

Information Item

Joint Meeting of the CSAC and EDFUND Audit Committees

Internal Audit Update

A summary is provided which describes the completed audits, audits in progress and other activities performed by EDFUND's Internal Audit staff during the period of November 21, 2006 through January 25, 2007.

A tracking spreadsheet is also provided to keep the Committees apprised of overall progress in meeting the audit plan that was approved in November 2006.

Recommended Action:

No action pertaining to this agenda item is required.

Responsible Staff: Diane Manning
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Internal Audit Activities Update November 21, 2006 through January 25, 2007

Audit Completed - Pending Validation and Receipt of Management Response

Business Continuity Management Program

Internal Audit released the *Business Continuity Management Program Review* draft report to EdFund's Finance & Administration Division and Technology Solutions & Services Division on January 12, 2007 for staff's final validation of Internal Audit's understanding of the applicable business processes and for management to develop their responses to the audit recommendations. Internal Audit anticipates that the final report will be issued to the Joint Audit Committee in early February 2007.

The Business Continuity Management Program Review is an audit of the activities performed by EDFUND staff in developing and maintaining a program to help ensure the maintenance and recovery of critical business operations and systems in the event of a disaster, including but not limited to a technological failure, terrorism, human errors or a natural disaster such as an earthquake or flood.

Internal Audit compared EDFUND'S current practices in developing and managing its Business Continuity Management Program against industry best practices. Specifically, Internal Audit reviewed the processes for preparing the business impact analysis, risk assessment and the development and maintenance of the business continuity and disaster recovery plans. Internal Audit also reviewed the processes performed by EDFUND staff for testing the business continuity and disaster recovery plans and the incident management and escalation processes designed to ensure resumption of systems and business operations during adverse circumstances.

Audits in Progress

Form 2000

This is an audit of the annual Form 2000 filing process, which is the document that all guaranty agencies participating in the FFEL Program are required to file with the U. S. Department of Education. The form is used to report collection activities, claim reimbursements and the status of loans in the guaranty agency's loan portfolio (e.g., loans in good standing, defaulted loans, subrogated loans, etc.)

As part of this audit, Internal Audit is reviewing processes for the creation of selected lines on the FAPS AR Guaranty Agency Financial Report and preparation and submission of AR Form 2000, including the review and approval of the form. Internal Audit will also review the processes for resolving errors from the Department resulting from the Form 2000 submission and the retention of documentation supporting the filing.

Internal Audit is currently executing the test procedures associated with this audit. The completion date of this audit has been rescheduled for late February 2007 since additional IT audit resources were necessary to address the findings in the Business Continuity Management Program internal audit.

Loan Transfer Process

This audit includes a review of the processes performed by EDFUND's Settlement Unit when transferring loans out of EDFUND/CSAC's loan portfolio as a result of consolidation, rehabilitation and subrogation. As part of this audit, Internal Audit will evaluate compliance with applicable statutory regulations and internal procedures for determining and monitoring eligibility for consolidation, rehabilitation and subrogation and the subsequent transfer of such loans to a new lender, the lender's servicer, or the U.S. Department of Education.

Internal Audit is currently executing the test procedures associated with this audit. The anticipated completion date of this audit is March 2007.

Follow-Up Activities of Completed Audits

Internal Audit performed follow-up audit activities to evaluate management's progress towards implementing the recommended actions identified as part of previously issued audit reports. The status of each recommended action was determined based on discussions with key personnel, observing procedures performed, and/or reviewing supporting documentation.

The following follow-up audits were conducted during the current reporting period:

Table Maintenance

Internal Audit performed an initial follow up review in March 2006 to ensure that the recommendations identified as part of this audit had been implemented. At that time, only three of the eight items recommended by Internal Audit had been addressed. The remaining items, which involved developing and implementing companywide processes and procedures for performing and reviewing table maintenance activities and developing tools and implementing processes to facilitate user access reviews, had not been implemented. Therefore, Internal Audit performed a second follow up in October 2006. All remaining actions recommended by Internal Audit were implemented; therefore, Internal Audit considers this review closed.

Data Center Operations

Internal Audit performed an initial follow up review in February 2006 to ensure that the recommendations identified as part of this audit had been implemented. At that time, all actions recommended by Internal Audit were completed with the exception of one outstanding item, which dealt with developing service level agreements (SLAs) between TSS and the appropriate business units. Internal Audit performed a second follow up in December 2006 and determined that this recommendation remained partially incomplete. As a result, the VP of Audit Services escalated this item to the President for resolution. This item was subsequently resolved by the appropriate parties prior to any action being required from the President. Internal Audit considers this review closed.

Manual Journal Entry Process

This follow up review was completed in December 2006. Two of the five items recommended by Internal Audit have been addressed as of the date of the follow up. Three of the five open items involve developing and implementing comprehensive processes and procedures for processing manual journal entries, including defining the acceptable types of documentation that must be maintained as support for the journal entries.

