2021 Major Management Challenges for the Board
MEMORANDUM

DATE: March 8, 2021

TO: Board of Governors

FROM: Mark Bialek
Inspector General

SUBJECT: 2021 Major Management Challenges for the Board

We are providing you with the major management challenges facing the Board of Governors of the Federal Reserve System in 2021. These challenges represent what we believe to be the areas that, if not addressed, are most likely to hamper the Board’s accomplishment of its strategic objectives.

We identified the Board’s major management challenges by assessing key themes from our discussions with management and our knowledge of the agency’s programs and operations. Notably, in 2020, the COVID-19 pandemic required multiple branches of the federal government as well as state and local governments to take actions to control the spread of the virus and stabilize the economy. Given the Federal Reserve System’s role in promoting maximum employment and stable prices, as well as the stability of the financial system, the Federal Reserve System made use of many of its available tools to mitigate the effect of the virus on economic activity.

Because of the importance of these pandemic response measures, we identified a new related management challenge; moreover, issues related to the pandemic response ripple through many of our previously identified challenges. The Board’s major management challenges, in order of significance, are as follows:

- Designing and Operationalizing Emergency Lending Programs to Address the Economic Effects of the COVID-19 Pandemic
- Enhancing Organizational Governance and Risk Management
- Enhancing Oversight of Cybersecurity at Supervised Financial Institutions
- Ensuring an Effective Information Security Program
- Strengthening the Human Capital Program and Ensuring Workforce Safety
- Remaining Adaptable to External Developments While Supervising Financial Institutions
- Ensuring That Physical Infrastructure Effectively Meets Mission Needs
We monitor the Board’s efforts to address the management challenges we identify each year. Our monitoring work includes following up on open recommendations and conducting related audit and evaluation work. For information on our ongoing and planned audit and evaluation work, please see our Work Plan.

We appreciate the cooperation that we received from the Board during this year’s management challenges process. If you would like to discuss any of the challenges, please feel free to contact me.

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Designing and Operationalizing Emergency Lending Programs to Address the Economic Effects of the COVID-19 Pandemic

The economic disruptions caused by the COVID-19 pandemic resulted in an abrupt shock to financial markets and affected many credit channels relied on by households, businesses, and state and local governments. In response, the Board of Governors of the Federal Reserve System has taken steps to support the flow of credit to U.S. households and businesses. Notably, the Board used its emergency lending authority under section 13(3) of the Federal Reserve Act to create lending programs that ensure liquidity in financial markets and provide lending support to various sectors of the economy. While some of these facilities are modeled after those created during the 2008 financial crisis, others have been created in new and unique ways for the pandemic response. In addition, the Coronavirus Aid, Relief, and Economic Security Act authorized, among other things, the U.S. Department of the Treasury’s investment in lending programs established by the Board and mandated public reporting of information about the government’s pandemic response. The scope of the Board’s pandemic response has created new and complex management challenges both in the short and long term.

To address these new challenges, the Board will need to monitor and seek to continuously improve the execution of its lending programs, ensuring that it is meeting the spirit and intent of the programs and appropriately reaching the intended recipients. Further, the Board will need to ensure that governance and internal controls are sufficient for consistent execution of its lending programs and monitor vendor activities to accomplish program objectives. The Board will also need to ensure that effective information security controls are implemented within the information technology systems and related processes used by the Federal Reserve Banks to administer the lending facilities to safeguard the confidentiality, integrity, and availability of Board data. Finally, the Board will need to continue to take measures to encourage and foster lending during the pandemic response; encourage financial institutions to lend in a manner consistent with the spirit and intent of specific lending programs; and ensure that banking organizations’ participation in pandemic response programs is commensurate with their governance, risk management, and internal control capabilities.
Enhancing Organizational Governance and Risk Management

An effective governance system (1) provides leadership, direction, and accountability in fulfilling an organization’s mission; (2) helps to ensure appropriate stewardship of public resources; and (3) establishes clear lines of responsibility for results. Effective enterprise risk management (ERM) can provide an enterprisewide view of organizational risks that informs decisionmaking and resource prioritization. Together, effective governance and risk management can help facilitate the Board’s achievement of its objectives.

