OIG

Office of Inspector General

Semiannual Report to Congress

October 1, 2002 – March 31, 2003

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

OFFICE OF INSPECTOR GENERAL

April 29, 2003

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

Dear Chairman Greenspan:

The enclosed *Semiannual Report to Congress* summarizes the activities of the Office of Inspector General of the Board of Governors of the Federal Reserve System (Board) for the reporting period October 1, 2002, through March 31, 2003. During this reporting period, we continued to perform a variety of audits, reviews, investigations, and special projects that encompassed a number of legislative requirements and Inspector General community activities covering a wide range of the Board's programs and operations. For this reporting period, we have redesigned our report to reflect our goals and objectives, projects completed during the period, and ongoing projects. Our required statistical tables are included as appendixes to this report.

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,

Barry R. Snyder
Inspector General

Enclosure

Semiannual Report to Congress

October 1, 2002 – March 31, 2003

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

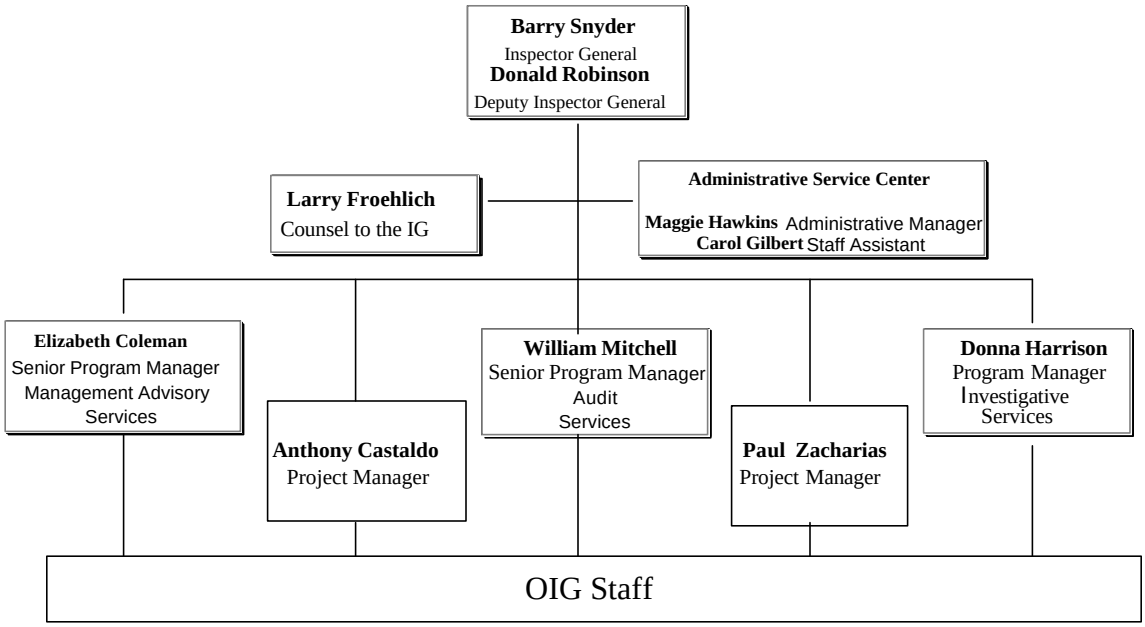
- conduct and supervise independent and objective audits, investigations, and other reviews of programs and operations of the Board of Governors of the Federal Reserve System (Board);
- promote economy, efficiency, and effectiveness within the Board;
- help prevent and detect fraud, waste, and mismanagement 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.

Office of Inspector General

January 2002



OIG Staffing

Auditors	**16**
EDP Auditors	**4**
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

Over the next few years, the Board will continue 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 are continuing 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 plan to 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

- continue to improve our business processes through the effective use of information technology and numerous process enhancements, and

- enhance our human capital through effective leadership and management of our staff.

