

REPORT

ON

**LIMITED REVIEW OF FEDERAL HOUSING FINANCE BOARD (FHFB)
COMPLIANCE WITH OFFICE OF MANAGEMENT AND BUDGET (OMB)
CIRCULAR NO. A-123**

FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 2008

PERFORMED FOR

FEDERAL HOUSING FINANCE BOARD



**OFFICE OF INSPECTOR GENERAL (OIG)
OIG REPORT NUMBER: 08-A-07-OM**

UNDER

CONTRACT: TPD-FHB-BPA-07-0004

TASK ORDER: 0002 (FHB-17000-08-0029)

REPORT DATE: OCTOBER 3, 2008

REPORT SUBMISSION DATE: OCTOBER 30, 2008

NOTICE OF EVENTS

On July 30, 2008, the President signed the “Housing and Economic Recovery Act of 2008” (Act). The Act gives the Finance Board responsibility for winding up the affairs of FHFB by July 30, 2009. Consequently, recommendations in this report that relate to matters associated with winding up the affairs of FHFB will be forwarded to the Chairman of FHFB for action under the authorities delegated to him by the FHFB.

**LIMITED REVIEW OF FEDERAL HOUSING FINANCE BOARD (FHFB)
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CIRCULAR NO. A-123**

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EXECUTIVE SUMMARY

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The Federal Housing Finance Board (FHFB), Office of Inspector General (OIG) contracted Deva & Associates, P.C. (D&A) to perform a limited review of FHFB's implementation of the requirements of Office of Management and Budget (OMB) Circular No. A-123 (Circular A-123) "Management's Responsibility for Internal Control" as revised December 21, 2004. OMB defines three objectives of internal control in Circular A-123: (1) effectiveness and efficiency of operations, (2) reliability of financial reporting, and (3) compliance with applicable laws and regulations.

Objective

D&A's objective was to determine whether FHFB complied with the OMB Circular A-123 implementation guidelines, which requires federal managers to establish a continuous process for evaluating, improving, and reporting on internal controls for which management is responsible.

Scope and Methodology

The limited scope review was performed in accordance with the American Institute of Certified Public Accountants (AICPA) Statements on Standards for Attestation Engagements and Generally Accepted Government Auditing Standards established by the Comptroller General of the United States.

D&A reviewed FHFB's management processes, policies and procedures for implementation of OMB Circular A-123 and the communication submitted to FHFB's Chairman, which included the review of reporting requirements in OMB Circular A-123 Appendix B "Improving the Management of Government Charge Card Programs," as revised April 28, 2006. The review did not include the requirements of Appendix A, which only applies to the cabinet level departments, and Appendix C, as FHFB's expenditures do not meet the threshold requirements established in this appendix.

1. Review OMB Circular A-123, including Appendix B, "Improving the Management of Government Charge Card Programs" and FHFB policies and procedures for implementing the requirements.
2. Review FHFB's implementation of requirements for the fiscal year ended September 30, 2008 to ascertain whether:
 - A senior level official was assigned to coordinate FHFB's implementation of OMB Circular A-123;
 - FHFB followed its policies and procedures for implementation;
 - Agency staff, both managers and staff level, were used in the evaluation process;
 - Office Directors or senior-level managers:
 - i. Completed the Vulnerability Assessment Profiles;
 - ii. Completed the Management Control Questionnaires; and
 - iii. Prepared the Letter of Assurance to the Chairman.

EXECUTIVE SUMMARY

3. Review the risk assessment and Management Control Questionnaires prepared by senior level managers for each Office and Department to determine whether:
 - Management Control Questionnaires and Vulnerability Assessment Profiles were consistent with assertion made in the Letters of Assurance, reports and other management information reviewed;
 - Documents submitted were complete; and
 - Letters of Assurance included plans and schedules to correct weaknesses.
4. Perform follow-up on management's implementation of recommendation from the FY 2007 limited review.

Conclusion and Recommendations

Overall, FHFB has adequately implemented the requirements of OMB Circular A-123 for the fiscal year ended September 30, 2008. However, the results of the review identified the following recommendations, which FHFB should address to improve the implementation of the requirements of OMB Circular A-123 or FHFB's internal control structure:

- A strategic sourcing policy should be considered when consolidating the credit card and purchasing policies and procedures of FHFB and the Office of Federal Housing Enterprise Oversight (OFHEO).
- Establishment of a senior management council, which would meet at least monthly, should be considered to monitor and manage internal control related matters during the merger of FHFB and OFHEO.
- Development of detailed departmental organization charts should be considered during the merger of FHFB and OFHEO to clearly define the departmental structure, significant responsibilities and lines of authority within each department.