The Board has a complex governance system with a decentralized structure and a consensus-driven culture; this system makes it difficult for the Board to use an enterprisewide approach for managing risks and certain administrative functions. While the Board continues to work on developing an enterprisewide risk management strategy, it has not yet completed an enterprisewide risk profile or developed processes for managing risk appetite and tolerance levels. The Board has tasked the Senior Officer Committee to serve as a forum for vetting Boardwide risk issues and advising the Executive Committee on risk strategy and appetite. The Board is also in the process of conducting baseline risk assessments and risk profiles for the divisions within the Office of the Chief Operating Officer, with the goal of expanding this effort across the agency’s divisions.

Aspects of the Board’s governance system and risk management processes have created challenges in managing certain administrative functions enterprisewide. For example, the decentralization of information technology services results in an incomplete view of the risks affecting the Board’s security posture. The Board has also faced challenges managing other processes enterprisewide, including enhancing its data-related capabilities through well-defined enterprise-level data governance policies and consistent data management standards and practices, in addition to other aspects of its information security program and workforce planning.

Although the Board has made progress toward implementing an ERM program and enterprisewide approaches to certain of its administrative functions, the Board should continue to focus on this challenge. Enhancing the Board’s governance system and ERM program can enable the Board to better evaluate the potential overall effect of risks as an interrelated portfolio and to effectively prioritize resource allocation.
Enhancing Oversight of Cybersecurity at Supervised Financial Institutions

As financial institutions have continued to adopt internet-based systems to conduct business, cyberthreats to the financial sector have increased dramatically in both number and sophistication. These threats can create significant operational risk, disrupt critical services, and ultimately affect financial stability. As a result, cybersecurity remains an area of significant focus for financial institutions and federal financial regulators. Accordingly, financial institutions and regulators must work to protect vital networks and data from cybersecurity threats and prepare to respond to potential cyberattacks.

Prior to the emergence of the pandemic, the Board chair described cybersecurity risk as one of the most significant risks facing the Board and financial institutions. The Board continues to refine its approach to cybersecurity supervision of financial institutions. As part of that refinement effort, the Board can strengthen the governance of its cybersecurity supervisory activities and clarify the roles and responsibilities of various groups involved in cybersecurity supervision and planning. Further, the Board should ensure that its supervisory approaches keep pace with evolving cyberthreats.
Ensuring an Effective Information Security Program

Information security continues to be a key risk area for federal government agencies, as demonstrated by recent breaches of sensitive data and a sharp increase in information security incidents reported by federal agencies over the past several years. To strengthen federal cybersecurity risk management practices, Congress passed the Federal Information Security Modernization Act of 2014. This act requires the Board to develop, document, and implement an information security program to protect its information systems and data. Although the Board continues to operate an effective information security program, opportunities exist for the Board to further strengthen its information security program in the areas of risk management, configuration management, information security continuous monitoring (ISCM), and third-party risk management.

As noted in the challenge titled Enhancing Organizational Governance and Risk Management, the decentralization of information technology services results in an incomplete view of the risks affecting the Board’s security posture. The Board’s Division of Information Technology, in coordination with the agency’s ERM team, is developing and implementing a new cybergovernance program. This program seeks to establish the normal range of acceptable cybersecurity risk and determine a cybersecurity residual risk threshold for each of the Board’s significant cybersecurity risk scenarios. As the Division of Information Technology matures this program, it will need to continue to ensure that the program is integrated with the agency’s ongoing ERM implementation.

The Board is working to implement the tools and technologies offered by the U.S. Department of Homeland Security’s Continuous Diagnostics and Mitigation program to gain efficiencies within its information security program and information technology governance framework and to strengthen its asset, configuration, and vulnerability management processes. As these new tools and capabilities are implemented, the Board will be challenged to ensure that its asset, configuration, and vulnerability management processes are implemented enterprisewide and operating effectively. The implementation of the tools offered through the Continuous Diagnostics and Mitigation program will also require the Board to update its ISCM strategy and associated processes. These activities should assist the agency in transitioning its ISCM program to one that supports ongoing authorizations and more timely risk management activities.

