IBM Center for
The Business of Government

Risk Series

# Risk Management for Grants Administration

## A Case Study of the Department of Education


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The George Washington University and Keleher & Associates, LLC

Risk Series 2015

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# Foreword

On behalf of the IBM Center for The Business of Government, we are pleased to present this report, *Risk Management for Grants Administration: A Case Study of the Department of Education,* by Young Hoon Kwak and Julia B. Keleher, George Washington University.

Daniel J. Chenok

In this report, Kwak and Keleher examine the experience of the U.S. Department of Education in implementing risk management initiatives, which it initiated in 2001. During this period, the department created its Risk Management Service, and expanded that office in 2007. At the same time, the department also continued to refine and revise its risk management tools, and now uses two new tools: the State Score Cards and the Entity Risk Review. This report explains how these two tools are being used and provides examples of how risk management tools have been used to track the progress of two high risk grantees: Detroit Public Schools and Puerto Rico.

Kirsten Schroeder

Based on their examination of the Department of Education's experience, Young and Keleher present a series of lessons learned and recommendations for other agencies. A major lesson is that the use of an automated, data-driven risk assessment tool enabled the department to apply uniform and consistent risk assessment procedures and make better use of audit data. The authors also learned that effective risk management is an iterative process that requires thoughtful use of existing data sources and consistent efforts to incorporate new ones.

In looking ahead to how other federal agencies can successfully implement risk management activities, the authors caution that risk management practices may represent a major change for some agencies and should be accompanied by training and capacity-building programs. The authors also note that agencies should take advantage of the U.S. Office of Management and Budget's new risk management requirements as an action-forcing event to improve risk management in the award and oversight of federal grants in their agencies.

This report continues the IBM Center's long interest in risk management in the federal government. The following IBM Center reports have examined other approaches to risk management in government:

- Karen Hardy examined how chief financial officers and financial managers can guide their agencies in taking a more holistic approach to risk management by implementing an Enterprise Risk Management (ERM) system (*Managing Risk in Government: An Introduction to Enterprise Risk Management*).
- James Bailey developed a checklist to assist government managers in implementing improved control and auditing programs in response to the demand for greater fiscal accountability and transparency (*Strengthening Control and Integrity: A Checklist for Government Managers).*
- Tom Stanton examined how federal credit programs can more effectively manage the risk inherent in their loan portfolios (*Federal Credit Programs: Managing Risk in the Information Age).*

We hope that government leaders who are interested in implementing risk management initiatives will find the Department of Education's experience helpful and instructive as they strive to improve the management and oversight of federal funds.

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# Executive Summary

This report provides a case study of how the U.S. Department of Education (ED) developed increased capacity to design and employ risk management practices to improve grants management. The strategies and tools presented in this report can provide other federal agencies with a roadmap for establishing and/or enhancing the use of risk management practices in their organizations. The accomplishments realized at ED also demonstrate how managers and leaders can leverage risk management practices to comply with the new requirements set forth in the U.S. Office of Management and Budget's (OMB) Uniform Administrative Requirements.

Section One, "Introduction," presents an overview of ED and outlines its strategic goals and objectives. The department's strategic plan is discussed and its grant making functions are described. This section also examines how risk management supports the agency's efforts to realize its strategic goals and objectives.

Section Two, "Framework for Risk Management in Federal Agencies," provides an overview of risk management practices in federal agencies.

Section Three, "Department of Education's Approach to Risk Management," explains why risk management has become a central component in federal grant making at ED. The section begins with a description of new federal requirements for agencies to assess risk among potential grantees before making a grant award. Next, information on ED's approach to risk assessment is explained. The section then discusses risk management across the grant life cycle. The section concludes by highlighting how current practices of ED's Risk Management Service (RMS) satisfy OMB's new requirements to conduct risk assessments prior to making grant awards.

Section Four, "Operationalizing Risk Management at Department of Education," documents how ED has been able to continually improve its understanding and use of risk management practices. The agency's initial approach to risk management is presented and the refinements that have been made to this approach are described. This section also illustrates how increases in the availability of data on federal grants and grantees and the proliferation of new technology tools have facilitated the expansion of risk management practices at ED. This section includes descriptions of the various risk assessment tools RMS has developed to identify potential risk in ED's grant portfolio. The section concludes with a discussion of the future directions for enhancing ED's current risk assessment capacity.

Section Five, "Case Studies of Risk Management Across the Grant Life Cycle," presents two case examples that illustrate the application of risk management practices at ED. The authors describe how ED updated its longstanding approach to risk assessment to improve the effectiveness and efficiency of these business processes.

Section Six, "Lessons Learned and Recommendations," concludes with a summary of the lessons learned from ED's efforts to incorporate risk assessment and risk mitigation practices into grants management. The section presents recommendations on how federal agencies can enhance the effectiveness of their risk management efforts and comply with OMB's new Uniform Administrative Guidelines.

There are four lessons learned from ED's risk management practices:

- **Lesson One:** The department benefited by creating a defined and codified business process for managing risk in the department's grants portfolio.
- **Lesson Two:** The use of an automated, data-driven risk assessment tool enabled the department to apply uniform and consistent risk assessment procedures and make better use of audit data.
- **Lesson Three:** The department's success in implementing a department-wide enterprise risk management program required the creation of new internal policies and support from agency leadership.
- **Lesson Four:** Effective risk management is an iterative process that requires thoughtful use of existing data sources and ongoing efforts to incorporate new ones.

Based on the lessons learned from ED, other agencies trying to implement risk management practices should do the following.

- **Recommendation One:** Agencies should move to a data-driven system to collect and manage data that can be used to make risk assessments.
- **Recommendation Two:** Agencies should create tools and processes that facilitate program officers' interpretation of data and standardize the decision-making process.
- **Recommendation Three:** Agencies should take advantage of the opportunity that the new OMB requirements create for improving risk management in awarding and overseeing federal grants.
- **Recommendation Four:** The introduction of new risk management practices may represent change for some federal agencies and should be accompanied by training and capacity-building programs.

Managers and leaders in grant-making federal agencies can use the information presented in this report to improve or create new risk management practices. ED's example provides managers and leaders with important insight into how they should structure planning and implementation activities. It also highlights the importance of creating the infrastructure necessary to support the development and use of risk management policies and tools. Developing a better understanding of the experience of their colleagues at ED will enable federal grants managers in other agencies to develop risk management practices that result in more effective and compliant stewardship of federal funds among grantees.

# Introduction

## The Department of Education

The Department of Education's (ED) mission is to promote student achievement and preparation for global competitiveness by fostering educational excellence and ensuring equal access to education. In order to realize its mission, ED offers grants to individuals, institutions of higher education, local education, nonprofit, state education agencies, and other organizations.[1] Thirty-three years after its creation, ED dedicated its $68 billion budget in 2013[2] to:

- Establishing policies on federal financial aid for education and on the monitoring of those funds
- Making grants to states, school districts, and other organizations that provide education and related services
- Collecting data on America's schools and disseminating research
- Focusing national attention on key educational issues
- Prohibiting discrimination and ensuring equal access to education

## The Department's Strategic Goals and Objectives

ED has outlined six goals in its 2014–2018 strategic plan.[3] The first three goals, which focus on specific education program areas, are to:

- Increase college access, affordability, quality, and completion by improving postsecondary education and lifelong learning opportunities for youths and adults. The grant programs that support this goal are related to postsecondary education, career and technical education, and adult education.
- Improve the elementary and secondary education systems' ability to consistently deliver excellent instruction aligned with rigorous academic standards while providing effective support services to close achievement and opportunity gaps, and ensure that all students graduate high school and college. Elementary and secondary education grant programs support this goal.
- Improve the health, social, emotional, and cognitive outcomes for all children from birth through third grade, so that all children, particularly those with high needs, are on track to graduate from high school and college and to become career ready. To support this goal, ED is making new grants related to early childhood education.

The remaining three goals address the crosscutting efforts within ED. They are to:

- Increase educational opportunities for underserved students and reduce discrimination so that all students are well positioned to succeed

1. www.ed.gov
2. http://www2.ed.gov/about/overview/budget/budget14/summary/14summary.pdf
3. http://www2.ed.gov/about/reports/strat/index.html?src=ln

- Promote continuous improvement of the U.S. education system by enhancing the system's ability to continuously improve through better and more widespread use of data, research and evaluation, evidence, transparency, innovation, and technology
- Improve ED's organizational capacities to implement its strategic plan

Risk management falls within the scope of the last cross-cutting goal. Within this goal, ED has defined the strategic objective of improving the department's program efficacy through comprehensive risk management, and grant and contract monitoring.

## Federal Grant Making

The federal government's discretionary grant programs are intended to enable agencies to accomplish their strategic performance goals and objectives.[4] Federal agencies need to make effective use of grants management best practices and internal controls to ensure effective administration of these grant programs. In addition, agencies must maintain necessary policies and procedures to ensure compliance with applicable laws, regulations, and published priorities.

Federal agencies award discretionary grants through a competitive process. The government and the public expect the process of competing for federal grants to be fair, objective, efficient, and transparent. In addition, the process should be executed consistently across all grantees. Despite these expectations, a 2012 Government Accountability Office (GAO) study found that, when internal controls in grants management and oversight are weak, federal grant-making agencies face challenges in achieving program goals and ensuring the proper and effective use of federal funds.[5] This finding suggests that efforts to examine the discretionary grant-making process and identify opportunities for improvement would be beneficial to grant-making agencies.