INDEPENDENT ACCOUNTANTS' REPORT


INDEPENDENT ACCOUNTANTS' REPORT

To the Office of the Inspector General
Federal Housing Finance Board
Washington, DC

We have performed the procedures referenced below, which were agreed to by the Federal Housing Finance Board (FHFB) Office of Inspector General's (OIG's) management, solely to assist the users in evaluating their implementation of requirements with the revised Office of Management and Budget (OMB) Circular No. A-123 (Circular A-123) "Management's Responsibility for Internal Control" for the fiscal year ended September 30, 2008. This agreed upon procedures engagement was performed in accordance with standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the specified users of the report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

The procedures applied throughout this engagement are enumerated in the Section 3 of this report. We were not engaged to, and did not, perform an examination, the objective of which would be the expression of an opinion on management's assertion. Accordingly, we do not express an opinion. We were not engaged to, and did not assess the FHFB's internal controls themselves. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the use of the FHFB OIG management.



Certified Public Accountants

October 3, 2008

SECTION 1

BACKGROUND

BACKGROUND

Office of Management and Budget (OMB) Circular No. A-123 (Circular A-123)

OMB Circular A-123, "Management's Responsibility for Internal Control" was revised December 21, 2004 to address management's responsibility for internal control. OMB defines three objectives of internal control in Circular A-123: (1) effectiveness and efficiency of operations, (2) reliability of financial reporting, and (3) compliance with applicable laws and regulations.

Under Section 2 of the Federal Managers Financial Integrity Act of 1982 (FMFIA), the head of each executive agency is required to annually submit to the President and the U.S. Congress (1) a statement on whether there is reasonable assurance that the agency's controls are achieving their intended objectives, and (2) a report on material weaknesses, if any, in the agency's controls.

Federal Housing Finance Board (FHFB)

FHFB is an independent federal agency established by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). FHFB is successor to the former Federal Home Loan Bank Board (FHLBB), which was established by the Federal Home Loan Bank Act of 1932. FHFB is charged with supervising and regulating the 12 Federal Home Loan Banks and has the statutory authority to ensure that the Federal Home Loan Banks operate in a financially safe and sound manner, maintain adequate capitalization, raise funds in the capital markets, and carry out their housing finance mission. FHFB also has the regulatory authority and supervisory oversight responsibility for the Office of Finance (OF), which is the fiscal agent for the 12 Federal Home Loan Banks. The Board of Directors (Board) of FHFB is comprised of five members, four of which are appointed by the President and confirmed by the Senate. The fifth member is the Secretary of the Department of Housing and Urban Development. Board members serve staggered seven-year terms. All Board members must have extensive experience or training in house finance or a commitment to providing specialized housing credit. At least one member must be from an organization with more than a two-year history of representing consumer or community interests in banking services, credit needs, housing, or financial consumer protections.

A management analyst with the Office of Management (OM) was assigned the task of coordinating FHFB's implementation of OMB Circular A-123 requirements. A management council was utilized to review the results of Office and Department assessments and communication of the results to the FHFB Chairman. The management council consisted of the Chief Financial Officer (CFO), Chief Information Officer (CIO), procurement official and management analyst.

On July 18, 2008, FHFB distributed a memorandum to all Office Directors with instructions to complete a set of evaluation documents to implement OMB Circular A-123 requirements. The memorandum included, as attachments: FHFB's Internal Control Procedures, the Vulnerability Analysis Profile with instructions, the Internal Control Questionnaire with instructions, and an

BACKGROUND

example Assurance Letter. The instructions emphasized that the evaluation process should include participation of both management and staff.

Office of Inspector General (OIG)

The mission of FHFBS's OIG is to support the agency's overall mission and goals established by the President, Congress and FHFBS. In accordance with the Inspector General Act of 1978, as amended, the OIG helps protect FHFBS from fraud, waste, and abuse. The OIG is responsible for the internal audits and investigations at FHFBS in accordance with generally accepted government auditing standards and investigative standards. OIG may also conduct audit or investigative activities at the 12 Federal Home Loan Banks.

