

October 30, 2002

The Honorable Michael M. Reyna  
Chairman of the Board and  
Chief Executive Officer  
Farm Credit Administration  
McLean, Virginia 22102

Dear Mr. Reyna:

Enclosed is the semiannual report on the activities of the Farm Credit Administration's (FCA or Agency) Office of Inspector General (OIG) for the period from April 1, 2002 through September 30, 2002. We are filing this report in accordance with the Inspector General Act of 1978, as amended (Act). This is the twenty-seventh report since creation of the office on January 22, 1989. Section 5(b) of the Act requires that you send this report to the appropriate Congressional committees and subcommittees within 30 days after the date of this transmittal, with management's report on the status of audit recommendations.

Under your leadership, the process of monthly briefings by the Audit Follow-up Official to the FCA Board has been beneficial. Management has made large strides to strengthen Agency programs and processes by taking action to implement OIG agreed upon actions.

Respectfully,

Stephen G. Smith  
Inspector General

Enclosure

## CONTENTS

REPORTING REQUIREMENTS	ii
EXECUTIVE SUMMARY	0
BACKGROUND	1
MANAGEMENT CHALLENGES	1
FARM CREDIT SYSTEM RISK	1
ORGANIZATIONAL LEADERSHIP	1
STRATEGIC PLANNING	2
HUMAN CAPITAL	2
FINANCIAL MANAGEMENT	2
SECURITY	2
LEVERAGING TECHNOLOGY	3
AUDIT AND INSPECTION REPORTS ISSUED	3
FCA CONTRACTING ACTIVITY	3
LEAVE BANK PROGRAM	4
PURCHASE CARD INSPECTION	4
BAR REVIEW	4
GISRA REVIEW	4
STATUS OF UNIMPLEMENTED AGREED UPON ACTIONS	4
AUDITS	5
INSPECTIONS	6
INVESTIGATIONS	6
LEGISLATION AND REGULATIONS	6
OTHER ACTIVITIES	7
MANAGEMENT ADVISORIES	7
FARM CREDIT SYSTEM INSURANCE CORPORATION	7
SURVEY OF FARM CREDIT SYSTEM INSTITUTIONS	7
OIG PERFORMANCE MEASURES	8
STAFF PARTICIPATION IN ACTIVITIES OF THE PROFESSIONAL COMMUNITY	8
STAFF PARTICIPATION IN AGENCY ORGANIZATIONS	8
AUDIT / INSPECTION REPORTS ISSUED BY FCA OIG	9
INSPECTOR GENERAL ISSUED REPORTS WITH QUESTIONED COSTS	10
INSPECTOR GENERAL ISSUED REPORTS WITH RECOMMENDATIONS THAT FUNDS BE PUT TO BETTER USE	11
FARM CREDIT ADMINISTRATION ORGANIZATION CHART	12
FCA OFFICE OF INSPECTOR GENERAL ORGANIZATION CHART	13

## REPORTING REQUIREMENTS

INSPECTOR GENERAL ACT CITATION AND REQUIREMENT	PAGE
Section 4(a)(2) Review of Legislation and Regulations .....	6
Section 5(a)(1) Significant Problems, Abuses and Deficiencies.....	none
Section 5(a)(2) Recommendations With Respect to Significant Problems, Abuses and Deficiencies .....	none
Section 5(a)(3) Prior Recommendations Not Yet Implemented .....	4-5
Section 5(a)(4) Matters Referred to Prosecutive Authorities .....	none
Section 5(a)(5) Summary of Instances Where Information .....	none
and 6(b)(2) Was Unreasonably Refused or Not Provided	
Section 5(a)(6) List of OIG Audit/Inspection Reports .....	3-4
Section 5(a)(7) Summary of Each Particularly Significant Report .....	3-4
Section 5(a)(8) Statistical Table on Management Decisions.....	10
on Questioned Costs	
Section 5(a)(9) Statistical Table on Management Decisions on.....	11
Recommendations that Funds be Put to Better Use	
Section 5(a)(10) Summary of Each Audit Over Six Months Old for .....	none
Which No Management Decision Has Been Made	
Section 5(a)(11) Significant Revised Management Decisions .....	none
Section 5(a)(12) Significant Management Decisions With Which .....	none
the Inspector General Disagrees	
Section 5(a)(13) Compliance of Agency Financial Management System .....	2

