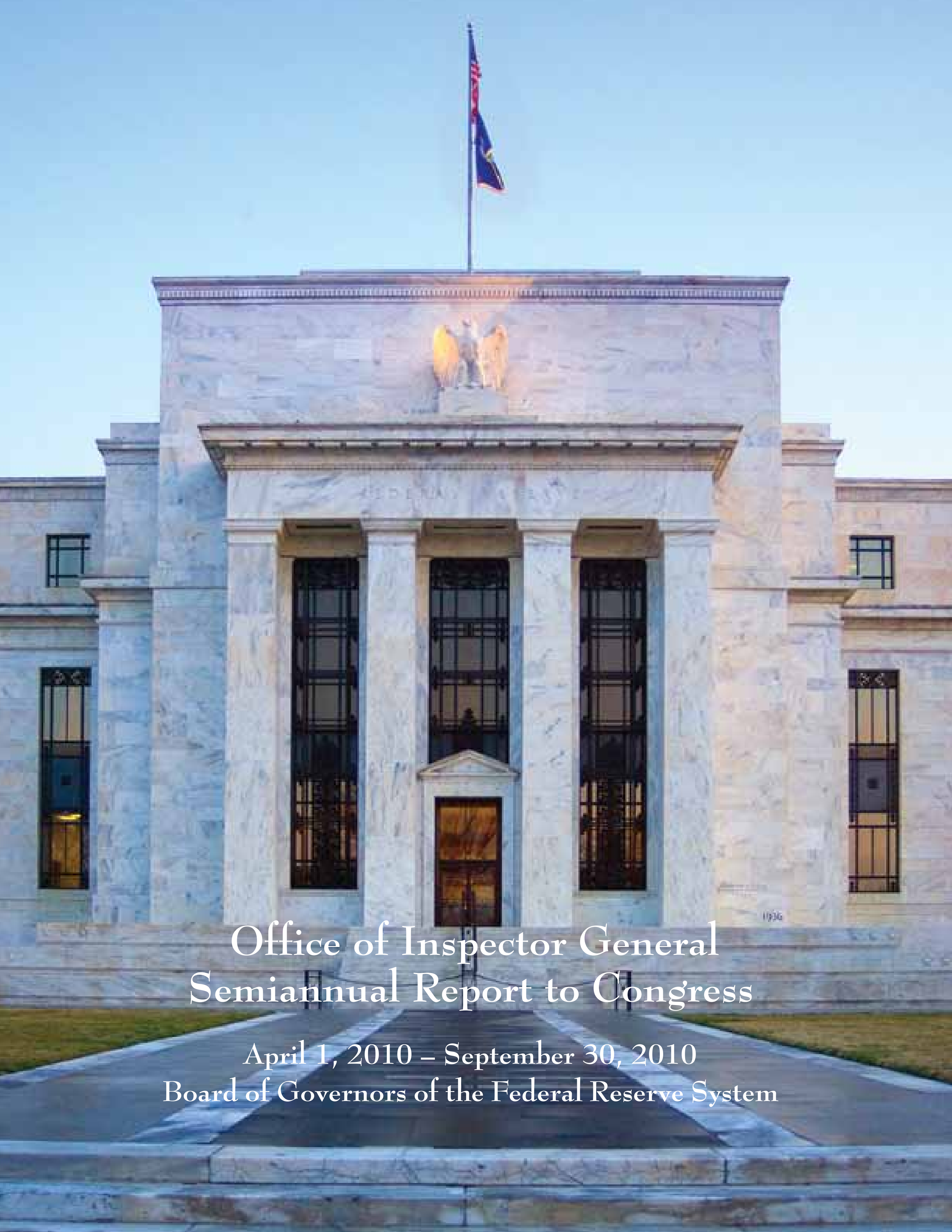


Office of Inspector General Semiannual Report to Congress

April 1, 2010 – September 30, 2010

Board of Governors of the Federal Reserve System

Message from the Inspector General

On behalf of the Office of Inspector General (OIG) of the Board of Governors of the Federal Reserve System (Board), I am pleased to present our *Semiannual Report to Congress* highlighting our accomplishments and ongoing work for the six-month period ending September 30, 2010. Challenges and opportunities stemming from the financial crisis remain our primary focus, from reviewing the supervision and regulation of failed Board-supervised banks, to reviewing the Federal Reserve's lending facilities to support overall market liquidity, to participating in nationwide efforts to investigate and prosecute mortgage-related crimes.

Of particular note during this reporting period, Congress passed and the President signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). The Dodd-Frank Act brings significant and wide-ranging reforms to the financial sector to promote the financial stability of the United States by improving accountability and transparency in the financial system, and to protect consumers from abusive financial services practices. In short, the Dodd-Frank Act seeks to prevent a repeat of the recent financial crisis.

Our office is already busy addressing our new responsibilities under the Dodd-Frank Act. For example, the act increases the threshold for conducting material loss reviews of failed banks to $200 million for losses that occur through December 31, 2011, and requires the Inspector General (IG) of the cognizant financial regulatory agency to review each bank failure with an estimated loss below the threshold to determine if unusual circumstances exist that warrant a more in-depth review. The act requires us to report semiannually on these determinations, and our first report on the 12 Board-supervised banks that fell below the threshold is included as part of this semiannual report. Collectively, these 12 institutions had total assets of about $3.8 billion and losses estimated at $626 million, or 16.6 percent of total assets.

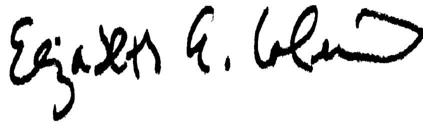
The Dodd-Frank Act also creates the Bureau of Consumer Financial Protection (Bureau) as an independent entity within the Federal Reserve System, and designates our office as the OIG for the Bureau. The Bureau's mission is to implement and, as applicable, enforce federal consumer law consistently to ensure that all consumers have access to markets for financial products and services, and that these markets are fair, transparent, and competitive. The Secretary of the Treasury—who is currently the acting head of the Bureau—has designated July 21, 2011, as the date that certain authorities will transfer from other agencies to the Bureau and that the Bureau will be able to exercise additional, new authorities. We are monitoring the activities that are already under way to create the new Bureau and coordinating our efforts with the U.S. Department of the Treasury's (Treasury's) OIG. We are also developing a strategic plan for fulfilling our new oversight responsibilities, and addressing budget and staffing requirements going forward.

In addition, the Dodd-Frank Act creates the Financial Stability Oversight Council (FSOC) to monitor emerging threats to financial stability, designate for supervision those nonbank financial firms and market utilities that could pose threats to financial stability, and identify gaps in the financial regulatory framework. The FSOC includes representatives from the key federal financial regulatory agencies, including the Board and the Bureau. At the

same time, the Dodd-Frank Act establishes the Council of Inspectors General on Financial Oversight (CIGFO), which consists of the IGs for the Federal agencies represented on the FSOC, as well as the IG for the Department of Housing and Urban Development and the Special IG for the Troubled Asset Relief Program. Under the leadership of the Treasury IG, the CIGFO meets at least quarterly to share information among the IGs and to discuss the ongoing work of each IG, with a focus on concerns that may apply to the broader financial sector and ways to improve financial oversight. In addition, the CIGFO is required to annually issue a report that highlights the IGs' concerns and recommendations, as well as issues that may apply to the broader financial sector. The CIGFO recently held its first meeting and is taking steps to fulfill this new mandate.

We look forward to working with the Board, the Bureau's transition team, and Congress to accomplish the new requirements of the Dodd-Frank Act and to enhance the economy, efficiency, and effectiveness of the Board and the Bureau in achieving their respective missions.

Sincerely,



Elizabeth A. Coleman
Inspector General

October 28, 2010

Semiannual Report to Congress

April 1, 2010 – September 30, 2010

OIG

Office of Inspector General

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Highlights

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), Public Law No. 111-203, enacted into law on July 21, 2010, creates, among other things, the Bureau of Consumer Financial Protection (Bureau) as an independent entity within the Federal Reserve System. The act also designates our office as the Bureau's Office of Inspector General (OIG). The new Bureau's mission is to implement and, as applicable, enforce federal consumer law consistently to ensure that all consumers have access to markets for financial products and services, and that these markets are fair, transparent, and competitive. The Secretary of the Treasury—who is currently the acting head of the Bureau—has designated July 21, 2011, as the date that designated consumer protection functions will transfer from the Board and other agencies to the Bureau.

Since the Dodd-Frank Act was only recently enacted, this semiannual report focuses on our work related to the programs and operations of the Board of Governors of the Federal Reserve System (Board). Going forward, the OIG will be providing appropriate monitoring and oversight of the Bureau's operations, consistent with the Inspector General Act of 1978, as amended (IG Act), 5 U.S.C. app. 3. The following are highlights of the OIG's work during this reporting period:

- We continued to direct a significant portion of our resources to reviews of failed state member banks. Eight state member banks failed during the last six months, bringing the total number of failed state member banks since December 2008 to 30, with the associated cumulative loss to the Deposit Insurance Fund (DIF) estimated to be $4.5 billion. During the reporting period, we issued eight reports on reviews of failed banks, and we initiated an assessment of our cumulative body of bank failure reviews to identify any cross-cutting themes and potential recommendations for improvements in the supervision of state member banks.

- Work also continued on our review of the status of the six lending facilities that the Board established, pursuant to its authority under section 13(3) of the Federal Reserve Act, to help stabilize financial markets and restore overall market liquidity. Currently, the report on the results of our review is being finalized, and we anticipate issuing it within the next several weeks.

- Our investigative staff had several successes during the reporting period.

    - One of the subjects of a multi-agency investigation into an "advance fee" scheme was sentenced to eight years in federal prison and was ordered to pay approximately $3.8 million in restitution to victims who were falsely promised low-interest, multi-million dollar loans.

- In a separate case, a Board employee entered a guilty plea in connection with an investigation into the theft of Board cell phones and the associated calling charges.

- In another multi-agency case, a subject pleaded guilty to one count of trafficking in counterfeit goods after a federal grand jury indictment on charges of money laundering and trafficking in counterfeit goods that included the "structured" purchase of Postal Money Orders valued at $579,865.

- Our investigative staff also continues to participate in nationwide efforts to prosecute mortgage-related crimes. An investigation by OIG special agents assigned to the Maryland Mortgage Fraud Task Force recently resulted in the arrest of three subjects involved in a mortgage fraud scheme that netted more than $1.2 million from three federally regulated financial institutions.

As events in the financial regulatory environment continue to unfold, we remain committed to appropriately balancing our statutory and risk-focused work to promote integrity, economy, efficiency, and effectiveness in Board programs and operations and to strengthen accountability to Congress and the public.

Introduction

With the enactment of the Dodd-Frank Act on July 21, 2010, which amended several provisions of the IG Act, the oversight responsibilities of the Board's OIG were expanded to include the Bureau. However, given the timing of the act, this semiannual report focuses on the OIG's work related to Board programs and operations. As the Bureau stands up and prepares for the designated transfer date of July 21, 2011, the OIG will provide monitoring and oversight of the Bureau's operations, consistent with the IG Act. During this reporting period, we focused on our mission to

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

Congress has also mandated additional responsibilities that influence where the OIG directs its resources, to include the following. Section 38(k) of the Federal Deposit Insurance Act (FDI Act) requires the OIG to review failed financial institutions supervised by the Board that result in a material loss to the DIF and to produce a report within six months. The Dodd-Frank Act amended section 38(k) of the FDI Act to raise the materiality threshold and to require the OIG to conduct an in-depth review and prepare a written report regarding any nonmaterial losses to the DIF that exhibit unusual circumstances warranting an in-depth review.