To assist FHFBS in evaluating its management control program, the OIG annually conducts a limited review of FHFBS's implementation of OMB Circular A-123, and the departmental assessments reported to FHFBS's Chairman. Deva & Associates, P.C. (D&A) was contracted by the FHFBS OIG to perform the limited review of FHFBS's compliance with OMB Circular A-123 for the fiscal year ended September 30, 2008.

SECTION 2

OBJECTIVES, SCOPE AND METHODOLOGY

OBJECTIVES, SCOPE AND METHODOLOGY

Within FHFB's organization structure, four offices and one division were required to submit the information relevant to assessing internal controls in accordance with OMB Circular A-123, as follows:

- Office of the General Counsel (OGC);
- Office of Inspector General;
- Office of Management;
- Office of Supervision (OS); and
- Information Systems and Technology Support Division (ISTS).

The Office of the Chairman prepared the submission for ISTS. The Office of Board of Directors was not required to submit information since this office is the recipient of the results of the assessments and evaluation.

Objective

D&A's objective was to determine whether FHFB complied with the OMB Circular A-123 implementation guidelines, which requires federal managers to establish a continuous process for evaluating, improving, and reporting on internal controls for which management is responsible.

Scope

The limited scope review was performed in accordance with the American Institute of Certified Public Accountants (AICPA) Statements on Standards for Attestation Engagements and Generally Accepted Government Auditing Standards established by the Comptroller General of the United States.

The limited scope review included the review of reporting requirements in OMB Circular A-123 Appendix B "Improving the Management of Government Charge Card Programs," as revised April 28, 2006.

The review did not include assessing FHFB's internal controls. In addition, FHFB's reporting requirement under OMB Circular No. A-123 does not include the requirements of Appendix A, which only applies to the cabinet level departments, and Appendix C, as FHFB's expenditures do not meet the threshold requirements established in this appendix.

Methodology

D&A reviewed FHFB's management processes, policies and procedures for implementation of OMB Circular A-123 and the communication submitted to FHFB's Chairman. The review was conducted from September 3, 2008 to October 10, 2008 at the office of FHFB in Washington, DC and at D&A's office in Rockville, Maryland.

SECTION 3

PROCEDURES APPLIED AND RESULTS

PROCEDURES APPLIED AND RESULTS

D&A assessed FHFB's compliance with OMB Circular A-123. The objective was to determine whether the process used by FHFB for assessing FHFB's internal controls is properly designed and implemented. The procedures performed for this limited review were as follows:

1. **Government Charge Card Programs" and FHFB policies and procedures for implementing the requirements.**

Results:

- A management analyst with the Office of Management was assigned the task of coordinating FHFB's implementation of OMB Circular A-123 requirements. A management council, consisting of the CFO, CIO, procurement official and management analyst, was utilized to review the results of Office and Department assessments and communication to the FHFB Chairman.
- FHFB's Charge Card Management Plan complied with the requirements of OMB Circular A-123 Appendix B, except the plan did not address strategic sourcing policies.
- OM documented the controls related to the accounting functions outsourced to the Bureau of Public Debt.
- FHFB offices did not utilize detailed organization charts as recommended in prior year reviews. OM created a "Who Does What Guide" which identified OM functions and the primary and backup staff responsible for the function. Although the guide identified staff responsibilities, the lines of authority which would be provided in a detailed organization chart were not identified in the guide.

2. **Review FHFB's implementation of requirements for the fiscal year ended September 30, 2008 to ascertain whether:**

- **A senior level official was assigned to coordinate FHFB's implementation of OMB Circular A-123;**
- **FHFB followed its policies and procedures for implementation;**
- **Agency staff, both managers and staff level, were used in the evaluation process;**
- **Office Directors or senior-level managers:**
 - i. **Completed the Vulnerability Assessment Profiles;**
 - ii. **Completed the Management Control Questionnaires; and**
 - iii. **Prepared the Letter of Assurance to the Chairman.**

Results:

- Office Directors for the OS, OM, OIG and OGC and the Assistant to the Chairman for the ISTS submitted the following documents:
 - i. Vulnerability Assessment Profiles;
 - ii. Management Control Questionnaires or equivalent; and
 - iii. Letter of Assurance.