## **EXECUTIVE SUMMARY**

This semiannual report to the Congress summarizes the activities and accomplishments of the Farm Credit Administration (FCA or Agency), Office of Inspector General (OIG) and covers the period April 1, 2002 through September 30, 2002. Our efforts were directed toward performing audits, inspections, and evaluations of the FCA programs and operations; conducting several investigations; and providing technical assistance and advice on FCA programs.

During the reporting period, the FCA Board returned to full strength. Moreover, the Board members are engaged in healthy discussions about regulatory and enforcement issues facing the FCA. The Board members are laying the foundation for a collegial relationship that is vital to the organization. We believe that prior work that we performed on governance will serve as a building block for a strong Board.

Under the Chairman's leadership, the FCA has made significant strides towards resolving agreed upon management actions. The focus on progress towards resolving agreed upon actions and recommendations at monthly Board briefings has resulted in corrective action on several long-standing issues and quick resolution of new agreed upon actions.

For example, FCA continues in its strides to develop performance budgeting at the Agency. FCA now has the mechanisms in place to tie resources to Agency products, services, and projects. Additionally, management resolved five of six agreed upon actions within three weeks of a report issuance.

In the investigative area, we substantiated allegations of misuse of Government purchase cards and travel cards in three investigations. The OIG recommended additional controls to prevent future incidents.

The OIG advised managers on multiple issues that came to our attention. This advice encourages managers to take proactive actions. For example, we contributed to the FCA efforts to recruit and retain the high quality employees by identifying attractive features of working at FCA as well as identifying the need for Agency policy on professional memberships and accreditation. We also contributed to improved efficiency and controls. For example, we suggested the need for an OIG function at the FCA sister organization – the Farm Credit System Insurance Corporation.

## **BACKGROUND**

The FCA is an independent Federal agency of the United States government responsible for the regulation, examination and supervision of institutions chartered under the Farm Credit Act of 1971, as amended. FCA is a nonappropriated agency with a fiscal year (FY) 2002 budget of \$38,033,000 for administrative costs. The FY 2002 budget for the Office of Inspector General (OIG) was \$829,601. FCA is a “designated Federal entity” within the meaning of the Inspector General Act of 1978, as amended.

FCA currently has 273 employees, about half of which are examiners located at five field offices. Also included in the Agency positions are five approved positions for the OIG. Appendix II displays the current organizational structure of FCA and Appendix III displays the OIG within that structure.

## **MANAGEMENT CHALLENGES**

This section of the report outlines major challenges confronting the Farm Credit Administration as it works to fulfill its mission. These challenges fall into two general categories. First are the challenges related to the FCA’s core mission of ensuring a dependable supply of credit to agriculture through the institutions it has chartered. These challenges are often shaped and influenced by events that are outside the control of the Agency. Second, but no less important, are those challenges related to the Agency’s operations. These management challenges were incorporated in the previous semiannual report but have been updated to reflect changes and progress in meeting the challenges.

### **Farm Credit System Risk**

The Farm Credit System (FCS) is a single industry lender and therefore is vulnerable to economic swings in the industry. The FCA is challenged to balance the often-competing demands of ensuring the FCS fulfills its public purpose, proactively examining risk in the regulated institutions both individually and systemically, and controlling the cost of the regulator.

### **Organizational Leadership**

The Farm Credit Act provides for a full time three-member Board of Directors. The Board members are appointed by the President and confirmed by the Senate. The rapidly changing complex financial and banking environment makes the Board’s task both challenging and important. The Board must be able to engage in professional policy debate and set a sound course for the Agency.

