	

**NOTE:** If a foreign institution has an administrative capability or compliance reporting problem, the Secretary may require the compliance audit to be performed at a higher level of engagement, and may require a compliance audit to be submitted annually.



# Compliance Audits

- If, after receiving notification of eligibility for 3-year Alternative compliance audit, FY funding exceeds \$500,000, school must submit within six months of FY end
  - standard compliance audit and
  - alternative compliance audit(s) for prior FY period(s)

# Compliance Audits

- IPAs must design and perform procedures that can be reasonably expected to detect significant fraud or other illegal acts. To do this, IPAs must be aware of fraud and high risk areas and must recognize any basic weaknesses in internal control. Examples of some high risk indicators that IPAs may encounter while performing compliance engagements are provided in section 1.5.1. An IPA must exercise due professional care when pursuing any indication of fraud or other illegal acts, so potential future investigations or legal proceedings are not compromised.
- If any fraud or any other illegal act is detected, the IPA must report it immediately to the ED Office of Inspector General, Investigation Services (OIG/IS):

Assistant Inspector General for Investigation

U.S. Department of Education

400 Maryland Avenue, SW

MES, Room 4122

Washington, D.C. 20202-1510 USA

Phone: 202-205-8762 Fax: 202-205-9449



# Top 10 Audit Findings

- Student Confirmation Report Filed Late/Not Filed/Not Retained/Inaccurate
- Information in Student Files Missing/Inconsistent
- Lack of Administrative Capability
- Improper Certification of FFEL
- Attendance Records Missing/Policy Inadequate

# Top 10 Audit Findings (con't)

- Entrance/Exit Counseling Deficiencies
- Enrollment Status Not Verified Before Disbursement
- Maximum Annual or Cumulative FFEL Award Exceeded
- Return of Title IV (R2T4) Calculation Errors
- FFEL Cost of Attendance Not Documented/Incorrect

# Compliance Audit Resolution

- FSA's Program Compliance Office resolves compliance audits
  - Compliance audits help institutions identify errors and implement corrective actions to prevent their recurrence
- Preliminary Audit Determination Letter may be sent to school requesting additional information detail and status of corrective actions taken

# Compliance Audit Resolution (cont.)

- A Final Audit Determination Letter resolves the deficient audit
  - May establish monetary liabilities to make the Department “whole” for improper costs incurred by ED due to school error
  - Identifies record-keeping requirements and possible sanctions if findings are repeated
  - Identifies appeal rights, if a monetary liability is asserted
- A school with serious compliance deficiencies or recurring deficiencies may be referred for fine or other administrative action

# Foreign School Assessment

- Please visit <http://ifap.ed.gov/ForeignSchoolInfo/ForeignSchoolInfo.html> to either assist you in creating a new policy and procedure or to test your current policies and procedures to ensure compliance with Title IV, HEA Program

# Audited Financial Statements and Standards of Financial Responsibility



# Financial Statement Submission Requirements – 34 C.F.R. § 668.23 (h)

Title IV Funds Received During Fiscal Year	Public & Private Non-Profit		For-Profit
	Home Country GAAP	U.S. GAAP & GAGAS	Home Country GAAP & U.S. GAAP & GAGAS
\$10,000,000 +	Required annually, in English	Required annually, in English	Required annually, in English
\$9,999,999 - \$3,000,000	Required annually, in English	Required annually, in English, may omit for 2 consecutive years <u>after</u> U.S. GAAP & GAGAS audit	
\$2,999,999 - \$500,000	Required annually, in English	Not Required	
Less than \$500,000	Not required, <i>except during Initial Certification</i>	Not Required	
<p><b>NOTE:</b> If a foreign institution has a financial condition or financial reporting problem, the Secretary may require the foreign institution to submit audited financial statements in a manner specified by the Secretary.</p>			



# Standards of Financial Responsibility

## 34 C.F.R. Part 668, Subpart L

- § 668.171 – General
- § 668.172 – Financial Ratios
- § 668.173 – Refund Reserve Standards
- § 668.174 – Past Performance
- § 668.175 – Alternative Standards and Requirements

# General Standards

## § 668.171 – General (summary)

*Purpose.* To begin and to continue to participate in any Title IV, HEA program, an institution must demonstrate to the Secretary that it is financially responsible.