## Goals and Objectives of Report

The goal of this report is to identify how risk management can be used to strengthen internal controls in grants management and improve grants administration practices in federal agencies. While risk management is widely used in the private sector, it is an emerging process in the federal space. It is becoming increasingly important for public sector leaders to understand risk management in the context of grants management for several reasons. First, the federal government uses grants to advance its policy goals. If risks in the grant-making process are not identified and managed, it is less likely that the grant programs will achieve the desired outcomes. Second, the amount of funds administered through federal grant programs continues to increase. It represented 20 percent of the federal budget in 2010. Given the large dollar value associated with federal grant programs, it is critical that federal employees have access to tools and practices that will ensure they are good stewards of these funds.

The authors believe that risk management has the potential to positively impact grants management and improve the effectiveness and efficiency of distributing federal funds. ED's decision to incorporate risk management practices into its strategic plan underscores the importance agency leadership is giving to this new practice. ED's experience provides other federal agencies with an opportunity to learn from its implementation of risk management and to identify best practices and approaches that can be replicated and/or scaled in their organizations.

4. http://www.gao.gov/products/GAO-12-1016
5. http://www.gao.gov/products/GAO-12-1016

# Framework for Risk Management in Federal Agencies

## Risk Management: Overview

Originally evolved from the financial sector, risk management encompasses all aspects of risk including financial, technical, managerial, and organizational risk. Practitioners and researchers have also used different words, that serve the same purpose such as "Uncertainty Management" (Ward and Chapman, 2003), "Surprise Management" (Smith and Merritt, 2002), and "Failure-Proof Management" (Kendrick, 2003). However, government agencies often manage risks in unstructured, disorganized, and random ways. Moreover, the agencies often do not understand the benefits of risk management and the implementation process to identify and mitigate risks.

In a report to the IBM Center for the Business of Government, Bailey (2010)[6] proposed a three-phased risk-management process for financial controls and integrity.

- **Phase One:** Government managers identify opportunity and threat outcomes. They prioritize the high-impact outcomes over the low-impact outcomes. The managers focus the organization's attention on the high-impact outcomes.
- **Phase Two:** Organizations manage resources and processes to achieve the high-impact opportunity outcomes and minimize high-impact threat outcomes.
- **Phase Three:** Government managers evaluate the high-impact outcomes. When management completes the evaluation, the process begins again.

In another report to the IBM Center, Hardy (2010)[7] describes the benefits and challenges of Enterprise Risk Management (ERM) in federal government. Benefits of ERM include:

- Gaining a cultural understanding of the importance of sustaining high credibility as an agency
- Affording the opportunity for agencies to make more educated decisions
- Increasing knowledge and understanding of risk across the organization
- Improving risk culture
- Aligning risks with agency/program goals and objectives
- Providing for a more efficient and effective means of managing risk
- Agreeing on core values and on the necessity for a broadly integrated risk management approach

6. http://www.businessofgovernment.org/sites/default/files/BaileyReport.pdf
7. http://www.businessofgovernment.org/report/managing-risk-government-introduction-enterprise-risk-management

## Risk Management: Key Definitions

**Risk:** "An event that has a potentially negative impact and the possibility that such an event will occur and adversely affect an entity's assets, activities, and operations."

**Risk Management:** "The continuous process of assessing risks, reducing the potential that an adverse event will occur, and putting steps in place to deal with any event that does occur. Risk management involves a continuous process of managing—through a series of mitigating actions that permeate an entity's activities—the likelihood of an adverse event and its negative impact. Risk management addresses risk before mitigating an action, as well as the risk that remains after countermeasures have been taken." Source: Government Accountability Office, Report # GAO-06-91, December 2005.

**Enterprise Risk Management (ERM):** "a process, effected by an entity's … management and other personnel, applied in a strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives" Source: COSO, 2004.

More information on definitions and other key elements of ERM frameworks can be found through commonly accepted ERM frameworks, including:

- COSO (Committee of Sponsoring Organizations of the Treadway Commission): www.coso.org
- ISO 31000 — Risk Management: http://www.iso.org/iso/home/standards/iso31000.htm

Hardy also describes the challenges of ERM which include:

- Providing the appropriate foundation, assessment, and management platform
- Insufficient sponsorship of ERM at the executive level
- Positioning ERM as a strategic management practice and not as an additional task
- Competing priorities—key ERM staff participate in various special projects and initiatives that are risk related but do not directly support the implementation of an ERM program
- Federal government regulations and requirements
- Lack of understanding about risk management
- Lack of qualified risk management professionals and expertise
- An internal competitive culture that is prone to "stovepiping"
- Aligning risk reward and incentive programs with strategic objectives

In his report to the IBM Center, Davenport (2008)[8] claims that government organizations and agencies use analytics to enable and drive their strategies and performance in an ever-more volatile and turbulent environment. But he also points out that analytics and fact-based decision making can make just as much or even more of a powerful contribution to the achievement of governmental missions as they can to the accomplishment of corporate business objectives.

The GAO Risk Management Framework was developed so that individual phases of the approach, such as risk assessment, do not become ends in themselves, but provide a full cycle of related activities: from strategic planning through implementation and monitoring.

8. http://www.businessofgovernment.org/sites/default/files/Strategic%20Analytics.pdf

The process is dynamic, and although the various phases appear to be linear, new information can be entered at any phase. The GAO framework can be used to inform agency officials and decision makers about the basic components of a risk management system or as a stand-alone guide. It is designed to be flexible in that the approach may be applied at various organizational levels, ranging from that of a department of a multiagency organization, down to that of a specific project or program. Because there is no one uniformly accepted approach to risk management, terms and activities may differ across organizations (GAO, 2005).

## Office of Management and Budget New Risk Management Requirements For Grant Recipients

The core mission of the Office of Management and Budget (OMB) is to serve the president of the United States in implementing his vision across the executive branch. OMB carries out its mission through five critical processes:

- Budget development and execution
- Management and oversight of agency performance
- Coordination and review of all significant federal regulations
- Legislative clearance and coordination
- Issuing Executive Orders and Presidential Memoranda to agency heads[9]

In 2013, OMB released the *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Administrative Requirements).* This new guidance represents an effort to more effectively focus federal resources and improve the performance and outcomes realized by federal agencies. The *Uniform Administrative Requirements* create a government-wide framework for ensuring effective fiscal management of federal grants. In addition, they reduce the administrative burden on grantees that receive awards by increasing the size of awards that will trigger annual audits.

The *Uniform Administrative Requirements* also present significant enhancements to the risk management practices federal agencies are required to perform. Under the new guidelines, federal agencies must review the risk associated with a potential recipient prior to making a federal grant award. This involves a review of audit data as well as information from the Do Not Pay system. This system includes information on criminal charges, suspensions, and debarments. Once these specific information sources have been reviewed, agencies are directed to examine additional relevant data and information and make a data-driven assessment of the following factors regarding potential grant recipients:

- Financial stability
- Quality of internal management systems
- History and/or record in complying with applicable reporting requirements and conformance to the terms and conditions
- Frequency of and capacity to resolve audit findings
- Ability to effectively implement statutory, regulatory, or other requirements imposed on nonfederal entities

9. http://www.whitehouse.gov/omb/organization_mission/

The *Uniform Administrative Requirements* also recommends that federal agencies consider programmatic factors such as:

- Previous experience with a grantee
- Size and complexity of the program
- Number of years the program has been in existence and the recency of any changes to programmatic or fiscal requirements
- Administrative requirements throughout the course of the grant life cycle
- Size of award

If federal agencies identify potential risk in connection with a particular grantee, the *Uniform Administrative Requirements* enables agencies to impose specific conditions on the grant award. Such conditions may include requiring:

- Payments as reimbursements rather than advance payments
- Submission of evidence of acceptable performance for a specific portion of the grant's period of performance
- Additional detailed financial reports
- Additional monitoring activities
- Grantee participation in technical assistance and/or whether they receive management assistance from ED and/or
- Additional prior approvals

# Department of Education's Approach to Risk Management

## Risk Management Service

The Risk Management Service (RMS), which is housed within the Office of the Deputy Secretary within ED, is responsible for ensuring that the agency provides effective oversight of its discretionary grants. To this end, RMS develops and coordinates an agency-wide risk management strategy. ED's risk management strategy focuses on:

- Ensuring high-quality management of ED's formula and discretionary grants
- Developing risk analysis tools and creating and codifying risk mitigation strategies
- Providing training that increases the agency's internal capacity to engage in risk management

Effective implementation of these strategies should enable grant-making program offices to administer grants in ways that bring about the realization of the intended education goals. In addition, these strategies promote prudent stewardship of public dollars.

For more than 25 years, ED has recognized the importance of assessing grantee risk. The Education Department General Administrative Regulations (EDGAR) establish how ED assesses and responds to risk. According to EDGAR, risk conditions are present if a grantee demonstrates:

- A history of poor performance or poor business practices
- Financial instability and/or
- Lack of a management system that meets the required financial management standards (EDGAR §§ 74.14 and 80.12)

ED incorporated the EDGAR risk assessment requirements into its Discretionary Grants Handbook (DGH).[10] The DGH requires program officers to ensure before awarding federal funds that grant recipients are competent, responsible, and committed to achieving grant objectives. Building on the EDGAR requirements, the DGH directs program officers to examine the following five factors when determining an applicant's ability to realize grant objectives:

- Applicant's financial stability
- Applicant's previous experience, if any, in administering federal grants
- Whether the applicant has adequate internal, fiscal and administrative controls (EDGAR §§ 74.21 and 80.21)
- Applicant's performance under other ED awards [EDGAR § 75.217 (d)(3)(ii)]
- Any adverse information regarding the applicant's officials or key employees that calls into question the applicant's ability to perform satisfactorily

10. http://www2.ed.gov/policy/gen/leg/foia/foia-hb-01.pdf

The DGH also establishes the requirement that program officers examine grantee audits before issuing a grant award. Audits, as referred to in the DGH, could be federal or nonfederal. Federal audits are those conducted by the GAO or the Office of the Inspector General (OIG) within ED. ED staff considers performance issues identified through GAO or OIG audits to be valid and meaningful. The investigations conducted by these offices tend to have a narrow scope, involve extensive data collection and analysis, and produce accurate findings. As such, they provide program officers with valuable insights into potential risks. Private firms usually conduct nonfederal audits. Examples include A-133 or A-123 audits. Historically, nonfederal audits are completed by states, local governments, and nonprofit organizations that expend more than $500,000 in federal funds each year.[11]

It should be noted that OMB's *Uniform Administrative Requirements,* discussed earlier in the previous section, increased the funding threshold for nonfederal audits to $750,000. Nonfederal audits generally involve a review of financial statements, expenditures, and internal control systems. This review helps to ensure that federal funds were spent in a way that is consistent with the goals and requirements of the funding source. In addition to reviewing the findings of the audit, RMS suggests that program officers also determine whether or not a grantee completed the required audit on time.