The Board is in an important period of transition. On August 6, 2002, the Board returned to full strength ending a 19-month period with only two Board members. The President has nominated another person to replace the current Board member whose term expired. The return to a full strength Board is an important element in setting clear priorities and deliberating fully on the issues.

A relatively small full-time Board also presents a challenge in terms of defining the roles and responsibilities of the Board members relative to the governance of the Agency. As

the membership on the Board changes, it needs to update its rules of operation to ensure it fulfills its statutory role in the governance of FCA.

## **Strategic Planning**

The FCA Strategic Plan was updated and revised in Fiscal Year (FY) 2000 to reflect the FCA Board's priorities at that time. The current FCA Strategic Plan reflects an environment that has changed significantly since it was adopted – the composition of the Board, the economy, the structure of the FCS, and the President's Management Agenda. The FCA Board's challenge is to take a fresh look at the substance of FCA's mission, goals and objectives. The Board will have the opportunity to set a course for FCA that focuses on the results that it wants to achieve through clear and balanced performance measures. The change in the Board's composition will allow the new Board to develop a new perspective that is not unduly constrained by past practices but builds on the experience of prior Boards.

## **Human Capital**

The President identified human capital as a critically needed management reform in the Federal government. FCA needs to develop a comprehensive, integrated approach to human capital issues. In light of the changes in the competitive environment, advances in technology, and the tenure of its workforce; the Agency will be challenged to closely evaluate business processes, their associated costs, and alternatives available through competitive sourcing. The General Accounting Office's (GAO) *High-Risk*<sup>1</sup> report outlined four pervasive human capital challenges that the government faces:

- Planning strategic human capital and organizational alignment;
- Planning for succession and leadership continuity;
- Acquiring and developing staffs whose size, skills, and deployment meet agency needs; and
- Creating results-oriented performance cultures.

## **Financial Management**

Last year, FCA successfully implemented a new financial management system using the services of the Department of Interior's National Business Center. FCA received an unqualified audit opinion. However, financial management success goes beyond an unqualified financial statement audit opinion. Management's challenge is to leverage the system to deliver timely financial information that is critical for making well-informed management decisions. Meeting this challenge requires new measures of success. Measures such as delivering financial information that managers can use for day-to-day operations; and developing reports that capture the full cost of programs and projects can help bring about a transition.

## **Security**

In the recent report on information security, the OIG found a strong foundation for security practices. However, the speed of change in the security environment will be a challenge for all government organizations. This is especially true for smaller organizations like FCA

---

<sup>1</sup> GAO-01-263

where an increased emphasis on physical and information security will compete with program areas for tight budget funding and therefore, security remains a major challenge for the Agency.

### **Leveraging Technology**

The Agency has recognized that in order to meet the constraints of its budget, it must be able to maximize its return on investment in technology. FCA will need effective mechanisms to ensure that current and future staff has the technical skills to use technology to operate in an efficient manner.

## **AUDIT AND INSPECTION REPORTS ISSUED**

We issued an audit report and three inspection reports during the reporting period. In addition, we completed a "Government Information Security Act Review." We conduct all audits in accordance with the standards established by the Comptroller General of the United States for audits of Federal organizations, programs, activities, and functions. Inspections are in accordance with the President's Council on Integrity and Efficiency's Quality Standards for Inspections. Copies of OIG reports are available on FCA's Web site ([www.fca.gov/oig](http://www.fca.gov/oig)), by contacting the OIG on 703/883-4030, or by e-mail at [IG\\_information@fca.gov](mailto:IG_information@fca.gov).

### **FCA Contracting Activity**

The OIG completed an audit on the FCA contracting activity. The objectives of the audit were to determine if FCA's contracting environment and process being used provide adequate controls and safeguards to prevent fraud, waste and abuse. The audit was also a follow-up on a procurement management letter issued July 24, 2001. We found that many of the procurement actions resulted in cost efficient purchases of goods and services. However, we found problems with 41 percent of the procurement actions reviewed. Many of the problems identified are attributed to procurement staff's inattention to contract management responsibilities. Specifically, inadequate acquisition planning, unauthorized commitments and lax procurement oversight have made the Agency vulnerable to waste and abuse. Management agreed to recommendations to promote competition, validate needs, review contract files, track contractor costs, update policy and procedures, and review procurement office staffing.

