



Semiannual Report to Congress

April 1 – September 30, 2003

OIG

Office of Inspector General



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

OFFICE OF INSPECTOR GENERAL

October 30, 2003

The Honorable Alan Greenspan
Chairman
Board of Governors of the Federal Reserve System
Washington, DC 20551

Dear Chairman Greenspan:

We are pleased to present our *Semiannual Report to Congress* which summarizes the activities of our office for the reporting period April 1 through September 30, 2003. The Inspector General Act requires that you transmit this report to the appropriate committees of Congress within thirty days of receipt, together with a separate management report and any comments you wish to make.

Sincerely,

/signed/

Barry R. Snyder
Inspector General

Enclosure



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OIG

Office of Inspector General

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Introduction

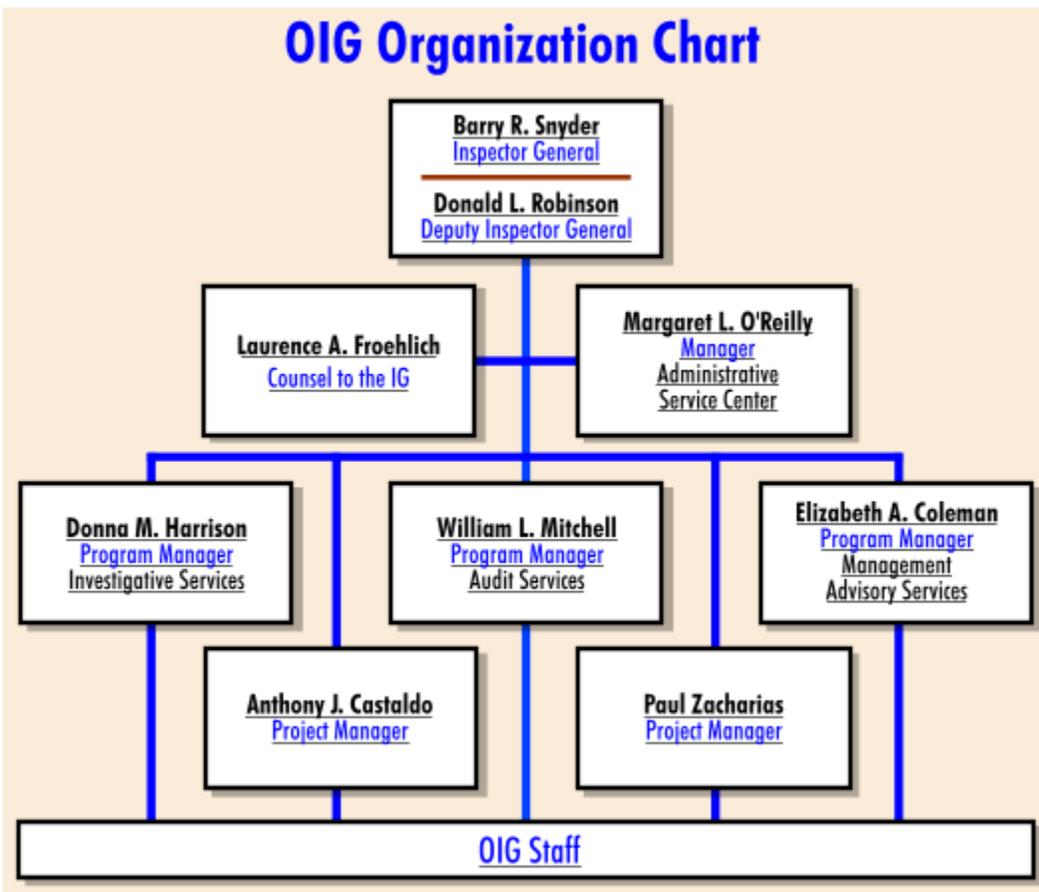
The mission of the Office of Inspector General (OIG), as prescribed by the Inspector General Act of 1978 (as amended), requires that we

- conduct and supervise independent and objective audits, investigations, and other reviews of programs and operations of the Board of Governors of the Federal Reserve System (Board);
- promote economy, efficiency, and effectiveness within the Board;
- help prevent and detect fraud, waste, and mismanagement in the Board's programs and operations;
- review and make recommendations regarding possible improvements to existing and proposed legislation and regulations relating to Board programs and operations; and
- keep the Chairman and Congress fully and currently informed of problems.

Additionally, the Federal Deposit Insurance Act (FDI Act), as amended, requires us to review failed financial institutions supervised by the Board that result in a material loss to the bank insurance fund (BIF) and to produce, within six months of the loss, a report that includes suggestions for improving the Board's banking supervision practices. Further, through an agreement with other financial institutions regulatory agency Inspectors General charged with the same legislative requirement, we will address any relationship of Board-regulated holding companies to material losses to the fund from failed financial institutions supervised by any of these agencies.