## Procedures for Designating a Grantee High Risk

If, after conducting the required EDGAR and DGH reviews discussed above, a program officer determines a grantee evidences risk, the officer has the option of designating the grantee as high risk. High-risk designations can be made for either a specific grant program or all grant programs an entity receives. The first step in making a risk designation is for a program officer to consult with a program attorney and review the grantee's past performance. The program attorney's role is to determine whether the designation is warranted. This determination is made by reviewing the grantee's past performance in light of applicable requirements in statutes, regulations, and grant conditions.

If both the program officer and the program attorney believe the EDGAR requirements for a high-risk designation are met, they may designate the program high risk. If the program officer and program attorney believe the high-risk designation should be applied to *all* grant programs an entity receives, they must consult with RMS. The purpose of the high-risk designation is to ensure that the grantee takes appropriate actions to increase its capacity to effectively manage the federal funds, administer the program, and realize the grant objectives.

## Risk Management Across the Grant Life Cycle

The foregoing description of risk management at ED has focused on risk assessments that are conducted prior to making a grant award. However, it should be noted that a risk designation can be made before or after a grant award has been made.

There are four phases in the grants life cycle:

- **Pre-award:** The pre-award process involves reviewing submitted grant applications, making funding decisions, and preparing the grant award notice.
- **Award:** The award process involves creating the legal documentation required to make the grant award and notifying the grantee of the terms and conditions of the funding.

11. http://www.whitehouse.gov/sites/default/files/omb/assets/omb/circulars/a133/a133.html

- **Post-award:** The post-award process begins after the grant has been awarded. This phase requires program officers to conduct various administrative, financial, and programmatic oversight activities.
- **Closeout:** The closeout process requires the grantee to report on the fiscal, programmatic, and other grants-related activities it has completed. During this phase, the program officers conduct activities to ensure that the grantee has complied with all other federal guidelines.

ED's approach to risk management across the grants life cycle is presented in Figure 1. The strategy of formalizing the risk management practices in each aspect of the grant life cycle is a recent development at ED. As such, the work to institutionalize this framework is ongoing and is considered a work in progress. ED intends to capture the lessons learned from these activities and use them to inform future changes to the agency's grants management guidance and polices.

Figure 1 is intended to clarify the risk management activities that should take place during the grant life cycle. During the pre-award process, risk management involves the use of data, information, and analytics before the grant award is made. The types of data and information used during pre-award have been discussed at length in the preceding paragraphs. During the award phase, program officers engage in risk mitigation and define the types of supports necessary to ensure the effective and compliant administration of federal funds. During the post-award phase, risk management involves ongoing oversight of grantees with careful attention given to how they execute their grants management responsibilities. During the closeout process, risk management involves making sure that all required reporting has been completed. The data and information gathered during the closeout process is often used as an input in the next iteration of the pre-award process.

**Figure 1: Risk-Based Grant Oversight at Department of Education**

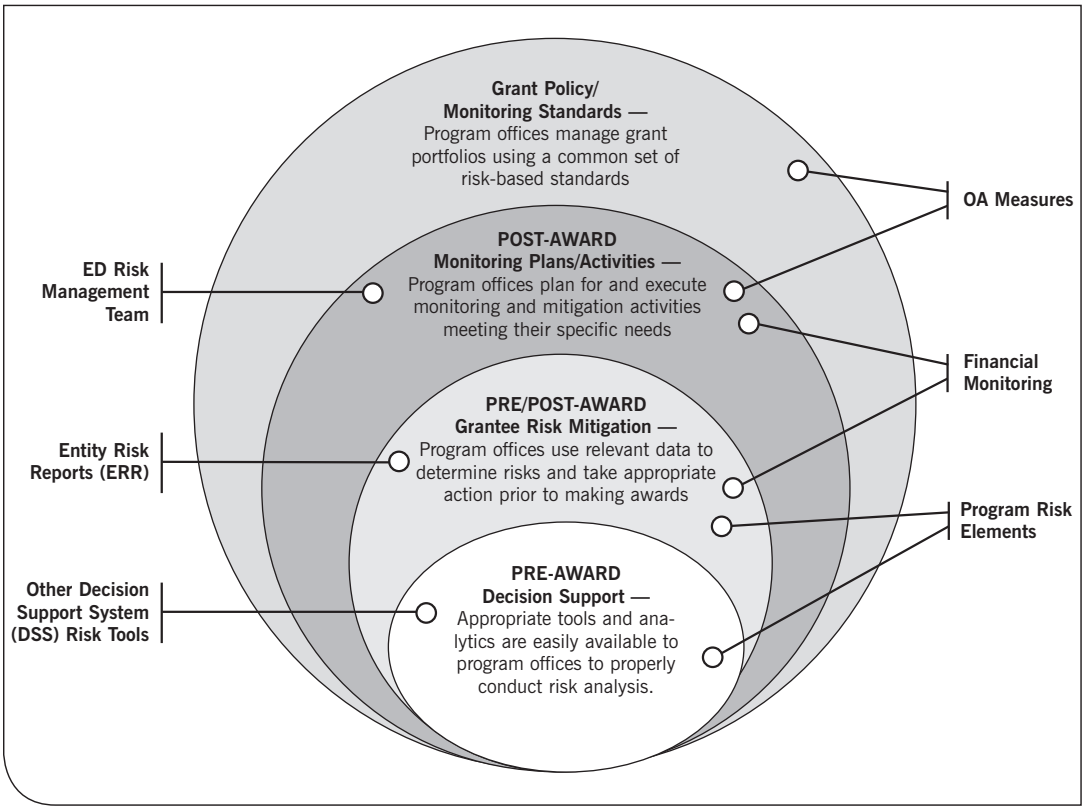
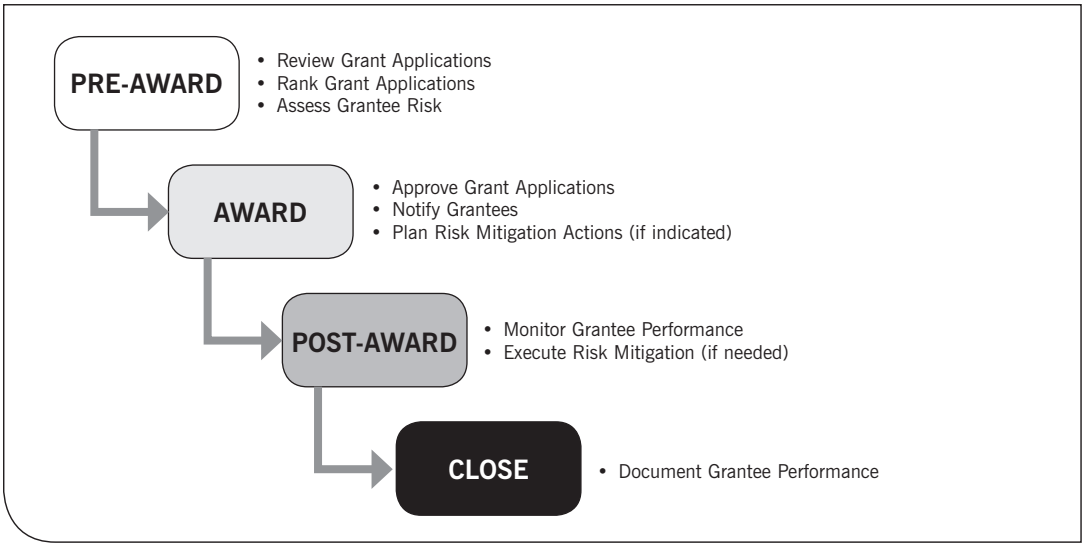


Figure 2 illustrates the application of ED's risk management practices for one grant program. The risk management practices are similar across most grant programs within ED.

**Figure 2: Risk Management Across the Grant Life Cycle**




## Creating New Risk Assessment Policies

In 2010, ED created an official policy requiring program offices to conduct more extensive pre-award risk assessments. This internal policy established an agency-wide requirement for program offices to assess an entity's risk by reviewing, at a minimum, prior and/or current financial and performance information, which includes the following information in ED's grants management system (called G5):

- Information on compliance with federal audit requirements
- Relevant findings in audit reports and monitoring reports
- Progress on corrective actions to resolve audit findings

ED also provided guidance regarding the types of information to be considered to help identify risk, possible mitigation strategies, or actions that may be taken to proactively manage risk, and policy addressing the inclusion of risk assessments in funding award decisions.

There were three driving forces behind the creation of this new policy. First, ED's risk policy affirmed the Obama Administration's commitment to ensuring effective stewardship of federal funds. Second, the creation of a policy requirement for risk assessment helped clarify the role and importance of the RMS at ED. Third, the new risk policy provided a context for program offices to understand the relevance of the newly available risk assessment tools (called the Entity Risk Review (ERR), which is discussed in the next section).