Internal Audit will perform a second follow up in April 2007 to determine if these items have been addressed. At that time, if it is determined that the recommended actions have not been completed and that the resulting level of risk assumed by management is unacceptable as a result of not addressing such items, the VP of Audit Services will escalate the matter to the President.

Remittance Process

This follow up review was completed in December 2006. Two of the four items recommended by Internal Audit have been addressed as of the date of the follow up. Of the two items that remain open; one involves enhancing the remittance process to require all incoming cash receipts to be processed in dual custody. As of the date of Internal Audit's follow up review, Finance staff revised their procedures to require processing receipts in dual custody but had not yet fully implemented the revised procedure. The second open item addresses developing and implementing a companywide process for requesting, approving, and processing manual adjustments to borrowers' accounts, referred to as "CMOs". As part of the follow up review, Internal Audit identified three instances out of ten tested where the CMO request was approved by an individual that did not have proper signing authority. Finance staff indicated that these errors appear to be the result of the business units having misinterpreted certain sections of the revised procedures and the CMO form. Finance staff are working with the business units to address the ambiguities and update the procedures and CMO form accordingly.

Internal Audit will perform a second follow up in March 2007 to determine if these items have been addressed. At that time, if it is determined that the recommended actions have not been completed and that the resulting level of risk assumed by management is unacceptable as a result of not addressing such items, the VP of Audit Services will escalate the matter to the President.

Other Activities

Quality Assurance Review Preparation

The Institute of Internal Auditors (IIA) standards require that the VP of Audit Services "develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit activity and continually monitor its effectiveness. This program includes periodic internal and external quality assessments and ongoing internal monitoring." Internal assessments include ongoing review of the performance of internal audit activity and periodic reviews through self-assessments, while external reviews are conducted at least once every five years by a qualified independent

reviewer. The intent of the internal and external assessment process is to provide assurance that the internal audit activity conforms to IIA standards and the Code of Ethics.

One of the audit recommendations in the BSA Performance Audit Report, issued in April 2006, states that an external assessment of the internal audit unit should be performed to ensure compliance with (IIA) standards. Internal Audit anticipates engaging the services of an independent reviewer to conduct an external review of its audit activities no later than during the third quarter of FY 2007-08.

The AVP of Audit Services and two Senior Internal Auditors recently attended a training seminar sponsored by the IIA designed to help organizations prepare for an external assessment review. Based on this training, Internal Audit received validation that its current practices are consistent with the internal audit standards, specifically with regard to the audit planning process, including the development of the risk assessment and audit plan, and the report preparation and follow up review processes. There are, however, additional procedures and tools that Internal Audit became aware of through this training that audit management and staff intend to implement during the current fiscal year to enhance its internal assessment processes and help prepare for the external assessment.

Internal Audit Activity Tracking Spreadsheet

The chart below summarizes Internal Audit's progress towards completing the audit activities on the revised audit plan for Fiscal Year 2005-06 and 2006-07 as approved by the Joint Audit Committee in November 2006. The audit statuses shaded reflect changes since the last update to the Audit Committee.

Internal Audit Activities	Audit Status	
	2005 - 06	2006 - 07
A. Follow- Up Reviews On Previously Issued Audits <i>The follow-up reviews listed below were not individually identified in the initial approved audit plan. Instead, a single line item titled "Follow-Up Audits" was presented with the total estimated number of hours for performing all follow-up reviews.</i>		
<u>Data Center Operations – Follow Up</u> Five of Internal Audit's six recommendations cited in the audit report issued in September 2005 were addressed as of the date of the initial follow up. Internal Audit performed a second follow up in December 2006 and determined that a portion of the one remaining recommendation had not been implemented. As a result, the VP of Audit Services escalated this item was to the President for resolution. This item, however, was subsequently resolved by the appropriate parties prior to requiring any action by the President. Internal Audit considers this review closed.	Initial Follow Up Complete	Follow Up Complete; Audit Closed
<u>Default Claims Adjudication – Follow Up</u> All actions recommended in the audit report issued in June 2005 have been addressed, therefore, this audit is considered closed.	Follow Up Complete; Audit Closed	
<u>External Collections – Follow Up</u> All actions recommended in the audit report issued in March 2005 have been addressed, therefore, this audit is considered closed.	Follow Up Complete; Audit Closed	
<u>Internal Collections – Follow Up</u> All actions recommended in the audit report issued in July 2005 have been addressed, therefore, this audit is considered closed.	Follow Up Complete; Audit Closed	