We currently perform our duties and responsibilities under three major program areas – audits, investigations, and management advisory services – as shown in the organizational chart that follows.

OIG Organization Chart



OIG Staffing	
Auditors.....	15
EDP Auditors	5
Investigators	4
Attorney	1
Administrative.....	2
Information Systems Analysts.....	2
Total Positions	29

Goals and Objectives

Goal 1: Provide Value-Added Customer Service to the Board

The Board continues to operate in a dynamic environment, shaped by legislative reform, increased emphasis on results and performance management, and innovations in the banking industry that require corresponding changes in the Board's supervision and regulation programs, as well as its Federal Reserve System (System) oversight functions. In addition, the Board faces certain challenges in ensuring that it has the people, processes, and technology needed to meet the evolving and varying needs of its clients and to provide a wide range of high-quality services in a cost-effective manner.

Our strategic objectives within this changing environmental context are to

- improve and enhance the Board's program operations,
- strengthen and streamline the Board's operational infrastructure,
- promote the Board's effective use of technology, and
- help the Board limit risk and ensure compliance.

Goal 2: Enhance Coordination and Information Sharing with the Congress, IG Community and Others

To achieve our mission, we will need to work closely with Board management, the Congress, the Inspector General (IG) community, the General Auditors at the Reserve Banks, and other stakeholders. We also plan to continue and expand our coordination with the IG community.

By law, the OIG has a duty and responsibility to keep Congress fully and currently informed by means of semiannual and other reports. We continue to look for opportunities to improve our timeliness to Board management and staff, congressional staff, and others concerning allegations of wrongdoing and to enhance our communications with the general public regarding their potential concerns with the Board's programs and operations and their need for information.

Our strategic objectives within this goal are to

- develop and enhance relations with the Congress;

- improve our responsiveness to allegations of fraud, waste, abuse, or mismanagement and to the public requests for information;
- continue to take a positive leadership role in the IG community; and
- foster interagency approaches to cross-cutting issues.

Goal 3: Enhance the Efficiency and Effectiveness of Internal Operations

We continually review our own processes, systems, and resources in an effort to improve our service delivery and to serve as an efficient and effective organization within the Board.

Our strategic objectives within this goal are to

- improve our business processes through the effective use of information technology and numerous process enhancements, and
- enhance our human capital through effective leadership, management, and development of our staff.

Projects Completed during this Reporting Period

Audit of the Board's Information Security Program

On December 17, 2002, the President signed into law the E-Government Act of 2002 (P.L. 107-347) which includes Title III, the Federal Information Security Management Act of 2002 (FISMA). FISMA permanently reauthorized the framework laid out in the Government Information Security Reform Act (GISRA) which expired in November 2002, including the requirement for each agency Inspector General to conduct an annual independent evaluation of their agency's information security program and practices. Our audit objectives, based on FISMA's requirements for conducting independent evaluations, were to evaluate the effectiveness of security controls and techniques for selected information systems and to evaluate the Board's compliance with FISMA and related information security policies, procedures, standards, and guidelines.

To test security controls and techniques, we selected four applications for review and evaluation and followed up on the status of the recommendations made in our prior control reviews. Our control tests of the four applications did not identify any major security control weaknesses, although we found several areas where controls needed to be strengthened. Our follow-up work on recommendations made during the prior year's control reviews found that sufficient actions had been taken to close all recommendations. We provided our test results in restricted follow-up letters to management. We plan to follow up on implementation of our recommendations as part of our future audit and evaluation activities related to the Board's information security program.

To evaluate the Board's compliance with FISMA and related policies and procedures, we followed up on the open recommendations in our prior evaluations of the Board's information security program and practices. These recommendations were designed to help bring the Board into compliance with GISRA's requirements and further enhance the Board's information security program. Since FISMA contains most of the requirements and provisions set forth by GISRA, implementing our prior recommendations would also bring the Board into compliance with the new information security legislation.

Our follow-up work showed that the Board continues to make progress in developing a structured information security program as envisioned by the previous and current security-related legislation. Notwithstanding this progress, however, the Board has not achieved full compliance with FISMA's requirements and issues remain open related to five of the seven recommendations from our original 2001 information security report. These issues pertain to properly positioning the CIO and the Information Security Officer to effectively carry out their responsibilities, finalizing the Boardwide security program document and the application inventory, conducting security control reviews, developing a comprehensive information security awareness program, and identifying control weaknesses and documenting corrective actions. We continue to believe that

fully implementing these recommendations is essential for the Board to firmly establish the necessary managerial responsibilities, oversight structure, and clear, consistent guidance related to the Board's information security program; to bring itself into compliance with the security legislation's requirements; and to establish the organization and programmatic framework that is intended by the legislation.