The 2014 version of ED's risk policy states that data in the Entity Risk Reviews are intended solely to provide information about applicants and/or grantees of grant awards funded by ED and, when used with other relevant information, to identify potential areas of risk. This means that these reports are not intended to be the sole determinants of grantee risk. If a program officer identifies potential risk, the officer must clarify how the risk will be mitigated. Common risk mitigation activities include:

- Increasing the frequency or scope of monitoring
- Providing targeted technical assistance

- Requiring additional progress reporting
- Applying special conditions

## Alignment between Risk Management at ED and the New OMB Requirements

In comparing OMB's *Uniform Administrative Requirements* and ED's EDGAR and the Discretionary Grants Handbook, one finds a high degree of consistency and overlap. Both agencies' policies require an examination of a grantee's financial stability and internal management capacity. Both agencies' policies require the review of audit data and historical performance. Finally, both agencies encourage the use of multiple data sources when assessing risk. One notable difference between the two agencies' policies is that only OMB has formalized risk criteria that take into consideration the unique aspects and characteristics of a grant program.

ED's current policy on pre-award risk assessment satisfies the new OMB risk assessment requirements. While the *Uniform Administrative Requirements* have not changed RMS's role, they have served to underscore the importance of risk management. In addition, they have created a new opportunity for RMS to play a leadership role in promoting the expansion of risk

### The Department of Education Risk Policy

ED's risk policy was revised in March of 2014 to provide additional guidance for the implementation of risk assessments. The new policy outlines a series of questions program officers can ask when assessing risk. Examples of these questions include:

- Is the applicant a novice applicant?
- Is the applicant associated with a high-risk entity?
- Did the applicant have a previous award with ED? If so, was the previous award completed appropriately?
- Are there budget item concerns (unallowable and/or unreasonable costs) identified in the application project budget?
- Do the data provided in the Entity Risk Reviews (ERR) reveal risks or a potential for risks?
- Has the grant or entity been designated high risk?
- Is the grantee implementing its project in accordance with any special risk-related conditions or risk-mitigation strategies that were previously imposed upon the grant award?
- Were there any excessive drawdowns during the previous budget period?
- Is there a large available balance at the end of the performance period?
- Has there been turnover of key personnel?
- Has substantial progress been made; if not why?
- Have all required reports been submitted?
- If applicable, has progress been made on corrective actions?
- Are there any A-133 audit findings or is the grantee making progress in resolving prior A-133 audit findings?
- Is the grant on schedule to achieve its objectives?
- Will more time be needed to complete projects?

management practices across the agency. ED's program officers can clearly identify how the ongoing work of RMS enables the agency to comply with the new risk assessment requirements. OMB's new guidance clearly establishes the role that program officers must play in effective risk management. They also frame risk management as a uniform practice that falls within the scope of work for all federal employees who are responsible for grants administration. In addition, program officers have adopted a more proactive approach in seeking assistance from RMS staff to ensure they have reviewed all relevant data prior to making a grant award.

As is explained in the next section, it took RMS several years to develop an agency-wide capacity to engage in grant risk management. The next section explains how RMS began the process of formalizing its approach to grant risk management and of disseminating these practices across the agency before creating new risk assessment policies and procedures.

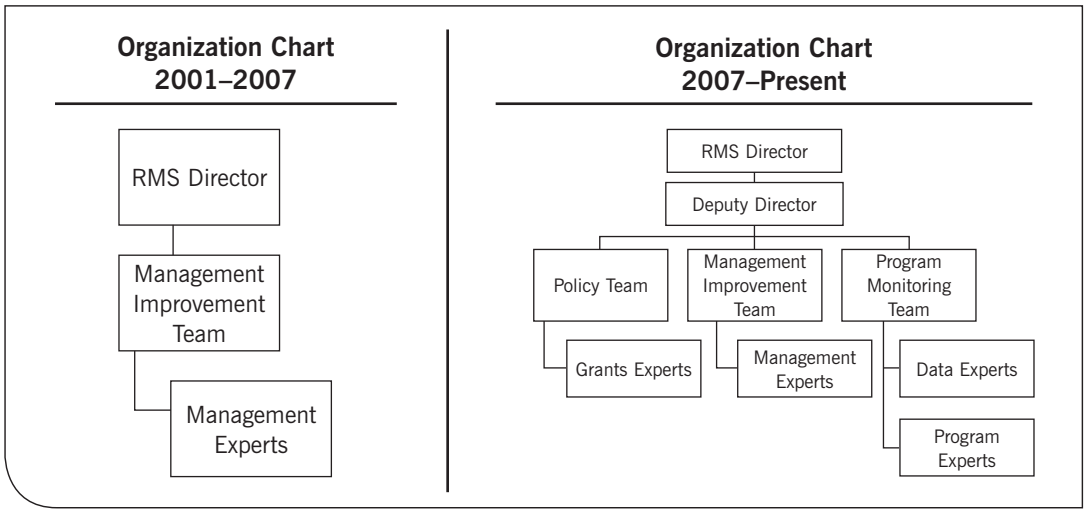
# Operationalizing Risk Management at Department of Education

## Creating an Organizational Structure

The size and scope of risk management efforts has changed and expanded greatly since 2001. Figure 3 shows how the organizational structure and scope of work of the Risk Management Service (RMS) has expanded over the past decade. In 2001, RMS had five employees, all of whom focused on management practice. Today, RMS has 25 members and three distinct teams: Management Improvement, Policy, and Program Monitoring. These three teams provide critical support to the grant-making process and enable the department to effectively administer its grants.

The Policy Team drafts policies and provides technical assistance to program officers who are responsible for administering ED's grants. The Program Risk Monitoring Team uses data and analytic tools to assess grantee risk. The Management Improvement Team uses portfolio management techniques to develop customized technical assistance services to grantees. This expansion in size and focus area within RMS evidences the increasingly important role the organization is playing within the agency.

**Figure 3: Evolution of RMS's Internal Organization**




## The Need to Improve the Effectiveness of Risk Designation

RMS identified several limitations to ED's approach to making risk designations using EDGAR and the Discretionary Grants Handbook criteria. The first limitation was the fact that this assessment and decision-making process was a decentralized and nonstandardized process. As a result, different program officers in different program offices could review the same data and information on a grantee and make different determinations of risk. The second limitation was that program officers used the same set of criteria to make risk determinations for programs

and for grantees. Program officers felt that the EDGAR criteria were not useful for programmatic risk determinations because they only assessed serious failures of internal administrative systems rather than programmatic capacity to implement a federal education program. The third limitation was that EDGAR and the DGH criteria did not establish clear performance thresholds to determine "poor performance" or "financial instability." Each of these three limitations, when taken together, result in the creation of a risk assessment system that is largely subjective.

RMS realized that program officers needed improved risk assessment methods if they were going to be able to effectively identify risk. There was also concern about the degree to which the current risk management practices were failing to identify the risk inherent in the grant-making process. As a result, RMS sought to provide program officers with access to new types of data and information related to grantees' capacity to administer education programs. It also began to explore new ways of identifying other factors that inform assessments of grantees' future capacity to implement federal grants. These changes in approach marked the initial shift away from using risk management to respond to observed performance issues. The agency as a whole was beginning to search for a more proactive approach to avoiding or minimizing risk and increasing the likelihood of grantee success.

## Creating New Risk Management Tools

### State Score Cards

RMS's initial effort to standardize the collection and review of data to inform risk assessments was the creation of a state profile. To create the state profile, RMS staff had to sort through a variety of paper reports and collect individual data on states that received funding from ED. Once collected, this information was matched to fiscal data extracted from ED's grants management system (Figure 4).

The state profile included the following indicators:

- **Program-related indicators** include scores from the National Assessment of Education Progress (NAEP), drop-out rates, timeliness of required data submission to ED, and school improvement status, and submissions to the Education Data Exchange Network (EDEN)
- **Management-related indicators** include existence of special conditions, A-133 audit findings, and OIG audit findings
- **Financial indicators** include bond ratings and total amount of funding

The determination of risk in a state profile was based on professional judgment about the significance of performance reported for each indicator. A formula was used to combine the assessment of programmatic, management, and fiscal indicators and create a risk assessment result. The risk assessment results were color-coded: red indicated high risk, yellow indicated moderate risk, and green indicated low risk.

RMS shared these state profiles with various program offices to gather feedback on the utility of the data and information presented. On balance, the program officers found the uniform report on state performance to be useful. In most cases, program officers confirmed that the entities identified as having risk had also been identified as having weaknesses in some areas. Program officers also indicated that, while they had concerns about certain grantees whose risk assessment result was red, these concerns did not warrant the application of a high-risk designation. One limitation of the state profile was that disproportionate weight was given to the amount of funds a state received. As a result, states that received the greatest amount of federal funds were determined to be the most risky.

