The CFPB Can Strengthen Its Controls for Identifying and Avoiding Conflicts of Interest Related to Vendor Activities

March 15, 2017
Report Contributors
Daniel Novillo, Project Lead and OIG Manager
Rachael Young, Senior Auditor
Safal Bhattarai, Auditor
Kelly Friday, Audit Intern
Michael VanHuysen, Senior OIG Manager for Supervision and Regulation
Melissa Heist, Associate Inspector General for Audits and Evaluations

Abbreviations

<table>
<thead>
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<th>Abbreviation</th>
<th>Description</th>
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<tr>
<td>CFPB</td>
<td>Consumer Financial Protection Bureau</td>
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<tr>
<td>COR</td>
<td>contracting officer’s representative</td>
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<tr>
<td>Dodd-Frank Act</td>
<td>Dodd-Frank Wall Street Reform and Consumer Protection Act</td>
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<td>ECOA</td>
<td>Equal Credit Opportunity Act</td>
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<td>FAI</td>
<td>Federal Acquisition Institute</td>
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<td>FAR</td>
<td>Federal Acquisition Regulation</td>
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<td>GAO</td>
<td>U.S. Government Accountability Office</td>
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<td>HMDA</td>
<td>Home Mortgage Disclosure Act</td>
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<td>OFLEO</td>
<td>Office of Fair Lending and Equal Opportunity</td>
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<td>OIG</td>
<td>Office of Inspector General</td>
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<td>Procurement Office</td>
<td>Office of the Chief Procurement Officer</td>
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<td>RMR</td>
<td>Division of Research, Markets, and Regulations</td>
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<td>RTOP</td>
<td>request for task order proposal</td>
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<td>SCC</td>
<td>service contract code</td>
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<td>SEFL</td>
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The CFPB Can Strengthen Its Controls for Identifying and Avoiding Conflicts of Interest Related to Vendor Activities

Purpose

The Office of Inspector General conducted this evaluation to assess whether the Consumer Financial Protection Bureau (CFPB) effectively mitigates the risk of potential conflicts of interest associated with using vendors to support fair lending compliance and enforcement analysis. We focused on a contract for fair lending enforcement analysis and expert witness services. Our scope did not include identifying potential or actual conflicts of interest related to the CFPB’s fair lending supervision contracts, and our findings are not reflective of all CFPB contracting practices. However, we reference the CFPB’s conflict of interest management practices, rather than a particular division’s practices, where our findings and recommendations have broader applicability. Our office is also conducting a separate review of the CFPB’s contract solicitation, selection, and award process. To minimize the duplication of efforts, and after reviewing initial documentation associated with all CFPB fair lending contracts from the CFPB’s inception in July 2011 through January 2016, we focused this evaluation on the CFPB’s management of a fair lending enforcement vendor’s potential conflicts of interest after the contract award.

Background

In 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act created the CFPB and required the agency to establish an Office of Fair Lending and Equal Opportunity (OFLEO). OFLEO oversees and enforces certain federal laws, including the Equal Credit Opportunity Act and the Home Mortgage Disclosure Act, to ensure that consumers have fair, equitable, and nondiscriminatory access to credit. To assist in executing this fair lending oversight function, the CFPB contracted with a vendor to perform statistical analysis services that include estimating supervised institutions’ compliance with fair lending laws and serving as an expert witness when needed. The CFPB’s Office of the Chief Procurement Officer and the program office (in this case, OFLEO) share responsibilities for identifying, evaluating, avoiding, and mitigating potential conflicts of interest with CFPB vendors.

Findings

During the CFPB’s engagement with the relevant vendor, the vendor’s past and ongoing relationships with entities supervised by the CFPB heightened the risk of possible conflicts of interest and increased the need to actively manage this relationship in accordance with agency expectations. We did not identify any actual conflicts of interest from June 2012 through January 2016 between the vendor and the firms subject to the vendor’s analysis. We did note that the vendor failed to disclose a relationship with a firm for nearly 2 years after the CFPB first included that firm on a task order. Although this firm was included in multiple task orders for potential analysis during those 2 years, the CFPB later confirmed that the vendor did not perform any work related to that firm.

We found that the CFPB can strengthen its controls for identifying and avoiding potential conflicts of interest by (1) ensuring that vendors comply with existing documentation requirements; (2) clarifying roles and responsibilities; and (3) better facilitating vendor disclosure of potential conflicts, or affirmation that no conflicts exist, at the issuance of each task order. In addition, although the CFPB currently performs some fair lending enforcement analysis internally, we found that the CFPB should evaluate the potential costs and benefits of performing more fair lending enforcement analysis internally.

