

September 30, 2019

Board of Governors of the Federal Reserve System

2019 Major Management Challenges for the Board



Office of Inspector General

Board of Governors of the Federal Reserve System
Bureau of Consumer Financial Protection




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MEMORANDUM

DATE: September 30, 2019

TO: Board of Governors

FROM: Mark Bialek 
Inspector General

SUBJECT: *2019 Major Management Challenges for the Board*

We are pleased to provide you with our 2019 list of the major management challenges facing the Board of Governors of the Federal Reserve System (Board). 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 identifying and assessing key themes from our audit and evaluation work as well as our understanding of the agency's programs and operations. The major management challenges, in order of significance, are as follows:

- Enhancing Organizational Governance and Risk Management
- Enhancing Oversight of Cybersecurity at Supervised Financial Institutions
- Ensuring That an Effective Information Security Program Is in Place
- Advancing Efforts to Improve Human Capital Management
- Adapting to Internal and External Developments While Refining the Regulatory and Supervisory Framework
- 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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Contents

Enhancing Organizational Governance and Risk Management	5
Enhancing Oversight of Cybersecurity at Supervised Financial Institutions	6
Ensuring That an Effective Information Security Program Is in Place	7
Advancing Efforts to Improve Human Capital Management	8
Adapting to Internal and External Developments While Refining the Regulatory and Supervisory Framework	9
Ensuring That Physical Infrastructure Effectively Meets Mission Needs	10
Abbreviations	11



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. The Board of Governors of the Federal Reserve System (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 managing certain administrative functions.

Enterprise risk management (ERM) provides an enterprisewide view of organizational risks that informs decisionmaking and resource prioritization; as such, it is integral to a governance framework. The Board is challenged to successfully implement an ERM program. It has not defined a risk management strategy, a risk appetite, a risk tolerance, or a risk profile, despite attempts since 2004 to implement ERM processes. The Board does not have a designated Chief Risk Officer or equivalent function focused on formulating and implementing risk management policies; this responsibility is delegated to the Chief Financial Officer position, which is also tasked with providing financial services and overseeing strategic planning. In 2017, the Board appointed an officer in the Division of Financial Management to provide strategic direction for and oversight of the design and implementation of an ERM program. In 2018, the Board established a risk committee and conducted pilot risk assessments in two divisions. Resources supporting ERM continue to be limited, however, and obtaining enterprisewide support for an ERM program continues to be a challenge.

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 other aspects of its information security program and workforce planning, as described in the challenges titled *Ensuring That an Effective Information Security Program Is in Place* and *Advancing Efforts to Improve Human Capital Management*.

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

In recent years, cyberthreats to the financial sector have increased dramatically, both in number and in sophistication. These threats can create significant operational risk, disrupt critical services, and ultimately affect financial stability. Accordingly, cybersecurity remains an area of significant focus for financial institutions and federal financial regulators; financial institutions and regulators must prepare for significant cyberattacks.

The Board Chairman has described cybersecurity as one of the most significant risks facing the Board and financial institutions. As such, the Board identified cyberrisk at supervised firms of all sizes as a priority that it will continue to monitor closely. The Board's supervisory program for financial institutions includes efforts to assess whether supervised financial institutions manage and mitigate the risks of and vulnerabilities to cyberattacks. The Board faces challenges in ensuring that its supervisory approaches keep pace with evolving cyberthreats as well as the concerns of the financial services sector. The Vice Chairman for Supervision has emphasized the Board's commitment to strategies that will result in measureable enhancements to the cyberresiliency of the financial sector.



Ensuring That an Effective Information Security Program Is in Place

Information security continues to be a key risk in the federal government, as demonstrated by recent incidents involving breaches of sensitive data and the sharp increase in information security incidents reported by federal agencies over the last several years. The Federal Information Security Modernization Act of 2014 (FISMA) requires the Board to develop, document, and implement an information security program to protect its information systems and data. Although the Board is operating its information security program at an overall effective level, there are opportunities for the Board to mature its information security program in the areas of configuration management and information security continuous monitoring (ISCM).

The Board faces challenges in implementing a centralized approach to configuration management. The Board does not have a comprehensive enterprise architecture and associated review processes that are enforced across the agency. An enterprise architecture would provide the Board with a blueprint for modernizing its information technology infrastructure as well as serve as a guide to establishing and maintaining the integrity of the Board's systems.

With respect to ISCM, the Board faces challenges in implementing agencywide processes for managing vulnerabilities and software inventories. The Board has opportunities to mature its ISCM program through further automation. The Board maintains data regarding its system authorizations and other ISCM-related functions in two FISMA compliance tools; the decentralization of these data into two tools hinders the Board's ability to deliver persistent situational awareness and to assess security risks across the organization. The completion of the Board's ISCM strategy should help address this issue but will depend on the implementation of the Continuous Diagnostics and Mitigation program and the Board's ongoing work with the U.S. Department of Homeland Security.

The Board relies on a variety of contractor-operated and contractor-maintained systems to meet its mission. In addition, the Board plans to further leverage cloud computing 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 should ensure that cloud providers are implementing FISMA requirements for records management, electronic discovery, privacy, and information security.