Internal Audit Activities	Audit Status	
	2005 - 06	2006 - 07
<p><u>Manual Borrower and Loan Status Updates – Follow Up</u></p> <p>All actions recommended in the audit report issued in August 2005 have been addressed, therefore, this audit is considered closed.</p>	<p>Follow Up Complete; Audit Closed</p>	
<p><u>Manual Journal Entries – Follow Up</u></p> <p>Two of the five items cited in the audit report issued in June 2006 were addressed as of the date of the initial follow up in December 2006. The three remaining items involve developing and implementing comprehensive processes and procedures for processing manual journal entries, including defining the acceptable types of documentation that must be maintained as support for the journal entries. Internal Audit will perform a second follow up in April 2007 to determine if these items have been addressed.</p>		<p>Initial Follow Up Complete; Second Follow Up Scheduled</p>
<p><u>Network Security – Follow Up</u></p> <p>A follow up to the recommendations cited in the audit report issued in July 2006 is scheduled for completion during FY 2006-07.</p>		<p>Follow Up Scheduled</p>
<p><u>Post Default Loan Discharges – Follow Up</u></p> <p>A follow up to the recommendations cited in the audit report issued in September 2006 is scheduled for completion during FY 2006-07.</p>		<p>Follow Up Scheduled</p>
<p><u>NSLDS Reporting and Lender Portfolio Reconciliation – Follow Up</u></p> <p>A follow up to the recommendations cited in the audit report issued in October 2006 is scheduled for completion during FY 2006-07.</p>		<p>Follow Up Scheduled</p>
<p><u>Property Survey Review – Follow Up</u></p> <p>All actions recommended in the audit report issued in January 2005 have been addressed, therefore, this audit is considered closed.</p>	<p>Follow Up Complete; Audit Closed</p>	

Internal Audit Activities	Audit Status	
	2005 - 06	2006 - 07
<p><u>Remittance Process – Follow Up</u></p> <p>Two of the four items cited in the audit report issued in September 2005 were addressed as of the date of the initial follow up in December 2006. Of the two items that remain open; one involves enhancing the remittance process to require all incoming cash receipts to be processed in dual custody. Finance staff have modified their procedures to require processing receipts in dual custody, but had not yet fully implemented the revised procedure as of the date of Internal Audit's follow up review. The second open item addresses developing and implementing a companywide process for requesting, approving and processing manual adjustments to borrowers' accounts, referred to as "CMOs". Internal Audit will perform a second follow up in March 2007 to determine if these items have been addressed.</p>		<p>Initial Follow Up Complete; Second Follow Up Scheduled</p>
<p><u>Table Maintenance – Follow Up</u></p> <p>Internal Audit performed an initial follow up review in March 2006 to ensure that the recommendations identified as part of this audit had been implemented. At that time, only three of the eight items recommended by Internal Audit had been addressed. The remaining items, which involved developing and implementing companywide processes and procedures for performing and reviewing table maintenance activities and developing tools and implementing processes to facilitate user access reviews, had not been implemented. Therefore, Internal Audit performed a second follow up in October 2006. All remaining actions recommended by Internal Audit were implemented; therefore, Internal Audit considers this review closed.</p>	<p>Initial Follow Up Complete</p>	<p>Follow Up Complete; Audit Closed</p>

Internal Audit Activities	Audit Status	
	2005 - 06	2006 - 07
B. High Risk Audits		
<p><u>Budget Development and Management</u></p> <p>The Finance and Administration Division recently implemented the budget module in Oracle Financials, which eliminated a number of manual processes previously performed in developing the budget. Additionally, the implementation of zero based budgeting helped strengthened internal controls by requiring management to provide detailed justifications for virtually all expenses. Budgets are subject to extensive levels of review by AVPs, VPs, EMT, the Finance Committee, the Board of Directors, Commission staff, and the Commission. As a result, Internal Audit determined that budget development and management are not a high risk area but will re-evaluate these activities when developing the next two year internal audit plan.</p>		No Longer Considered Necessary For This Two Year Audit Plan
<p><u>Business Continuity Management Program</u></p> <p>This audit was started during the last quarter of FY 2005-06 and was anticipated to be completed during the first quarter of FY 2006-07. Due to the number of findings, the draft report was provided to management instead in January 2007 for final validation and for management to develop responses to the recommendations. Internal Audit anticipates this report to be released to the Audit Committee in February 2007.</p>		Complete, Pending Validation & Management Responses
<p><u>Change Management</u></p> <p>This audit was not included in the initial audit plan. Based on knowledge gained by Internal Audit staff over the last year, it appears that a comprehensive change management process does not exist. The potential high risk to EDFUND due to the lack of an effective change management process warrants an audit.</p>		Scheduled for Completion
<p><u>Collection Cost Recovery</u></p> <p>This audit was rescheduled to FY 2006-07 due to audit resource constraints with the resignation of a Senior Internal Auditor during FY 2005-06.</p>		Scheduled for Completion