Recommendations

Our report contains recommendations designed to strengthen the CFPB’s identification and avoidance of potential conflicts of interest. The recommendations aim to reduce the agency’s exposure to operational and reputational risk. In its response to our draft report, the CFPB concurs with our recommendations. The agency describes completed actions and planned activities to improve the CFPB’s identification and avoidance of potential conflicts of interest.
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<th>Responsible office</th>
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<tr>
<td>1</td>
<td>12</td>
<td>Update policies and procedures as they relate to identifying and mitigating potential or actual conflicts of interest, to</td>
<td>Office of the Chief Procurement Officer and Division of Supervision, Enforcement, and Fair Lending</td>
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<td></td>
<td></td>
<td>a. clarify division-specific and job-specific roles and responsibilities for managing contracts.</td>
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<td>b. reinforce documentation requirements throughout the contract.</td>
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<td>2</td>
<td>12</td>
<td>Develop a strategy to ensure that contracting officer’s representatives have the required support to effectively identify and mitigate conflicts of interest.</td>
<td>Office of the Chief Procurement Officer and Division of Supervision, Enforcement, and Fair Lending</td>
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<td>3</td>
<td>12</td>
<td>Require that vendors submit a written response to each task order disclosing potential conflicts of interest or affirming that no conflicts of interest exist.</td>
<td>Office of the Chief Procurement Officer and Division of Supervision, Enforcement, and Fair Lending</td>
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<td>4</td>
<td>12</td>
<td>Determine an approach for specifying to vendors the firm or firms that may be subject to analysis at the issuance of each task order.</td>
<td>Office of the Chief Procurement Officer and Division of Supervision, Enforcement, and Fair Lending</td>
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<tr>
<td>5</td>
<td>15</td>
<td>Evaluate the potential costs and benefits of performing more of the fair lending enforcement analysis internally.</td>
<td>Division of Research, Markets, and Regulations and Division of Supervision, Enforcement, and Fair Lending</td>
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March 15, 2017

MEMORANDUM

TO: Distribution List

FROM: Melissa Heist
Associate Inspector General for Audits and Evaluations

SUBJECT: OIG Report 2017-SR-C-004: The CFPB Can Strengthen Its Controls for Identifying and Avoiding Conflicts of Interest Related to Vendor Activities

The Office of Inspector General has completed its report on the subject evaluation. We conducted this evaluation to assess whether the Consumer Financial Protection Bureau effectively mitigates the potential conflict of interest risks associated with using vendors to support analysis of fair lending compliance and enforcement.

We provided you with a draft of our report for review and comment. In your response, you concur with our recommendations and outline completed actions and planned activities to address our recommendations. We have included your response as appendix B to our report.

We appreciate the cooperation that we received from your staff during our evaluation. Please contact me if you would like to discuss this report or any related issues.

cc: David Bleicken, Deputy Associate Director, Division of Supervision, Enforcement, and Fair Lending
    Patrice Ficklin, Assistant Director, Office of Fair Lending and Equal Opportunity
    Frank Vespa-Papaleo, Principal Deputy Director, Office of Fair Lending and Equal Opportunity
    Ron Borzekowski, Assistant Director, Office of Research
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David Silberman, Acting Deputy Director, Consumer Financial Protection Bureau, and Associate Director, Division of Research, Markets, and Regulations
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Introduction

Objective

The Office of Inspector General (OIG) conducted this evaluation to assess whether the Consumer Financial Protection Bureau (CFPB) effectively mitigates the risk of potential conflicts of interest associated with using vendors to support its analysis of fair lending compliance and enforcement. We reviewed multiple contracts and, based on an initial review, focused on a contract for fair lending enforcement analysis and expert witness services. Our findings are not reflective of all CFPB contracting practices. However, we reference the CFPB’s conflict of interest management practices, rather than a particular division’s practices, where our findings and recommendations have broader applicability. Our office is also conducting a separate review of the CFPB’s contract solicitation, selection, and award process. To minimize the duplication of efforts, and after reviewing initial documentation associated with all CFPB fair lending contracts from the CFPB’s inception in July 2011 through January 2016, we focused this evaluation on the CFPB’s identification and avoidance of potential conflicts of interest related to a contract for fair lending enforcement analysis and expert witness services after the contract award. For details on our scope and methodology, please see appendix A.