To help the Board achieve these objectives, we updated our prior recommendations using the concepts, terms, and requirements contained in FISMA. In his response to our report, the Staff Director who serves as the Board's CIO, noted that the Board, like other small federal agencies, is challenged by the prescriptive standards contained in FISMA which he believes were written for the large, cabinet-level agencies. Nevertheless, the Staff Director indicated that he plans to strengthen the Boardwide emphasis regarding FISMA and look for alternative methods for meeting policy, compliance, and review responsibilities. The Staff Director stated the Boardwide security program is in final draft and efforts are underway to ensure FISMA's requirements, including the identification of all information systems, are met regarding contractors, the Reserve Banks, and other organizations supporting the Board's operations. In addition, additional security awareness measures are already in progress and the process of prioritizing, tracking, and managing security performance gaps will continue to be enhanced. We will evaluate actions taken in response to our recommendations as part of our continued work related to information security.

Evaluation of the Board's E-Government Initiatives

We initiated this evaluation to determine the extent of the E-Government (E-Gov) activities of the Board in light of the President's Management Agenda to expand the use of E-Gov to enhance communications, information sharing, service delivery, and business processes. Our specific objectives were to develop an inventory of the Board's completed, in-process, and planned E-Gov initiatives; and to identify any impediments or challenges the Board may face in implementing additional E-Gov initiatives.

During this reporting period, we issued our *Report on the Evaluation of the Board's E-Government Initiatives*. The report identified sixty-six E-Gov projects, some of which have been recognized for government E-Gov excellence awards. About two-thirds of these projects are primarily intended to improve internal efficiency and effectiveness. The remaining one-third can be categorized as government-to-citizen, government-to-business, or government-to-government initiatives, which are the principal focus areas of the federal government's E-Gov efforts.

Our report identified several challenges to maximize the potential benefits of E-Gov for the Board and suggested that the Board take the following actions:

- Continue its effort to promote a culture that supports E-Gov initiatives and technology innovations, and enhances user training to communicate potential benefits offered by automating the Board's business processes.
- Ensure that a customer-centered focus is applied to E-Gov initiatives by directly linking the success of the project to the benefits realized by the actual end users as well as to the accomplishment of a specific division mission.
- Ensure that the biennial planning and budget processes identify and evaluate potential Boardwide E-Gov investments.
- Develop a Boardwide approach to evaluating E-Gov investments.
- Continue to address the challenges concerning security issues related to new technologies.
- Develop and communicate guidance that identifies the key factors, including the appropriate legal considerations, to be considered in collaborating with Reserve Banks and other or federal agencies.

During the course of our evaluation, the E-Government Act of 2002 (P.L. 107-347) was enacted. The act presents several compliance considerations for Board management to address. Our report identified the following actions to address the broader compliance requirements imposed on the Chairman, as agency head, and the Staff Director for Management, as the Board's Chief Information Officer (CIO):

- Communicate to divisions and offices the Board's E-Gov goals and objectives and the results of the task force's assessment of what must be done to implement the E-Gov act.
- Develop a standard framework and guideline for presenting proposed projects for senior management's review and ensure that the impact on citizens and internal end users is adequately considered.
- Implement a process to develop and gather information needed to report on the status of the Board's E-Gov initiatives including how such initiatives including how such initiatives improve performance in delivering programs to constituencies or improve internal efficiency and effectiveness
- Incorporate the new E-Gov act information technology requirements along with those already required under the Federal Information Security Management Act of 2002 (FISMA) into the CIO's position description and assess the overall requirements in a global context as to how they will be effectively and practically managed and implemented by the CIO.

The report, characterized by Board officials as fair and accurate, completes our current E-Gov evaluation project; however, we may audit the Board's compliance with the E-Gov act at a later time.

Audit of the Retirement Plan Administration

This audit was performed to document and obtain an understanding of the retirement process for Board employees; assess the effectiveness of processes for monitoring vendor contracts and vendor performance; evaluate automated system controls and confirm the accuracy of employee data; determine whether Board employees and other key stakeholders are generally satisfied with the customer service provided; and obtain an understanding and evaluate the effectiveness of the governance structure for the retirement plan. Our review of the retirement process and vendor contract management, as well as our data verification and pension benefit recalculations, did not identify any significant control weaknesses, data discrepancies, or systemic processing errors. We found that staff in the Management Division (MGT) have worked with the Office of Employee Benefits (OEB) and the outsourcing contractor over the past two years to improve the accuracy of pension-related information, and to help the contractor become more familiar with aspects of the retirement plan. Our testing identified three minor discrepancies in pension benefit amounts for the retirees in our sample. We provided this information to the MGT staff and the necessary adjustments have been made. In addition, our customer satisfaction surveys showed that Board staff was generally satisfied with the retirement process and the accuracy of information received. However, we received several comments related to the availability and communication of retirement plan information which we included in a separate management letter report.

