

FEDERAL HOUSING FINANCE BOARD



OFFICE OF INSPECTOR GENERAL



SEMIANNUAL REPORT

**FOR THE PERIOD
APRIL 1, 2003 – SEPTEMBER 30, 2003**

REVISED



OFFICE OF INSPECTOR GENERAL

SEMIANNUAL REPORT

FOR THE PERIOD
APRIL 1, 2003 – SEPTEMBER 30, 2003

EDWARD KELLEY
INSPECTOR GENERAL

TABLE OF CONTENTS

<i>Executive Summary</i>	1
<i>Background on the FHLBank System, the Finance Board, And the Office of Inspector General</i>	3
<i>Audit Activity</i>	5
<i>Investigative Activity</i>	6
<i>Summary of “Section 5” Reporting Requirements</i>	7
Table A – <i>Listing of Completed Audits, Surveys, Limited Reviews, and Evaluations</i>	9
Table B – <i>Summary of Investigations</i>	10
Table C – <i>IG Reports with Questioned/Unsupported Costs</i>	11
Table D – <i>IG Reports Recommending Better Use of Funds</i>	12

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, 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, 2001 to March 31, 2006, and in accordance with the Inspector General Act of 1978, as amended (IG Act), we have relied on audits, investigations, and formal and informal technical assistance to accomplish our mission. The Finance Board's strategic plan continues to be under revision. However, we continued to coordinate with Finance Board management and to enhance our value to the Finance Board by regularly meeting with agency management and directly soliciting management suggestions for audits and/or investigations. The results of this coordination is incorporated into OIG's strategic plan and annual audit plan. 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. During this period, we have relied heavily on contracting and reimbursable arrangements to accomplish required audits and investigations. However, because two-budgeted FHFB-OIG audit positions were not funded, our ability to hire and properly monitor contractors' work was greatly limited. As a result, some planned audit work has had to be delayed.

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. Two audits were in process at the beginning of the reporting period. By the end of this reporting period, OIG had completed an audit of the Finance Board's Fiscal Year 2002 Financial Statements. Three audits remained in process at the end of the period: 1) an audit of the process for recruiting and retaining examiners, 2) an audit of the Finance Board's compliance with the Federal Information Security and Management Act, and 3) an audit of the Finance Board's Procurement Policies, Procedures, and Practices.

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 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 three allegations of possible wrongdoing in process. During the reporting period, we received one additional allegation. Three allegations were closed and one allegation remains 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, during the reporting period, OIG continued to monitor and provide input, as appropriate, into management efforts to enhance the agency's information technology function and efforts to enhance agency security and to provide guidance. We also

continued to coordinate with the General Accounting Office and other financial regulatory agencies 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 ECIE members' audit operations peer reviews – a mechanism for assuring quality audits by Inspectors General. We also responded to various inquiries involving the activities of the Inspector General community.



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) provide lending, deposit, and other services to member institutions. The FHLBank System has evolved from one where its membership was limited to thrift institutions and their membership was mandatory. Since the FHLBank System's inception, membership has included savings and loans, savings banks, cooperative banks, and a small number of insurance companies. As of August 1989, membership is also open to commercial banks and credit unions that meet a commitment to housing finance, as defined in law. Since that time, the number of commercial bank and credit union members has grown to comprise 73 percent and 8 percent of the member institutions, respectively, as of December 31, 2002. Further, as of May 13, 2000, all members are in the system voluntarily.

The 12 FHLBanks borrow funds in the nation's credit markets to lend to the FHLBank System member institutions, which numbered 8,011 as of December 31, 2002. These institutions, in turn, use the funds for home mortgages, to meet savings withdrawal needs, and for other authorized purposes. As of December 31, 2002, the FHLBanks had outstanding loans (Advances) to member institutions totaling \$470 billion for these purposes. In addition, through its Affordable Housing Program, the FHLBank System provided approximately \$1.7 billion to active and completed projects to help house some of America's neediest families. As of December 31, 2002, a total of 358,772 new housing units were approved, with approximately 64 percent of them of very-low-income households. Concurrent with affordable housing efforts, the FHLBank System has increased its efforts in overall community development through its Community Investment Program (CIP) and Community Investment Cash Advances (CICA) Programs. Total CIP/CICA lending for the life of the program is more than \$32 billion as of December 31, 2002. The Office of Finance is the fiscal agent for the FHLBank System. The Office of Finance's primary role is to manage the sale of the FHLBank System's consolidated obligations to investors and to service the FHLBank System's debt.

The Federal Housing Finance Board (Finance Board), with a fiscal year 2003 budget of approximately \$27.1 million and approximately 105 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 actual monitoring, examination, and regulation of individual member institutions is left to the Office of Thrift Supervision. The Finance Board is responsible for annually examining the 12 FHLBanks and the Office of Finance.

Approximately 77 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 FHLBanks 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 5, 2002, OIG issued its annual audit plan as an addendum to its five-year strategic plan. During the semiannual reporting period April 1, 2003 through September 30, 2003, OIG completed one audit. ([Table A](#) on page 9). At the conclusion of this period, OIG also had three audits in process. OIG continued to coordinate with the General Accounting Office and the Inspector General community on audits that impact the Finance Board. Specifically, OIG's audit activities included:

COMPLETED

An audit of the Federal Housing Finance Board's fiscal year 2002 Financial Statements

WORK-IN-PROCESS

An audit of the Finance Board's IT Security Program

An audit of the Finance Board's Procurement Policies, Procedures and Practices

An audit of the Effectiveness of the Examiner Recruitment and Selection Process

INVESTIGATIVE ACTIVITY

The number of investigative matters processed by the Office of Inspector General during this reporting period increased. We had three investigative matters in process at the beginning of the reporting period and we received one additional allegation of possible wrongdoing during the period. Two allegations were closed after preliminary investigations, and one allegation was closed after a full investigation. One allegation remains under full investigation at the end of the period. Those allegations resulting in OIG investigations involved false statements, conflicts of interest, and misuse of government property and services.

[Table B](#), on page 10, contains a numerical summary of investigations, allegations, preliminary inquires, 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](#).

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

None

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

See attached [Table C](#).

8. Statistical table – audits recommending better used of funds [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

AND EVALUATIONS

REPORT NUMBER

DATE COMPLETED

TITLE OF REPORT

03-A-01-OM

April 4, 2003

Federal Housing Finance
Board's Fiscal Year 2002
Financial Statements

SUMMARY OF INVESTIGATIONS

BEGINNING CASES

NUMBERS

Cases Pending at the Beginning of Period:

At the Finance Board.....	3
At the Department of Justice.....	0
At other agencies.....	0

NEW CASES RECEIVED

Allegations Received During Current Period.....	1
---	---

STATUS OF CASES (as of September 30, 2003)

Resulted in:

Allegations Pend. Completion of Prelim. Invest/Audit.....	0
Preliminary Investigation Completed- (Cases Closed).....	0
Cases Pending Completion of Full Investigation.....	0
Full Investigation Completed- (Cases Closed).....	1
Cases Scheduled for Audit/Ltd. Rev. -(Cases Closed).....	2
Cases Pending Decision by Finance Board management.....	0
Cases Pending Decision by Dept. of Justice.....	1
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

	<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.

TABLE D

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	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.