Advancing Efforts to Improve Human Capital Management

The Board's success in achieving its mission is contingent on attracting, developing, and retaining a qualified, diverse, and agile workforce. Continually evolving workforce expectations and a highly competitive hiring environment for specialized skills present challenges. In addition, current and long-term budget pressures and a projected increase in retirement-eligible Board employees in mission-supporting positions may contribute to gaps in leadership and institutional knowledge. Further, identifying a diverse workforce with the necessary technical, managerial, and leadership skills to effectively execute the Board's mission remains a challenge, as minorities and women continue to be underrepresented in internal and external candidate pools. The Board must continue to improve its human capital management to mitigate these challenges and meet its future workforce needs.

One of the Board's key human capital initiatives is workforce planning. 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 developing long-term workforce strategies for acquiring, developing, and retaining staff to achieve these goals. The Board has begun to take a more strategic approach to workforce planning. The Board has developed and piloted a preliminary enterprisewide workforce planning process in two divisions, and it has begun to develop workforce plans in two other divisions. We completed an evaluation of challenges to the Board's efforts to implement workforce planning enterprisewide in September 2019. In this evaluation, we identified several strategies that may help the Board mitigate its operational challenges associated with workforce planning.

The Board identified its workforce as a priority in its *Strategic Plan 2016–19*. In 2016, the Board published its *Diversity and Inclusion Strategic Plan 2016–19* as a companion to its strategic plan. Taken together, these plans can assist in the Board's efforts to successfully recruit, hire, train, promote, and retain a more diverse workforce, as well as to foster a culture that encourages collaboration, flexibility, transparency, and fairness.



Adapting to Internal and External Developments While Refining the Regulatory and Supervisory Framework

Promoting the safety, soundness, and stability of financial institutions and financial market infrastructures is a core activity related to the Board's mission. Although this activity is a current focus of the Board's supervisory strategy, the Board faces challenges in adapting to internal and external developments that may affect its regulatory and supervisory direction. In addition, the Vice Chairman for Supervision has outlined a regulatory and supervisory agenda for the Board that seeks to improve the effectiveness of the postcrisis regulatory framework through increased efficiency, transparency, and simplicity. As part of that effort, the Vice Chairman for Supervision supports an approach to financial institution supervision that is tailored to the risk profile and complexity of each supervised institution. Further, the Board continues to focus on tailoring regulations to reduce the burden for less-systemic firms and community banks.

Key approaches that can help the Board continually adapt to internal and external developments include (1) leveraging and enhancing technology and (2) fostering a culture that encourages employees to share their views on supervision matters. Information management continues to increase in importance and complexity. The Board must continue to leverage and enhance its information technology tools to improve the effectiveness and efficiency of its supervision activities. Further, given the complexity of assessing risks at many large financial institutions with nuanced business activities, the free flow of information between supervision employees and their leaders has proven to be crucial to the effectiveness of the Board's supervisory efforts. The Board should continue to foster a culture that encourages employees to share their views, including opposing views, so that decisionmakers reach informed conclusions and decisions about supervised entities.

Finally, to support the Board's goal to improve the effectiveness of the postcrisis regulatory framework, the Board should continue to cultivate and maintain strong cooperative relationships with the primary supervisors of holding company subsidiaries. Continued efforts to coordinate with other federal supervisory agencies are crucial to the Board's effective execution of its supervisory responsibilities because this coordination can (1) reduce potential duplication of efforts or eliminate gaps in supervisory coverage and (2) help the Board to monitor, identify, and respond to emerging systemic risks.



Ensuring That Physical Infrastructure Effectively Meets Mission Needs

Ensuring that the Board has the physical infrastructure it needs to execute its mission in a cost-effective manner presents significant risks and challenges, including those associated with contractor oversight, cost management, and disruptions to employees. Over the last decade, the Board has supplemented its owned space with leased space to accommodate overall staff growth and to house staff displaced by the infrastructure projects. 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: (1) the William McChesney Martin, Jr., Building; (2) the New York Avenue Building; and (3) the Murrin S. Eccles Building. Space planning during and after the renovations will also pose a challenge to the Board.

Within the portfolio of infrastructure projects, several are multiyear efforts that involve significant resources; these projects pose challenges due to their size, complexity, and interdependencies. The Martin Building renovation project, which is an estimated \$340 million expenditure, has faced scope changes, delays, and cost increases since the original concept was developed. Although additional concept changes were made as a result of the acquisition of 1951 Constitution Avenue NW, the Board expects the Martin Building project to be completed in early 2021. The Board has begun some renovation work in its New York Avenue Building and is considering options for a more comprehensive renovation of the building. The Board also has awarded a joint design contract for both the 1951 Constitution Avenue NW and Eccles Buildings. Managing relationships among the infrastructure projects is important in order to mitigate potential cascading effects on completion dates and costs.

In response to 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 noted that the project team has continued to manage the Martin Building renovation project through various challenges, including unforeseen conditions, modifications to support the overall workplace strategy, and midcourse adjustments in the construction schedule. Lastly, the Board implemented a steering committee to provide input into the space planning design for the entire campus.



Abbreviations

Board	Board of Governors of the Federal Reserve System
ERM	enterprise risk management
FISMA	Federal Information Security Modernization Act of 2014
ISCM	information security continuous monitoring

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