In addition, section 211(f) of the Dodd-Frank Act requires the OIG to review the Board's supervision of any covered financial company that is placed into receivership and produce a report that evaluates the effectiveness of the Board's supervision, identifies any acts or omissions by the Board that contributed to or could have prevented the company's receivership status, and recommends appropriate administrative or legislative action.

Further, section 989E of the Dodd-Frank Act established the Council of Inspectors General on Financial Oversight (CIGFO), which comprises the Inspectors General (IGs) of the Board, the Commodity Futures Trading Commission, the Department of Housing and Urban Development, the U.S. Department of the Treasury (Treasury), the Federal Deposit Insurance Corporation (FDIC), the Federal Housing Finance Agency, the National Credit Union Administration, the Securities and Exchange Commission, and the

Troubled Asset Relief Program (TARP). The CIGFO is required to meet at least quarterly to share information and to discuss the ongoing work of each IG, with a focus on concerns that may apply to the broader financial sector and ways to improve financial oversight. Additionally, the CIGFO is required to annually issue a report that highlights the IGs' concerns and recommendations, as well as issues that may apply to the broader financial sector.

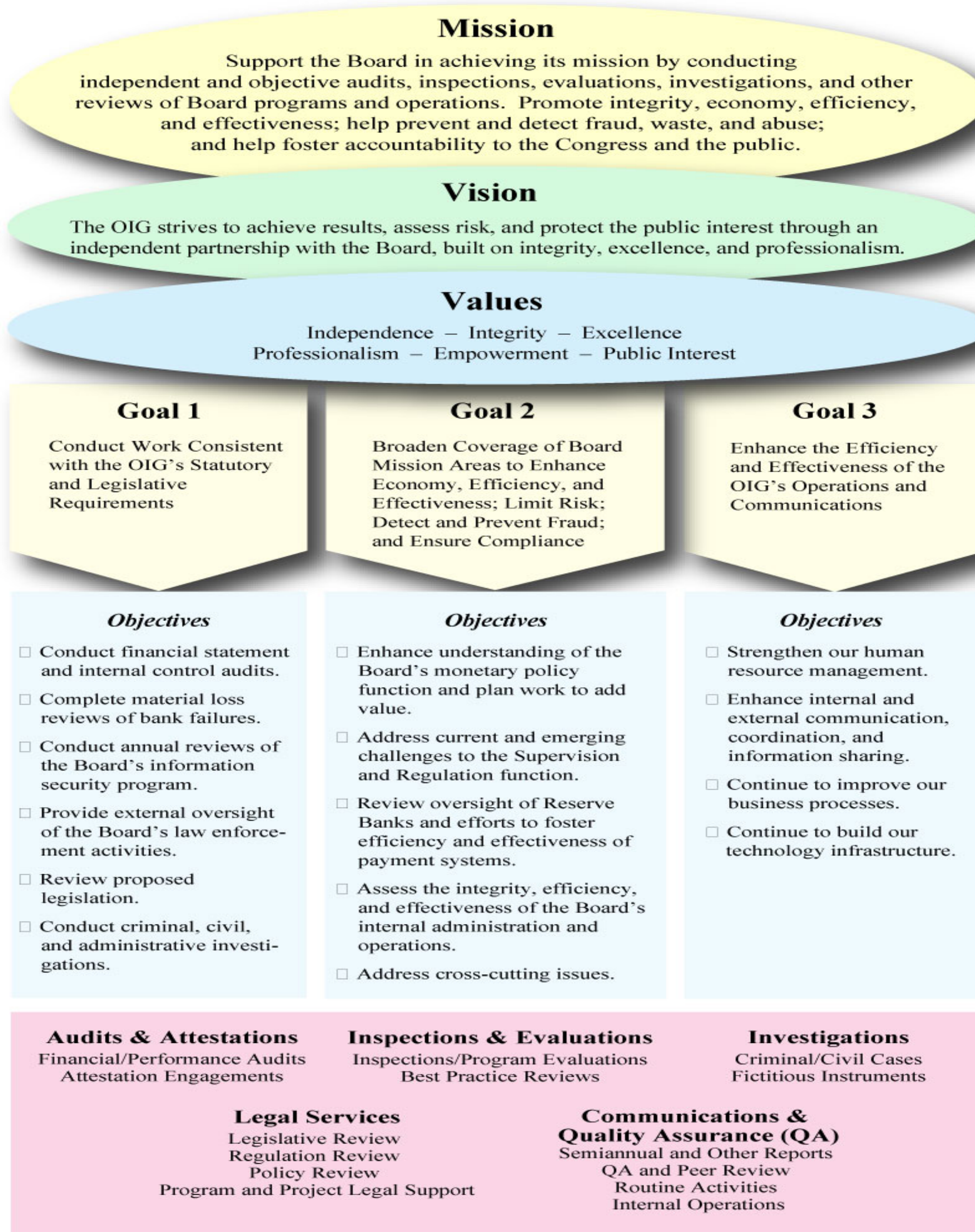
In the information technology arena, the Federal Information Security Management Act of 2002 (FISMA), Title III of Public Law No. 107-347, provides a comprehensive framework for ensuring the effectiveness of information security controls over resources that support federal operations and assets. Consistent with FISMA's requirements, we perform an annual independent evaluation of the Board's information security program and practices, which includes evaluating the effectiveness of security controls and techniques for selected information systems.

The USA PATRIOT Act of 2001, Public Law No. 107-56, grants the Board certain federal law enforcement authorities. Our office serves as the external oversight function for the Board's law enforcement program and operations.

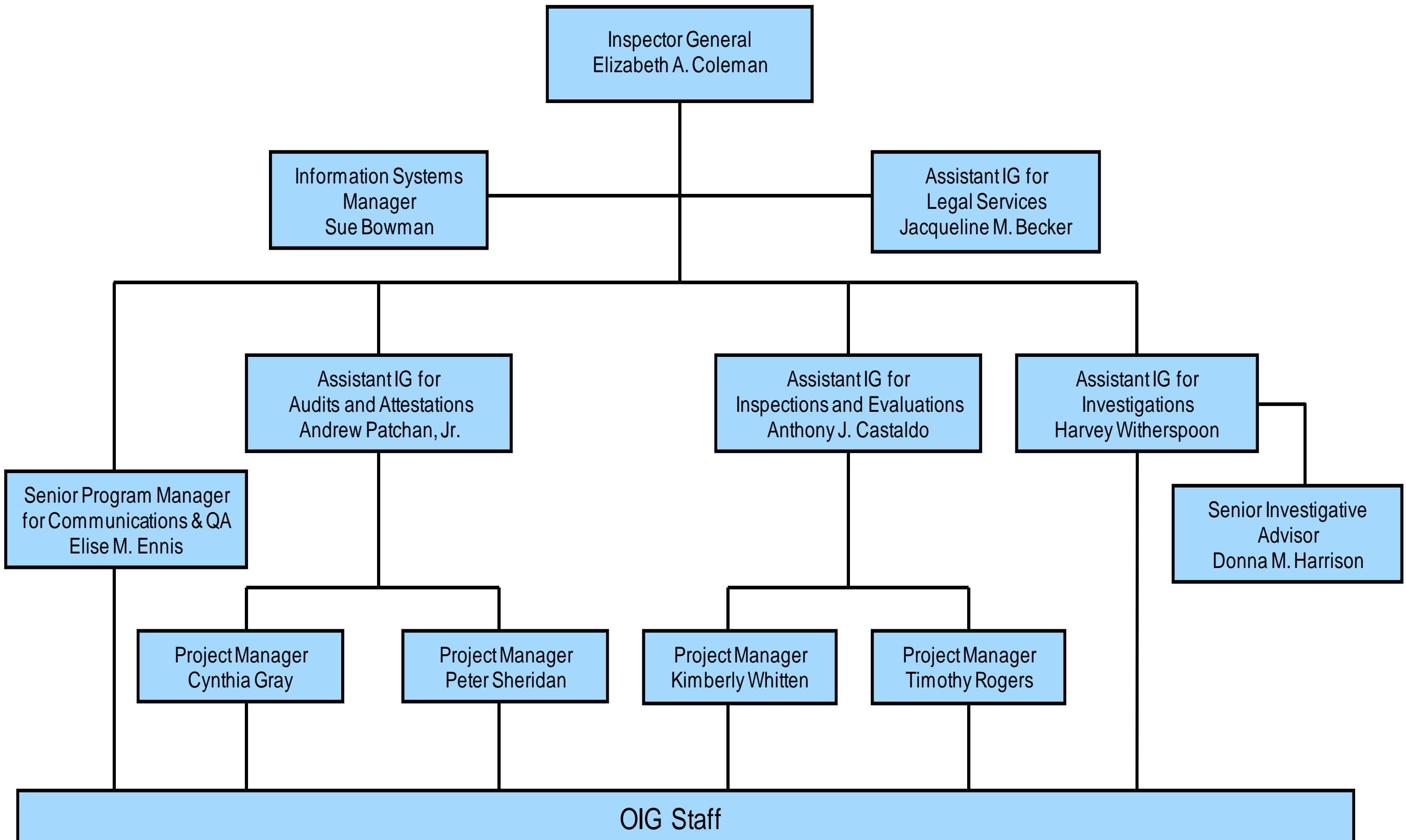
In addition, we oversee the annual financial statement audits of the Board and the Federal Financial Institutions Examination Council (FFIEC).

Overview of the OIG's Strategic Plan, 2008 – 2011

The following chart represents the structure of the OIG's existing Strategic Plan; however, we are currently updating the Strategic Plan to incorporate, among other things, new requirements under the Dodd-Frank Act, including our responsibilities as the OIG for the new Bureau of Consumer Financial Protection.



Organization Chart



OIG Staffing	
Auditors (including Information Technology)	42
Investigators	11
Attorneys	4
Administrative and Hotline	5
Information Systems Analysts	3
Total Authorized Positions	65

Audits and Attestations

The Audits and Attestations program assesses certain aspects of the economy, efficiency, and effectiveness of the Board's programs and operations. For example, the office of Audits and Attestations conducts audits of (1) the presentation and accuracy of the Board's financial statements and financial performance reports; (2) the effectiveness of processes and internal controls over the Board's programs and operations; (3) the adequacy of controls and security measures governing the Board's financial and management information systems and the safeguarding of the Board's assets and sensitive information; and (4) compliance with applicable laws and regulations related to the Board's financial, administrative, and program operations. As mandated by the IG Act, OIG audits and attestations are performed in accordance with the *Government Auditing Standards* established by the Comptroller General. The information below summarizes OIG work completed during the reporting period and ongoing work that will continue into the next semiannual reporting period.

COMPLETED AUDIT WORK

Security Control Review of the Lotus Notes and Lotus Domino Infrastructure

To evaluate the security controls and techniques of the information systems of the Board, the OIG reviews controls over associated major applications on an ongoing basis. Consistent with the requirements of FISMA, we conducted a security control review of the Board's Lotus Notes and Lotus Domino infrastructure. The Lotus Notes and Lotus Domino infrastructure is a component of the general support system supported by the Board's Division of Information Technology. The general support system infrastructure provides network and general computing capabilities for the Board's end-user community. The Lotus Notes application provides users with access to e-mail, calendar, and other databases that reside in a Lotus Domino server environment.

Our audit objective was to evaluate the adequacy of selected security controls for protecting the Lotus Notes and Lotus Domino infrastructure from unauthorized access, modification, destruction, or disclosure. To accomplish our objective, we developed a control assessment methodology based on the security controls identified in the National Institute of Standards and Technology Special Publication 800-53, *Recommended Security Controls for Federal Information Systems*. This document provides a baseline of security controls for organizations to use in protecting their information systems. The controls are divided into 17 "families," such as access control, risk assessment, and personnel security.