**Figure 4: State Score Cards—Example of Concentration of Risk-State Summary (2006)**

| STATE | Program-Related Indicators (a) | Management-Related Indicators (b) | Financial Indicators Due to Title I Scale (c) | NAEP Scores | Event Drop-Out Rate | School Status in School Improvement Categories | ED Program Watch Lists | A-133 Audit Status | OIG Audits | Bond Ratings | Submissions to EDEN | FY 04 Formula Grant Funding ($) millions | FY 04 Title I Grant Funding ($) millions | Rating Score (a+b) x c |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| State 1 | RED | RED | RED | GR | YEL | YEL | RED | YEL | RED | YEL | RED | $8,122 | $1,242 | 18 |
| State 2 | RED | RED | RED | WH | WH | WH | RED | RED | RED | WH | YEL | $1,766 | $449 | 18 |
| State 3 | RED | YEL | RED | RED | WH | YEL | RED | YEL | YEL | RED | YEL | $10,821 | $1,766 | 15 |
| State 4 | YEL | RED | RED | YEL | YEL | YEL | YEL | RED | YEL | YEL | YEL | $5,199 | $575 | 15 |
| State 5 | RED | YEL | RED | YEL | RED | YEL | RED | YEL | YEL | YEL | RED | $4,946 | $523 | 15 |
| State 6 | RED | RED | YEL | RED | RED | RED | RED | RED | YEL | RED | RED | $826 | $49 | 12 |
| State 7 | RED | RED | YEL | RED | RED | RED | YEL | RED | RED | GR | YEL | $3,025 | $382 | 12 |
| State 8 | YEL | RED | YEL | GR | WH | GR | RED | YEL | GR | RED | RED | $1,643 | $115 | 10 |
| State 9 | YEL | RED | YEL | GR | YEL | GR | YEL | RED | RED | GR | RED | $1,945 | $105 | 10 |
| State 10 | YEL | RED | YEL | RED | YEL | YEL | YEL | RED | GR | YEL | RED | $734 | $115 | 10 |
| State 11 | YEL | GR | RED | YEL | YEL | YEL | YEL | GR | GR | YEL | YEL | $7,159 | $1,111 | 9 |
| State 12 | YEL | YEL | YEL | RED | RED | YEL | YEL | YEL | YEL | RED | RED | $4,237 | $230 | 8 |
| State 13 | YEL | YEL | YEL | RED | YEL | YEL | GR | YEL | YEL | YEL | YEL | $1,688 | $187 | 8 |
| State 14 | YEL | YEL | YEL | RED | YEL | YEL | YEL | RED | YEL | YEL | GR | $1,347 | $171 | 8 |
| State 15 | YEL | YEL | YEL | RED | RED | YEL | GR | YEL | RED | RED | YEL | $1,717 | $268 | 8 |
| State 16 | YEL | YEL | YEL | YEL | YEL | YEL | YEL | YEL | YEL | GR | YEL | $1,504 | $164 | 8 |
| State 17 | YEL | YEL | YEL | GR | GR | YEL | YEL | YEL | WH | YEL | YEL | $2,616 | $234 | 8 |
| State 18 | YEL | YEL | YEL | YEL | WH | YEL | YEL | YEL | GR | YEL | GR | $3,445 | $417 | 8 |
| State 19 | YEL | YEL | YEL | RED | YEL | YEL | YEL | YEL | YEL | YEL | YEL | $1,111 | $161 | 8 |
| State 20 | YEL | YEL | YEL | GR | YEL | YEL | YEL | YEL | YEL | YEL | YEL | $3,907 | $400 | 8 |
| State 21 | YEL | YEL | YEL | GR | YEL | YEL | RED | YEL | YEL | YEL | RED | $4,727 | $433 | 8 |
| State 22 | YEL | YEL | YEL | GR | WH | YEL | YEL | YEL | WH | YEL | RED | $1,787 | $171 | 8 |
| State 23 | GR | RED | YEL | GR | GR | GR | YEL | RED | GR | RED | RED | $1,614 | $161 | 8 |
| State 24 | YEL | GR | YEL | GR | YEL | YEL | YEL | RED | YEL | GR | YEL | $2,251 | $185 | 6 |
| State 25 | RED | RED | GR | RED | WH | WH | RED | RED | RED | WH | WH | $29 | $8 | 6 |
| State 26 | RED | RED | GR | RED | WH | WH | RED | RED | RED | WH | WH | $53 | $7 | 6 |
| State 27 | GR | YEL | YEL | GR | WH | GR | GR | YEL | YEL | WH | YEL | $2,164 | $167 | 6 |
| State 28 | GR | YEL | GR | WH | WH | WH | GR | RED | YEL | WH | WH | $19 | $3 | 3 |
| State 29 | YEL | GR | GR | GR | YEL | GR | YEL | GR | GR | GR | YEL | $756 | $51 | 3 |
| State 30 | GR | YEL | GR | GR | YEL | GR | GR | RED | WH | WH | GR | $256 | $30 | 3 |
| State 31 | GR | GR | GR | YEL | RED | YEL | YEL | GR | GR | WH | YEL | $464 | $42 | 2 |
| State 32 | GR | GR | GR | GR | GR | GR | YEL | YEL | GR | WH | GR | $1,336 | $65 | 2 |
| State 33 | GR | GR | GR | GR | GR | GR | GR | GR | WH | WH | YEL | $327 | $30 | 2 |
| State 34 | GR | GR | GR | YEL | YEL | YEL | GR | GR | YEL | YEL | YEL | $531 | $46 | 2 |
| State 35 | GR | GR | GR | GR | YEL | YEL | YEL | GR | WH | WH | YEL | $378 | $35 | 2 |

**KEY**:

RED = Red (High Risk)  YEL = Yellow (Moderate Risk)  GR = Green (Low Risk)  WH = White (No Data Available)

Learning from its experience with the state profile, RMS set out to create new ways to standardize the reporting of performance information for ED grantees. These standardized reports would help program officers by reducing the amount of time needed to gather information on each of ED's 7,000-plus competitive grant recipients. RMS recognized the potential value these standardized reports would have for program officers, but also realized that a significant amount of time and human resources would be needed to create them. To respond to this challenge, RMS began to explore ways to automate the process of collecting and summarizing data on grantees.

Over the next year, RMS continued to refine its approach to collecting and analyzing data on grantees. During this time period, the Obama Administration began implementing the Government Performance and Results Modernization Act (GPRAMA). RMS's efforts to create an automated risk assessment tool represented one way ED could demonstrate progress toward attaining its strategic goals and optimize the use of existing human resources.

## Entity Risk Review

RMS began working on developing an automated method for extracting data from various systems to create these standardized reports. RMS found this to be a challenging task because the agency's internal data systems were not interoperable. RMS also needed a strategy for incorporating audit data from the Federal Audit Clearinghouse (FAC). RMS decided to focus on audit data because it was the most readily available, most reliable, and largest data source on grantee performance. Most program officers believed audit findings would provide an indication of the degree to which a grantee has the necessary administrative processes and infrastructure to effectively administer federal funds and implement grant programs. Once the data had been collected and integrated, RMS wanted to run an automated program that would analyze and score the information.

By late 2009, RMS had created a viable prototype of the new automated risk assessment tool, the Entity Risk Review (ERR). The ERR consolidated the disparate data sources into one report and included data from Dunn & Bradstreet (DUNS), ED's internal G5, and FAC. Data elements within each of the three categories (administrative, financial, and internal control risks) were scored to create a risk indicator.

### *The Administrative Risk*

This score represents the applicant's previous history with the department and its past compliance with grant requirements. Particular attention is given to applicants whose grants are designated as high risk:

- Applicants that had grants closed due to noncompliance in recent years
- Applicants that have failed to make substantial progress on past grants

For purposes of this score, applicants that do not have a previous or recent history with the department are designated as "inexperienced."

An overall score equal to or greater than 100 will turn this category red, and a score greater than or equal to 50 will turn this category yellow. An individual data element will be shaded red if it carries a score equal to or greater than 50. An individual data element will be shaded yellow if it carries a score greater than 0, but less than 50. The relative scores for each of these variables are presented Table 1.

**Table 1: Entity Risk Review—Administrative Score Data**

| Administrative Score Data | Recommended Risk Factor Score |
|---|---|
| High Risk" Grantee | 100 |
| "High Risk" Awards Made to Grantee (Count) | 100 |
| Number of ED Awards Closed in "Noncompliance" in the Past Two Years | 25, 50<br>if the award has the same CFDA as the program under review |
| Date of Startup or Ownership Change – 3 years from today | 25 |
| Inexperienced Grantee (only if no purple color coded) | 25 |
| Grantee Failed to Meet Substantial Progress Requirements on ED Awards Within Five Years | 25, 50<br>if the award has the same CFDA as the program under review |
| Terminate (adverse accreditation actions to be combined into one row) | 100 |
| Withdraw Accreditation (adverse accreditation actions to be combined into one row) | 100 |
| Closure (adverse accreditation actions to be combined into one row) | 100 |
| Show Cause (adverse accreditation actions to be combined into one row) | 75 |
| On Probation (adverse accreditation actions to be combined into one row) | 50 |

***The Financial Risks***

This score represents the applicant's fiscal health, creditworthiness, and history of paying bills in a timely fashion. This score also captures data elements that indicate how well the applicant previously managed funds through G5. This score is affected by how the applicant conducts its finances, not only with the department, but also with the wider business world.

An overall score equal to or greater than 100 will turn this category red, and a score equal to or greater than 25 will turn this category yellow. An individual data element will be shaded red if it carries a score equal to or greater than 50. An individual data element will be shaded yellow if it carries a score greater than 0, but less than 50. The relative scores for each of these variables are presented in Table 2.

**Table 2: Entity Risk Review—Financial Score Data**

| Financial Score Data | Risk Score |
|---|---|
| Financial Stress Score 5 (to be part of "Financial Weakness") | 50 |
| Commercial Credit Score 5 (to be part of "Financial Weakness") | 25 |
| 3-Month Paydex Score Average (to be part of "Financial Weakness") | 50 |
| Criminal Activity Indicator | 100 |
| Out of Business Indicator | 100 |
| Bankruptcy Indicator in the Past Five Years | 100 |
| Stop Payment Flag on the Grantee or the Grantee's Awards (each condition) | 50 |
| Route Payment Flag on the Grantee or the Grantee's Awards (each condition) | 50 |
| Total Number of Awards "On-Reimbursement" Within 5 Years | 50 |
| Grantee on Offset Schedule | 50 |

***Internal Controls Risk***

This score represents both the degree to which the applicant's financial and grants management systems adequately process and account for federal funds, and the effectiveness of the internal policies the applicant has established to meet the requirements of a federal program. This information is based on the findings of independent auditors. DSS uses the applicant DUNS number to locate the A-133 audit and further connects the applicant to associated entities that share the same A-133 audit in the FAC. This makes audit data accessible to department staff and summarizes it into an understandable score.