PROCEDURES APPLIED AND RESULTS

- OS conducted a staff survey. Only staff members included on the management council were excluded from the survey. Two survey forms were utilized. The non-management staff survey excluded questions that applied only to management. The results of the survey were accumulated, summarized in a memorandum and submitted in lieu of completing the Management Control Questionnaire. Although the instructions and questions distributed to staff were not included in the information submitted, OS subsequently provided a copy for review. The survey was conducted in accordance with the FHFB policies and procedures for implementing the OMB Circular A-123 review.
 - All Letters of Assurance indicated that the staff was involved in the internal control evaluation.
 - The following audit report is pending:
 - i. FY 2008 annual audit.
 - The FY 2007 annual audit was issued with an unqualified opinion. The CFO indicated that no management comments were received.
3. **Review the risk assessment and Management Control Questionnaires prepared by senior level managers for each Office and Department to determine whether:**
- **Management Control Questionnaires and Vulnerability Assessment Profiles were consistent with assertion made in the Letters of Assurance, reports and other management information reviewed;**
 - **Documents submitted were complete; and**
 - **Letters of Assurance included plans and schedules to correct weaknesses.**

Results:

- The Management Control Questionnaires and Vulnerability Assessment Profiles submitted by OS, OM, OIG, OGC and ISTS were consistent with the Letters of Assurance submitted to the Chairman and other reports and management information reviewed.
- The documents submitted were complete.
- The following weaknesses in policies and procedures were noted as a result of this limited review:
 - i. The organization charts had not been modified to provide better detail of responsibilities and lines of authority;
 - ii. FHFB's guidance for conducting surveys should require the agency to include the instruction(s) and questionnaire(s) created for the survey as part of the required submission;
 - iii. The FY 2008 Privacy Audit identified one repeat finding from FY 2006 relating to logging all computer-readable data extracts from databases; and

PROCEDURES APPLIED AND RESULTS

iv. The FY 2008 Federal Information Security Management Act (FISMA) audit identified one reportable condition and several management comments. The reportable condition identified that the interconnection service agreement (ISA) between FHFBS's Call Reporting System (CRS) and the Office of Finance Financial Reporting System is out of date.

- No material weaknesses were reported by FHFBS or noted during this review.
- No plans or schedules were provided in the Letters of Assurance to correct weaknesses.
- The Federal Housing Finance Regulatory Reform Act of 2008 was enacted on July 30, 2008. The law established the Federal Housing Finance Agency (FHFA) an independent federal agency created as the successor regulatory agency resulting from the statutory merger of the FHFBS and the office of Federal Housing Enterprise Oversight (OFHEO). FHFA absorbed the powers and regulatory authority of both entities, with expanded legal and regulatory authority. One year after the law was signed, OFHEO and FHFBS will go out of existence. All existing regulations, orders and decisions of OFHEO and FHFBS remain in effect until modified or superseded. The director of OFHEO, is the director of the FHFA. OM indicated that process improvements and corrective action to audit and review findings will be considered in the overall effort to develop new systems, processes and procedures for FHFA.

4. Perform follow-up on management's implementation of recommendation from the FY 2007 limited review.

Results:

- The prior year limited A-123 review recommended that FHFBS monitor the procurement activities to ensure compliance with sound procurement practices and avoid conflicts of interest situations. FHFBS management did not address this comment in the current year internal control evaluation. Discussion with FHFBS management indicated that management continually attempts to maintain sound procurement practices and avoid conflict of interest situations. For additional follow-up to the prior year's comment see Section 4 – Prior Year Comment and Follow-up to Management's Response.

SECTION 4

**PRIOR YEAR COMMENT AND FOLLOW-UP TO MANAGEMENT'S
RESPONSE**

PRIOR YEAR COMMENT AND FOLLOW-UP TO MANAGEMENT'S RESPONSE

Prior Year Comment and Recommendation

During the prior year review, the auditor indicated that the Acting Director does not initiate a purchase requisition or sign a payment voucher, and does not serve as Contracting Officer's Technical Representative (COTR). FHFB's response to the prior year draft report clarified that the Acting Director is a COTR on an interagency agreement with the Office of Personnel Management (OPM) and approves Intra-governmental Payment and Collection (IPAC) System vouchers. The prior year auditor concluded the roles and responsibilities of the Acting Director (or Program Manager), Chief Procurement Office (or Contracting Officer) and COTR might have a conflict of interest in the following procurement acquisition phases: (1) strategic planning, (2) investment review, (3) project initiation, (4) requirement analysis, (5) acquisition planning, (6) Pre-RFP considerations, (7) RGQ preparation and issuance, (8) evaluating offices, (9) source selection, (10) contract management, (11) contract changes and (12) contract closeout. The assessment process does not ensure adequate controls in segregation of duties to avoid conflict of interest situations for these roles and responsibilities.