The Board relies on a variety of third-party-operated and third-party-maintained systems to meet its mission. In addition, the Board is increasingly leveraging cloud computing–based technology to meet its information technology needs. The risks associated with these systems is heightened because the agency may have limited insight into or knowledge of the security processes of third-party providers. The Board’s cloud computing strategy and information security program processes will need to ensure the adequate protection of the agency’s data in the cloud and that requirements for records management, electronic discovery, privacy, and information security are met by its cloud service providers.
Strengthening the Human Capital Program and Ensuring Workforce Safety

The Board’s success in achieving its mission is contingent on attracting, developing, and retaining a qualified, diverse, and agile workforce with the necessary technical, managerial, and leadership skills. As the Board takes steps to further its mission through the advancement of its human capital program, it must also ensure that its workforce is provided with a safe and healthy work environment. In March 2020, the Board’s Human Resources (HR) function within the Division of Management, in cooperation with the Office of the Chief Operating Officer, helped Board divisions adapt to workplace changes due to the COVID-19 pandemic. HR actively assisted Board divisions’ leadership in moving to a full-time telework environment for all but certain essential Board personnel and began following safety and health guidelines established by the Centers for Disease Control and Prevention; Johns Hopkins University; and the Washington, DC, Joint All Hazards Operations Center; among other sources. Using such guidelines, and in consultation with a medical epidemiologist, the Board updated its communicable disease plan, made changes to its work environment, and coordinated with other federal agencies to identify best practices for teleworking. However, prolonged operation in a telework environment may result in workforce challenges related to work-life balance and employee engagement. To address these challenges and meet its future workforce needs, the Board must continue (1) to strengthen its human capital program and (2) to adapt to a changing environment.

The Board had begun replacing its human capital management, financial, and procurement systems with modern, cloud-based technology before the pandemic; this modernization has taken on increased importance in a continually evolving workforce environment. The successful transition of human capital records and processes to the new cloud-based system will likely be time and resource intensive; however, modernizing these and other systems can help support the efficient administration of workforce services and workforce collaboration in the digital workspace.

Moreover, although the Board has also begun developing a plan for teleworking employees’ eventual return to the office, the return-to-work plan, which involves a phased return of employees, is still being developed because of the evolving nature of the pandemic and key health and safety considerations, such as employees’ reliance on public transportation, preexisting health conditions, and family care situations. As the circumstances related to the COVID-19 pandemic evolve, the Board must continue to carefully monitor and respond to changing conditions to protect the health of its workforce.

Throughout the Board’s transition to a telework environment, the agency has continued to strengthen its human capital program. For example, HR has provided assistance, including issuing HR workforce planning guidance as well as establishing a workforce planning process with clearly defined HR roles and responsibilities, to certain divisions implementing workforce planning initiatives, and HR plans to continue assisting other divisions with their workforce planning efforts. Workforce planning can help the Board strengthen its human capital management by aligning its human capital program with its current and emerging mission and programmatic goals and by developing long-term workforce strategies for acquiring, developing, and retaining staff.
The Board will need to continue to be strategic in how it addresses changes to its workplace environment while simultaneously progressing on its ongoing human capital and diversity initiatives. The importance of the Board’s workforce is highlighted in both its Strategic Plan 2020–23 and Diversity and Inclusion Strategic Plan 2016–19. These plans can support the Board’s efforts to foster a culture that encourages collaboration, flexibility, transparency, and fairness during a time of rapid change and assist in the Board’s efforts to successfully recruit, hire, train, promote, and retain a more diverse workforce.
Promoting the safety, soundness, and stability of financial institutions is a core mission of the Board. The COVID-19 pandemic has presented novel challenges that have affected consumers, businesses, and communities as well as the financial institutions that serve them. Current areas of focus for the Board’s supervision and regulatory strategy include being nimble and adaptable to changes and ensuring that institutions can continue providing credit and services to their customers while promoting the stability of financial institutions. Challenges in this environment include (1) providing institutions the flexibility and support needed to serve their customers while implementing revised supervisory approaches to evaluate the safety and soundness of institutions, (2) leveraging and enhancing technology, and (3) continuing to maintain strong cooperative relationships with other supervisory agencies.