Overall, the audit showed that controls were generally well-designed and well-implemented. However, we found opportunities to strengthen information security controls in the control families that we evaluated. For those control families where control objectives were not met, we identified the aspect of the control that was deficient or where improvements could be made, and we

highlighted recommended action. The Director of the Division of Information Technology generally agreed with our recommendations and identified corrective actions that have been taken, are under way, or are planned to enhance the specific controls highlighted in the report. We will follow up on the implementation of the recommendations as part of our future audit activities related to the Board's continuing implementation of FISMA.

ONGOING WORK

Review of the Federal Reserve's Section 13(3) Lending Facilities to Support Overall Market Liquidity

During this reporting period, we issued to Board officials, for review and comment, our draft report on the six lending facilities that the Federal Reserve established to support overall market liquidity. In response to the financial crisis, the Board initiated a number of lending facilities to restore liquidity in the economy and preserve financial and economic stability. The six lending facilities that we reviewed were established pursuant to the Board's authority under section 13(3) of the Federal Reserve Act to authorize Federal Reserve Banks, in unusual and exigent circumstances, to extend credit to individuals, partnerships, and corporations that are unable to obtain adequate credit accommodations from other banking institutions. Under Board authorization, the Federal Reserve Bank of New York managed five of the lending facilities, and the Federal Reserve Bank of Boston managed the sixth. Through their respective facilities, the Federal Reserve Banks of New York and Boston collectively provided loans to depository institutions, bank holding companies, commercial paper issuers, and primary dealers.

We performed an independent review of these six lending facilities to inform the Board, the Congress, and the public regarding the lending facilities' function, status, and risks. The objectives of our review were to (1) obtain information on the various Federal Reserve lending facilities, including their overall function and status, how they operated, the financial markets they were intended to support, the financial utilization of the facilities, the total amount of loans extended, and the current outstanding balances; and (2) identify risks in each facility for the Board's review in exercising its monetary policy function and in its general supervision and oversight of the Federal Reserve Banks. We anticipate issuing our final report early in the next reporting period.

Audit of the Board's Financial Statements for the Year Ending December 31, 2010, and Audit of the Federal Financial Institutions Examination Council's Financial Statements for the Year Ending December 31, 2010

We contract for an independent public accounting firm to annually audit the financial statements of the Board and the FFIEC. (The Board performs the accounting function for the FFIEC.) The accounting firm, currently Deloitte & Touche LLP, performs the audits to obtain reasonable assurance that the financial statements are free of material misstatement. The OIG oversees the activities of the contractor to ensure compliance with generally accepted government auditing standards. The audits include examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. The audits also include an assessment of the accounting principles used and significant estimates made by management, as well as an evaluation of the overall financial statement presentation.

To determine the auditing procedures necessary to express an opinion on the financial statements, the auditors will review the Board's and the FFIEC's internal controls over financial reporting. The auditors will also express an opinion on the effectiveness of the Board's internal controls over financial reporting based on the *Government Auditing Standards* and the Public Company Accounting Oversight Board standards. As part of obtaining reasonable assurance that the financial statements are free of material misstatement, the auditors also will perform tests of the Board's and the FFIEC's compliance with certain provisions of laws and regulations, since noncompliance with these provisions could have a direct and material effect on the determination of the financial statement amounts. The audit reports will be issued in the next reporting period.

Survey of Supervision and Systemic Risk

We began an audit survey of the Board's approach and activities in the areas of supervision and systemic risk in response to the recently enacted Dodd-Frank Act. The Dodd-Frank Act provides for a number of new requirements and responsibilities for the Federal Reserve System, including the Board's membership on the new Financial Stability Oversight Council and the supervision of systemically important financial companies. The objective of this survey is to obtain information on the Board's Division of Banking Supervision and Regulation's activities regarding (1) the supervision of bank holding companies and systemically important financial institutions, and (2) the monitoring of and response to emerging systemic risks in the U.S. financial system in support of the Board's role as a member of the Financial Stability Oversight Council. Based on this survey, we plan to identify specific areas for future audits, as appropriate.

Audit of the Board's Information Security Program

We began an audit of the Board's information security program and practices. This audit was initiated pursuant to FISMA, which requires that each agency IG conduct an annual independent evaluation of the agency's information security program and practices. Our specific audit objectives, based on FISMA's requirements, are to evaluate the effectiveness of security controls and techniques for selected information systems and to evaluate compliance by the Board with FISMA and related information security policies, procedures, standards, and guidelines. In accordance with revised reporting requirements, our FISMA review includes an analysis of the Board's security-related processes in the following areas: certification and accreditation, continuous monitoring, plans of action and milestones, account and identity management, remote access, security configuration management, security training, contractor oversight, contingency planning, and incident response and reporting. We expect to complete this project and issue our final report in the next reporting period.

Security Control Review of the Internet Electronic Submission System

During this period, we issued to management, for review and comment, a draft report on our security control review of the Internet Electronic Submission (IESub) system developed and maintained by the Federal Reserve Bank of New York's Research and Statistics Group. IESub is a major third-party application on the Board's FISMA application inventory under the Division of Monetary Affairs. It provides an interface for the respondents of regulatory and statistical reports to submit their data via the internet. Our objectives are to (1) evaluate the effectiveness of selected security controls and techniques for protecting IESub from unauthorized access, modification, or destruction and (2) ensure compliance with the Board's information security program. We expect to complete this project and issue our final report in the next reporting period.

Security Control Review of the Board's Public Website

We began a security control review of the Board's public website (PubWeb). PubWeb is listed as a major application on the Board's FISMA inventory for the Office of Board Members. As part of the Board's Publications Program, PubWeb provides the public with timely and accurate information about the mission and work of the Board. This information includes materials required by the Federal Reserve Act and other federal legislation. PubWeb also provides information related to the functions of the Federal Reserve System, including financial information such as monetary policy reports, testimony and speeches, economic research and data, reporting forms, and consumer information.

Our objectives are to evaluate the effectiveness of selected security controls and techniques for protecting PubWeb from unauthorized access, modification, or destruction; and to ensure compliance with the Board's information security program. We expect to complete this project and issue our final report in the next reporting period.

Security Control Review of the Visitor Registration System

We began a security control review of the Board's Visitor Registration System. The Visitor Registration System is listed as a major application on the Board's FISMA inventory. The Visitor Registration System allows Board employees to register Board visitors; provides administrative users the ability to manage registered visitors, run reports, and manage access roles; and provides law enforcement officer users the ability to sign visitors in and out, print badges, and manage registered visitors.

Our objectives are to evaluate the effectiveness of selected security controls and techniques for protecting the Visitor Registration System from unauthorized access, modification, or destruction; and to ensure compliance with the Board's information security program. We expect to complete this project and issue our final report in the next reporting period.

Security Control Review of the National Remote Access Services

We began a security control review of the Federal Reserve System's National Remote Access Services (NRAS). The Board and the 12 Federal Reserve Banks use NRAS for remotely accessing Board and Federal Reserve Bank information systems. Our objectives are to evaluate the effectiveness of selected security controls and techniques to ensure the Board maintains a remote access program that complies with FISMA requirements. We expect to complete this project and issue our final report in the next reporting period.

Security Control Review of the FISMA Assets Maintained by the Federal Reserve Bank of Richmond

Pursuant to the requirements of FISMA, we began a security control review of two Lotus Notes applications listed on the Board's FISMA inventory and maintained by the Federal Reserve Bank of Richmond. The two database applications are used by the Federal Reserve Bank of Richmond to support bank examinations. Our objectives are to evaluate the effectiveness of selected security controls and techniques for protecting the two Lotus Notes applications from unauthorized access, modification, or destruction; and to ensure compliance with

the Board's information security program. We expect to complete this review and issue our final report in the next reporting period.

Audit of the Board's Transportation Subsidy Program

We issued to management, for review and comment, a draft report on our audit of the Board's transportation subsidy program. The Board supports federal government initiatives to conserve energy, reduce traffic congestion, and improve air quality in operating a $1.2 million subsidy program for approximately 1,100 Board employees who commute to work using public transportation. We initiated this audit in response to reports of abuse and fraud in the federal transit benefits program at other government agencies. Our objective is to determine the extent to which the Board's transportation subsidy program is properly controlled and administered. We expect to complete this project and issue our final report in the next reporting period.

Multi-disciplinary Work

Inquiry into Allegations of Undue Influence

During this reporting period, our office began an inquiry into allegations of inappropriate political influence on Federal Reserve System officials, resulting in hidden transfers of resources to facilitate crimes during the Watergate scandal in the 1970s and to Iraq for weapon purchases during the 1980s. These allegations were raised at a February 2010 House Committee on Financial Services hearing. Our inquiry was initiated in response to a request from the Chairman of the House Committee on Financial Services, which the Board referred to our office.

Inspections and Evaluations

The Inspections and Evaluations program encompasses OIG inspections, program evaluations, enterprise risk management activities, process design and life-cycle evaluations, and legislatively-mandated reviews of failed financial institutions that the Board supervises. Inspections are generally narrowly focused on a particular issue or topic and provide time-critical analysis that cuts across functions and organizations. In contrast, evaluations are generally focused on a specific program or function and make extensive use of statistical and quantitative analytical techniques. Evaluations can also encompass other preventive activities, such as reviews of system development life-cycle projects and participation on task forces and workgroups. OIG inspections and evaluations are performed according to the *Quality Standards for Inspections* issued by the Council of the Inspectors General on Integrity and Efficiency (CIGIE).

COMPLETED INSPECTION AND EVALUATION WORK

Material Loss Reviews

Section 38(k) of the FDI Act requires that the IG of the appropriate federal banking agency complete a review of the agency's supervision of a failed institution and issue a report within six months of notification from the FDIC IG when the projected loss to the DIF is material. Under section 38(k) of the FDI Act, as amended, a material loss to the DIF is defined as an estimated loss in excess of $200 million. Pursuant to the Dodd-Frank Act, this threshold applies if the loss occurs between January 1, 2010, and December 31, 2011.

The material loss review provisions of section 38(k) require that the IG

- review the institution's supervision, including the agency's implementation of prompt corrective action (PCA);
- ascertain why the institution's problems resulted in a material loss to the DIF; and
- make recommendations for preventing any such loss in the future.

The Dodd-Frank Act also contains specific requirements for bank failures that result in losses below the materiality threshold. In these situations, the IG must review the failure to determine, among other things, whether the loss exhibits unusual circumstances that warrant an in-depth review. In such cases, the IG must prepare a report in a manner that is consistent with the requirements of a material loss review. Pursuant to the Dodd-Frank Act, the IG must semiannually report the dates when each such review and report will be completed. However, if it is determined that a loss did not involve unusual circumstances, the IG is

required to provide an explanation of its determination in the above mentioned semiannual report. The OIG has included its report on nonmaterial loss bank failures in this *Semiannual Report to Congress* (see pages 29 and 30).

During this reporting period, we issued reports on seven failed state member banks where losses to the DIF exceeded the materiality threshold. We also issued one report on a failed state member bank with a loss that did not meet the materiality threshold but that presented unusual circumstances.[1] These banks had total assets of approximately $8.4 billion and total losses estimated at $2 billion, or approximately 24 percent of total assets.