Projects Completed during this Reporting Period

Report on the Failure of the Oakwood Deposit Bank Company

The Oakwood Deposit Bank Company (Oakwood), was a small, two office community bank located in rural Paulding County, Ohio. This state-chartered member bank of the Federal Reserve System reported assets totaling approximately $72.3 million on December 31, 2001. Oakwood was closed by the Superintendent of the State of Ohio Division of Financial Institutions on February 1, 2002, after the bank's Executive Vice President, Mr. M. Steven Miller, confessed to fraudulent activity of sufficient magnitude to render the bank insolvent.

The objectives of our material loss review, as established by section 38(k) of the FDI Act, were to review the Board's supervision of the failed financial institution to

- ascertain why the institution's problems resulted in loss to the BIF, and
- make recommendations for preventing any such loss in the future.

Oakwood failed because a trusted senior executive exploited a weak corporate governance environment and inadequate internal control structure to perpetrate a massive and pervasive fraud. We recognize that such a fraud can be difficult to detect, particularly when it involves senior executives in trusted positions, and that the examination process is not necessarily designed to detect every possible fraud. Nevertheless, we found that Federal Reserve examiners did not properly apply risk-focused examination principles that would have warranted more in-depth testing, even though they had identified significant internal-control weaknesses and a lack of responsiveness by Oakwood management to regulatory criticisms. Examiners also relied on the work performed by an outside Certified Public Accountant (CPA), who was viewed as both the internal and external auditor, without reviewing or assessing the CPA's work.

We also found that examiners overlooked obvious red flags that we believe could have led to uncovering the fraud earlier and may have reduced the loss to the BIF. While we did not identify any deficiencies in the Federal Reserve's supervisory guidance and procedures, we believe that lapses in appropriately applying the risk-focused approach to Oakwood's examinations were caused by the oversights of an inexperienced examination staff that was inadequately supervised and failed to consistently exercise appropriate professional skepticism.

Our report provided a number of lessons learned that we believe will be of value to staff and managers involved in planning and conducting community bank examinations. In our view, a primary lesson learned from the Oakwood failure is that a bank with a weak board of directors, a dominant senior executive, inadequate separation of duties, a weak or nonexistent internal and external audit program, and a history of internal control deficiencies, should be acknowledged

as a high-risk institution. We noted that banks with these problems should be subjected to more intensive supervisory scrutiny including detailed reviews and testing of key accounting transactions and the internal control environment.

The Reserve Bank that supervised Oakwood has already made significant changes in response to our report that included:

- Implementing an internal control operational review program, under which all community banks in the district will be subject to a periodic expanded, detailed review of operations and controls, including considerable transaction testing. At a minimum, each bank will be subject to an expanded review once every three years, but the interval will be set much shorter for banks shown to have internal controls or other operational problems.

- Designating a senior examiner as the Reserve Bank's review examiner. The review examiner is responsible for reviewing and evaluating examination workpapers and draft reports for both community banks and large complex banking organizations. As part of this program, the Reserve Bank is requiring that all examination supervisors carefully review examination workpapers before the package is submitted to the review examiner.

- Conducting thorough reviews of community bank internal audit work papers. In addition to assessing the quality of the auditor's work, examiners will be looking for red flags or any other evidence of internal control deficiencies.

- Adding an internal controls component to the Reserve Bank's community bank board of directors training program with the objective of demonstrating what could happen without a strong corporate governance structure.

In addition, the Director of the Board's Division of Banking Supervision and Regulation (BS&R) noted that corrective measures and provisions are being carefully evaluated for Systemwide applicability.

Our report did not include formal recommendations because our observations were based only on the experience of one failed institution. However, we presented several matters for the Board's consideration designed to enhance the System's bank examination process. These matters for consideration include:

- using the Fraud Information Network (FIN) to communicate lessons learned from the Oakwood failure,

- expanding the use of surprise examinations,

- consider requiring independent financial statement audits for small community banks with weak risk management processes and internal controls, and

- enhancing examiner training in fraud and internal control testing and reconcilement techniques.