Although we did not identify any significant weaknesses or systemic errors, we believe that opportunities exist to strengthen the retirement plan administration and oversight. Our report contains four recommendations describing policy decisions that the Board, either internally or through representation on other System oversight committees, needs to strengthen oversight and administration of the retirement plan. The four recommendations address

- modifying the methodology for including lump-sum payments in final average-salary calculations for certain retirement plan members to ensure that retirees receive full credit for payments received;
- revising the methodology for allocating OEB expenses to the Board and Reserve Banks to provide an equitable distribution for expenses;
- establishing clear guidance for the continuing role of MGT staff in retirement processing and ensuring that staff have appropriate access to retirement-related information; and

- revising the audit committee structure and establishing a written charter to clearly define the audit committee's roles and responsibilities.

As part of our recommendation regarding the allocation of OEB expenses, we classified \$585,630 as questioned costs in expenses paid, or expected to be paid, by the Board in 2003 for benefits programs in which the Board is not participating. We also classified \$1.726 million as funds for better use. The figure represents projected savings for 2003 through 2005 that would result from the implementation of our recommendation to change the allocation methodology from a salary liability basis to an allocation based on staffing levels.

We provided our report to the Staff Director for Management for comment. The Staff Director concurred with recommendations 1 and 3, partially concurred with recommendation 2, and did not concur with recommendation 4. The director of the Division of Reserve Bank Operations and Payment Systems also provided a written response addressing part of recommendation 2 and recommendation 4. The director's response generally parallels the Staff Director's response.

Audit of the Federal Reserve System's Surveillance Function

During this period, we completed a survey of surveillance activities conducted by Federal Reserve Systems (System) supervision and regulation personnel. The System's surveillance function tracks the condition and performance of individual banking institutions, assesses macro trends in the banking industry and the economy, and provides statistical and analytical support to the examination staff. Our objective was to develop an understanding of the purpose, content, and interrelationship of the Board's and Reserve Bank's surveillance systems and processes to determine if any issues warranted further audit attention.

Overall, our work helped us develop a working understanding of the content, interrelationships, and uses for Board and Reserve Bank surveillance data. In doing so, we learned that Reserve Bank staff view surveillance data received from the Division of Banking Supervision and Regulation's (BS&R) Analysis and Surveillance Section as reliable, timely and useful. We developed and shared with key BS&R staff a detailed internal summary that provided our understanding of surveillance data and tools, as well as an overview and diagram of the Board's core surveillance program, a description of the surveillance activities impact banking supervision.

In August 2003, we issued a letter to the director of BS&R informing him that our work had not surfaced any surveillance issues where we believe additional audit work would be worthwhile at this time. We explained that this conclusion was influenced substantially by the fact that surveillance is not managed as a separate program and, as such, we believe that some issues we identified, with respect to efficiency and effectiveness, should be evaluated in a larger context. We

understand that the System is working to address these issues and we plan to monitor these efforts and then decide what future audit work we might perform.

Evaluation of the Board's Emergency Preparedness

The September 11, 2001, terrorist attacks reinforced the importance of a comprehensive emergency preparedness strategy to provide for the continuity of the Board's operations if a future incident adversely affected Board facilities, infrastructure, or staff. Since that time, emergency preparedness has taken on increased importance and numerous efforts are underway to ensure that federal agencies effectively assess, prevent and respond to threats and emergency situations to protect the workforce and ensure ongoing operations.

During this reporting period, we completed a scoping review of the Board's emergency preparedness efforts aimed at (1) gaining an understanding of the Board's management and control structure for emergency preparedness and (2) identifying and determining the status of the Board's efforts to prevent, detect, mitigate, and respond to emergencies. Using this information, we selected and prioritized specific aspects of the Board's emergency preparedness for the next phase of our work—a series of more focused audits, reviews, and inspections.

Follow-Up on the Audit of the Federal Reserve's Background Investigation Process

During the reporting period, we completed follow-up work related to our October 2001 *Report on the Audit of the Federal Reserve's Background Investigations Process*. Our audit report contained three recommendations to improve the Board's background investigations program. Specifically, we recommended that the Staff Director for Management 1) update and clarify the current policy for background investigations, 2) develop guidance for conducting and documenting background investigations for contractors, and 3) develop policies and procedures for conducting background investigations for summer interns, temporary employees, and transferred employees.