The Board is adjusting its supervisory approaches to assess financial institutions’ evolving risks in this dynamic environment. In addition, the Board, in conjunction with other regulatory agencies, has released examiner guidance to promote consistency and flexibility. Given the uncertainty surrounding the duration and effect of the COVID-19 pandemic, the Board will likely have to continue to adapt its regulatory and supervisory approaches to further its financial stability mission in a manner that supports the needs of consumers, businesses, and communities. The Board must also continue to leverage and enhance its information technology tools to effectively and efficiently conduct its supervision and surveillance activities. Leveraging and enhancing technology is particularly important in light of the Board’s decision to shift to offsite supervisory activities during the pandemic. Finally, the Board must continue to maintain strong cooperative relationships with other supervisory agencies. Continued efforts to coordinate with other supervisory agencies are crucial to the Board’s effective execution of its supervisory responsibilities because this coordination can reduce the potential for duplicative efforts or gaps in supervisory coverage and help monitor, identify, and respond to emerging risks.
Ensuring That Physical Infrastructure Effectively Meets Mission Needs

The Board is committed to ensuring that it has the physical infrastructure it needs to execute its mission in a cost-effective and safe manner. Over the past decade, the Board has supplemented its owned space with leased space to accommodate overall staff growth and to house staff displaced by renovation projects. However, because maintaining supplemental, leased space is costly and may hamper employee engagement, the Board’s goal is to create a campus for all employees that will allow for improved collaboration and communication while reducing operating costs. To achieve that goal, the Board acquired an additional property at 1951 Constitution Avenue NW and is renovating it and three other Board-owned buildings: William McChesney Martin, Jr.; New York Avenue; and Marriner S. Eccles. However, these renovation projects present significant risks and challenges, including those associated with contractor oversight, cost management, disruptions to employees, and the COVID-19 pandemic.

Several of these renovation projects are multiyear efforts that involve significant resources; these projects pose challenges due to their size, complexity, and interdependencies. For example, the Martin building project, which is an estimated $436.5 million expenditure, has faced scope changes, delays, and cost increases since the original concept was developed. Even though additional concept changes were made to this project as a result of the acquisition of the 1951 Constitution Avenue NW building, the Board expects the Martin building project to be completed in the third quarter of 2021. The Board has also awarded a joint design contract for both the 1951 and Eccles buildings. While the Board has completed some renovation work on its New York Avenue building, it has decided to suspend a more comprehensive renovation of the building until completion of the 1951 and Eccles buildings. Moreover, these projects require space planning during and after the renovations, which will pose a challenge to the Board, particularly in light of the uncertainty associated with the pandemic. The Board is challenged to ensure a safe work environment that limits the potential to spread infectious diseases.

In response to the challenges associated with these infrastructure projects, the Board hired dedicated project managers and responsible officials to monitor project schedules and milestones and to provide oversight governance bodies with periodic status reports. The Board has noted that the project team has managed the Martin building renovation project through various challenges, including unforeseen conditions, modifications to support the overall workplace strategy, and midcourse adjustments to the construction schedule. The Board has also established a steering committee to provide input into the space planning design for the entire campus. In response to the pandemic, the Board has contracted with a vendor to conduct research and analysis regarding post-COVID-19 best practices and provide a tactical implementation assessment of these practices for consideration during the design of Board facilities.
## Abbreviations

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<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>ERM</td>
<td>enterprise risk management</td>
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<td>HR</td>
<td>Human Resources</td>
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<td>ISCM</td>
<td>information security continuous monitoring</td>
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