Management did not agree with two recommendations. The OIG recommended discontinuing a car lease that was not adequately utilized and cost FCA \$7.69 per mile. Management rejected the recommendation but agreed to perform a cost-benefit analysis to determine whether the car lease is needed. The OIG made another recommendation to either obtain the Chief Executive Officer's approval for an exception to the Federal Acquisition Regulation on a personal service contract or terminate the contract immediately. Management rejected this recommendation and amended the contract for an additional two months. The General Counsel issued a legal opinion that this was not a personal service contract and management stated the contract will not be amended again. The Inspector General believes the recommendations remain appropriate but management is taking alternative actions.

## **Leave Bank Program**

The OIG conducted an inspection of the Agency's leave bank program to determine whether the program is administered according to internal guidelines. We found the administration of the leave bank program is sound and the program has accomplished its purpose of reducing the financial impact of medical emergencies on employees. We also determined the value of the leave bank balance is properly reflected in the Agency's financial records. There were no findings that required formal action or follow up.

## **Purchase Card Inspection**

We completed an inspection of how effectively government purchase cards are used in the Agency. Generally, management and staff are effectively and efficiently administering the program. Cardholders are making appropriate use of the program to acquire goods and services for their offices. The Agency agreed to six actions to improve the purchase card system including educating cardholders, performing internal reviews, and improving standard procedures. These actions will improve internal controls over the program.

## **Bar Review**

We reviewed the bar status of FCA attorneys to determine if they are licensed to practice law. FCA and the Office of Personnel Management require personnel in the 0905 classification series be licensed as an attorney and a member in good standing of the bar in a state, territory of the United States, District of Columbia, or the Commonwealth of Puerto Rico. Our review determined FCA attorneys are members in good standing of a state bar. However, FCA did not have a process in place to document and periodically verify bar status of each attorney. Management agreed to require documentation of bar membership before an offer of employment and to conduct a periodic review to verify bar status.

## **GISRA Review**

OIG engaged the independent audit firm, Clifton Gunderson LLP, to conduct a review of the information security in accordance with procedures essential for establishing compliance with the Government Information Security Reform Act (GISRA). The Federal Financial System, Consolidated Reporting System, Lotus Notes, Windows NT, Firewall System and the FCA Web site were reviewed as mission critical systems. This was the second consecutive year where the evaluators found no security issues concerning the Agency-wide security program.

## **STATUS OF UNIMPLEMENTED AGREED UPON ACTIONS**

At the beginning of the period there were 16 unimplemented agreed upon actions. During the reporting period, management took final action on 9 of these. During this period, we issued reports containing 15 agreed upon actions and 2 recommendations. Management took action on 12 agreed upon actions and rejected the 2 recommendations. At the end of this reporting period, 10 agreed upon actions remain open.

**Audits**

The following table summarizes the final actions management took on open agreed upon actions. One new audit report was issued concerning FCA contracting activity containing eight agreed upon actions and two recommendations.

<b>AUDIT AGREED UPON ACTIONS</b>			
<b>Audit Report</b>	<b>Open during this 6-month period</b>	<b>Final Management Actions during this period</b>	<b>Open on 10/01/2002</b>
Performance Budgeting .....Issued March 23, 2001	10	6	4
Office of Chief Financial Officer .....Issued January 24, 2002	4	1	3
FCA Contracting Activity .....Issued August 27, 2002	8	6	2
<b>Totals</b>	<b>22</b>	<b>13</b>	<b>9</b>

The audit report of Performance Budgeting was issued more than 18 months ago. Four of the original 14 agreed upon actions remain open. The management actions taken during this period has now enabled the Agency to be able to track its resource usage by individual projects, products and services, as well as by organizational unit and object class. Once the Agency takes actions on the remaining 4 agreed upon actions, FCA should be capable of continuously monitoring its performance achievement against the related costs.