Our follow-up work determined that a new suitability policy, which includes a proposed policy on background investigations, was drafted in May 2003 and is currently under review by Board officials. The issuance of this new policy is an essential element to addressing our three recommendations because it establishes the framework for using background investigations for judging the suitability of prospective and current employees and contractors. We are leaving our three recommendations open pending final issuance and dissemination of the policy document.

Follow-Up on the Audit of the Board's Efforts to Implement Performance Management Principles Consistent with the Results Act

Congress passed the Government Performance Results Act of 1993 (GPRA) as part of a legislative framework to instill performance-based management in the federal government. Although not statutorily subject to GPRA, the Board decided, in July 1997, to voluntarily comply with the act's substance. Our July 2001 *Report on the Board's Efforts to Implement Performance Management Principles Consistent with the Results Act* observed that the Board had not achieved its objective of incorporating the performance management concepts of strategic planning and performance measurement into its planning and budgeting process. Specifically, our report recommended that the Board

- establish a framework to adopt a more results-oriented performance management approach;
- revise its strategic planning process to develop a long-range, Boardwide strategic plan;
- establish specific, quantifiable results-oriented performance measures that are aligned from the strategic plan to the performance objectives and expectations of division officers, managers, and staff; and
- revise internal performance reports to include comparisons of actual program results with established performance goals and measures.

Our follow-up work determined that the Board is current with the reporting requirements as a result of issuing its *Government Performance and Results Act Strategic Planning Document, 2001-05* in December 2001, and the *Government Performance and Results Act Biennial Performance Plan 2002-2003* and *Government Performance and Results Act Performance Report 2001-01* in December 2002. The issuance of these documents also represents a necessary first step to systematically building performance plans, budgets, and performance measures around the achievement of strategic goals and outcomes. In that regard, the current planning and budgeting process for 2004-2005 is the first opportunity for the Board to fully implement the report's recommendations. Consequently, we are leaving our recommendations open at this time but will review actions taken once the current planning and budgeting process is completed.

Investigative Activity

During the reporting period, we opened three formal investigations and continued work on nine cases that were opened during previous reporting periods. Of our twelve active cases, we closed five cases that were opened from previous reporting periods.

One of the five cases closed involved the conviction of the owner of a bomb detection dog business after a year-long investigation. In August 2003, a jury in the Eastern District of Virginia convicted Mr. Russell Lee Ebersole, owner of a Virginia bomb detection dog business known as Detector Dogs Against Drugs and Explosives (DDADE), on twenty-five counts of wire fraud and two counts of submitting false statements to the United States.

On September 8, 2003, Mr. Ebersole was sentenced to seventy-eight months imprisonment and ordered to pay restitution in the amount of \$708,000. According to the U. S. Attorney overseeing this prosecution, “Not only did Mr. Ebersole steal from this country at its most vulnerable time, but by supplying such ill-trained bomb dogs and handlers, he deliberately endangered the lives of many government workers, the public in general and his own employees.”

Shortly after September 11, 2001, and continuing through May 2002, Mr. Ebersole provided bomb detection dogs and handler services to several government agencies, including the Board. Mr. Ebersole offered to have his bomb detection teams patrol the perimeters of the buildings so as to protect the employees working there. In proposals that Mr. Ebersole submitted in order to obtain government contracts, he made a series of false statements about DDADE, its training procedures, and the qualifications of its dogs and handlers. DDADE dogs failed explosive detection tests administered on five different occasions.

There were additional prosecutorial actions pursued against Mr. Ebersole. In August 2003, Mr. Ebersole pleaded guilty to charges of causing explosives to be transported by air and witness tampering in the Western District of Virginia. The maximum sentence that Mr. Ebersole faces as a result of these charges is fifteen years in prison and a fine of \$500,000. In April 2003, Mr. Ebersole was also tried for perjury by the Commonwealth of Virginia. He allegedly perjured himself before a Virginia Department of Criminal Justice Services hearing. Evidence for the perjury charge was obtained during the federal investigation. The jury was deadlocked and the judge declared a mistrial. The Commonwealth of Virginia dropped the charges after Mr. Ebersole was convicted in U. S. District Court.

The investigation of Mr. Ebersole had begun as an administrative investigation into alleged procurement irregularities. As the criminal merits of the case progressed, we closed the administrative investigation. The investigation into Mr. Ebersole’s activities was conducted by a task force of special agents from our office and the Offices of Inspector General of Department of State, Department of Homeland Security, Department of the Treasury IG for Tax Administration, Department of Transportation, and the Bureau of Alcohol, Tobacco, Firearms, and Explosives.