Failed Bank Reviews Completed during the Reporting Period

State Member Bank	Location	Federal Reserve Bank	Asset size (in millions)	Projected Loss (in millions)	Closure Date	FDIC IG Notification Date[a]
Irwin Union Bank and Trust	Columbus, IN	Chicago	$2,700.0	$552.4	09/18/2009	10/29/2009
Warren Bank	Warren, MI	Chicago	$ 530.9	$276.3	10/02/2009	10/29/2009
San Joaquin Bank	Bakersfield, CA	San Francisco	$ 771.8	$ 90.4	10/16/2009	11/12/2009
Bank of Elmwood	Racine, WI	Chicago	$ 339.1	$ 90.6	10/23/2009	11/12/2009
Orion Bank	Naples, FL	Atlanta	$2,700.0	$593.8	11/13/2009	12/14/2009
SolutionsBank	Overland Park, KS	Kansas City	$ 510.1	$119.0	12/11/2009	01/04/2010
Barnes Banking Company	Kaysville, UT	San Francisco	$ 745.5	$266.3	01/15/2010	03/03/2010
Marco Community Bank[b]	Marco Island, FL	Atlanta	$ 126.9	$ 36.9	02/19/2010	N/A

a. Date that our office received notification from the FDIC IG that the projected loss to the DIF would be material.
b. Marco Community Bank did not meet the materiality threshold; however, we determined that the bank's failure presented unusual circumstances warranting an in-depth review.

1. A total of 30 state member banks failed from December 2008 through September 2010. Of those, 17 material loss reviews have been completed by the OIG, 1 in-depth (unusual circumstances) failed bank review has been completed, 1 material loss review is ongoing, 1 in-depth (unusual circumstances) failed bank review is in progress, and 10 failed state member banks did not meet the materiality or unusual circumstances threshold established in the Dodd-Frank Act. The total estimated loss to the DIF for the 30 banks is approximately $4.5 billion.

Material Loss Review of Irwin Union Bank and Trust

Irwin Union Bank and Trust (IUBT) was supervised by the Federal Reserve Bank of Chicago (FRB Chicago), under delegated authority from the Board, and by the Indiana Department of Financial Institutions (State). The State closed IUBT in September 2009, and the FDIC was named receiver. On October 29, 2009, the FDIC IG notified our office that IUBT's failure would result in an estimated loss to the DIF of $552.4 million, or about 20.5 percent of the bank's $2.7 billion in total assets.

IUBT failed because of the convergence of several factors. The Board of Directors and management pursued an aggressive growth strategy between 2000 and 2005 that relied upon high-risk business models. Management also depended on volatile non-core funding sources to support the bank's growth strategy, which emphasized high-risk, high-yielding assets, such as 125 percent combined loan-to-value ratio loans. Meanwhile, management maintained few sources of liquidity support, which further increased IUBT's risk profile. During the 2000 to 2005 growth period, the Board of Directors and management failed to ensure that the bank's key corporate control functions and risk management practices kept pace with the bank's expansion, increasingly complex operations, and escalating risk profile. The Board of Directors' and management's aggressive growth strategy resulted in IUBT's total assets almost tripling between 2000 and 2005. However, for five consecutive years (2004 through 2008), the bank's net income decreased.

In 2007, reduced secondary market demand for mortgages hampered, and eventually eliminated, an IUBT subsidiary's ability to sell its loans. As a result, the subsidiary was forced to hold the loans that it had originated to sell (including 125 percent combined loan-to-value ratio loans) in a declining real estate environment, which exposed IUBT to significant asset quality deterioration. In addition, IUBT's exposure to real estate market declines was compounded by a significant concentration in commercial real estate (CRE) loans. As the value of IUBT's assets continued to deteriorate, its Board of Directors and management adopted a strategy of selling more profitable business lines and branch offices to preserve the bank's capital. However, IUBT's remaining assets continued to deteriorate and deplete capital, which raised concerns about the bank's viability and eventually resulted in IUBT losing access to key funding sources. On September 18, 2009, the State closed IUBT because of the imminent danger of a liquidity shortfall and appointed the FDIC as receiver.

Our analysis of FRB Chicago's supervision of IUBT indicated that examiners identified key weaknesses in 2002 and 2003 regarding corporate governance, risk management systems, and internal controls, but missed multiple subsequent opportunities to take more forceful supervisory action. The fundamental risk management weaknesses, corporate governance issues, and key compliance deficiencies raised by FRB Chicago during examinations in 2002 and 2003 were early warning signs regarding IUBT's Board of Directors' and management's

capability to effectively manage a geographically dispersed, large, and complex banking organization. Based on the 2002 and 2003 examination findings, FRB Chicago issued two informal enforcement actions. In 2003 and 2004, IUBT was unable to fully resolve the issues noted in the informal enforcement actions, and unresolved issues noted during the continuous supervision process began to accumulate. We believe that FRB Chicago had multiple opportunities between 2002 and 2009 to take additional and stronger supervisory actions.

For example, we believe that the fundamental corporate governance issues and comprehensive liquidity risk management weaknesses noted during the January 2002 examination provided an early warning sign that management was not effectively managing the risks associated with adding a new bank subsidiary engaged in high loan-to-value lending. In our opinion, the examination findings warranted a stronger supervisory action, including an additional downgrade of the management CAMELS component rating to reflect that management was less than satisfactory.[2] We also believe that FRB Chicago should have considered requesting that management refrain from additional growth or corporate restructurings affecting IUBT until the bank fully addressed the fundamental flaws noted during this examination. We believe that strong supervisory action would have alerted management to the urgent need to address these weaknesses before pursuing further changes or additional growth in the lines of business.

A 2005 full scope examination cited that management's failure to enhance its market risk management capabilities contributed to a decrease in the bank's annual earnings and, in our opinion, warranted a stronger supervisory response. During the 2005 examination, FRB Chicago also noted new and recurring violations of laws and regulations in the bank's mortgage lending business lines, which we believe warranted a stronger enforcement action. In addition, a 2006 full scope examination once again revealed IUBT's difficulties in resolving items contained in informal enforcement actions and raised by the continuous supervision process. We believe that IUBT's inability to fully resolve, in a complete and timely manner, prior informal supervisory actions and issues noted during the continuous supervision process warranted an earlier formal enforcement action.

In late 2007, when economic conditions caused a liquidity disruption that reduced the bank's access to the funding necessary to operate its home equity lending business, FRB Chicago reiterated the risk associated with IUBT's dependence on uninterrupted liquidity in the secondary markets as a significant issue. Examiners raised the same concern almost five years earlier in a 2003 examination report, but did not hold the Board of Directors and management accountable for addressing that risk in the intervening years. We believe that an earlier and stronger supervisory action, such as a liquidity component ratings downgrade or a

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2. The CAMELS acronym represents six components: **C**apital adequacy, **A**sset quality, **M**anagement practices, **E**arnings performance, **L**iquidity position, and **S**ensitivity to market risk. Each component and overall composite score is assigned a rating of 1 through 5, with 1 having the least regulatory concern.

formal enforcement action related to liquidity risk management, might have addressed this fundamental liquidity planning weakness.

IUBT's failure offered valuable lessons learned. Specifically, IUBT's failure illustrated the importance of supervisors

- confirming effective Board of Directors and management oversight before a bank makes key strategic and operational changes, such as adding new, high-risk business lines;
- ensuring that a bank's risk management practices and internal control processes keep pace with the institution's growth, increasingly complex operations, and heightened risk profile;
- focusing on the key risks within each business line and ensuring that the Board of Directors and management comprehend, manage, and mitigate those risks;
- assigning CAMELS composite and component ratings consistent with the significance of comments raised in the narrative sections of examination reports to ensure that management understands the urgency of implementing the required corrective action measures; and
- assuring that examination reports are forward looking and anticipate potential risk issues that management should address, in addition to raising concerns and observations based on events that have already occurred.

The Director of the Board's Division of Banking Supervision and Regulation concurred with our conclusions and lessons learned.

Material Loss Review of Warren Bank

Warren Bank was supervised by FRB Chicago, under delegated authority from the Board, and by the Michigan Office of Financial and Insurance Regulation (State). The State closed Warren Bank on October 2, 2009, and the FDIC was named receiver. On October 29, 2009, the FDIC IG notified our office that Warren Bank's failure would result in an estimated loss to the DIF of $276.3 million, or 52 percent of the bank's $530.9 million in total assets.

Warren Bank failed because its Board of Directors and management did not adequately manage loan portfolio risks as regional economic conditions began a protracted decline. Management placed a high reliance on (1) the bank's familiarity with borrowers and (2) the collateral pledged to secure loans. Warren Bank's Board of Directors and management were overly optimistic about the

bank's ability to withstand the economic downturn and did not adequately mitigate the risks associated with a loan portfolio that was highly concentrated in CRE. In some instances, management renewed and extended loans and advanced additional funds to existing customers, apparently in the hope that market conditions would improve. However, management did not properly analyze the value of the underlying collateral and the borrowers' creditworthiness. The bank's asset quality deteriorated as underlying collateral values declined and loan defaults increased. The resulting losses eliminated earnings and depleted capital, which ultimately led to Warren Bank's failure.

With respect to supervision, our analysis revealed that examiners repeatedly criticized the bank's loan grading practices and allowance for loan and lease losses (ALLL) methodology. Despite recurring supervisory comments and findings, improvements made by bank management were insufficient to ensure that the bank's credit risk management practices were commensurate with its risk profile. Examiners also cited recurring concerns regarding Warren Bank's capital position. In 2003, examiners suggested that management maintain capital well above the PCA minimums due to the bank's high risk profile. Management was encouraged to set capital levels above its industry peer group. Similar concerns were expressed in subsequent examination reports; however, Warren Bank's year-end risk weighted capital levels never exceeded its peers.

Examiners did not issue an enforcement action compelling the bank to rectify recurring regulatory concerns regarding loan grading, the ALLL, and capital levels until September 2008. In our opinion, recurrent examination comments and findings warranted an enforcement action as early as 2006. In addition, we believe that an earlier supervisory action requiring the bank to maintain a higher capital threshold commensurate with its high risk profile could have reduced the cost of the failure to the DIF.

Warren Bank's failure offered a lesson learned that can be applied when supervising banks with similar characteristics and circumstances. Specifically, Warren Bank's failure illustrated the importance of an early and forceful response to recurring supervisory concerns, particularly when examiners determine that capital levels are not commensurate with an institution's overall risk profile.

The Director of the Board's Division of Banking Supervision and Regulation agreed with our conclusion and concurred with the lesson learned.

Material Loss Review of San Joaquin Bank

San Joaquin Bank (San Joaquin) was supervised by the Federal Reserve Bank of San Francisco (FRB San Francisco), under delegated authority from the Board, and by the California Department of Financial Institutions (State). The State closed San Joaquin on October 16, 2009, and the FDIC was named receiver. On

November 12, 2009, the FDIC IG notified our office that San Joaquin's failure would result in an estimated loss to the DIF of $90.4 million, or 11.7 percent of the bank's $771.8 million in total assets.

San Joaquin failed because its Board of Directors and management did not effectively control the risks associated with the bank's rapid loan growth that led to a high concentration in CRE loans and, in particular, construction, land, and land development (CLD) loans tied to the Bakersfield, California, real estate market. The loan growth and high concentrations occurred when the Bakersfield real estate market was experiencing significant price appreciation. A decline in the local real estate market, coupled with the bank's failure to effectively manage the increased credit risk associated with San Joaquin's highly concentrated loan portfolio, resulted in deteriorating asset quality and significant losses. Mounting losses impaired earnings, eroded capital, and strained the bank's liquidity. Efforts to meet a regulatory deadline requiring San Joaquin to be acquired by or merge with another financial institution were unsuccessful, and the State closed the bank and appointed the FDIC as receiver.

With respect to the bank's supervision, we believe that an April 2007 examination performed by FRB San Francisco provided an opportunity for stronger supervisory action. Examiners noted that San Joaquin's CRE loan concentration ranked among the highest for state member banks supervised by FRB San Francisco. Examiners also cited management's plan for additional loan growth, despite signs of a slowing real estate market. In our opinion, these circumstances offered an early opportunity for FRB San Francisco to encourage management to mitigate the risk of asset quality deterioration from further market declines.