<b>AUDIT RECOMMENDATIONS</b>			
<b>Audit Report</b>	<b>Open during this 6-month period</b>	<b>Final Management Actions during this period</b>	<b>Open on 10/01/2002</b>
FCA Contracting Activity .....Issued August 27, 2002	2	2 <sup>2</sup>	0
<b>Totals</b>	<b>2</b>	<b>2</b>	<b>0</b>

<sup>2</sup> Both recommendations rejected

## Inspections

The following table summarizes the final actions management took on open agreed upon actions. Three new inspection reports were issued containing seven agreed upon actions.

<b>INSPECTION AGREED UPON ACTIONS</b>			
<b>Inspection Report</b>	<b>Open during this 6-month period</b>	<b>Final Management Actions during this period</b>	<b>Open on 10/01/2002</b>
Personnel Security Program .....Issued December 20, 2001	2	2	0
Leave Bank Program .....Issued April 10, 2002	0	0	0
Bar Review of FCA attorneys .....Issued April 22, 2002	1	1	0
Purchase Card Program .....Issued September 9, 2002	6	5	1
<b>Totals</b>	<b>9</b>	<b>8</b>	<b>1</b>

Management closed the remaining two agreed upon actions on the Personnel Security Program inspection and the one agreed upon action on the Bar Review during this semiannual reporting period. Management also took prompt action and closed five of six agreed upon actions on the Purchase Card Program Inspection.

## Investigations

Most OIG Hotline calls and emails dealt with FCS borrower complaints and were referred to the FCA office responsible for researching such matters. All other Hotline calls and emails did not require investigative work by this office and were referred to the appropriate FCA office or other Federal agency.

There was one open investigation at the beginning of this reporting period. This investigation was not substantiated and was closed during this period. Four new investigations were opened this period, with one being closed unsubstantiated. The other three investigations substantiated allegations of misuse of government purchase cards and travel cards.

## Legislation And Regulations

OIG staff reviewed several FCA regulations in both proposed and final form. Statutory and regulatory compliance issues were reviewed as they arose in audits, inspections and investigations. Also, we reviewed and commented on proposed legislation affecting the Inspectors General community through the legislation committee of the President's Council on Integrity and Efficiency and the Executive Council on Integrity and Efficiency (PCIE/ECIE).

During this period, OIG reviewed S. 2530 concerning law enforcement authority for Inspectors General. H.R. 4561, concerning privacy issues was reviewed as well as H.R.

4685, Accountability of Tax Dollars Act of 2002, requiring audited financial statements for executive agencies not otherwise covered under the Chief Financial Officer Act. We also were actively involved in commenting on a GAO audit on consolidation of Inspectors General.

## **Other Activities**

### **Management Advisories**

During this reporting period, the OIG has continued the use of management advisories. These advisories provide management with feedback on issues that came to our attention during the process of performing other OIG work. In this 6-month period, we advised Agency managers on issues including supervisory practices in an office, credit card issuance and monitoring processes, Office of Management and Budget Bulletin 02-05, travel policies, security practices, and use of copyright material.

### **Farm Credit System Insurance Corporation**

The Farm Credit System Insurance Corporation (FCSIC or Corporation) has assets exceeding \$1.7 billion. The mission of FCSIC is closely tied to the mission of FCA. The Farm Credit Act (Act) (12 USC 2277a-8) recognizes the interrelationship between FCA and FCSIC by establishing a common board structure. The Act also states “To the extent practicable, the Corporation shall use the personnel and resources of the Farm Credit Administration to minimize duplication of effort and to reduce costs.”

The Inspector General advised the FCSIC Board that there is no explicit authority providing the FCA Inspector General the authority to examine FCSIC activities without FCSIC’s permission. However, the legislative history of the Inspector General Act indicates that Federal entities, such as FCSIC, may obtain the needed level of internal audit from an appropriate authority such as an existing OIG. The Inspector General believes it is in the FCSIC Board’s best interest to have an appropriate level of independent audit oversight that the OIG can provide.

