

# *FEDERAL HOUSING FINANCE BOARD*



*Photos from "Habitat for Humanity"*

## OFFICE OF INSPECTOR GENERAL



# *SEMIANNUAL REPORT*

*FOR THE PERIOD  
October 1, 2005 - March 31, 2006*



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EDWARD KELLEY  
INSPECTOR GENERAL

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## EXECUTIVE SUMMARY

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The mission of the Office of Inspector General (OIG) at the Federal Housing Finance Board (Finance Board) is to support the agency's overall mission and goals established by the President, the Congress, and the Finance Board, while helping to protect the agency from fraud, waste, and abuse. Consistent with OIG's strategic plan for the period, April 1, 2004 to March 31, 2009, and in accordance with the Inspector General Act of 1978, as amended (IG Act), we continue to rely on audits, investigations, and formal and informal technical assistance to accomplish our mission. OIG's strategic plan and annual audit plan are designed to support the Finance Board's strategic plan. In that regard, we have continued evaluating the examination and supervision function and industry reporting requirements. We remained an active member in the federal Inspector General community to facilitate our statutory mandate to participate in government-wide efforts to prevent fraud, waste, and abuse and to remain current on matters affecting the IG community as well as the Finance Board. We continued to rely heavily on contracting for resources to accomplish required audits and investigations.

We conducted audits and audit recommendation follow-up of agency program and administrative functions. These audits were conducted in accordance with generally accepted government auditing standards issued by the Government Accountability Office. Five audits were in process at the beginning of the reporting period and three audits were initiated during the period. By the end of this reporting period, OIG had completed: 1) a Limited Review of the Finance Board's implementation of OMB Circular A-123, 2) a survey of the Office of Supervision, and 3) an audit of the Finance Board's Fiscal Year 2005 Financial Statements. Five audits were in process at the end of the reporting period. They are: 1) an audit of the disposition off IT equipment, 2) an audit of the quality of guidance provided to examiners, 3) an audit of the accuracy of FHFB merit pay calculations, 4) an audit of the Finance Board's compliance with the privacy provisions of the Consolidated Appropriation, and 5) an audit of the data integrity of the Call Reporting System. In addition, we completed the process of automating our audit working papers to improve process efficiency and security.

Our investigative activity was performed in accordance with [Quality Standards for Investigations](#) issued by the President's Council on Integrity and Efficiency (PCIE) and the Executive Council on Integrity and Efficiency (ECIE). As a result, during the reporting period, we received an unqualified peer review report on our operations. Investigative matters were appropriately coordinated with officials in the Department of Justice, the Federal Bureau of Investigations, and other law enforcement entities. We continued to focus on resolving investigative matters expeditiously and identifying control weaknesses that may contribute to possible fraud or abuse. We began the period with one allegation of possible wrongdoing in process and no investigation in process. During the reporting period, we received no additional allegations and referred the allegation in-process at the beginning of the period to the audit department for disposition. Consequently, no allegation remained in process at the end of the period.

We continued to maintain positive working liaisons with: 1) Finance Board officials, in efforts to identify and correct management problems and to clarify OIG authorities and responsibilities; 2) the Congress, in order to keep them appropriately informed; 3) external auditors, to facilitate timely and accurate reporting on Finance Board operations; and 4) the Inspector General community, to keep apprised of evolving issues that affect the Finance Board. Specifically, OIG continued to monitor and provide informal input, as appropriate, into management efforts to enhance the agency's procurement function, bill payment procedures, payroll function, and information technology function. We also continued to coordinate with other financial regulatory agencies and the Government Accountability Office on audits and reviews impacting the Finance Board. In addition, OIG participated in activities involving the entire Inspector General community. As part of our affiliation with the ECIE, we continued to coordinate peer reviews of ECIE members' audit operations – a mechanism for assuring quality audits by Inspectors General. We also responded to various inquiries involving the activities of the Inspector General community.

A handwritten signature in cursive script, appearing to read "Edward Kelley".

Edward Kelley  
Inspector General

***BACKGROUND ON THE FHLBANK SYSTEM, THE FINANCE BOARD,  
AND THE OFFICE OF INSPECTOR GENERAL***

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The Federal Home Loan Bank System (FHLBank System) was created in 1932 to promote home ownership and a strong home finance industry. Its network of 12 district Federal Home Loan Banks (FHLBanks) provides lending, deposit, and other services to member institutions. Originally, the FHLBank System's membership was limited to thrift institutions, whose membership was mandatory. Since the FHLBank System's inception, membership has grown to include savings and loans, savings banks, cooperative banks, and a small number of insurance companies. As of August 1989, membership was opened to commercial banks and credit unions that meet a commitment to housing finance, as defined in law. As of May 13, 2000, membership for all financial institutions in the system became voluntary.