Internal Audit Activities	Audit Status	
	2005 - 06	2006 - 07
<p><u>Data Maintenance (Loan Operations and Default Mgmt)</u></p> <p>This audit was deferred to FY 2006-07 to allow Loan Operations and Default Management adequate time to accumulate documentation using the newly implemented data maintenance processes, which Internal Audit will test.</p>		Scheduled for Completion
<p><u>Electronic Borrower and Loan Status Updates</u></p> <p>Internal Audit recently completed the NSLDS Reporting and Lender Portfolio Reconciliation audit which addressed key internal controls that would have been tested during the Electronic Borrower and Loan Status Updates audit. Audit Services Management, therefore, has determined that this audit would not provide significant additional assurances and will re-evaluate the business activities when developing the next two year audit plan.</p>		No Longer Considered Necessary For This Two Year Audit Plan
<p><u>Forms 2000 Reporting</u></p> <p>This audit was started during the last quarter of FY 2005-06 and is scheduled for completion during the second quarter of FY 2006-07.</p>		In Progress
<p><u>Information Security Program</u></p> <p>EDFUND experienced turnover in the Information Security Officer (ISO) position during FY 2005-06. As a result, Internal Audit deferred this audit to provide the new ISO, who was hired in June 2006, an opportunity to refine the Information Security Program. Internal Audit anticipates conducting this audit during the next two year audit cycle which ends September 30, 2009.</p>		Deferred to Subsequent Year
<p><u>Loan Guarantee Process</u></p> <p>Audit Services Division management redirected the Senior Information System Auditor scheduled to perform this audit to assist with the technical components of two CSAC Cal Grant audits in FY 2005-06 and deferred this audit to FY 2006-07.</p>		Scheduled for Completion

Internal Audit Activities	Audit Status	
	2005 - 06	2006 - 07
<p><u>Loan Transfer Process</u></p> <p>This audit was started during FY 2005-06; however the Senior Internal Audit assigned to the effort resigned from EDFUND prior to completing the audit. By the time Internal Audit management filled this vacancy and was prepared to resume the audit, the business unit impacted by this audit requested that the effort be postponed to FY 2006-07 due to workload issues with which Audit Services Division management concurred.</p>		In Progress
<p><u>Manual Journal Entries</u></p> <p>Audit complete; report issued during June 2006.</p>	Complete	
<p><u>Network Security and Firewall</u></p> <p>Audit complete; report issued during July 2006. This audit was initially scheduled for completion during FY 2006-2007, however, Internal Audit accelerated the timing of this effort due to the rescheduling of the Data Maintenance audit, as discussed above.</p>	Complete	
<p><u>NSLDS Reporting and Lender Portfolio Reconciliation</u></p> <p>Audit complete; report issued in October 2006.</p>	Complete	
<p><u>Post Default Loan Discharges</u></p> <p>Audit complete; report issued in September 2006.</p>	Complete	
<p><u>User Access</u></p> <p>Scheduled for completion during FY 2006-07.</p>		Scheduled for Completion
<p><u>Voluntary Flexible Agreement (VFA)</u></p> <p>The auditors from USED Region 9 recently completed an extensive review of the existing VFA. Additionally, EDFUND and USED have not yet finalized a renegotiated VFA prior to the beginning of FY 06-07. As a result, Internal Audit intends to defer this audit and will consider this area when developing the next two year audit plan.</p>		Deferred to Subsequent Year

Internal Audit Activities	Audit Status	
	2005 - 06	2006 - 07
<p><u>Wage Garnishments and Tax Offsets</u> Scheduled for completion during FY 2006-07.</p>		Scheduled for Completion
C. Required Audits		
<p><u>Conflicts of Interest</u> Legal Counsel is now reporting any reported conflicts of interest directly to the Joint Audit Committee as a standing agenda item; therefore, Internal Audit is no longer performing this activity.</p>	No Longer an Internal Audit Activity	No Longer an Internal Audit Activity
<p><u>Policy 009 Compliance – Employment of Applicants and Employees with Guaranteed Student Loans</u> FY 2005-06 audit completed; report issued in July 2006. This is an annual recurring compliance audit performed by Internal Audit. The FY 2006-07 audit is scheduled for completion.</p>	Complete	Scheduled for Completion
<p><u>Quarterly Review of Transactions on Employee FFEL Loans</u> Internal Audit performs this review each quarter of employees with FFEL Loans for which EDFUND provides guaranty services. This review stems from a BSA compliance audit finding which stated the need for additional controls to prevent employees from modifying or deleting their own records. Management's response to this finding stated that Internal Audit would periodically sample and review system activity on loans associated with EDFUND employees. Internal Audit does not issue audit reports summarizing the results of each quarterly review. Instead, the audit procedures performed and the results are included as part of the Policy 009 Compliance audit report.</p>	Complete	Scheduled for Completion