### **Survey of Farm Credit System Institutions**

OIG administers an ongoing Agency survey of the regulated institutions of the FCS. This survey is designed to provide the FCA Board and senior management with independent feedback about how well FCA performs its examination and enforcement activities. The feedback is based on confidential responses received from FCS institutions. We surveyed the Chairman of the Board and the Chief Executive Officer of each FCS institution, following their receipt of FCA’s report of examination, for their voluntary feedback on the quality and consistency of the examination and enforcement processes. OIG reports the results of the survey annually. During this 6-month semiannual period we mailed 46 surveys and received 34 responses, which equates to a 74 percent response rate. Overall, the average rating for the questions answered during this reporting period was slightly less favorable (1.66) [1=completely agree; 5=completely disagree] than the prior semiannual reporting period (1.38). The overall response rate for FY 2002 was slightly more favorable (1.51) than the overall response rate for FY 2001 (1.61).

### **OIG Performance Measures**

OIG's performance measures were developed in 1995. Each year we issue a report on our performance. It is available on the FCA OIG Web page at [www.fca.gov/OIG](http://www.fca.gov/OIG).

### **Staff Participation in Activities of the Professional Community**

OIG staff members are encouraged to take part in organizations that contribute to the mission of the Inspector General community, as well as their individual professional development. Most staff is actively involved in one or more professional organizations as well as ad hoc activities of the PCIE/ECIE.

### **Staff Participation in Agency Organizations**

Staff is active on several Agency workgroups and task forces. During this reporting period the OIG was represented on Blacks in Government, FCA Employees' Council, Administrative Burden Reduction Workgroup, the Federal Women's Program, the Continuity of Operations Plan task force, the Budget and Planning task force and the Employee Pay Workgroup.

**APPENDIX I**

**Audit / Inspection Reports Issued By FCA OIG**

<b>TITLE OF REPORT</b>	<b>NUMBER OF RECOMMENDATIONS/ AGREED UPON ACTIONS</b>	<b>QUESTIONED COSTS</b>	<b>RECOMMENDATIONS THAT FUNDS BE PUT TO BETTER USE</b>
FCA Contracting Activity	10	\$ 0	\$ 0
Bar Review	1	\$ 0	\$ 0
Purchase Card Activity	6	\$ 0	\$ 0
<b>Total</b>	<b>17</b>	<b>\$ 0</b>	<b>\$ 0</b>

APPENDIX Ia

**INSPECTOR GENERAL ISSUED REPORTS WITH QUESTIONED COSTS**

	Number		Dollar Value	
	Reports	Recs.	Questioned Costs	Unsupported Costs
A. For which no management decision has been made by the commencement of the reporting period	0	0	\$ 0	\$ 0
B. Which were issued during the reporting period	0	0	\$ 0	\$ 0
Subtotals (A+B)	0	0	\$ 0	\$ 0
C. For which a management decision was made during the reporting period	0	0	\$ 0	\$ 0
(i) dollar value of disallowed costs	0	0	\$ 0	\$ 0
(ii) dollar value of costs not disallowed	0	0	\$ 0	\$ 0
D. For which no management decision has been made by the end of the reporting period	0	0	\$ 0	\$ 0
E. For which no management decision was made within six months of issuance	0	0	\$ 0	\$ 0

APPENDIX Ib

**INSPECTOR GENERAL ISSUED REPORTS WITH  
 RECOMMENDATIONS THAT FUNDS BE PUT TO BETTER USE**

	Number		Dollar Value
	Reports	Recs.	
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 recommendations that were agreed to by management	0	0	\$ 0
--based on proposed management action	0	0	\$ 0
-- based on proposed legislative action	0	0	\$ 0
(ii) dollar value of recommendations that were not agreed to by management	0	0	\$ 0
D. For which no management decision has been made by the end of the reporting period	0	0	\$ 0
E. For which no management decision was made within six months of issuance	0	0	\$ 0

**Farm Credit Administration Organization Chart**

**FCA Office of Inspector General Organization Chart**