Of the remaining three closed cases, one case involved a monitoring effort by the OIG of the failure of the Oakwood Deposit and Banking Company, a state member bank. During a bank examination exit conference with staff from the

Federal Reserve Bank of Cleveland (FRB Cleveland), the former Executive Vice President and Chief Executive Officer, Mr. Mark Steven Miller, admitted to an FRB Cleveland examiner that he had embezzled approximately \$40,000,000 from Oakwood by using cash received from certificates of deposit and funneling it to Stardancer Casino boats, a ferry boat enterprise. Mr. Miller also admitted to altering bank records to make it appear that the bank had less money than it actually had. It was this discrepancy that initially alerted the FRB Cleveland examination team that Oakwood had problems with the amount of assets it claimed. FRB Cleveland staff then contacted the local Federal Bureau of Investigation (FBI) office, whose agents arrested Mr. Miller on February 1, 2002.

On February 27, 2002, the U. S. District Court for the Northern District of Ohio, Western Division, indicted Mr. Miller on three counts: bank embezzlement; money laundering; and, forfeiture of cash. On December 17, 2002, a superseding indictment against Mr. Miller was issued for two more counts—one for embezzlement and the other for wire fraud. On May 16, 2003, Mr. Miller pled guilty to bank embezzlement and money laundering.

On September 6, 2003, Mr. Miller, was sentenced in the U. S. District Court in Toledo, Ohio, to fourteen years in prison, as well as court ordered restitution of \$48.7 million for his role in the failure of Oakwood. Our investigators assisted the receiver, the Federal Deposit Insurance Corporation's OIG, the lead investigative agency, the FBI, in conjunction with the U. S. Attorney's Office, Northern District of Ohio, and other law enforcement agencies in their request for records, assistance, and analysis.

In addition, we closed a fourth case that involved a request for our assistance from the U. S. Attorney's Office in the Eastern District of Texas, Tyler, Texas. We participated with special agents of the FBI, Internal Revenue Service's Criminal Investigation Division, U. S. Customs Service, in a multiagency task force in the investigation by a federal grand jury of various financial crimes, including potential bank fraud, loan fraud, obstruction of bank examination(s) and other issues related to a state member bank of the Federal Reserve System. Our investigative activity curtailed when allegations of criminal and civil wrongdoing by the FRB examination staff, or bank officials in the financing of aircraft loans, were unsubstantiated.

The fifth closed investigation involved potentially threatening telephone calls to two Board switchboard operators. With the assistance of the FBI Washington Field Office's Joint Terrorism Task Force, our investigators identified the perpetrator and resolved the potential security threat.

The investigative findings in one of our seven active cases involved the alleged violation of the Board's internet access service and other ethics violations by an employee. We referred it to a local prosecutor who declined prosecution in favor of administrative action. This matter is currently under review by the Board

pending management action. At the end of this reporting period, we had seven active cases. Our summary statistics on investigations are provided in the table that follows:

Summary Statistics on Investigations for the Period April 1 through September 30, 2003

Investigative Actions	Number
Investigative Caseload	
Investigations Opened during Reporting Period	3
Investigations Open from Previous Period	9
Investigations Closed during Reporting Period	5
Total Investigations Active at End of Reporting Period	7
Investigative Results for this Period	
Referred to Prosecutor	2
Referred for Audit	0
Referred for Administrative Action	1
Oral and/or Written Reprimand	0
Terminations of Employment	0
Suspensions	0
Debarments	0
Indictments	0
Counts	27
Convictions	1
Monetary Recoveries	\$0
Civil Actions (Fines and Restitution)	\$0
Criminal Fines: Fines & Restitution	\$708,000

Hotline Operations

Our investigators continue to address allegations of wrongdoing related to the Board's programs and operations, as well as violations of the Board's standards of conduct. During this reporting period, we received 111 complaints, of which sixty-eight were from our hotline operation. Most hotline callers were consumers with complaints or questions about practices of private financial institutions. Those inquiries involved matters such as funds availability, account fees and charges, and accuracy and availability of account records. We continued to receive numerous questions concerning how to process Treasury securities and savings bonds. Other callers contacted us seeking advice about programs and operations of the Board, Federal Reserve Banks, other OIGs, and other financial regulatory agencies. We directed those inquiries to the appropriate Board offices, Reserve Banks, or federal or state agencies. We closed all but eight of the sixty-eight hotline complaints after our initial analysis and contact with the complainants.