Some actions have already been taken by the Board. For example, our Oakwood report has been posted on the FIN web page. In addition, Reserve Bank examiners have cited chronically weak internal controls as the reason for (1) conducting a surprise examination and (2) requiring an institution with less than $100 million in assets to obtain an independent financial audit. On-line training for evaluating bank operations is now available and provides examiners with an opportunity to review examination techniques such as reconcilements and other transaction testing. Finally, BS&R is considering adding a course in fraud detection to the core examiner training curriculum.

Report on the Review of the Supervision of Hamilton Bancorp, Inc.

On January 11, 2002, the Office of the Comptroller of the Currency (OCC) closed Hamilton Bank, N. A. (Hamilton), and the Federal Deposit Insurance Corporation (FDIC) was appointed as Receiver. Hamilton was a wholly owned bank subsidiary of Hamilton Bancorp, Inc. (Bancorp), a noncomplex bank-holding company supervised by the Board. The Hamilton failure was expected to result in a loss to the BIF that would exceed the material loss threshold established under section 38(k) of the amended FDI Act. Since the OCC was Hamilton's primary regulator, the FDI Act required that the OIG of the Department of Treasury (Treasury) review OCC's supervision of Hamilton.

In accordance with our Memorandum of Understanding with the IGs of the Board, Treasury, and FDIC, we reviewed the actions taken by Bancorp to determine if they contributed to the failure of Hamilton and the anticipated material loss to the BIF. We also assessed the Board's supervision of Bancorp. We coordinated our work with the Treasury OIG, and used information contained in their final report to corroborate our findings and conclusions.

Overall, we believe that Bancorp did not contribute to either the failure of Hamilton or the anticipated material loss to the BIF. Specifically, Bancorp management had limited opportunities to engage in high-risk behavior through the holding company because it was noncomplex and conducted no substantial activities or operations. In addition, we did not find any intercompany transactions, such as management fees and dividends, that adversely affected Hamilton. Rather, when possible, Bancorp served as a source of financial strength through capital injections. No issues regarding the Federal Reserve's supervision of Bancorp were noted during the course of our review.

Audit of the Board's Financial Statements for the Year Ended December 31, 2002, and Audit of the Federal Financial Institutions Examination Council's (FFIEC) Financial Statements for the Year Ended December 31, 2002

Each year, we contract for an independent public accounting firm to audit the financial statements of the Board and the Federal Financial Institutions Examination Council (FFIEC), for which the Board provides the accounting function. KPMG LLP, our current contracted auditors, planned and performed the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The audits included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. The audits also included an assessment of the accounting principles used and significant estimates made by management, as well as an evaluation of overall financial statement presentation. In the auditors' opinion, the Board's and FFIEC's financial statements present fairly, in all material respects, the financial position of each as of December 31, 2002; and the results of operations and cash flows for the year then ended were in conformity with accounting principles generally accepted in the United States of America.

To determine the auditing procedures needed to express an opinion on the financial statements, the auditors considered the Board's and the FFIEC's internal controls over financial reporting. Although the auditors' consideration of the internal controls would not necessarily disclose all matters that might be material weaknesses, they noted no such matters. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, the auditors also performed tests of the Board's and the FFIEC's compliance with certain provisions of laws, regulations, contracts, and grants, since noncompliance with these provisions could have a direct and material effect on the determination of the financial statement amounts. The results of the auditors' tests disclosed no instances of noncompliance required to be reported under *Government Auditing Standards*.

Peer Review of the Securities and Exchange Commission Office of Inspector General

We were requested to conduct an external review of quality control for the audit function of the OIG for the Securities and Exchange Commission in effect for the year ended September 30, 2002. We conducted the review in conformity with standards and guidelines established by the President's Council on Integrity and Efficiency (PCIE) and the General Accounting Office's *Government Auditing Standards*. In accordance with those guidelines, we issued a report to the Securities and Exchange Commission's Inspector General.