Background

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act)\(^1\) established the CFPB in 2010 to consolidate responsibility for supervising and enforcing compliance with certain federal consumer protection laws, including certain federal laws designed to promote fair lending.\(^2\) With respect to the federal consumer protection laws related to fair lending, the CFPB has responsibility for the Equal Credit Opportunity Act (ECOA) and the Home Mortgage Disclosure Act (HMDA).\(^3\)

The Dodd-Frank Act required the CFPB to establish an office of fair lending and equal opportunity with the following duties and authorities:

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3. ECOA and Regulation B (12 C.F.R. part 1002) prohibits creditors from discriminating against any applicant with respect to any aspect of a credit transaction (1) on the basis of race, color, religion, national origin, sex, marital status, or age; (2) because all or part of the applicant’s income derives from any public assistance program; or (3) because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. HMDA and Regulation C (12 C.F.R. part 1003) require covered financial institutions to collect, report, and disclose certain mortgage data, such as the ethnicity, race, sex, and gross annual income of mortgage applicants and borrowers. This information is aggregated, and certain data fields are redacted prior to public disclosure to protect the privacy of applicants and borrowers.
• providing oversight and enforcement of certain federal laws to ensure fair, equitable, and nondiscriminatory access to credit
• coordinating the CFPB’s fair lending efforts with other federal and state regulators
• working with private industry, fair lending, civil rights, consumer, and community advocates on the promotion of fair lending compliance and education
• providing annual reports to Congress

The Office of Fair Lending and Equal Opportunity and Other CFPB Divisions Responsible for Fair Lending Efforts

In response to the Dodd-Frank Act, the CFPB created the Office of Fair Lending and Equal Opportunity (OFLEO). OFLEO is one of four offices in the agency’s Division of Supervision, Enforcement, and Fair Lending (SEFL), as shown in figure 1. As of early 2016, OFLEO employed 32 staff members in the following four functional sections: (1) operations and policy; (2) research, prioritization, and regulations; (3) enforcement; and (4) supervision. OFLEO conducts fair lending–related supervisory examinations and enforcement activities on financial institutions.

Other CFPB offices assist OFLEO with its fair lending efforts. In the Operations Division, the Office of the Chief Procurement Officer (Procurement Office) oversees purchasing for the agency and compliance with federal procurement rules and regulations. This office coordinates with other program offices, including OFLEO, to solicit and award contracts. From 2012 to 2015, the CFPB engaged multiple vendors to support OFLEO’s fair lending analyses, in addition to receiving internal analytical support from the Office of Research within the Division of Research, Markets, and Regulations (RMR) as well as conducting its own analysis. As of May 2015, RMR and OFLEO have been conducting all fair lending analyses for supervision activities. Currently, in addition to internal analytical support from the Office of Research and OFLEO’s own analysis, the CFPB contracts with external vendors to conduct fair lending enforcement analysis and expert witness services. This report focuses on the CFPB’s management of conflicts of interest related to fair lending enforcement analysis work performed by vendors.
OFLEO Supervision and Enforcement Activities and Use of an Enforcement Vendor

OFLEO’s supervision activities range from programmatic assessments of an institution’s fair lending compliance management systems to in-depth reviews of products or activities that may pose heightened fair lending risks to consumers. OFLEO conducts three types of fair lending reviews: ECOA baseline reviews, ECOA targeted reviews, and HMDA verification reviews. Although OFLEO’s reviews historically have focused on three priority areas—mortgages, indirect auto lending, and credit cards—the office is expanding its efforts to review small business lending and other product areas. OFLEO’s supervisory examination results do not become public information.

OFLEO’s Enforcement section conducts investigations of potential violations of ECOA and HMDA. If OFLEO identifies a potential violation of law, the CFPB can file a complaint either through its administrative enforcement process or in federal court. Like other federal bank regulators, the CFPB refers matters to the U.S. Department of Justice when it has reason to

4. ECOA baseline reviews seek to identify and analyze risks of ECOA violations, to identify certain types of ECOA and Regulation B violations, and to inform fair lending prioritization decisions for future CFPB reviews. ECOA targeted reviews include an in-depth look at a specific area of fair lending risk. HMDA reviews include transactional testing for HMDA data accuracy. In the housing finance market, HMDA data allow regulators to assess a specific institution’s risk, as well as risk across the market, in order to identify those institutions or segments that appear to present heightened fair lending risk to consumers.
believe that a creditor has engaged in a pattern or practice of lending discrimination. When the CFPB refers a matter to the U.S. Department of Justice, however, the agency can proceed in parallel with an independent action to address a violation.