In addition to the hotline complaints, the investigative services program received forty-three allegations that were referred to the OIG from Board program staff and other sources. As a result of those allegations, the OIG opened three investigations. In addition, we are continuing our review of fictitious instrument

fraud complaints. Fictitious instrument fraud schemes are those in which promoters promise very high profits based on fictitious instruments they claim are issued, endorsed, or authorized by the System or a well-known financial institution. Our summary statistics of the hotline results are provided in the table that follows:

Summary Statistics on Hotline Results for the Period of April 1 through September 30, 2003

Investigative Actions	Number
Complaints Referred for Investigation	
Hotline Referrals	68
Audit Referrals	0
Referrals from Other Board Offices	41
Referrals from Other Sources	2
Proactive Efforts by OIG	
Investigations Developed by OIG	0
Results of all Complaints Referred and Proactive Efforts	
Resolved	103
Pending	8
Total Received during Reporting Period	111

Executive Council on Integrity and Efficiency Participation

As Vice Chair of the ECIE, the Board’s IG provides leadership, vision, direction, and initiatives for the ECIE on behalf of the Council Chair (Deputy Director for Management, Office of Management and Budget). Collectively, the members of the ECIE have continued to work with the members of the PCIE to help improve government programs and operations.

October 2003 marks the 25th anniversary of the Inspector General Act of 1978. Recognizing the significance of this milestone, the ECIE collaborated with the PCIE to reflect on the IG concept and identify possible legislative and other enhancements to strengthen the community and chart new directions for the future. The 25th anniversary provided an excellent opportunity to inform and educate others—the Congress, the agencies, and the public—about our mission, roles, and objectives in addressing the numerous challenges facing the federal government today and in the near future.

Review of Legislation and Regulations

As part of fulfilling our mission under the IG Act, we review existing and proposed legislative and regulatory items both as part of our routine activities and on an *ad hoc* basis. We routinely keep track of proposed and pending legislation and regulations by researching relevant documents and databases, reviewing lists prepared by the Board's law library, sharing information with others in the IG community, and coordinating with Board programs that also review new and proposed legislation. We then independently analyze the effect that the new or proposed legislation or regulation may have on the efficiency and effectiveness of Board programs and operations.

As part of our audit of the Board's information security program pursuant to FISMA, we conducted additional analysis of the act by completing a section-by-section comparison of FISMA's requirements to those contained in the prior information security legislation (the Government Information Security Reform Act). Our analysis was designed to identify any new or deleted information security requirements to help us evaluate the Board's compliance with the legislation. We also shared the results of our analysis with Board staff responsible for information security for their use in understanding and complying with the new legislation.

Working on a project with the PCIE Legislation Committee, we drafted part of what is likely to become a model bill for certain amendments to the Inspector General Act. That provision will, if enacted, provide for the replacement of the ECIE and the PCIE with a single, statutorily-established IG Council.

Our review of legislation and regulations includes reviewing and commenting on revisions or additions to the Board's management policy statements and internal administrative procedures. For example, we analyzed and provided comments on proposed updates to the policy governing the Academic Assistance Program for Board employees.

Ongoing Projects

Audit of the Board's Outsourcing Efforts

Over the years, the Board has outsourced several of its functions, such as the human resources benefits program, cafeteria and food services, and cleaning and housekeeping maintenance. The objectives of this audit are to assess the Board's management of the contracts for outsourced services and to evaluate its processes for identifying and evaluating other competitive sourcing opportunities. We have issued a draft report to Board management officials for comment and will issue our final report during the next period. In addition, we are preparing a separate report on a service contract with one vendor that we will also issue during the next period.

Review of Internal Control Assessments Performed During Community Bank Examinations

Our previous *Report on the Failure of the Oakwood Deposit Bank Company* revealed that a senior executive was able to conceal a massive fraud by systematically exploiting weak corporate governance and an inadequate internal control structure. The objective of this project is to evaluate the depth and adequacy of risk-focused internal control reviews performed during community bank examinations conducted throughout the System, and to identify and share best practices. To accomplish our objectives, we reviewed workpapers and reports for thirty-six safety and soundness examinations conducted by four different Reserve Banks: Richmond, Chicago, Kansas City, and Minneapolis. We also assessed Reserve Bank initiatives for improving internal control reviews. Field work has been completed and we expect to issue our final report during the next report period.

Review of the Board's Fine Arts Program

We have begun a review of the Board's Fine Arts Program which involves two key activities: collecting art and organizing exhibitions. It is staffed by a full-time program director who operates within the Management Division. The program's two-year budget is approximately \$300,000, and it has been granted tax exempt status under section 170 of the Internal Revenue Code. The Fine Arts Program director manages a collection of about 300 works of art. Much of the collection is on long-term loan from museums, privately owned galleries, and individuals. In addition, artwork has been acquired by using the proceeds of cash contributions made to the Board's tax exempt Fine Arts Program.