Further, we believe that the significance of the issues raised during a 2008 State examination warranted a timely enforcement action compelling management to mitigate credit risk management weaknesses and the risks associated with the declining real estate market. The State examination report issued in July 2008 noted that San Joaquin's financial condition had become less than satisfactory. Examiners noted that actual asset growth for 2007 was 16 percent, or double management's projection. In addition, the bank's level of construction, residential, and lot development loans had increased notably, yet the sharp decline in the Bakersfield real estate market had not been analyzed by management.

According to examiners, despite declining collateral values, San Joaquin continued to grant credit extensions without obtaining updated appraisals or reevaluating borrowers' creditworthiness. Examiners also questioned whether earnings would remain positive and continue to augment capital. An informal enforcement action in the form of a Memorandum of Understanding developed jointly with the State was issued in December 2008, approximately five months after the State's examination report was issued. While we believe that a stronger supervisory action in 2007 and a more timely enforcement action in 2008 were

warranted, it is not possible to determine the degree to which any such actions would have affected the bank's subsequent decline or the failure's cost to the DIF.

We believe that San Joaquin's failure pointed to a valuable lesson learned that can be applied when supervising community banks with similar characteristics. In our opinion, San Joaquin's failure illustrated that banks with exceptionally high CRE and CLD loan concentrations require a swift and forceful supervisory response when signs of market deterioration first become evident.

The Director of the Board's Division of Banking Supervision and Regulation concurred with our conclusion and lesson learned.

Material Loss Review of Bank of Elmwood

The Bank of Elmwood (Elmwood) was supervised by FRB Chicago, under delegated authority from the Board, and by the State of Wisconsin Department of Financial Institutions Division of Banking (State). The State closed Elmwood on October 23, 2009, and the FDIC was named receiver. On November 12, 2009, the FDIC IG notified our office that Elmwood's failure would result in an estimated loss to the DIF of $90.6 million, or about 26.7 percent of the bank's approximately $339.1 million in total assets.

Elmwood failed because its Board of Directors and management pursued a risky loan growth strategy that featured new loan products and out-of-market lending without developing adequate credit risk management controls. The growth strategy, coupled with insufficient credit risk management controls, resulted in poorly underwritten loans. Bank management's inability to adequately address loan portfolio weaknesses led to asset quality deterioration and significant losses. Mounting losses eliminated earnings, depleted capital, and strained liquidity, which ultimately led to the State closing Elmwood.

Our analysis of FRB Chicago's supervision of Elmwood revealed that FRB Chicago had opportunities for earlier and more forceful supervisory actions. Elmwood's loan strategy was first discussed in a 2004 State examination report that also noted that the bank's earnings performance "continued to be deficient" and capital ratios remained below peer bank averages. State examiners noted that Elmwood should control further loan growth until the bank demonstrated that it could produce "sufficient retention of earnings to provide the bank with adequate internal capital generation." In its 2005 examination report, FRB Chicago observed that the bank increased its loan portfolio by about 30 percent over the previous two years by strategically expanding into new geographical markets and purchasing CRE loan participations to enhance income. However, examiners once again cited weak earnings and capital levels that remained below peer averages.

We also believe that credit risk management weaknesses noted by examiners in 2006 and 2007 provided early warning signs regarding (1) the potential for asset quality deterioration in Elmwood's growing loan portfolio, and (2) management's ability to control the bank's increasing credit risk profile. The examination reports issued during this period highlighted credit administration deficiencies, such as inadequate monitoring of out-of-market CRE participation loans, incomplete financial data on borrowers and projects, and weak loan underwriting standards. Examiners warned that credit administration deficiencies could make it difficult for management to detect and promptly correct credit problems. Additionally, the 2007 examination report noted a significant increase in classified assets and a corresponding rise in past due and non-accrual loans, yet the bank received a "fair" rating for its asset quality. In our opinion, the weaknesses cited by examiners, coupled with continued marginal earnings and capital levels below peer averages, warranted an appropriate supervisory response in 2007 compelling bank management to immediately correct the identified deficiencies.

While we believe that FRB Chicago had opportunities for earlier and more forceful supervisory actions, it was not possible for us to predict the effectiveness or impact of any corrective measures that might have been taken by the bank. Therefore, we could not evaluate the degree to which an earlier or alternative supervisory response would have affected Elmwood's financial deterioration or the ultimate cost to the DIF.

With respect to lessons learned, Elmwood's failure illustrated the risks posed when a bank with modest earnings and capital levels below peer averages implements a risky loan growth strategy that features new product lines or out-of-market lending. In these situations, examiners should ensure that management has implemented a robust credit risk management infrastructure and is effectively addressing shortcomings in the bank's earnings and capital. Elmwood's failure also demonstrated that banks exhibiting significant growth require heightened supervisory attention and should be subject to an immediate and forceful supervisory response when signs of credit risk management deficiencies first appear.

The Director of the Board's Division of Banking Supervision and Regulation agreed with our conclusion and lessons learned.

Material Loss Review of Orion Bank

Orion Bank (Orion) was supervised by the Federal Reserve Bank of Atlanta (FRB Atlanta), under delegated authority from the Board, and by the Florida Office of Financial Regulation (State). The State closed Orion on November 13, 2009, and

named the FDIC as receiver.[3] On December 14, 2009, the FDIC IG advised our office that the bank's failure would result in an estimated loss to the DIF of $593.8 million, or 22 percent of the bank's $2.7 billion in total assets.

Orion failed because its Board of Directors and management did not control the risks associated with rapid growth and an extremely high concentration in CRE and, in particular, acquisition, development, and construction (ADC) loans. Under the direction of the Chief Executive Officer (CEO), who had a dominant role in the bank and held a controlling interest in the parent bank holding company, Orion aggressively expanded its CRE and ADC loan portfolios in the south Florida market from 2004 through 2006. A subsequent rapid decline in the Florida real estate market led to deteriorating asset quality and significant losses, particularly in the ADC portfolio. Bank management failed to acknowledge the extent of the real estate market downturn and was slow in recognizing and mitigating credit risk exposure. Mounting loan losses eliminated the bank's earnings, depleted capital, and ultimately led the State to close Orion.

Our analysis of FRB Atlanta's supervision of Orion revealed that a State examination report issued in March 2007 identified a notable change in the bank's risk profile resulting from a deteriorating real estate market and newly identified weaknesses in credit risk management and Board of Directors oversight. We believe the findings included in the State examination report should have signaled to FRB Atlanta that additional, timely supervisory attention was warranted earlier in 2007, instead of waiting until December 2007 to begin on-site examination work.

The State's March 2007 examination report revealed that the real estate market in Orion's service areas had deteriorated; however, the bank's CRE and ADC loan concentrations continued to increase. In addition, examiners noted that a $533 million, or 70 percent, increase in CRE loans registered during the 12-month period ending March 31, 2006, and a $406 million, or 84 percent, increase in ADC loans registered during the same period exposed the bank to "greater credit risk." In contrast to the generally favorable assessment cited in a March 2006 FRB Atlanta examination report, State examiners described Orion's loan review program as ineffective and noted that the bank's internal loan grading did not identify certain problem loans. Examiners warned that "the untimely identification of loan problems could expose the bank to additional credit losses." The State examination report also raised concerns that "appraisals made at the height of the real estate market in 2004 and 2005 may not represent the realistic

3. On November 9, 2009, the Federal Reserve Board issued an enforcement action that included a provision ordering the removal of Orion's Chief Executive Officer, who also served as the bank President and the Chairman of the Board of Directors. The enforcement action stated that, in the July 2009 timeframe, the bank's Chief Executive Officer made false statements to the Federal Reserve and, among other things, permitted the bank to make loans that (1) exceeded and, therefore, violated the Florida legal lending limit statute; (2) had inadequate analysis of the borrower's creditworthiness or capacity for repayment; and (3) were structured in a manner to make it appear that Orion was reducing its level of classified assets. The enforcement action also indicated that the Chief Executive Officer had knowledge that these loans were used to acquire Orion's common and preferred stock and to purchase low quality assets from the bank. We provided our report to the OIG's Investigations section for further review and analysis.

fair value of the collateral today," and that Orion's ALLL methodology should be reconsidered in light of the residential real estate market slowdown and the bank's concentration in CRE loans. In addition, contrary to the positive opinion expressed in FRB Atlanta's 2006 examination report, State examiners commented that Orion's Board of Directors seemed to offer little direction or supervision and that the CEO appeared to view the Board of Directors as a hindrance more than anything else.

While we believe that the circumstances presented in the March 2007 State examination report provided an opportunity for an earlier supervisory response in 2007, given the rapid decline in the real estate markets served by Orion, it was not possible to determine whether earlier supervisory attention would have affected Orion's subsequent decline or the failure's cost to the DIF.

We believe that Orion's failure offered a valuable lesson learned that could be applied when supervising banks with similar characteristics and circumstances. In our opinion, Orion's failure illustrated that financial institutions with a dominant CEO, a weak Board of Directors, and extremely high concentrations in risky assets such as CRE and ADC loans require (1) heightened supervisory attention even when financial performance is strong, and (2) an immediate and forceful supervisory response when signs of market deterioration or weaknesses in credit risk management first become apparent.

The Director of the Board's Division of Banking Supervision and Regulation agreed with our conclusion and lesson learned.

Material Loss Review of SolutionsBank

SolutionsBank (Solutions) was supervised by the Federal Reserve Bank of Kansas City (FRB Kansas City), under delegated authority from the Board, and by the Office of the State Bank Commissioner of Kansas (State). The State closed Solutions in December 2009, and the FDIC was named receiver. On January 4, 2010, the FDIC IG notified our office that Solutions' failure would result in an estimated loss to the DIF of $119.0 million, or 23.3 percent of the bank's $510.1 million in total assets.

Solutions failed because its Board of Directors and management did not control the risks associated with an aggressive growth strategy, funded by non-core deposit sources, that expanded the scope of the bank's traditional activities. This strategy resulted in the bank developing significant CRE and CLD lending concentrations that made the bank particularly vulnerable to real estate market declines. As real estate markets served by the bank weakened, asset quality deterioration strained earnings and depleted capital.

Our analysis of FRB Kansas City's supervision of Solutions revealed that examiners had opportunities in early 2008 for an earlier and more forceful supervisory action given the bank's aggressive growth strategy. In a January 2008 examination report, FRB Kansas City noted softening in the nationwide real estate market and that the bank's loan portfolio included a large concentration of CRE and CLD loans. Examiners also observed that the bank's already below peer capital levels had declined and that the bank increased its reliance on non-core funding sources. In our opinion, these findings presented an opportunity to question the advisability of management continuing its aggressive growth strategy, but FRB Kansas City only required the bank to develop a more robust capital plan and enhance CRE risk management processes. The case for a stronger supervisory response in the early 2008 timeframe is supported by a January 2009 examination report, which concluded that management's decision to execute an aggressive growth strategy without the support of adequate capital resulted in the bank's unsatisfactory financial condition.

While we believe that FRB Kansas City had an opportunity for an earlier and more forceful supervisory action, it was not possible for us to predict the effectiveness or impact of any corrective measures. Therefore, we could not evaluate the degree to which an earlier or more forceful supervisory response might have affected Solutions' financial deterioration or the failure's ultimate cost to the DIF.

We believe that Solutions' failure offered lessons learned that can be applied to supervising banks with similar characteristics and circumstances. First, a community bank with large CRE and CLD loans relative to its total assets is particularly vulnerable to real estate market declines. Second, the failure underscored the risk of pursuing a new business strategy that features growth in high-risk lending outside of an institution's traditional market area. Finally, we believe the failure demonstrated that examiners should assess capital needs based on an institution's strategy and growth targets in addition to the quantitative regulatory capital levels established by PCA.