The 12 FHLBanks borrow funds in the nation's credit markets to lend to the FHLBank System member institutions, which numbered 8,092 as of June 30, 2005. These institutions, in turn, use the funds for home mortgages, to meet savings withdrawal needs, and for other authorized purposes. As of June 30, 2005, the FHLBanks had outstanding loans (Advances) to member institutions totaling \$616 billion for these purposes. Through the Affordable Housing Program (AHP), the Federal Home Loan Bank System has provided approximately \$2.6 billion to help house some of America's neediest families. As of 2005, a total of more than 517,000 housing units were approved. Under the competitive application program, the AHP funded almost 471,000 units of which 70% were for very-low income households.

Concurrent with the Affordable Housing Program, the Federal Home Loan Bank System has increased its efforts in overall community development through its Community Investment Cash Advance (CICA) Programs including the Community Investment Program (CIP). CICA lending, not including AHP, since the inception of the program is more than \$44 billion as of December 31, 2005.

The Federal Housing Finance Board (Finance Board), with a fiscal year 2006 budget of approximately \$35.9 million and 131 employees, is the regulator of the FHLBank System. It is an independent agency established by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. The Finance Board's function is to ensure that FHLBanks: 1) operate in a safe and sound manner; 2) carry out their housing finance mission; and 3) remain adequately capitalized and able to raise funds in the capital markets. The Finance Board receives its operating funds from assessments levied against the 12 FHLBanks.

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The Finance Board has only indirect involvement – through the 12 FHLBanks – with the FHLBank System’s member institutions. Unlike its predecessor, the Federal Home Loan Bank Board, the Finance Board neither monitors nor examines any of the individual members of the FHLBank System. The Office of Thrift Supervision, a separate federal government agency, monitors, examines, and regulates individual member institutions. The Finance Board is only responsible for annually examining the 12 FHLBanks and the Office of Finance.

As of April 1, 2006 approximately 69 percent of the Finance Board’s staff resources are dedicated, in whole or in part, to: 1) examining the safety and soundness of the 12 FHLBanks and the Office of Finance; 2) reviewing and evaluating the work of each FHLBank’s internal audit staff; 3) monitoring FHLBank System compliance with laws, regulations, policies, and procedures; 4) assessing the FHLBank System’s financial condition; 5) modeling and analyzing the implementation of financial policies; 6) maintaining and promulgating membership policies; 7) monitoring the election and appointment of FHLBank Directors; 8) collecting information on individual FHLBank policies and marketing activities; and 9) monitoring and reviewing FHLBank and members’ compliance with requirements of the Affordable Housing Program and the Community Investment Program.

The Office of Inspector General (OIG) is responsible for the conduct of audits and investigations at the Finance Board in accordance with generally accepted government auditing standards and investigative standards. OIG may also conduct audit or investigative activities at the 12 FHLBanks and other related entities when: 1) requested to do so by the Chairman; 2) necessary to obtain information on the Finance Board’s administration of its program; and 3) aimed at detecting fraud or inefficiency in the administration or operation of Finance Board programs.

## AUDIT ACTIVITY

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On April 19, 2004, OIG issued its Strategic Plan for the period April 1, 2004 to March 31, 2009. OIG's annual audit plan for the period April 1, 2006 to March 31, 2007, is included as an Exhibit to the five-year strategic plan. Both can be viewed at OIG's website <http://intranet.fhfb.gov/FBOffices/oig.htm>. During the semiannual reporting period October 1, 2005 through March 31, 2006, OIG completed three audits ([Table A](#) on page 9). At the conclusion of this period, OIG also had five audits in process. OIG continued to coordinate with the Government Accountability Office and the Inspector General community on audits that impact the Finance Board. Specifically, OIG's audit activities included:

### COMPLETED

- A limited review of FHFB's compliance with OMB Circular A-123,
- An audit of FHFB's financial statements for fiscal year 2005, and
- A survey of FHFB's Office of Supervision.

### WORK-IN-PROCESS

- An audit of FHFB's disposition of IT equipment,
- An audit of the quality of examiners' guidance,
- An audit of FHFB Merit Promotion Pool Calculations,
- An audit of FHFB Data Integrity of the Call Reporting System, and
- An audit of the Adequacy of FHFB's Privacy and Data Protection Procedures and Policies.

## INVESTIGATIVE ACTIVITY

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The number of investigative matters processed by the Office of Inspector General during this reporting period declined to zero. We had one investigative matter in process at the beginning of the reporting period and we received no additional allegations. The one allegation involved the propriety of a sole source contract award. By the end of the period, the allegation was closed after the preliminary investigation stage.

During this reporting period OIG underwent a voluntary peer review of its investigative function. The peer review was performed by the Commodity Futures Trading Commission Office of Inspector General and they concluded that OIG was in full compliance with the PCIE/ECIE Quality Standards for Investigations.

Table B, on page 10, contains a numerical summary of investigations, allegations, preliminary inquires, and referrals.