We have two major objectives for this review. First, we will assess the organizational placement of this program. Second, we will assess the adequacy of the program's internal controls, including the policies, procedures, and processes

for securing and preserving the Board's art collection, valuing the collection for insurance and financial reporting purposes, and receiving and disbursing contributions.

Appendixes

Appendix 1

Audit Reports Issued with Questioned Costs for the Period April 1 through September 30, 2003

Reports	Number	Dollar Value	
		Questioned Costs	Unsupported
For which no management decision had been made by the commencement of the reporting period	0	\$0	\$0
That were issued during the reporting period	1	\$585,630	\$0
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
For which no management decision had been made by the end of the reporting period	1	\$585,630	\$0
For which no management decision was made within six months of issuance	0	\$0	\$0

Appendix 2

Audit Reports Issued with Recommendations that Funds be Put to Better Use for the Period April 1 through September 30, 2003

Reports	Number	Dollar Value
For which no management decision had been made by the commencement of the reporting period	0	\$0
That were issued during the reporting period	1	\$1,725,672
For which a management decision was made during the reporting period	0	\$0
(i) dollar value of recommendations that were agreed to by management	0	\$0
(ii) dollar value of recommendations that were not agreed to by management	0	\$0
For which no management decision had been made by the end of the reporting period	1	\$1,725,672
For which no management decision was made within six months of issuance	0	\$0

Appendix 3

OIG Audit Reports With Outstanding Recommendations

Report No.	Audits Currently Being Tracked	Issue Date	Recommendations			Status of Recommendations ¹		
			No.	Mgmt. Agrees	Mgmt. Disagrees	Follow-up Completion Date	Closed	Open
A9702	Business Process Review of the Board's Travel Administration	07/97	9	9	0	01/99	1	8
A9710	Audit of the Federal Reserve System's Application Commitment Processing	01/98	5	5	0	06/99	4	1
A0004	Audit of the Board's Efforts to Implement Performance Management Principles Consistent with the Results Act	07/01	4	4	0	08/03	0	4
A0011	Audit of the Federal Reserve Board's Government Travel Card Program	01/02	5	5	0	–	–	–
A0106	Audit of the Board's Information Security Program	09/01	7	7	0	09/03	7	0
A0107	Audit of the Federal Reserve's Background Investigation Process	10/01	3	3	0	09/03	0	3
A0109	Audit of the Board's Use of and Controls Over Purchase Cards	05/02	3	3	0	–	–	–
A0203	Audit of the Board's Security-Related Directed Procurements	09/02	3	2	1	–	–	–
A0302	Audit of the Board's Information Security Program	09/03	7	7	0	–	–	–

¹ A recommendation is closed if (1) the corrective action has been taken; (2) the recommendation is no longer applicable, or (3) the appropriate oversight committee or administrator has determined, after reviewing the position of the OIG and division management, that no further action by the Board is warranted. A recommendation is open if (1) division management agrees with the recommendation and is in the process of taking corrective action or (2) division management disagrees with the recommendation and we have referred it to the appropriate oversight committee or administrator for a final decision.

Appendix 4

Cross-References to the Inspector General Act

Indexed below are the reporting requirements prescribed by the Inspector General Act of 1978, as amended, for the reporting period:

Section	Source	Page(s)
4(a)(2)	Review of legislation and regulations	16
5(a)(1)	Significant problems, abuses, and deficiencies	None
5(a)(2)	Recommendations with respect to significant problems	None
5(a)(3)	Significant recommendations described in previous Semiannual Reports on which corrective action has not been completed	None
5(a)(4)	Matters referred to prosecutory authorities	11
5(a)(5)	Summary of instances where information was refused	None
5(a)(6)	List of audit reports	5-17
5(a)(7)	Summary of significant reports	None
5(a)(8)	Statistical Table—Questioned Costs	21
5(a)(9)	Statistical Table—Recommendations that Funds Be Put to Better Use	22
5(a)(10)	Summary of audit reports issued before the commencement of the reporting period for which no management decision has been made	23
5(a)(11)	Significant revised management decisions made during the reporting period	None
5(a)(12)	Significant management decisions with which the Inspector General is in disagreement	None



*Inspector General Hotline
1-202-452-6400
1-800-827-3340*

*Report: Fraud, Waste or Mismanagement
Information is confidential
Caller can remain anonymous*

*You may also write the:
Office of Inspector General
HOTLINE
Mail Stop 300
Board of Governors of the Federal Reserve System
Washington, DC 20551*