The Director of the Board's Division of Banking Supervision and Regulation concurred with our conclusion and lessons learned.

Material Loss Review of Barnes Banking Company

Barnes Banking Company (Barnes) was supervised by FRB San Francisco under delegated authority from the Board, and by the Utah Department of Financial Institutions (State). The State closed Barnes in January 2010, and the FDIC was appointed receiver. On March 3, 2010, the FDIC IG notified our office that Barnes' failure would result in an estimated loss to the DIF of $266.3 million, or 35.7 percent of the bank's $745.5 million in total assets.

Barnes failed because its Board of Directors and management did not effectively control the risks associated with the bank's aggressive growth strategy that led to a CRE loan concentration, particularly in residential CLD loans. The bank continued to originate CLD loans in 2007 and 2008, despite apparent weaknesses in Utah's real estate market and economy. The Board of Directors' and management's failure to effectively manage the resulting credit risk, in conjunction with declining market conditions, led to rapid asset quality deterioration. The resulting loan losses depleted earnings and eroded capital, which ultimately led the State to close Barnes.

With respect to supervision, we believe that circumstances noted during a 2007 full scope examination—including repeated regulatory criticisms, declining market trends, and continuing growth of Barnes' CLD loan portfolio—provided FRB San Francisco an opportunity to pursue earlier, more forceful supervisory action. The examination cited several deficiencies regarding credit risk management, CRE concentrations monitoring, ALLL methodology, and other critically important control processes. Additionally, examiners expressed concern over (1) Barnes' aggressive growth in CRE lending despite evidence of pronounced economic weaknesses within that market segment, and (2) "continued inaction" by the bank to resolve prior recommendations. We believe that other supervisory actions were warranted at the conclusion of the 2007 examination, such as downgrading CAMELS ratings or executing an informal enforcement action.

We also believe that a June 2008 credit risk target examination provided another opportunity to pursue earlier, more forceful supervisory action. The target examination provided strong evidence that Barnes' risk profile and financial condition had significantly changed, and examiners repeated prior criticisms. While FRB San Francisco subsequently performed a separate ratings assessment and downgraded several CAMELS ratings, an enforcement action was not executed until May 2009, nearly one year after the target examination was initiated. Further, although not explicitly required by supervisory guidance, examiners decided not to attend a full Board of Directors meeting following the target examination or assessment. Given the history of repeated recommendations, continued market deterioration, and additional growth of the bank's CLD loan portfolio, FRB San Francisco could have taken such actions as (1) conducting a formal exit meeting with the Board of Directors, (2) considering more aggressive ratings downgrades, or (3) executing an enforcement action.

While we believe that FRB San Francisco had opportunities for earlier and more forceful supervisory actions, it was not possible for us to predict the effectiveness or impact of any such actions. Therefore, we could not evaluate the degree to which earlier or more forceful supervisory responses might have affected Barnes' financial deterioration or the failure's cost to the DIF.

Barnes' failure offered valuable lessons learned because it illustrated (1) the need for close regulatory scrutiny and a forceful supervisory response when financial institutions increase credit risk exposure within a weakened or deteriorating market segment; and (2) although not explicitly required by supervisory guidance, examiner attendance at a Board of Directors meeting can be a prudent supervisory practice when a target examination notes a significant change in the institution's financial condition and risk profile.

The Director of the Board's Division of Banking Supervision and Regulation agreed with our conclusion and concurred with the lessons learned.

Review of the Failure of Marco Community Bank

Marco Community Bank (Marco) was a de novo bank supervised by FRB Atlanta, under delegated authority from the Board, and by the Florida Office of Financial Regulation (State). The State closed Marco on February 19, 2010, and named the FDIC as receiver. The FDIC IG estimated that Marco's failure would result in a $36.9 million loss to the DIF, or 29.1 percent of the bank's $126.9 million in total assets. While the loss did not exceed the materiality threshold established in the Dodd-Frank Act, we conducted an in-depth review after determining that Marco's failure presented unusual circumstances because (1) during its second year of operations, tier 1 capital dipped beneath the minimum required by regulatory guidance, and (2) the bank relied heavily on its holding company to augment the bank's capital throughout Marco's limited history.

Marco failed because its Board of Directors and management did not provide adequate oversight of the bank's lending activities. Following its inception, the bank operated with a weak internal control environment due, in part, to frequent management turnover, vacancies in key positions, and inadequate staff expertise. The bank grew more quickly than management anticipated in its business plan and relied on capital injections from its holding company to sustain operations. The growth resulted in Marco developing high concentrations in (1) the CLD component of the bank's CRE loan portfolio, and (2) home equity lines of credit. Also, in 2006 and 2007, the bank executed management's strategic decision to supplement its declining loan production by purchasing a pool of short-term acquisition and renovation loans on properties primarily located in two counties in Florida. These loan pools created an additional concentration risk for Marco. As the real estate market in Marco Island weakened, the bank's asset quality deteriorated significantly and resulted in large provision expenses that eliminated earnings and depleted capital.

Our analysis of FRB Atlanta's supervision of Marco revealed that FRB Atlanta did not fully comply with the Board's supervisory standards for de novo banks. Specifically, FRB Atlanta did not comply with examination frequency guidelines

and put Marco on a standard examination cycle despite noting issues that should have raised concerns about the bank's ability to operate on a sound basis—a consideration when determining if a de novo bank should be transitioned to a standard examination frequency cycle.

We believe that FRB Atlanta should not have transitioned Marco to the standard examination cycle after FRB Atlanta and the State had only conducted two full scope examinations. In hindsight, we believe that many of the issues noted during these first two examinations foreshadowed the bank's future problems. Nevertheless, it was not possible to determine the degree to which strict adherence to the supervisory guidelines for de novo banks may have altered the course of the bank's financial decline or affected the failure's cost to the DIF.

We believe that Marco's failure pointed to valuable lessons learned that can be applied when supervising de novo banks with similar characteristics. First, Marco's failure underscored that de novo banks require close supervision and that examiners should only implement the standard examination cycle when—consistent with regulatory guidance—the bank's corporate governance, financial condition, and internal controls warrant the transition. Second, this failure highlighted the importance of examiners closely monitoring a de novo bank's performance when, as was the case with Marco, there are significant deviations from the business plan submitted as part of the application to become a state member bank.

The Director of the Board's Division of Banking Supervision and Regulation concurred with our conclusion and lessons learned.

ONGOING INSPECTION AND EVALUATION WORK

Failed Bank Reviews

With the enactment of the Dodd-Frank Act, the OIG is required to review failed banks where the losses to the DIF are above the materiality threshold or are below the threshold but exhibit unusual circumstances warranting an in-depth review. Pursuant to the Dodd-Frank Act, a $200 million threshold applies for losses that occur between January 1, 2010, and December 31, 2011. As discussed below, we are currently conducting two failed bank reviews. These banks had total assets of approximately $3.7 billion and total losses estimated at $222 million, or approximately 6 percent of total assets.

Independent Bankers' Bank

On December 18, 2009, Independent Bankers' Bank (IBB), Springfield, Illinois, was closed by the Illinois Department of Financial and Professional Regulation.

At closure, the FDIC reported that IBB had $585.5 million in total assets as of September 30, 2009. In January 2010, the FDIC informed us that the cost of the failure was estimated to be $20.8 million, which did not meet the materiality threshold as defined under Section 38(k) of the FDI Act. However, as is discussed in more detail in the next section (see page 29), under the Dodd-Frank Act, the IG of each federal banking agency is required to review all losses to the DIF that occurred after October 1, 2009, and determine if unusual circumstances existed. We have determined that IBB's business model presents unusual circumstances related to payment systems risks and, therefore, have begun an in-depth review. We expect to issue our report in the next reporting period.

Midwest Bank and Trust Company

On May 14, 2010, Midwest Bank and Trust Company (Midwest), Elmwood Park, Illinois, was closed by the Illinois Department of Financial and Professional Regulation. At the time of closure, Midwest had approximately $3.1 billion in total assets. On June 8, 2010, the FDIC IG notified our office that the FDIC had estimated a $200.7 million loss to the DIF, which exceeds the statutory threshold requiring us to conduct a material loss review.

Analysis of Lessons Learned from OIG Bank Failure Reviews

We have begun a cross-cutting review of lessons learned from our cumulative body of bank failure reviews. Our work is focused on identifying (1) emerging themes related to the cause of state member bank failures and Federal Reserve supervision of these institutions, and (2) potential recommendations for improvements in bank supervisory policies and practices. We plan to complete our analysis and issue a report during the next reporting period.

Information on Nonmaterial Losses to the Deposit Insurance Fund, as Required by the Dodd-Frank Act

The Dodd-Frank Act requires the IG of the appropriate Federal banking agency to report, on a semiannual basis, certain information on financial institutions that incurred nonmaterial losses to the DIF and that failed during the respective six-month period.[4] However, for this first report since the enactment of the Dodd-Frank Act, the reporting period is October 1, 2009, through September 30, 2010. As shown in the table on the next page, 12 failed state member banks had losses to the DIF that did not meet the materiality threshold. Cumulatively, these institutions had total assets of approximately $3.8 billion and losses estimated at $626 million, or 16.6 percent of total assets.

Pursuant to the Dodd-Frank Act, the IG is required to determine (1) the grounds identified by the State for appointing the FDIC as receiver, and (2) whether losses to the DIF presented unusual circumstances that would warrant an in-depth review. If no unusual circumstances are identified, the IG is required to provide an explanation of its determination.

We reviewed each of the 12 state member bank failures to determine if the resulting loss to the DIF exhibited unusual circumstances that would warrant an in-depth review. We considered a loss to the DIF to present unusual circumstances if the conditions associated with the bank's deterioration, ultimate closure, and supervision were not addressed in any of our prior bank failure reports or involved potential fraudulent activity. To make this determination, we analyzed key data from the five-year period preceding the bank's closure. This data generally comprised Federal Reserve Bank and State examination schedules; Reports of Examination, including CAMELS ratings and financial data; informal and formal enforcement actions and other supervisory activities, such as visitations; and PCA determinations. As shown in the table on the next page, we determined that losses to the DIF for two state member banks exhibited unusual circumstances warranting an in-depth review. We did not find unusual circumstances in the remaining institutions.

4. In accordance with the Dodd-Frank Act, a loss to the DIF that occurs between January 1, 2010, and December 31, 2011, is material if it exceeds $200 million. The Dodd-Frank Act changed the long-standing material loss threshold of the FDI Act, which had been defined as the greater of $25 million or 2 percent of the bank's total assets.