Investigative Activity

During the reporting period, we opened five formal investigations and continued work on nine cases that were opened during previous reporting periods. Of our fourteen active cases, we closed six cases that were opened from previous reporting periods. One of the six cases closed involved alleged frequent flyer abuse by a former Board official and had earlier required the OIG to refer it to a local prosecutor to determine whether it merited criminal prosecution. The U. S. Attorney's Office had declined prosecution of this investigation in favor of administrative action. The action taken by the Board in this case resulted in a management letter to the personnel file of the former Board official. The Board has also updated its travel policy to provide more guidance regarding the accumulation and use of frequent flyer awards.

Of the remaining five closed cases, one case involved the theft of Board computer equipment by a Board employee. The U.S. Attorney's Office declined prosecution in this matter in favor of administrative action. In this case, the Board terminated the employee. Another case involved the theft of Board employees' personal property. Our investigators identified the perpetrator and recovered the stolen property, valued at around $600. The investigation was referred to the U. S. Attorney's Office, which declined prosecution in lieu of administrative action. The action taken by the Board in this case resulted in the termination of the contract employee responsible for the theft. A third investigation involved the alleged violation of the Board's Internet access service by an employee. We referred it to a local prosecutor who declined prosecution in favor of administrative action. The administrative action taken by the Board in this matter resulted in the employee's termination.

In addition, we closed a fourth case that involved the theft of two Board laptop computers from an inventory storage room. Our investigators gathered evidence revealing that a security officer had opened the inventory room containing computer equipment, for a Board contractor to perform work, then left the area unattended. Several hours later, the door was found open and, subsequently, two laptop computers were reported stolen. The evidence further revealed that the two computers had not been configured and contained no Board data. Since this incident, security procedures have been upgraded and improved.

The fifth closed investigation involved the theft of an employee's FRB Federal Credit Union debit card and personal identification number (PIN) that had been sent via interoffice mail. An unknown individual used the employee's debit card and PIN to make unauthorized withdrawals, totaling $1,108, from the employee's credit union account. After exhausting all relevant investigative leads, this case was closed due to inadequate surveillance footage from the various automatic teller machine (ATM) locations involved. We also confirmed that the FRB Federal Credit Union has implemented improved procedures regarding mass mailings of employees' debit cards and PINs.

The investigative findings in one of our eight active cases has led to multiple indictments against the owner of a bomb detection dog business after a year-long investigation. The indictments, totaling thirty-four counts, brought in two federal jurisdictions (Eastern and Western districts of Virginia), include counts of wire fraud, false statements, false claims against the government, witness tampering, and explosives-related violations. If convicted on all counts, the defendant faces a total of 180 years imprisonment and nearly $3 million in fines. Further, as a result of this investigation, the owner was indicted and prosecuted on one count of perjury by the Commonwealth of Virginia. The prosecution ended in a mistrial. This investigation is being led by one of our special agents working with OIG investigators from the Department of State, Department of Homeland Security, Department of the Treasury IG for Tax Administration, and the Department of Transportation, and investigators from the Bureau of Alcohol, Tobacco, Firearms, and Explosives.

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

Summary Statistics on Investigations for the Period of October 1, 2002, through March 31, 2003

Investigative Actions	Number
Investigative Caseload	
Investigations Opened during Reporting Period	5
Investigations Open from Previous Period	9
Investigations Closed during Reporting Period	6
Total Investigations Active at End of Reporting Period	8
Investigative Results for this Period	
Referred to Prosecutor	2
Referred for Audit	0
Referred for Administrative Action	2
Oral and/or Written Reprimand	1
Terminations of Employment	3
Suspensions	0
Debarments	0
Indictments	3
Counts	35
Convictions	0
Monetary Recoveries	0
Civil Actions (Fines and Restitution)	$600
Criminal Fines: Fines & Restitution	$0
	$0

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 123 complaints, of which ninety-seven 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 seven of the ninety-seven hotline complaints after our initial analysis and contact with the complainants.