The prior year auditor recommended that FHFB monitor the procurement activities to ensure compliance with sound procurement practices and avoid conflicts of interest situations.

Follow-up to Prior Year Management's Response

The OM Acting Director provided a response to the final draft report for the fiscal year ended September 30, 2007 indicating that there were no current year comments. The response did clarify that due to FHFB's small size, the workload for a full-time Chief Procurement Officer or Chief Privacy Officer was insufficient. The current year review did not address this recommendation. The OM Director, who serves as the Contracting Officer, indicated that management attempts to maintain sound procurement practices and avoid conflict of interest situations whenever possible.

D&A recommends that FHFB continue to monitor opportunities to strengthen procurement practices. The statutory merger of FHFB and OFHEO into the Federal Housing Finance Agency (FHFA) provides another opportunity review procurement practices and establish policies and procedures that avoid conflicts of interest and allow for greater segregation of duties. FHFB's transition team should include this recommendation in the implementation plan as part of the overall effort to develop new systems, processes and procedures for FHFA.

SECTION 5

CURRENT YEAR FINDINGS AND RECOMMENDATIONS

CURRENT YEAR FINDINGS AND RECOMMENDATIONS

Overall, FHFB has adequately implemented the requirements of OMB Circular A-123 for the fiscal year ended September 30, 2008. However, during the review the following recommendations were noted, which FHFB should address to improve the implementation of the requirements of OMB Circular A-123 or FHFB's internal control structure.

FHFB's Credit Card Management Plan did not include implementation policies and practices to ensure strategic sourcing as addressed in Chapter 8 of Appendix B in OMB Circular A-123. Strategic sourcing is the process of continually analyzing the way agencies spend funds, including through the government purchase card program, in order to ensure that agencies are:

- Leveraging their sourcing power by seeking opportunities to achieve discounts on commonly purchased goods and services; and
- Applying discounts to all charge card transactions, as appropriate.

Strategic sourcing is important because each transaction has the potential to increase the sourcing power of the government. Purchase card program managers should be aware of any agency-wide or multi-agency wide contracts that will yield better pricing and ensure that cardholders are aware of agency policies for using these contracts. Section 8.3 of Appendix B provides guidance on what agencies are required to do to implement a strategic sourcing for a purchase card program.

FHFB management indicated that approximately \$194,000 (75 percent) of purchase card transactions made in FY 2008 was for non-commodity items such as training, subscriptions, software, building maintenance and professional dues. Based on the volume and number of cardholders, developing a detailed process would most likely be more costly than any potential benefits received.

Although FHFB's purchase card transactions are not materially significant and would not warrant a detailed strategic sourcing plan, a process can be implemented that is cost effective. In addition, the strategic sourcing plan should not be limited to purchase card transactions. The plan should apply to the entire procurement process. FHFB could identify agencies with existing purchasing contracts, which could benefit FHFB or determine if BPD has any established procedures in place that can be used by FHFB to comply with this requirement. At a minimum, a strategic sourcing plan should be implemented during the transition to FHFA and incorporated for both credit card and other purchasing programs.

A senior management council should be established and meet at least monthly to oversee the transition to FHFA. FHFB management is responsible for maintaining a strong internal control system throughout the year. FHFB's management council meets near the end of the year to begin the internal control review process. Larger agencies have senior management councils that meet regularly throughout the year due to the complexity of the agency.

FHFB management indicated that it was not aware of any plans in place for the transition to FHFA. The transition to FHFA will bring challenges for maintaining strong internal controls for

CURRENT YEAR FINDINGS AND RECOMMENDATIONS

the two agencies merging and the new successor agency. A senior management council should be established to coordinate and manage OMB Circular A-123 activities, including review, documentation and testing of internal controls as new systems, policies and procedures are developed.

In prior year reviews, departmental organization charts did not provide adequate detail. Finding recommended that departmental organization charts be revised to show the departmental hierarchy as well as duties. Although management has subsequently documented or demonstrated the roles and responsibilities of departmental staff by revising the organization chart and/or creating additional documents, the current organization charts do not document a comprehensive picture of a department's structure, responsibilities and hierarchy. A detailed organizational chart for each department would provide senior management an effective tool to understand segregation of duties and other departmental controls and provide all staff with a document that defines departmental structure, responsibilities and hierarchy.

To continue to improve the organization charts and related documentation, detailed departmental organization charts should be considered during the merger of FHFB and OFHEO to clearly define the departmental structure, significant responsibilities and lines of authority within each department.

