

FEDERAL HOUSING FINANCE BOARD



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OFFICE OF INSPECTOR GENERAL



SEMIANNUAL REPORT

FOR THE PERIOD
April 1, 2007 – September 30, 2007



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EDWARD KELLEY
INSPECTOR GENERAL

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EXECUTIVE SUMMARY

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, 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 examined agency efforts to hire and retain qualified examiners. We continued to address agency administrative policies and procedures related to financial reporting, privacy, and information technology security. We remained an active member in the federal Inspectors 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 and assistance from other members of the Inspector General community 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. Two audits were in process at the beginning of the reporting period and five audits were initiated during the period. By the end of this reporting period, OIG had completed an audit of the Finance Board's compliance with the Federal Information Security Management Act. Six audits remained in process at the end of the reporting period. They are: 1) an audit of the Finance Board's Fiscal Year 2007 Financial Statements, 2) a limited review of the Finance Board's implementation of OMB Circular A-123, 3) an audit of the Thoroughness of Examinations, 4) an audit of the Finance Board's Continuity of Operations Plan, 5) an audit of the Disposition of IT equipment, and 6) an audit of the Finance Board's Merit Pay Increase Process.

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). Investigative matters continue to be appropriately coordinated with officials in the Department of Justice, the Federal Bureau of Investigation, 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. During the reporting period, we received two allegations. After a preliminary review, one of the allegations was closed and the second 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's mission, authorities and responsibilities; 2) 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 stay 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 human resources function, bill payment procedures, payroll function, and information technology security 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 Inspector Generals - and began hosting the monthly meetings of the ECIE. We also began serving on the PCIE/ECIE audit committee and responded to various inquiries involving the activities of the Inspector General community.

A handwritten signature in cursive script, reading "Edward Kelley". The signature is written in black ink and features a large, sweeping initial "E" and a long, horizontal flourish at the end.

Edward Kelley
Inspector General

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

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 totaled 8119 as of June 30, 2007. These institutions, in turn, use the funds for home mortgages, to meet savings withdrawal needs, and for other authorized purposes. As of June 30, 2007, the FHLBanks had outstanding loans (Advances) to member institutions totaling \$642.1 billion for these purposes. Also, through December 31, 2006 the Affordable Housing Program (AHP) of the Federal Home Loan Bank System has provided approximately \$2.9 billion to help house some of America's neediest families. As of December 31, 2006, more than 575,000 housing units were approved. Under the competitive application program, the AHP funded almost 518,000 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). From 1990 through 2006, the CIP has provided more than \$37 billion in advances for housing, and CICA and CIP together have provided \$11.4 billion in advances and grants for economic development projects benefiting targeted communities and households.

The Federal Housing Finance Board (Finance Board), with a fiscal year 2007 budget of approximately \$35.9 million and 143.5 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.

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, 2007 approximately 80 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

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, 2007 to March 31, 2008, is included as an Exhibit to the five-year strategic plan. Both can be viewed at the OIG's web page located at <http://www.fhfb.gov/Default.aspx?Page=100> . During the semiannual reporting period April 1, 2007 through September 30, 2007, OIG completed one audit (**Table A**, on page 9). At the conclusion of this period, OIG also had six audits in process. OIG continued to coordinate with the Government Accountability Office and the Inspector General community on audits that impact the Finance Board. In this regard, the Inspector General was appointed to serve on the IG community's Audit Committee and continued to coordinate audit peer reviews that each ECIE IG's office is required by statute to undergo every three years. Specifically, OIG's audit activities at the Finance Board included:

COMPLETED

An audit of the Finance Board's Compliance with the Federal Information Security Management Act.

WORK-IN-PROCESS

A limited scope review of the Finance Board's compliance with OMB Circular A-123,

An audit of the Finance Board's financial statements for fiscal year 2007,

An audit of the Thoroughness of Examinations,

An audit of the Finance Board's Continuity of Operations Plan,

An audit of the Finance Board's disposition of IT equipment, and

An audit of the Finance Board's Merit Pay Increase Process.

INVESTIGATIVE ACTIVITY

During this reporting period OIG continued to operate in full compliance with the PCIE/ECIE Quality Standards for Investigations. The number of investigative matters processed by the Office of Inspector General during this reporting period remained constant. We had no investigative matters in process at the beginning of the reporting period but did receive two allegations during the period. One of the allegations was closed after the preliminary investigation stage. The second matter remained under preliminary review at the end of the reporting period.

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

SUMMARY OF "SECTION 5" REPORTING REQUIREMENTS

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**, on page 9.

6. **Summary of significant reports** [5a(7)]

In accordance with the Federal Information Security Management Act, OIG contracted for an audit of the Finance Board's security over electronic information processing. While several matters were noted, none were significant. The agency's Chief Information Officer and his staff have a commendable program for continually identifying potential information security threats and hardening the agency's security measures to counter the potential security threats.

7. **Statistical table – audits with questioned/unsupported costs** [5a(8)]

See attached **Table C**, on page 11.

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8. **Statistical table – audits recommending that funds be put to better use** [5a(9)]
See attached **Table D**, on page 12
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

<u>REPORT NUMBER</u>	<u>DATE COMPLETED</u>	<u>TITLE OF REPORT</u>
07-A-03-ISTS/OM	September 21, 2007	Audit of the Finance Board's Compliance with the Federal Information Security Management Act

SUMMARY OF INVESTIGATIONS

<u>BEGINNING CASES</u>	<u>NUMBERS</u>
Cases Pending at the Beginning of Period:	
At the Finance Board.....	0
At the Department of Justice.....	0
At other agencies.....	0
 <u>NEW CASES RECEIVED</u>	
Allegations Received During Current Period.....	
 <u>STATUS OF CASES</u> (as of March 31, 2006)	
Resulted in:	
Allegations Pend. Completion of Prelim. Invest/Audit.....	1
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 the Finance Board Management- (Cases Closed).....	0
Referred to Other Agencies- (Cases Closed).....	0
 <u>DISPOSITION</u>	
Civil.....	0
Criminal.....	0
Administrative Sanctions.....	0
Corrective Action Taken.....	0
Other (Pending/Referrals, etc.).....	0

**INSPECTOR GENERAL REPORTS
WITH QUESTIONED/UNSUPPORTED COSTS**

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

Note: Boldface type entries reflect actual statutory language.

**INSPECTOR GENERAL REPORTS
RECOMMENDING THAT FUNDS BE PUT TO BETTER USE**

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

Note: Boldface entries reflect actual statutory language