In addition to the hotline complaints, the investigative services program received twenty-six allegations that were referred to the OIG from Board program staff and other sources. As a result of those allegations, the OIG opened four 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 October 1, 2002, through March 31, 2003

Investigative Actions	Number
Complaints Referred for Investigation	
Hotline Referrals	97
Audit Referrals	0
Referrals from Other Board Offices	20
Referrals from Other Sources	6
Proactive Efforts by OIG	
Investigations Developed by OIG	0
Results of all Complaints Referred and Proactive Efforts	
Resolved	116
Pending	7
Total Received during Reporting Period	123

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.

During this reporting period, the Board's IG, in his role as ECIE Vice Chair, collaborated with the PCIE Vice Chair to lead the production of *A Progress Report to the President*, an annual publication highlighting the significant accomplishments of the federal IG community during fiscal year 2002. Developing this report is a substantive undertaking that involves gathering and consolidating statistical data on thousands of audits, evaluations, and investigations conducted across the federal IG community. The report also focuses attention on the role that the IG community plays in fostering improvement in meeting the numerous challenges facing the federal government today and in the near future. Under the Vice Chairs' leadership, a simplified data collection process and a redesigned report format is greatly expediting report processing, streamlining message delivery, and enhancing report readability.

Review of Legislation and Regulations

As part of fulfilling our mission under the IG Act, we review existing and proposed legislative and regulatory items as part of our routine activities and on an *ad hoc* basis. During this reporting period, we reviewed a number of legislative requirements for their potential impact on either the Board or the OIG, and provided advice as appropriate. For example, we reviewed portions of the Homeland Security Act of 2002, Public Law 107-296 (enacted November 25, 2002), which contains a grant of law enforcement authorities to certain OIGs. Under the act, the Department of Justice must issue guidelines for the use of these authorities (*i.e.*, the power to arrest, search, and carry a firearm) that the affected IG offices must follow, and we reviewed and commented upon a draft of these guidelines.

Our legislative review also included an analysis of the new Federal Information Security Management Act of 2002 (FISMA), which is title III of the new E-Government Act of 2002 (e-Gov), Public Law 107-347 (enacted December 17, 2002). These provisions closely parallel the requirements set forth in title X of the Homeland Security Act of 2002, cited above (and also known as FISMA). Both sets of information security requirements were intended to reauthorize the Government Information Security Reform Act, whose provisions expired on November 30, 2002.

As part of our review of legislation and regulations, we review and provide comments on revisions or additions to the Board's management policy statements and to internal administrative procedures. With the heightened governmentwide concern over computer security, for example, the Board proposed internal procedures to address incidents involving actual or potential breaches of computer security. We commented on the Board's draft "Computer Security Incident

Notification Procedures," providing a number of suggestions and recommendations that were generally accepted by the Board. Most recently, we also reviewed, concurrent with the Board, federal statutes that permit the Board to pay additional monies to its employees who are serving in the military reserves, so that they do not experience a large drop in compensation during their time of service.

Ongoing Projects

Review of Internal Control Assessments Performed During Community Bank Examinations

Our recent *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. During this period, we began scoping work at the Board and the Federal Reserve Bank of Richmond. We are in the process of analyzing the data gathered during our scoping visit, designing our approach and methodology, and selecting additional Reserve Banks to be visited during the next phase of this assignment.

Audit of Retirement Plan Administration

The Office of Employee Benefits (OEB) was originally established to administer the Federal Reserve System's retirement plans. Over time, OEB's responsibilities have grown to include several other benefit plans such as the thrift plan, the long-term disability plan, and the personal accident insurance plan. During 2001, we participated with the Reserve Bank General Auditors in an audit of the OEB. The audit included a recalculation of pension payments for each retirement election option from a sample of retired employees throughout the System and a verification of information for active employees. The limited work we performed in support of the audit identified several discrepancies in the information maintained by the contracted retirement plan administrator—Hewitt Associates. Late last year, we began a separate audit of retirement plan administration, focusing on the retirement plans and processes for Board employees. Our objectives are to evaluate governance of, and controls over, plan administration, as well as to review controls over the maintenance of employee information. We will complete fieldwork during the next quarter and provide the results to management.