# General Standards

## § 668.171 – General (summary)

- General standards of financial responsibility.* An institution is considered financially responsible if the Secretary determines that the institution
- has equity, primary reserve, and net income ratios that yield a composite score of at least 1.5
  - has enough cash to return unearned Title IV HEA program funds
  - is current in its debt payments
  - is meeting its financial obligations

# General Standards

## § 668.171 – General (summary)

*Public institutions.* A foreign public institution is financially responsible if it:

- Notifies the Secretary that it is properly designated as a public institution and
- Provides appropriate documentation and
- Is not in violation of a past performance requirement

# General Standards

## § 668.171 – General (summary)

*Audit opinions and past performance provisions.*

Even if an institution satisfies general standards, the institution is not financially responsible if

- adverse, qualified, or disclaimed opinion present in the audited financial statements, or the auditor expresses doubt about ongoing concern, or
- the institution or its officials/owners violated a Title IV, HEA program requirement and they owe a liability that is not being repaid



# General Standards

## § 668.171 – General (summary)

*Administrative actions.* If an institution is not financially responsible under general or alternative standards, or if it does not submit financial and compliance audits by the date permitted and in the manner required, the Secretary may—

- Fine the institution, or limit, suspend, or terminate the institution's participation in the Title IV, HEA programs, or
- Revoke the participation of a provisionally certified institution



# Financial Ratios

## Composite Score

Weighted numeric score of financial responsibility derived from audited financial statement data using three financial ratios:

- Primary Reserve Ratio
- Net Income Ratio
- Equity Ratio

# Financial Ratios

## Primary Reserve Ratio

Measures a school's expendable or "liquid" resources based on its overall operating size. Determines a margin or cushion against adversity.

# Financial Ratios

## Primary Reserve Ratio (cont.)

Foreign For-Profit Institutions:

Adjusted Equity/Total Expenses

(Adjusted Equity = Total Equity – intangible assets – unsecured related party receivables – PP&E + post employment and retirement liabilities + all debt retained for long term purposes)

Foreign Private, Non-Profit and Public Institutions :

Expendable Net Assets/Total Expenses

(Expendable Net Assets = Unrestricted Net Assets + Temporarily Restricted Net Assets – annuities, term endowments, and life income funds that are temporarily restricted – intangible assets – net PP&E + post-employment and retirement liabilities + Long term debt – unsecured related party receivables)

# Financial Ratios

## Equity Ratio

Represents a measure of an institution's capital resources and its ability to borrow. The Equity Ratio provides a measure of the amount of an institution's assets that are subject to claims of third parties.

# Financial Ratios

## Equity Ratio (cont.)

For Foreign For-Profit Institutions:

### Modified Equity / Modified Assets

- **Modified Equity = Total Equity – Intangible Assets – Unsecured Related Party Receivables**
- **Modified Assets = Total Assets – Intangible Assets – Unsecured Related Party Receivables**

For Private, Non-Profit Institutions:

### Modified Net Assets / Modified Assets

- **Modified Net Assets = Unrestricted Net Assets + Temporarily Restricted Net Assets + Permanently Restricted Net Assets – Intangible Assets – Unsecured Related Party Receivables**
- **Modified Assets = Total Assets – Intangible Assets – Unsecured Related Party Receivables**

# Financial Ratios

## Net Income Ratio

Represents a measure of an institution's profitability. The Net Income ratio provides a direct measure of an institution's ability to operate within its means.