## SUMMARY OF "SECTION 5" REPORTING REQUIREMENTS

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1. Significant problems, abuses, deficiencies disclosed by management and IG's recommended corrective actions [5a(1) and (2)]  

None
2. Previously reported significant recommendations with incomplete corrective actions [5a(3)]  

None
3. Prosecution, convictions, and referrals [5a(4)]  

None
4. Reports on failure to provide information or assistance [5a(5)]  

None
5. List of issued audit reports [5a(6)]  

See attached [Table A](#).
6. Summary of significant reports [5a(7)]  

OIG completed an audit of FHFB's compliance with the Federal Information Security Management Act and identified a continued problem with the lack of an organizational structure to promote the independence of the CIO in addressing FHFB information technology operations. However, the Chairman has taken action to realign the Finance Board operations to eliminate the organizational independence issue.

OIG completed a survey of FHFB's Office of Supervision (OS). The survey resulted in the identification of several audits that will be performed by OIG or OIG contractors to assess OS' efforts to identify safety, soundness, and affordable housing issues at the twelve Federal Home Loan Banks and OS' success in facilitating the resolution of these issues. OIG has initiated a detailed audit of the adequacy of examiner guidance as a result.

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7. Statistical table – audits with questioned/unsupported costs [5a(8)]  
See attached [Table C](#).
8. Statistical table – audits recommending that funds be put to better use [5a(9)]  
See attached [Table D](#).
9. Summary of prior-period audits with no current management decisions [5a(10)]  
None
10. Reasons for revisions of significant management decisions [5a(11)]  
None
11. OIG disagreement with management decisions [5a(12)]  
None

TABLE A

**LISTING OF COMPLETED AUDITS, SURVEYS, LIMITED REVIEWS,  
AND EVALUATIONS**

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<u>REPORT NUMBER REPORT</u>	<u>DATE COMPLETED</u>	<u>TITLE OF</u>
05-A-04-OS	October 27, 2005	OIG Survey Results of the FHFB's Office of Supervision
05-A-05-OM	October 24, 2005	Audit of Federal Housing Finance Board Financial Statements
05-R-06-OM	October 31, 2005	Limited Review of FHFB Implementation of Office of Management and Budget Circular A-123

**SUMMARY OF INVESTIGATIONS**

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**BEGINNING CASES** **NUMBERS**

Cases Pending at the Beginning of Period:

At the Finance Board.....	1
At the Department of Justice.....	0
At other agencies.....	0

**NEW CASES RECEIVED**

Allegations Received During Current Period.....	0
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**STATUS OF CASES** (as of March 31, 2006)

Resulted in:

Allegations Pend. Completion of Prelim. Invest/Audit.....	0
Preliminary Investigation Completed- (Cases Closed).....	1
Cases Pending Completion of Full Investigation.....	0
Full Investigation Completed- (Cases Closed).....	0
Cases Scheduled for Audit/Ltd. Rev. – (Cases Closed).....	0
Cases Pending Decision by Finance Board management.....	0
Cases Pending Decision by Dept. of Justice.....	0
Cases Pending Decision by Other Agencies.....	0
Cases Referred to FHFB Management- (Cases Closed).....	0
Referred to Other Agencies- (Cases Closed).....	0

**DISPOSITION**

Civil.....	0
Criminal.....	0
Administrative Sanctions.....	0
Corrective Action Taken.....	0
Other (Pending/Referrals, etc.).....	0

TABLE C

INSPECTOR GENERAL REPORTS  
WITH QUESTIONED/UNSUPPORTED COSTS

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	<u>DOLLAR VALUE</u>		
	<u>NUMBER OF REPORTS</u>	<u>QUESTIONED COSTS</u>	<u>UNSUPPORTED COSTS</u>
a. For which no management decision has been made by the commencement of the reporting period.....	0	0	0
b. Which were issued during the reporting period.....	0	0	0
Subtotals (a+b).....	0	0	0
c. For which a management decision was made during the reporting period.....	0	0	0
(i) dollar value of disallowed costs..	0	0	0
(ii) dollar value of costs not disallowed.....	0	0	0
d. For which no management decision has been made by the end of the reporting period.....	0	0	0
e. Report for which no management decision was made within six months of issuance.....	0	0	0

Note: Boldface type entries reflect actual statutory language.

INSPECTOR GENERAL REPORTS  
RECOMMENDING THAT FUNDS BE PUT TO BETTER USE

TABLE D

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	<u>NUMBER OF REPORTS</u>	<u>DOLLAR VALUE</u>
a. For which no management decision has been made by the commencement of the reporting period.....	0	0
b. Which were issued during the reporting period.....	0	0
Subtotals (a+b).....	0	0
c. For which a management decision was made during the reporting period.....	0	0
(i) dollar value of recommendations that was agreed to by management.....	0	0
- based upon proposed management action....	0	0
- based upon proposed legislation action.....	0	0
(ii) dollar value of recommendations that were not agreed to by management.....	0	0
d. For which no management decision has been made by the end of the reporting period.....	0	0
e. Reports for which no management decision was made within six months of issuance.....	0	0

Note: Boldface entries reflect actual statutory language.