Audit of the Board's Outsourcing Efforts

In September 2002, we began an audit of the Board's outsourcing efforts. Over the years, the Board has outsourced several of its functions, such as the servicing of its Human Resources benefits program, its cafeteria and food services, and its 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 are continuing our analysis of selected contracts for outsourced activities and anticipate completing this audit during the next reporting period.

Audit of the Federal Reserve System's Surveillance Function

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. Surveillance activities are performed at the Board and at each Reserve Bank. The importance of the surveillance function has increased now that the System has implemented a risk-focused approach to examination, which requires more intensive preexamination planning and scoping to ensure that examiners focus their efforts on areas that pose the greatest risks to an institution's safety and soundness.

The objective of this audit is to evaluate the economy and efficiency of the System's surveillance program. Our work entailed a Systemwide look at the surveillance efforts; the coordination between the Board, the Reserve Banks, and other regulators; and the overall efficiency of the System's surveillance activities. We have completed our survey work and will be reporting our results during the next reporting period.

Evaluation of the Board's Implementation of E-Gov Services

Advances in the use of information technology and the Internet are transforming the way federal agencies communicate, use information, deliver services, and conduct business. One of the five governmentwide initiatives of "The President's Management Agenda" is to expand the use of electronic government (e-Gov) as a way of securing and providing greater services at lower costs. While the Board is emphasizing more web-based technology in providing information to the public and in managing certain internal operations, its strategy for using e-Gov in other areas is less clear.

The objectives of this project are to determine the status of the Board's implementation of e-Gov concepts and systems, identify potential challenges, and recommend strategies to address these challenges. We have completed our fieldwork on this evaluation and will be reporting our results during the next period.

BOND Life Cycle Assessment

BS&R and the Division of Information Technology (IT) are developing the Banking Organization National Desktop (BOND), an automated application

intended to support the supervision process by facilitating secure information-sharing and collaboration across the System and with certain other financial regulators. BS&R is implementing the BOND application in phases and has asked the OIG to provide an independent perspective on the process. Our objective is to help ensure that the BOND application is being implemented in an efficient and effective manner, with proper attention to the control framework.

We are continuing to attend key BOND meetings as BS&R and IT implement the next phase of the BOND development effort—providing web-enabled, access capabilities. As part of our routine activities going forward, we will continue to observe the progress in BOND implementation and anticipate concluding our work during the next reporting period.

OIG Internal Systems Replacement

The use of Lotus NOTES as our applications platform has allowed us to automate the majority of our core business processes. However, the original design of most of our key systems was completed in an early release of NOTES, making continued maintenance and support difficult and time consuming. Last year we began a review of commercial off-the-shelf software (COTS) to determine the availability and usability of a COTS product for all OIG requirements (audit, audit-related, investigations, and management information). We convened user groups from each of these areas to fully define application requirements and crosswalk those requirements against current functionality. We completed that assessment during the first quarter of 2003, and have developed an acquisition strategy designed to minimize customization while ensuring that the product acquired fully meets all OIG business requirements. We anticipate completing the procurement and customization processes during the next reporting period, with a goal of full implementation by the fourth quarter of 2003.

Appendixes

Appendix 1

Audit Reports Issued with Questioned Costs for the Period October 1, 2002, through March 31, 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	0	$0	$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	0	$0	$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 October 1, 2002, through March 31, 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	0	$0
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	0	$0
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	–	–	–
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	09/02	1	6
A0107	Audit of the Federal Reserve's Background Investigation Process	10/01	3	3	0	–	–	–
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	–	–	–

[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	12
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	9
5(a)(5)	Summary of instances where information was refused	None
5(a)(6)	List of audit reports	5-16
5(a)(7)	Summary of significant reports	None
5(a)(8)	Statistical Table—Questioned Costs	19
5(a)(9)	Statistical Table—Recommendations that Funds Be Put to Better Use	20
5(a)(10)	Summary of audit reports issued before the commencement of the reporting period for which no management decision has been made	21
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