# Financial Ratios

## Net Income Ratio (cont.)

### For Foreign For-Profit Institutions:

Net Income Before Taxes/Total Revenues

### For Foreign Public and Private, Non-Profit Institutions:

Change in Unrestricted Net Assets/Total Unrestricted Revenue

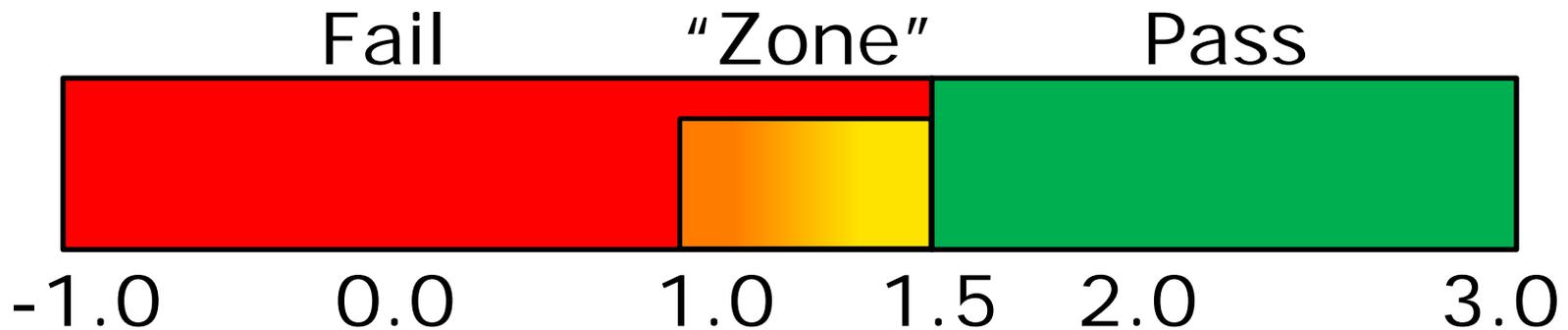
# Financial Ratios

- “Strength factors” are applied to individual ratio scores
- “Relative weights” are applied to the strength factor scores

# Financial Ratios

Lastly, the weighted scores are added together to create the composite score. Composite scores can range from negative 1.0 through positive 3.0.

Any score less than 1.5 is a failing score, but some schools fall in the "zone" with a score between 1.0 and 1.4



# Alternatives

## Participating Institutions

- Zone Alternative

(score 1.0 – 1.4, not exceed 3 consecutive years), Zone reports, Method of Payment HCM-1 & audit attestation

- Provisional Certification

10% LOC (minimum), Provisional certification, Zone reporting requirements, Restricted Method of Payment HCM-1 or HCM-2, audit attestation

- Letter of Credit only

50% LOC (minimum), can be considered financially responsible. No “Zone” reporting, no Method of Payment restrictions, no audit attestation

# Alternatives

## New/Reinstatement Institutions

- Letter of Credit only

50% LOC (minimum), can be considered financially responsible. No "Zone" reporting, no Method of Payment restrictions, no audit attestation



# Alternatives

- Institutions that participate under the Zone or Provisional Certification must adhere to “Zone” reporting requirements
  - Must self-report certain financial events
    - Adverse action
    - Bankruptcy filing
    - Realization of contingent liability
    - Violation of any loan agreement
    - Failure to make payment on debt obligation
    - Withdrawal of owner’s equity/net assets
    - Extraordinary losses
  - Report within 10 days of occurrence
  - May report current/future operations or submit of financial statements early



# Government Guaranty

## Foreign Public Institution – Letter

- Notifies the Secretary that it is designated as a public institution by the country or other government entity that has the legal authority to make that designation
- Provides documentation from an official of that country or other government entity confirming that the institution is
  - a public institution and
  - is backed by the full faith and credit of the country or other government entity

# Government Guaranty

## Foreign Public Institution

- Public institution with documented government guaranty is not required to participate under an alternate financial responsibility standard (LOC/provisional /zone), even if it has a failing score (less than 1.5)
- Government guarantee letter **does not** exempt school from U.S. GAAP/GAGAS reporting

# Other Compliance Issues

- Late Submission of Audits and Financial Statements

# Questions?

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