In 2015, the CFPB’s fair lending supervisory and public enforcement actions required approximately $108 million in restitution to consumers. To assist in executing this fair lending oversight function, OFLEO’s Enforcement section contracts with external resources to conduct statistical analysis designed to assess an institution’s compliance with fair lending laws and to serve as an expert witness when needed.

For the contract we reviewed, OFLEO’s enforcement vendor employs statistics and economics experts who have advised government agencies and private-sector entities, including financial institutions, on a wide variety of issues that require quantitative expertise. The CFPB has supervisory oversight responsibility for some of these financial institutions, which may expose the agency to the risk of conflicts of interest. Specifically, the vendor’s business activities with financial institutions supervised by the CFPB may give rise to potential appearance issues for the agency, at a minimum, and could give rise to actual conflicts depending on the services provided by the vendor. OFLEO has planned for encountering an actual conflict of interest with a vendor by annually budgeting for an alternate vendor.

**Conflict of Interest Standards**

According to the *Federal Acquisition Regulation* (FAR),\(^5\) which the CFPB follows as a matter of policy, “Government business shall be conducted in a manner above reproach and, except as authorized by statute or regulation, with complete impartiality and with preferential treatment for none.”\(^6\) The FAR encourages strict avoidance of any conflicts of interest, including situations that may give rise to the appearance of a conflict of interest.

As the FAR states, an organizational conflict of interest may arise because (1) other activities or relationships with other persons may make a person unable, or potentially unable, to render impartial assistance or advice to the government; (2) the person’s objectivity in performing the contract work is or might be otherwise impaired; or (3) a person has an unfair competitive advantage.

The U.S. Government Accountability Office (GAO) has provided additional guidance for various situations that may pose a conflict of interest.\(^7\) GAO has identified *impaired objectivity* as one of three types of organizational conflicts of interest.\(^8\) Impaired objectivity conflicts of interest include cases in which a vendor’s work under one government contract

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5. The FAR is the primary regulation guiding federal executive agencies in their acquisition of supplies and services with appropriated funds. Although the CFPB has determined that it is not required to follow the FAR, the agency has made a policy decision to conduct all of its procurements in accordance with the FAR.

6. FAR 3.101-1.

7. Bidders or other interested parties may protest federal government procurement contract awards. GAO’s Procurement Law Division adjudicates those protests, providing agencies with additional examples and definitions of conflicts of interest.

8. The other two types of organizational conflicts of interest identified by GAO are unequal access to information and biased ground rules.
could entail evaluating itself, either through an assessment of performance under another contract or an evaluation of proposals. In these impaired objectivity cases, one concern to the government is that the vendor’s relationship with the firm whose work the vendor is evaluating could appear to undermine its ability to render impartial advice. We sought to assess whether the CFPB’s contract with an enforcement vendor created such a conflict.

In assessing whether a possible conflict exists, the FAR encourages agencies to examine each individual contracting situation on the basis of its particular facts and the nature of the proposed contract. It emphasizes that the exercise of common sense, good judgment, and sound discretion is required in determining whether a significant potential conflict exists and how to resolve it.

Managing Potential Vendor Conflicts of Interest

According to the FAR, procurement contracting officers must analyze planned acquisitions to

- identify and evaluate potential organizational conflicts of interest as early in the acquisition process as possible
- avoid, neutralize, or mitigate significant potential conflicts before contract award

The CFPB’s Vendor Communication Policy requires staff to avoid, neutralize, or mitigate to the maximum extent possible all conflicts of interest or appearances of such conflicts with vendors throughout the contract term.

The CFPB’s contracts for fair lending analysis require the vendor to prepare a detailed written disclosure of all actual conflicts, potential conflicts, or matters that may present the appearance of a conflict under the FAR prior to performing work under a new task order. The contracts also require the vendor to provide a detailed written plan explaining the steps the vendor will undertake to avoid or mitigate such conflicts.

The CFPB’s task order issuance process begins with a request for task order proposal (RTOP) submitted to the vendor by the contracting officer. The RTOP includes items such as the CFPB’s requirements for the project; the location of the work, as appropriate; the period of performance and any deliverable deadlines; and the task order proposal submission deadlines. Generally, the CFPB issues the corresponding task order within 7 days of the vendor’s response.

In its contracts, the CFPB informs the vendor that failure to make full and timely disclosure of actual, potential, or apparent conflicts of interest, as well as failure to comply with the FAR or CFPB conflicts of interest policies and procedures, are serious concerns. A vendor’s failure to comply with these contract provisions may result in corrective action, including termination of the contract for default or debarment of the contractor from federal contracting, among other potential actions.