Nonmaterial State Member Bank Failures, October 1, 2009, through September 30, 2010

State Member Bank	Location	Asset size (millions)	Projected Loss (millions)	Closure Date	OIG Summary of State's Grounds for Receivership	OIG Determination
Independent Bankers' Bank	Springfield, IL	$ 585.5	$ 20.8	12/18/2009	Operating in an unsafe and unsound manner	Unusual circumstances identified; report to be issued by 03/31/2011 (see page 27)
Marco Community Bank	Marco Island, FL	$ 126.9	$ 36.9	02/19/2010	Imminent insolvency	Unusual circumstances identified; report issued on 09/30/2010 (see page 26)
Bank of Illinois	Normal, IL	$ 205.3	$ 53.7	03/05/2010	Capital impaired, unsound condition, operating in an unsafe and unsound manner	No unusual circumstances noted
Sun American Bank	Boca Raton, FL	$ 543.6	$103.0	03/05/2010	Imminent insolvency	No unusual circumstances noted
Old Southern Bank	Orlando, FL	$ 351.0	$ 90.5	03/12/2010	Imminent insolvency	No unusual circumstances noted
1st Pacific Bank	San Diego, CA	$ 327.3	$ 75.1	05/07/2010	No reasonable prospect for rehabilitation	No unusual circumstances noted
Metro Bank of Dade County	Miami, FL	$ 442.3	$ 67.6	07/16/2010	Insolvency due to losses from operations	No unusual circumstances noted
Home Valley Bank	Cave Junction, OR	$ 251.8	$ 37.1	07/23/2010	Insolvency due to excessive non-performing assets	No unusual circumstances noted
Sterling Bank	Lantana, FL	$ 407.9	$ 45.5	07/23/2010	Insolvent; no prospect for replacement capital	No unusual circumstances noted
Thunder Bank	Sylvan Grove, KS	$ 32.6	$ 4.5	07/23/2010	Capital to total assets equal to or less than 2 percent	No unusual circumstances noted
Pacific State Bank	Stockton, CA	$ 312.1	$ 32.6	08/20/2010	No reasonable prospect for rehabilitation	No unusual circumstances noted
Horizon Bank	Bradenton, FL	$ 187.8	$ 58.9	09/10/2010	Imminent insolvency	No unusual circumstances noted

Investigations

The Investigations program conducts criminal, civil, and administrative investigations of the Board's programs and operations. OIG investigations are conducted in compliance with the CIGIE's *Quality Standards for Investigations*.

In June 2010, the U.S. Attorney General granted statutory law enforcement authority to the Board OIG, which vested our special agents with the authority to carry firearms, make arrests without a warrant, seek and execute search and arrest warrants, and seize evidence. Previously, OIG special agents relied on a blanket special deputation arrangement with the U.S. Marshals Service for their law enforcement authority. The Attorney General's authorization is an indicator of the important function our special agents play in the investigation of complex criminal matters that may affect Board-related programs and operations. This authority bolsters the OIG's ability to engage in joint task force and other criminal investigations involving matters such as bank fraud, mortgage fraud, money laundering, and other financially-related crimes impacting federally regulated financial institutions.

ONGOING INVESTIGATIVE ACTIVITIES

Our criminal investigative activities involve leading or participating in a number of multi-agency investigations. OIG special agents conduct investigations of alleged criminal or otherwise prohibited activities relating to the Board's programs and operations. During this reporting period, we opened six new investigations and closed one investigation. Due to the sensitivity of these investigations, we only report on activities that have resulted in criminal, civil, or administrative action. The following are highlights of our significant investigative activity over the last six months.

Board Employee Entered Guilty Plea for Stealing and Distributing Board Cell Phones

As noted in our last semiannual report, in late 2007 the OIG initiated an investigation into the alleged theft of government cell phones. The investigation determined that at least 26 cell phones were missing and that the Board incurred associated charges in excess of $215,000, primarily due to international calls to Jamaica, Brazil, Costa Rica, and the United Kingdom. A Board employee was indicted in October 2009 for selling at least 10 cell phones, some for as much as $250 each. Other phones were allegedly traded for services, such as discounts for hairstyling services. The employee was charged with theft of government property, trafficking in unauthorized access devices, and tampering with witness testimony.

During the current reporting period, the Board employee pleaded guilty to one count of theft of government property. She is scheduled to be sentenced in

December 2010 and faces up to one year in prison under federal sentencing guidelines. According to the government's evidence, the employee stole at least seven cell phones and told recipients of the phones that the phones came with unlimited calling plans. The recipients proceeded to incur approximately $60,000 in cell phone charges that were billed to the Board.

California Woman Sentenced to Eight Years in Prison for False Personation of a Federal Reserve Official in an Advance Fee Scam

In June 2010, a California woman was sentenced to 96 months in federal prison for participating in an advance fee scheme that collected approximately $3.8 million from victims who were falsely promised low-interest, multi-million dollar loans from the "Federal Reserve Bank." As part of the sentence, the subject was ordered to pay approximately $3.8 million in restitution, which represented losses to victims resulting from the fraudulent scheme. In addition, the government seized appropriately $1 million from the subject's bank accounts that will be used to help repay the victims.

As we indicated in our last semiannual report, the OIG initiated its investigation into this matter in late 2008. This investigation was conducted jointly with the Federal Bureau of Investigation, U.S. Immigration and Customs Enforcement, the U.S. Postal Inspection Service, and the Los Angeles Police Department.

The subject held herself out as an employee of the Federal Reserve Bank and fraudulently promised 30-year business loans at a fixed rate of 2.3 percent to her victims. The subject maintained that she was a loan consultant and that she could secure the loans without any standard documentation because she worked directly with the head underwriter of the Federal Reserve Bank. As part of the loan scheme, the subject induced victims to make up-front cash payments, which were generally about 5 percent of the loan amount. None of the victims received a loan or saw the return of their advance payments.

In January 2010, the subject pleaded guilty to a criminal information charging wire fraud, money laundering, false personation of an employee of a Federal Reserve Bank, and causing an act to be done.

Individual Pleaded Guilty to Trafficking in Counterfeit Goods

During this reporting period, an individual pleaded guilty to one count of trafficking in counterfeit goods and is awaiting sentencing. As was previously reported, the OIG initiated its investigation based on a request for assistance from the U.S. Postal Inspection Service concerning alleged money laundering and structured deposits by two subjects. The investigation determined that, over a one-year period, the subjects deposited approximately $1 million of Postal Money

Orders into bank accounts at various financial institutions, including several Board regulated institutions. Information developed during the investigation revealed that the subjects were aware of the Postal Money Order purchasing requirements and patterned their purchases to avoid detection.

In December 2009, a federal grand jury indicted the subjects on charges of money laundering and trafficking in counterfeit goods. The indictment charged that the subjects knowingly conducted financial transactions affecting interstate and foreign commerce with the structured purchase of 636 Postal Money Orders valued at $579,865, which involved the proceeds from the unlawful sale of counterfeit merchandise throughout the United States. During this investigation, OIG special agents worked closely with Postal Inspectors analyzing financial transactions in support of the potential money laundering violations.

OIG Participation in Nationwide Effort to Combat Financial Fraud

The OIG is continuing its participation in the nationwide effort by the Federal Bureau of Investigation and the U.S. Attorney's Office to investigate and prosecute mortgage-related crimes. The President established the interagency Financial Fraud Enforcement Task Force to wage an aggressive, coordinated, and proactive effort to investigate and prosecute financial crimes. The task force includes representatives from a broad range of federal agencies, regulatory authorities, OIGs, and state and local law enforcement who, working together, bring to bear a powerful array of criminal and civil enforcement resources. The task force is working to improve efforts across the federal executive branch, as well as with state and local partners, to investigate and prosecute significant financial crimes, ensure just and effective punishment for those who perpetrate financial crimes, combat discrimination in the lending and financial markets, and recover proceeds for victims of financial crimes.

Subjects Pleaded Guilty in Mortgage Fraud Task Force Investigation

An investigation by OIG special agents assigned to the Maryland Mortgage Fraud Task Force recently resulted in the arrest of three subjects involved in a mortgage fraud scheme that netted more than $1.2 million from three federally regulated financial institutions. This investigation was conducted in conjunction with the President's Financial Fraud Enforcement Task Force. The investigation disclosed that between June and September 2007, the subjects submitted false mortgage applications for three properties that included false certifications of occupancy and inflated income. Each of the properties went into foreclosure or short sale, resulting in a total loss to the banks of more than $850,000.

Two of the subjects arrested have since pleaded guilty to conspiracy to commit wire fraud and are awaiting sentencing. Each faces a maximum sentence of up to 30 years in prison and a $1 million fine.

Summary Statistics on Investigations during the Reporting Period

Investigative Actions	Number
Investigative Caseload	
Investigations Open at End of Previous Reporting Period	36
Investigations Opened during Reporting Period	6
Investigations Closed during Reporting Period	1
Total Investigations Open at End of Reporting Period	41
Investigative Results for Reporting Period	
Referred to Prosecutor	7
Joint Investigations	28
Referred for Audit	0
Referred for Administrative Action	1
Oral and/or Written Reprimands	0
Terminations of Employment	0
Arrests	3
Suspensions	0
Debarments	0
Indictments	3
Criminal Information	0
Convictions	4
Monetary Recoveries	$0
Civil Actions (Fines and Restitution)	$0
Criminal Fines (Fines and Restitution)	$3,810,000

Hotline Operations

Consistent with the mission, goals, and objectives of the OIG, the Hotline system serves as a means for individuals to report allegations of fraud, waste, abuse, and mismanagement involving Board programs and operations. During this reporting period, the Hotline received 586 complaints.

The OIG continued to receive a significant number of complaints concerning fictitious instrument fraud and "phishing" scams. Many of these schemes are in the form of advance fee, lottery, and Nigerian scams, and some invoke the Federal Reserve name. These solicitations attempt to obtain the personal identifying information or financial information of the recipient. While the content of these types of schemes can differ, they can include a solicitation from an individual purporting to represent the Board or a Reserve Bank, falsely claim that the recipient has been awarded a large sum of money, and request information from the recipient to further process an alleged transfer of funds. The Hotline advises all individuals that neither the Board nor the Reserve Banks endorse these solicitations or have involvement in them. As appropriate, these complaints may be investigated by the OIG. Hotline staff is currently monitoring and analyzing these types of complaints to detect patterns and trends.

A number of other Hotline complaints were from consumers wanting to file non-criminal consumer complaints against financial institutions. We typically refer these complaints to the Federal Reserve Consumer Help (FRCH) unit, a centralized operation of the Federal Reserve System that assists consumers in filing complaints involving financial institutions. As indicated in FRCH's website, if a complaint is against a financial institution that the Federal Reserve supervises, it will be investigated by 1 of the 12 regional Federal Reserve Banks. Other hotline complaints were from individuals seeking advice or information regarding monetary policy and consumer protections. These inquiries were referred to the appropriate Board offices and other federal or state agencies.

Summary Statistics on Hotline Activities during the Reporting Period

Hotline Complaints	Number
Complaints Pending from Previous Reporting Period	133
Complaints Received during Reporting Period	586
Total Complaints for Reporting Period	**719**
Complaints Resolved during Reporting Period	677
Complaints Pending	42

Legal Services

The Legal Services program serves as the independent legal counsel to the IG and the OIG staff. The Legal Services staff provides comprehensive legal advice, research, counseling, analysis, and representation in support of OIG audits, investigations, inspections, evaluations, and other professional, management, and administrative functions. This work provides the legal basis for the conclusions, findings, and recommendations contained within OIG reports. Moreover, Legal Services keeps the IG and the OIG staff aware of recent legal developments that may affect the activities of the OIG and the Board.

In accordance with section 4(a)(2) of the IG Act, the Legal Services staff conducts an independent review of newly enacted and proposed legislation and regulations to determine their potential effect on the economy and efficiency of the Board's programs and operations. During this reporting period, Legal Services reviewed 22 legislative and 3 regulatory items.

Communications and Coordination

While the OIG's primary mission is to enhance the economy, efficiency, and effectiveness of Board programs and operations, we also coordinate externally and work internally to achieve our goals and objectives. Externally, we regularly coordinate with and provide information to Congress and congressional staff. We are also active members of the broader IG professional community, and we promote collaboration on shared concerns. Internally, we consistently strive to enhance and maximize efficiency and transparency in our infrastructure and day-to-day operations. Within the Board and the Federal Reserve System, we continue to provide information about the OIG's roles and responsibilities and participate, in an advisory capacity, on various Board work groups. Highlights of our activities follow.

Congressional Coordination and Testimony

The OIG has been communicating and coordinating with various congressional committees on issues of mutual interest. During the reporting period, we provided 15 responses to congressional members and staff.