An overall score equal to or greater than 100 will turn this category red, and a score equal to or greater than 50 will turn this category yellow. An individual data element will be shaded red if it carries a score equal to or greater than 50. An individual data element will be shaded yellow if it carries a score greater than 0, but less than 50. The relative scores for each of these variables are presented in Table 3.

**Table 3: Entity Risk Review—Internal Control Risk Data**

| Auditor's Opinion of Auditee—Most Recent Audit | Risk Factor Score |
|---|---|
| Going Concern of Financial Statements | 120 |
| Qualified Audit of Financial Statements (combined) | 15 |
| Disclaimed Audit of Financial Statements (combined) | 60 |
| Adverse Audit of Financial Statements (combined) | 60 |
| Qualified Audit of at Least One Major ED Program, as Determined by FAC (combined) | 15 |
| Disclaimed Audit of at Least One Major ED Program, as Determined by FAC (combined) | 60 |
| Adverse Audit of at Least One Major ED Program as Determined by FAC (combined) | 30 |
| Questioned Costs | 10 |

| Auditor's Opinion of ED Programs—Most Recent Audit | Most Recent Audit Factor Score |
|---|---|
| Allowable Cost Findings | 10 |
| Activities Allowed Findings | 10 |
| Cash Management Findings | 10 |
| Eligibility Findings | 10 |
| Matching, Level of Effort, Earmarking | 10 |
| Procurement and Suspension and Debarment Findings | 10 |
| Equipment and Real Property Management Findings | 10 |
| Period of Availability Findings | 5 |
| Program Income Findings | 5 |
| Reporting Findings | 5 |
| Special Tests and Provisions Findings | 10 |
| Sub-recipient Monitoring Findings | 10 |
| Davis – Bacon Act | 10 |
| Real Property Acquisition and Relocation Assistance | 10 |
| Other Finding | 10 |

Figure 5 illustrates the summary page of the ERR report. One grantee appears in each row and each row contains hyperlinks that, when clicked, take the user to a detail page. The detail page presents the example of individual data elements and corresponding scores for individual grantees.

**Figure 5: Sample Entity Risk Review**

| Recipient Name | Recipient State | Administrative Risk Score | Financial Risk Score | Suspected Late Audit | Internal Control Risk Score |
|---|---|---|---|---|---|
| School District 1 | | 25 | 0 | 2007 | 35 |
| School District 2 | | 0 | 0 | 2003 | 35 |
| School District 3 | | 25 | N | No | 0 |
| School District 4 | | 0 | 25 | No | N |
| School District 5 | | 0 | 0 | 2011 | 0 |
| School District 6 | | 25 | 0 | No | 10 |
| School District 7 | | 0 | 0 | No | 0 |
| School District 8 | | 0 | 0 | No | 0 |
| School District 9 | | 100 | 75 | No | 205 |
| School District 10 | | 25 | 0 | No | 0 |
| School District 11 | | 25 | 0 | No | 0 |
| School District 12 | | 0 | 0 | No | 0 |
| School District 13 | | 0 | 0 | 2011 | 5 |
| School District 14 | | 0 | 0 | 2012 | 60 |
| School District 15 | | 0 | 0 | No | 0 |
| School District 16 | | 0 | 0 | No | 0 |
| School District 17 | | 0 | 0 | No | 0 |
| School District 18 | | 0 | 0 | No | 0 |
| School District 19 | | 0 | 0 | No | 0 |
| School District 20 | | 25 | 0 | No | 0 |
| School District 21 | | 25 | 0 | No | 10 |
| School District 22 | | 25 | 0 | No | 80 |
| School District 23 | | 25 | 0 | No | 10 |
| School District 24 | | 0 | 0 | No | N |
| School District 25 | | 0 | 0 | No | 0 |
| School District 26 | | 25 | N | No | 0 |
| School District 27 | | 0 | 0 | No | 95 |

**Note:** The higher the score, the greater the risk. N = Information not available.

In 2010, RMS initiated an agency-wide pilot of the ERR. The objectives of the ERR pilot were to determine whether RMS's tool could be used as the agency's standardized set of risk indicators. In addition, the pilot was intended to assess whether the new data-driven tool facilitated program offices' efforts to analyze grantee risk prior to making awards and during the life of a grant project. Pilot participants were asked to determine whether the ERR made it easier for them to access and understand audit findings and other available information about organizations' fiscal health.

The Obama Administration was also interested in determining whether the ERR could facilitate data sharing across grant programs and among department offices. Based on feedback from program officers at the end of the pilot, the ERR effectively reduced the amount of time and effort program officers needed to put into the pre-award review of grantees financial capacity. It also has helped program officers develop a more nuanced understanding of how a grantee's administrative and financial management behaviors could signal risk.

## Building Capacity to Use the Entity Risk Review

When RMS began producing the ERR for all grant programs within ED, it held general orientation sessions to introduce the concepts of risk management and the ERR tool to program officers. The orientation sessions provided an overview of the data elements that could be considered when conducting a risk assessment and discussed the meaning and relevance of each data element. The purpose of the orientations was to help program officers become more familiar with the data elements and data analysis process. The orientation sessions also provided an opportunity for program officers to ask questions about the risk assessment process. RMS also created new communication mechanisms and leveraged the agency's SharePoint site to ensure that all staff could access guidance and information on how to conduct risk assessments.

In order to help program officers incorporate the new risk assessment practices into their daily business practices, RMS developed customized training sessions for each program office. These training sessions focused on teaching program officers how to analyze and interpret risk assessment data that were most relevant to their programs. The training sessions also included strategies and techniques for identifying and responding to grant-specific risks.

RMS continues to work on developing the agency's capacity to implement risk management principles. Program officers have requested additional training and guidance on the use of the ERR and effective mitigation strategies. The nature and complexity of this conversation continues to evolve and is much different from the types of conversations that took place in 2007. The original conversations about risk management focused on immediate interventions with challenged grantees. Now, RMS's current work with program offices is more focused on developing specific responses to the technical and programmatic risks program officers believe are most relevant to their program goals.

## Refining the Entity Risk Review

Since 2011, RMS has worked hard to improve the user-friendliness of the ERR. The original ERR was an Excel spreadsheet with various tabs. Program officers found the spreadsheet to be cumbersome and difficult to navigate. As of December 2014, RMS is finalizing a new delivery format for the ERR, using a Web interface. Initial user feedback during testing indicates that program officers find the website easier to navigate and more comfortable for those who are unfamiliar with Excel. An additional benefit of the Web-based ERR is that it facilitates the storing and sharing of ERRs across the agency.

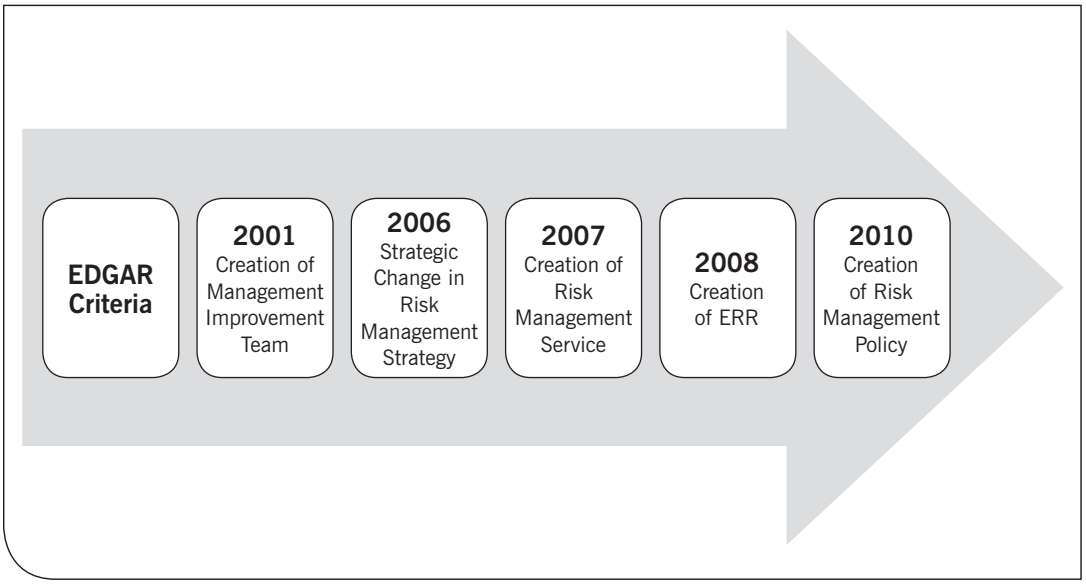
During the past three years, RMS has made modifications to improve the ERR. These modifications have focused on:

- Increasing the accuracy of indications of risk
- Reducing the instances of identifying risk that are not significant enough to require further investigation

Additional efforts to enhance the ERR are focusing on ways risk analyses could be customized, based on program offices' needs. As program officers gain increased capacity to engage in risk management, they have begun to request customized risk assessment tools. RMS is working on developing custom ERRs that would be based on a set of grant-specific performance indicators. These customized risk assessments will be much shorter than the standard ERR because they include only elements program officers are requesting. RMS envisions these custom risk assessments being used in addition to the risk assessment provided by the ERR.

RMS is pursuing several ideas for future development of the ERR. First, RMS feels that it is important to incorporate into the ERR information captured by the program officers when they conduct performance and compliance monitoring reviews of their grantees during the post-award and closeout phases. RMS believes data from program officers' ongoing monitoring efforts are key to identifying potential risks. Progress on realizing this enhancement has been slow because ED does not have one uniform process or system for capturing and storing monitoring and performance data. A second enhancement to the ERR would involve incorporating data on the risk mitigation activities that have been executed, such as the completion of audit and monitoring corrective actions. Both of these future development efforts would require the capacity to incorporate unstructured (usually text) data into the existing databases used to create the ERR. Figure 6 summarizes the evolution of risk management services at ED.

**Figure 6: Evolution of Risk Management at ED**



# Case Studies of Risk Management Across the Grant Life Cycle

When RMS was created, the majority of its work focused on intervening with grantees that had demonstrated significant difficulty in administering grants. RMS's Management Team intervened with grantees when:

- A program officer had designated an entity as high risk before making a grant award
- A program officer identified significant and/or pervasive performance issues for a grantee during the grant period

In both instances, RMS's primary efforts focused on risk mitigation as opposed to risk assessment. RMS's management team worked directly with grantees to improve their fiscal and management systems. They also helped program officers to identify effective strategies for providing technical assistance to high-risk grantees. These interventions focused on developing the policies, procedures, and practices necessary for effective grants management.

The following cases of the Detroit Public Schools and Puerto Rico Department of Education illustrate the evolution of risk management practices at ED. The cases begin with a description of the performance weaknesses each entity demonstrated. Next, the risk mitigation efforts provided for each entity are described. The cases conclude with a sample ERR report for each entity.

## Detroit

Detroit was named high risk by the state of Michigan in August of 2008. The high-risk designation followed a 2008 report issued by ED's Office of Inspector General (OIG) after auditing Detroit's federal Title I records for 2004 to 2006. In response to the report, Michigan's Department of Education placed Detroit Public Schools in high risk status.[12] The high-risk designation was issued at a time when Detroit Public Schools had a deficit of more than $65 million,[13] declining student enrollment, and poor academic achievement scores.

The high-risk designation was based on a variety of findings and performance weaknesses. The OIG cited $54 million of unallowable and inadequately documented spending. The district's financial management systems were found to be antiquated, insufficient, and mismanaged. The district lacked effective operating manuals and staff were not properly trained or held accountable for complying with administrative procedures and internal controls.[14] Additionally, the district evidenced poor capacity to manage its assets; 500 computers, with an estimated worth of $600,000, were stolen.[15] There were additional questions about the

12. http://www.michigan.gov/som/0,4669,7-192-29939_34761-316617--,00.html
13. http://content.time.com/time/magazine/article/0,9171,1953694,00.html
14. http://www.bruman.com/wp-content/uploads/2014/04/May-8-1300-Detroit-The-Successful-Story-of-a-Previously-Designated-High-Risk-District.pdf
15. http://content.time.com/time/magazine/article/0,9171,1953694,00.html

appropriateness of the district's academic improvement plans and the degree to which they were being implemented.[16, 17]

## Detroit Post-Award Risk Mitigation

RMS took a leading role in supporting risk mitigation efforts in Detroit. RMS worked closely with the emergency financial manager and academic accountably auditor for the Detroit Public Schools. RMS provided technical assistance to ensure that Detroit made an appropriate selection of a certified public accounting (CPA) firm to monitor the district and approve expenses. RMS collaborated with the Michigan Department of Education (MDE) to provide guidance on strategies to ensure effective fiscal management within the district. MDE ultimately withheld 20 percent of funds requested by Detroit Public Schools[18] and required the district to obtain state approval for individual expenditures of more than $25,000.[19] This approval process provided the state with an increased view of district-level fiscal management decisions and reduced the risk of misuse of federal funds.

The Detroit Public Schools has made substantial improvements, including:

- Establishing key fiscal policies and procedures (e.g., procurement, personnel timekeeping, allowable use cost principles, conflict of interest)
- Demonstrated improvements in single-audit findings and special testing procedures monitored by its CPA firm
- Developing stronger human resource systems for teacher assignment, evaluation, and training
- Improving the district's curriculum, instruction, and evaluation systems
- Effectively conducting district summer school and implementing technology related to instruction
- Improving the quality and timeliness of financial drawdowns on federal funds
- Showing early signs of improvements in academic performance[20]

The district was taken off high-risk status in November 2013 and the state-appointed emergency manager was put in charge of the district after the high-risk designation was removed. Detroit Public Schools can now apply for more state and federal grants.[21] MDE and Detroit Public Schools signed a Memorandum of Agreement that allows MDE to continue with ongoing monitoring of Detroit Public Schools, including:

- Monitoring continued improvements in student achievement for all students and all student groups represented in the district
- Monitoring continued implementation of established policies and procedures, and updating and providing transparency on other district policies and procedures
- Monitoring improvements on single audits and fiscal special testing procedures

16. http://www.bruman.com/wp-content/uploads/2014/04/May-8-1300-Detroit-The-Successful-Story-of-a-Previously-Designated-High-Risk-District.pdf
17. http://www.michigan.gov/mde/0,4615,7-140--316617--,00.html
18. http://www.bruman.com/wp-content/uploads/2014/04/May-8-1300-Detroit-The-Successful-Story-of-a-Previously-Designated-High-Risk-District.pdf
19. http://www.freep.com/article/20131118/NEWS01/311180119/Detroit-Public-Schools-dps-high-risk-status-MDE
20. http://detroitk12.org/content/2013/11/18/michigan-department-of-education-removes-high-risk-designation-from-detroit-schools/
21. http://www.freep.com/article/20131118/NEWS01/311180119/Detroit-Public-Schools-dps-high-risk-status-MDE

- Monitoring submission of grant applications to ensure their timeliness, which include:
  - Implementing supplementary academic services to students early in the year
  - Timely and appropriate drawing down of federal funds
- Monitoring the calculation and use of district required grant set asides timely and appropriately
- Monitoring each grant program for specifics
- Monitoring continued implementation of systems[22]

### Updated Detroit Pre-Award Risk Assessment

Figure 7 represents the ERR score of Detroit Public Schools. The ERR was created during the pre-award process. The results clearly indicate that Detroit is not currently evidencing significant risk.

**Figure 7: ERR of Detroit Public Schools**

| Recipient Name | Recipient State | Administrative Risk Score | Financial Risk Score | Suspected Late Audit | State Audit ? | Internal Control Risk Score |
|---|---|---|---|---|---|---|
| Detroit Public Schools | MI | 0 | 50 | N | N | 50 |

## Puerto Rico

The Puerto Rico Department of Education (PRDE) was named a high-risk grantee in May 2002. In response to this designation, RMS led a Cooperative Audit Resolution and Oversight Initiative (CAROI) with PRDE. The goal of CAROI was to provide PRDE with technical assistance, which could address the systemic problems that gave rise to repeated and unresolved audit findings. Working collaboratively with PRDE, RMS led a cross-functional team of ED staff and provided technical assistance to address problems, develop corrective actions, and monitor changes in internal practices.

Two years later, in 2004, PRDE and ED entered into a compliance agreement. The purpose of the compliance agreement was to ensure that PRDE's management of federal education grants complied with programmatic and fiscal requirements. The need for a compliance agreement arose following a series of monitoring and audit reports that identified significant material weaknesses in PRDE's operations and management. The compliance agreement defined specific areas in which PRDE needed to improve its performance in order to continue to receive federal funds. Failure to satisfy the compliance agreement would have led to reapplying the high-risk designation, which would have further complicated PRDE's capacity to qualify for and receive federal funds.[23]

### Puerto Rico: Post-Award Risk Mitigation

RMS led agency-wide efforts to address PRDE's inability to comply with the major programmatic requirements on the following federal grant programs: Titles I, II, and IV of the Elementary and Secondary Education Act (ESEA), Title IV of the Higher Education Act of 1965, and the Individuals with Disabilities Education Act (IDEA) (covered federal programs). RMS worked directly with PRDE staff to help them develop improved capacity to provide the

22. http://www.michigan.gov/mde/0,4615,7-140--316617--,00.html
23. Compliance Agreement Among the Commonwealth of Puerto Rico, The Puerto Rico Department of Education, and the United States Department of Education

services required by these programs. RMS provided guidance on how PRDE could develop the necessary IT infrastructure to collect, analyze, and report student performance data. RMS also provided critical guidance in the development of fiscal systems that would allow for compliant reporting of grants management activities related to procurement, time, and attendance reporting, and accounting.[24]

The three-year period of performance for the compliance agreement concluded in 2007. However, because PRDE's final quarterly report indicated that work remained to be done on certain action steps, PRDE and ED entered into an MOA. ED determined that it would take PRDE more than one year to completely resolve its performance issues. In addition, ED believed PRDE needed additional time to institutionalize the continued cooperation of other parts of the Puerto Rico government, such as the Puerto Rico Department of the Treasury (Hacienda) and the Puerto Rico Office of Management and Budget (OMB). Thus, the MOA provided PRDE with another three-year period in which to finalize the improvements it had initiated as part of the compliance agreement. This second agreement provided similar protections from the high-risk designation.[25] Nevertheless, ED applied department-wide special conditions on all of PRDE's grants.

ED staff provided Puerto Rico and PRDE with extensive technical assistance continuously for 12 years. The support of ED program officers was coordinated through RMS. ED provided technical assistance related to individual grant program requirements as well as fiscal and operational issues, such as payroll reporting, time and attendance reporting, integrating financial management systems, centralizing procurement, developing effective property management practices, establishing an adequate IT infrastructure, and effectively managing human resources. Members of the PRDE team demonstrated tremendous commitment and hard work throughout this process and were ultimately successful in addressing the identified risks. RMS provided the necessary oversight to ensure that the performance issues were tracked and that PRDE's progress was assessed quarterly (as shown in Figure 8). RMS coordinated this oversight through the office of the Secretary and worked directly with the governor of Puerto Rico. In 2011, as agreements were nearing completion, Secretary of Education Arne Duncan visited Puerto Rico and, through a press release, said he was pleased at the progress he saw through PRDE's progress reports.[26]

## Updated Puerto Rico Pre-award Risk Assessment

Figure 8 represents the ERR score of the Puerto Rico Department of Education. The ERR was created during the pre-award process. The results clearly indicate that the Puerto Rico Department of Education continues to have some risk related to financial management and audit findings. The Financial Risk Score and Internal Control Risk Score provide program officers across the agency with notification that additional investigation into these two aspects of the grantee's performance should be undertaken before a grant award is made.