Council of Inspectors General on Financial Oversight

Section 989E of the Dodd-Frank Act established the CIGFO, which comprises the IGs of the Board, the Commodity Futures Trading Commission, the Department of Housing and Urban Development, the Treasury, the FDIC, the Federal Housing Finance Agency, the National Credit Union Administration, the Securities and Exchange Commission, and the TARP. The CIGFO is required to meet at least quarterly to facilitate the sharing of information among the IGs and to discuss the ongoing work of each IG, with a focus on concerns that may apply to the broader financial sector and ways to improve financial oversight. The first meeting of the CIGFO was held in October 2010. In addition, the CIGFO is required to annually issue a report that highlights the IGs' concerns and recommendations, as well as issues that may apply to the broader financial sector.

Council of the Inspectors General on Integrity and Efficiency

The IG serves as a member of the CIGIE. Collectively, the members of the CIGIE help improve government programs and operations. The CIGIE provides a forum to discuss government-wide issues and shared concerns. The IG also serves as a member of the CIGIE Legislation Committee, which is the central point of information regarding legislative initiatives and congressional activities that may affect the community.

Financial Regulatory Coordination

To foster cooperation on issues of mutual interest, including issues related to the current financial crisis, the IG meets regularly with the IGs from other federal financial regulatory agencies: the FDIC, the Treasury, the National Credit Union Administration, the Securities and Exchange Commission, the Farm Credit Administration, the Commodity Futures Trading Commission, the Pension Benefit Guarantee Corporation, the Export-Import Bank, and the Federal Housing Finance Agency. We also coordinate with the Government Accountability Office. In addition, the Assistant IG for Audits and Attestations and the Assistant IG for Inspections and Evaluations meet with their financial regulatory agency OIG counterparts to discuss various topics, including bank failure material loss review best practices, annual plans, and ongoing projects.

Other Committee, Workgroup, and Program Participation

The IG continues to serve on various Board committees and work groups, such as the Senior Management Council. In addition, OIG staff members participate in a variety of Board working groups, including the Space Planning Executive Group, the Leading and Managing People Working Group, the Information Technology Advisory Group, the Core Response Group, the Management Advisory Group, the Information Security Committee, the Information Technology Strategic Committee, the Board Data Council, and the Continuity of Operations Working Group. Externally, the OIG legal staff are members of the Council of Counsels to the Inspector General. In addition, the Assistant IG for Audits and Attestations serves as co-chair of the Information Technology Committee of the Federal Audit Executive Council and works with audit staff throughout the IG community on common information technology (IT) audit issues.

Troubled Asset Relief Program Oversight

Our office participates with other financial regulatory OIGs on the TARP IG Council to facilitate effective cooperation among those entities whose oversight responsibilities relate to or affect the TARP.

OIG Information Technology

During the reporting period, the OIG IT team continued to monitor and maintain the OIG automated information system's FISMA compliance. Efforts included performing regular contingency tests of the OIG IT environment and ensuring that the OIG's staff, contractors, and interns completed their annual security awareness training. The team worked to ensure that OIG employees have reliable and uninterrupted technological services that enable them to operate effectively

and explored new technology to enhance the IT infrastructure. The IT team manages the OIG Microsoft Active Directory, network, and necessary applications and is working to implement a new investigative application to enhance Investigations' information management. Consistent with FISMA requirements, a security review of the OIG's IT infrastructure will be conducted during the next reporting period.

CIGIE Award

On October 19, 2010, Mr. Laurence A. Froehlich, former Assistant Inspector General for Legal Services, was posthumously awarded the CIGIE June Gibbs Brown Career Achievement Award. Mr. Froehlich was a champion of the IG community who dedicated himself to the furtherance of the community's mission, values, and goals. He served the federal government with distinction for over 33 years, all of which were spent working for OIGs. Mr. Froehlich's contributions to the IG community were extensive, and their impact immeasurable. His dedication to public service stands as an exemplar to the IG community.

Appendixes

Appendix 1
Audit, Inspection, and Evaluation Reports Issued with Questioned Costs during the Reporting Period[a]

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

a. Because the Board is primarily a regulatory and policymaking agency, our recommendations typically focus on program effectiveness and efficiency, as well as strengthening internal controls. As such, the monetary benefit associated with their implementation is often not readily quantifiable.

Appendix 2
Audit, Inspection, and Evaluation Reports Issued with Recommendations that Funds Be Put to Better Use during the Reporting Period[a]

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

a. Because the Board is primarily a regulatory and policymaking agency, our recommendations typically focus on program effectiveness and efficiency, as well as strengthening internal controls. As such, the monetary benefit associated with their implementation is often not readily quantifiable.

Appendix 3
OIG Reports with Recommendations that Were Open during the Reporting Period[a]

Report Title	Issue Date	Recommendations: No.	Recommendations: Mgmt. Agrees	Recommendations: Mgmt. Disagrees	Follow-up Completion Date	Status of Recommendations: Closed	Status of Recommendations: Open
Evaluation of Service Credit Computations	08/05	3	3	0	03/07	1	2
Security Control Review of the Central Document and Text Repository System (Non-public Report)	10/06	16	16	0	09/09	14	2
Audit of the Board's Payroll Process	12/06	7	7	0	03/10	3	4
Security Control Review of the Internet Electronic Submission System (Non-public Report)	02/07	13	13	0	09/09	12	1
Audit of the Board's Compliance with Overtime Requirements of the Fair Labor Standards Act	03/07	2	2	0	03/08	1	1
Security Control Review of the Federal Reserve Integrated Records Management Architecture (Non-public Report)	01/08	7	7	0	09/09	6	1
Review of Selected Common Information Security Controls (Non-public Report)	03/08	6	6	0	–	–	6
Security Control Review of the FISMA Assets Maintained by FRB Boston (Non-public Report)	09/08	11	11	0	–	–	11
Evaluation of Data Flows for Board Employee Data Received by OEB and its Contractors (Non-public Report)	09/08	2	2	0	–	–	2
Audit of the Board's Information Security Program	09/08	2	2	0	11/09	1	1
Control Review of the Board's Currency Expenditures and Assessments	09/08	6	6	0	03/10	5	1
Audit of Blackberry and Cell Phone Internal Controls	03/09	3	3	0	–	–	3
Inspection of the Board's Law Enforcement Unit (Non-public Report)	03/09	2	2	0	–	–	2
Security Control Review of the Audit Logging Provided by the Information Technology General Support System (Non-public Report)	03/09	4	4	0	–	–	4
Material Loss Review of First Georgia Community Bank	06/09	1	1	0	–	–	1
Material Loss Review of County Bank	09/09	1	1	0	–	–	1
Audit of the Board's Processing of Applications for the Capital Purchase Program under the Troubled Asset Relief Program	09/09	2	2	0	–	–	2
Audit of the Board's Information Security Program	11/09	4	4	0	–	–	4

a. 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 or are referring it to the appropriate oversight committee or administrator for a final decision.

Appendix 3—*continued*
OIG Reports with Recommendations that Were Open during the Reporting Period

Report Title	Issue Date	Recommendations			Status of Recommendations		
		No.	Mgmt. Agrees	Mgmt. Disagrees	Follow-up Completion Date	Closed	Open
Material Loss Review of Community Bank of West Georgia	01/10	1	1	0	–	–	1
Material Loss Review of CapitalSouth Bank	03/10	1	1	0	–	–	1
Security Control Review of the Lotus Notes and Lotus Domino Infrastructure (Non-public Report)	06/10	10	10	0	–	–	10

Appendix 4
Audit, Inspection, and Evaluation Reports Issued during the Reporting Period

Title	Type of Report
Security Control Review of the Lotus Notes and Lotus Domino Infrastructure	Audit
Material Loss Review of Warren Bank	Evaluation
Material Loss Review of Irwin Union Bank and Trust	Evaluation
Material Loss Review of Bank of Elmwood	Evaluation
Material Loss Review of San Joaquin Bank	Evaluation
Material Loss Review of Orion Bank	Evaluation
Material Loss Review of SolutionsBank	Evaluation
Material Loss Review of Barnes Banking Company	Evaluation
Review of the Failure of Marco Community Bank	Evaluation

Total Number of Audit Reports: 1
Total Number of Inspection and Evaluation Reports: 8

Full copies of these reports are available on our website at
http://www.federalreserve.gov/oig/default.htm

Appendix 5
OIG Peer Reviews

Government auditing and investigative standards require that our audit and investigative units each be reviewed by a peer OIG organization every three years. Section 989C of the Dodd-Frank Act amended the IG Act to require that OIGs provide in their semiannual reports to Congress specified information regarding (1) peer reviews of their respective organizations and (2) peer reviews they have conducted of other OIGs. The following information is provided to address the Dodd-Frank Act requirements.

- No peer reviews of the OIG were conducted during this reporting period.
- The last peer review of the OIG's Audits and Attestations program was completed in September 2008 by the U.S. Government Printing Office OIG. No recommendations from this or any prior peer reviews are pending.
- The last peer review of the OIG's Investigations program was completed in March 2008 by the U.S. Government Printing Office OIG. No recommendations from this or any prior peer reviews are pending.
- The Board OIG did not conduct any peer reviews of other OIGs during this reporting period.

Copies of our peer review reports are available on our website at http://www.federalreserve.gov/oig/peer_review_reports.htm.

Appendix 6
Cross-References to the Inspector General Act, as amended

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

Section	Source	Page(s)
4(a)(2)	Review of legislation and regulations	36
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 prosecutorial authorities	34
5(a)(5);6(b)(2)	Summary of instances where information was refused	None
5(a)(6)	List of audit, inspection, and evaluation reports	47
5(a)(7)	Summary of particularly significant reports	None
5(a)(8)	Statistical table of questioned costs	43
5(a)(9)	Statistical table of recommendations that funds be put to better use	44
5(a)(10)	Summary of audit, inspection, and evaluation reports issued before the commencement of the reporting period for which no management decision has been made	None
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
5(a)(14), (15), and (16)	Peer Review Summary	48

Table of Acronyms and Abbreviations

ADC	Acquisition, Development, and Construction
ALLL	Allowance for Loan and Lease Losses
Barnes	Barnes Banking Company
Board	Board of Governors of the Federal Reserve System
Bureau	Bureau of Consumer Financial Protection
CEO	Chief Executive Officer
CIGFO	Council of Inspectors General on Financial Oversight
CIGIE	Council of the Inspectors General on Integrity and Efficiency
CLD	Construction, Land, and Land Development
CRE	Commercial Real Estate
DIF	Deposit Insurance Fund
Dodd-Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act
Elmwood	Bank of Elmwood
FDI Act	Federal Deposit Insurance Act
FDIC	Federal Deposit Insurance Corporation
FFIEC	Federal Financial Institutions Examination Council
FISMA	Federal Information Security Management Act of 2002
FRB Atlanta	Federal Reserve Bank of Atlanta
FRB Chicago	Federal Reserve Bank of Chicago
FRB Kansas City	Federal Reserve Bank of Kansas City
FRB San Francisco	Federal Reserve Bank of San Francisco
FRCH	Federal Reserve Consumer Help
FSOC	Financial Stability Oversight Council
IBB	Independent Bankers' Bank
IESub	Internet Electronic Submission
IG	Inspector General

Table of Acronyms and Abbreviations

IG Act	Inspector General Act of 1978, as amended
IT	Information Technology
IUBT	Irwin Union Bank and Trust
Marco	Marco Community Bank
Midwest	Midwest Bank and Trust Company
NRAS	National Remote Access Services
OIG	Office of Inspector General
Orion	Orion Bank
PCA	Prompt Corrective Action
PubWeb	Public Website
San Joaquin	San Joaquin Bank
Solutions	SolutionsBank
TARP	Troubled Asset Relief Program
Treasury	U.S. Department of the Treasury

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Washington, DC 20551

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