**Figure 8: ERR of the Department of Education of Puerto Rico**

| Recipient Name | Recipient State | Administrative Risk Score | Financial Risk Score | Suspected Late Audit | State Audit ? | Internal Control Risk Score |
|---|---|---|---|---|---|---|
| Department of Education of Puerto Rico | PR | 25 | 125 | N | N | 120 |

24. Compliance Agreement Among the Commonwealth of Puerto Rico, The Puerto Rico Department of Education, and the United States Department of Education

25. Memorandum of Agreement Among the Commonwealth of Puerto Rico, The Puerto Rico Department of Education, and the United States Department of Education

26. http://www.ed.gov/news/press-releases/us-department-education-pleased-progress-puerto-ricos-department-education

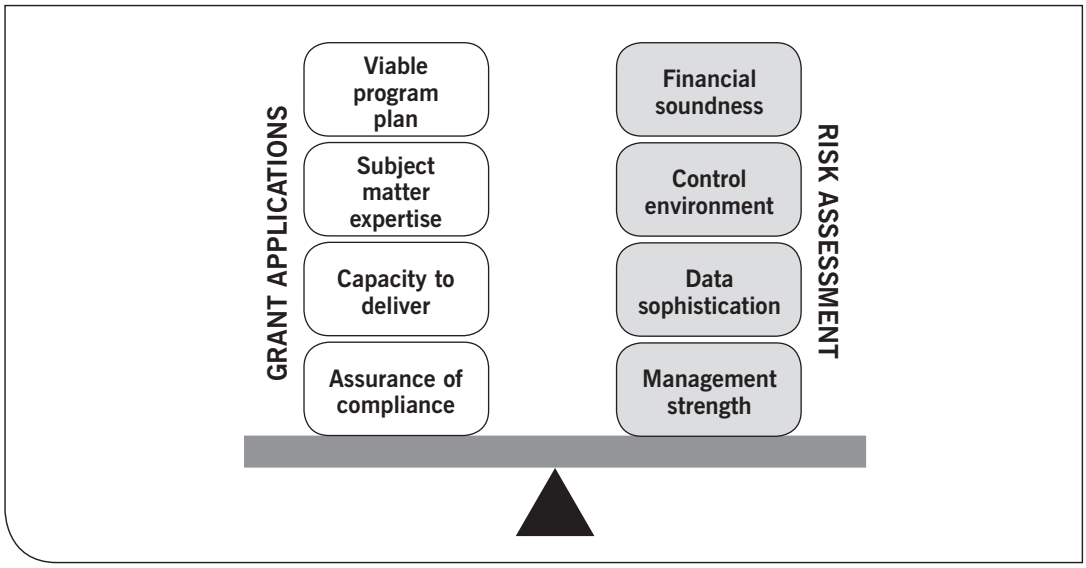
# Lessons Learned and Recommendations for Risk Management in Grants Administration

## Improved Data-Driven Decisions

RMS's work in developing risk assessment and risk mitigation activities has benefited ED greatly. In addition to ensuring that ED demonstrates compliance with federal requirements, RMS's efforts have fostered the creation of a culture that understands and values risk management. Recognition of the importance of assessing risk and sharing information about grantee risk has become a meaningful grants management activity. RMS's success in creating a common risk assessment tool has fostered the creation of an enterprise approach to risk management within ED. It has also led to an increase in the use of data-driven decision making as shown in Figure 9. These new practices decrease the potential for inconsistent risk assessment practices and uncoordinated risk management activities and are two important characteristics of effective approaches to risk management (Hardy, 2010).

The authors believe that RMS could increase the capacity and accuracy of risk assessments by expanding the information sources included in the ERR. RMS's current ideas to find ways to incorporate unstructured data—including text-based reports and public information—into risk assessment models are likely to produce more robust risk assessments. Similarly, we believe the agency will benefit from efforts to expand its capacity to identify and analyze the characteristics and impacts of programmatic risk, or those risks inherent in the grant program, by the nature of its requirements. Other interest areas include creating longitudinal data sets and conducting trend analyses to identify changes in grantee risk factors over time.

**Figure 9: Improved Data-Driven Decisions**



## Lessons Learned

There are several important lessons to be learned from RMS's experience in developing the Entity Risk Reviews. Capturing lessons learned makes it possible for an organization to gain greater insight into which practices were successful and which practices were not. Capturing lessons learned also makes it possible to share an organization's experience with others outside the organization and to foster their professional growth and learning.

**Lesson One: The department benefited by creating a defined and codified business process for managing risk in the department's grants portfolio.** Formalizing and standardizing the risk assessment process allowed ED to take a more proactive approach to identifying risk and promoting effective grants management. It helped employees develop a common understanding of how a risk assessment should be conducted and reduced the time and burden associated with the traditional approach to risk assessment. In addition, defining and codifying the process also made it possible for RMS to set expectations at specific points during the grant life cycle when risk management practices should be applied.

**Lesson Two: The use of an automated, data-driven risk assessment tool enabled the department to apply uniform and consistent risk assessment procedures and make better use of audit data.** The ERR enabled the agency to increase the objectivity and consistency of program officers' risk assessments. The automated data-driven risk assessment tool clarified the specific data elements that should be considered when assessing risk and provided standard thresholds against which performance on these elements could be assessed. The ERR also simplified the process of interpreting the relative importance of these data elements. In addition, the ERR facilitated consistent interpretation of audit data and reduced the amount of time and effort program officers needed to spend gathering audit information. RMS's consultation and training services also helped program officers gain new capacities to connect fiscal and management audit findings to the specific requirements of their programs.

**Lesson Three: The department's success in implementing a department-wide enterprise risk management program required the creation of new internal policies and support from agency leadership.** Because ED addressed risk assessment in EDGAR and the DGH, program officers at ED had some familiarity with the criteria for assessing grantee risk. These two policy directives, however, would not have been sufficient to ensure that all program officers made use of the ERR and conducted a pre-award risk assessment. The decision to create a new internal policy directive requiring the use of the ERR was an important one. The new risk assessment policy created an official, agency-wide expectation that program officers would engage in risk assessment during the pre-award process. It also helped to create increased visibility about agency leadership's support for risk management practices. Ongoing, visible and manifest support from agency executives helped create broad-based awareness of and interest in the ERR. RMS believes that, without the creation of the new risk policy and the support of senior leaders, its implementation of the ERR would not have been as successful as it was.

**Lesson Four: Effective risk management is an iterative process that requires thoughtful use of existing data sources and ongoing efforts to incorporate new ones.** The ERR increased the agency's capacity to strategically collect, store, and use existing data sources. It also helped RMS to identify new ways to make use of existing data sources. The process has also raised new interest among program officers and RMS staff in finding additional data sources. This suggests that the development and refinement of the ERR is an ongoing process in which each subsequent stage is informed by the preceding one. Despite general acceptance and approval of the ERR in its current form, both program officers and RMS staff are interested in creating new and/or slightly customized versions of the ERR.

## Recommendations for Federal Agencies

The following recommendations are based on the authors' analysis of RMS's efforts to implement new approaches to risk management at ED.

**Recommendation One: Agencies should move to a data-driven system to collect and manage data that can be used to make risk assessments.** Agencies that do not have interoperable data systems should seek to create them or find cost-effective means of joining these data. Agencies that have interoperable data systems and/or can join data from disparate systems should create internal guidelines for the management of these resources. The design and development of these systems should be flexible enough to allow for ongoing addition of new data elements. It should also accommodate various types of data. Creating data management systems will help program officers responsible for grant making to gather necessary information quickly and efficiently.

**Recommendation Two: Agencies should create tools and processes that facilitate program officers' interpretation of data and standardize the decision-making process.** Agencies should create tools that improve program officers' ability to interpret the meaning of different risk-related data elements. Creating frameworks for interpreting risk data will increase the consistency and accuracy of risk assessments. Ideally, agencies would create a risk assessment tool similar to the ERR that standardizes the decision-making process. One of the many strengths of the ERR is that its internal scoring system provides a common standard against which risk data is scored. Agencies are cautioned to ensure that the appropriate stakeholders are involved in the process of creating these common frameworks and scoring rubrics. RMS's experience highlights the importance of gathering input from program officers and of designing a collaborative process that is informed by the specific needs of program officers.

**Recommendation Three: Agencies should take advantage of the opportunity that the new OMB requirements create for improving risk management in awarding and overseeing federal grants.** Agencies that are interested in creating new risk assessment policies and tools should emphasize how these new internal processes will enable program officers to comply quickly and efficiently with OMB's new administrative requirements. Agencies should also emphasize how the introduction of new risk assessment practices within the agency is part of a larger movement across all federal agencies to develop increased capacity to implement risk management practices.

**Recommendation Four: The introduction of new risk management practices may represent change for some federal agencies and should be accompanied by training and capacity-building programs.** Attention should also be given to developing the necessary training and capacity-building programs so that program officers can understand and institutionalize these new business processes. RMS's success in sustaining the use of the new tool appears to have been due in large part to the sufficient amount of time and effort given to training new users and ensuring there is a consistent understanding of the tool.

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