For each contract, the procurement contracting officer designates a contracting officer’s representative (COR) in the relevant program office. This designation provides the COR with

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9. A task order must be issued before a vendor performs work under the associated contract. A task order contains the terms, conditions, and requirements of the work to be performed.
the authority to communicate technical direction to the vendor and recommend final acceptance or rejection of services to the contracting officer. The COR designation letter stipulates significant COR contract administration duties, including reporting to the contracting officer any suspected procurement fraud, bribery, conflicts of interest, or other improper conduct. For the CFPB’s contracts with its fair lending vendors, a contracting officer in the Procurement Office and the designated COR in OFLEO have shared responsibilities for identifying, evaluating, avoiding, and mitigating conflicts of interest.

The Federal Acquisition Institute’s (FAI) COR training guidelines recommend that CORs be able to identify potential conflicts of interest and, in certain cases, avoid those conflicts. The FAI has three levels of certification with varying requirements for training, experience, and continuous learning, depending on the contract type. Table 1 depicts the COR experience and training requirements for the three levels.

Table 1: COR Requirements by Level

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<th>COR level</th>
<th>Experience</th>
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<tr>
<td>Level I</td>
<td>None</td>
<td>8 hours</td>
<td>Low-risk contracts (e.g., supply contracts and orders)</td>
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<tr>
<td>Level II</td>
<td>1 year of previous COR experience required</td>
<td>40 hours</td>
<td>Moderate- to high-complexity contracts, including both supply and service contracts</td>
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<tr>
<td>Level III</td>
<td>2 years of previous COR experience required</td>
<td>60 hours</td>
<td>The most complex and mission-critical contracts in the agency</td>
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The FAI maintains a list of COR competencies, including those related to conflicts of interest, that distinguishes expected COR performance at each level. The competencies note that a Level I COR should be able to understand and identify potential conflicts of interest, and a Level II COR should be able to identify a potential conflict and understand how to avoid the conflict.

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10. The FAI maintains a list of essential COR competencies required to form the foundation for the knowledge, skills, and abilities to effectively perform as a COR. The CFPB expects its CORs to follow the FAI’s guidelines.
We found that the CFPB has not consistently documented its compliance with standards for managing conflicts of interest for the fair lending enforcement contract we reviewed.\textsuperscript{11} Specifically, the agency did not obtain conflict of interest disclosures or mitigation plans in conjunction with each task order. According to the contract, prior to work being performed under any new task order, the vendor should provide the agency with a detailed written disclosure of all actual conflicts, potential conflicts, or matters that may present the appearance of a conflict under the FAR. Additionally, in the event that the vendor has no conflicts of interest, certain task order documents require the vendor to submit a statement verifying this fact. We attribute this lapse in documentation to inconsistent enforcement of conflict of interest contractual provisions, inconsistent task order requirements, and a lack of clear roles and responsibilities for enforcing contract provisions. This documentation weakness could expose the agency to reputational and operational risk if a potential conflict of interest is not identified or mitigated prior to the enforcement vendor performing services that present an actual conflict or an appearance of a conflict. While the documentation weakness presents a vulnerability, based on our review of conflict of interest disclosures, task orders, and testimonial statements, we did not identify any actual conflicts of interest from June 2012 through January 2016.

The CFPB’s Conflict of Interest Documentation Was Insufficient

The CFPB Obtained Three Conflict of Interest Disclosures in Response to 16 Task Orders

During the period of our evaluation, from June 2012 through January 2016, the CFPB issued 16 task orders\textsuperscript{12} related to fair lending enforcement analysis services and obtained three conflict of interest disclosures from the vendor. The CFPB has not established a mandated method for obtaining conflict of interest disclosures; it has used three separate approaches when issuing task orders to the vendor: (1) not mentioning any financial institutions, (2) identifying specific financial institutions, or (3) including a list of 9 to 18 possible financial institutions to be assessed.

The CFPB signed the contract we reviewed in June 2012 and issued three task orders the same year without obtaining an associated conflict of interest disclosure from the vendor. Although two of these task orders specified the firm for vendor analysis, one did not identify the firms

\textsuperscript{11} Our evaluation focused on a CFPB contract for fair lending enforcement analysis and expert witness services, but we reference the CFPB’s conflict of interest management practices, rather than a particular division’s practices, where our findings and recommendations have broader applicability.

\textsuperscript{12} The CFPB issued one purchase order and 15 task orders under the relevant contract. For simplicity, we refer to each of these 16 documents as task orders throughout the report because both types of documents are materially similar.
on which the vendor was to conduct analysis,\footnote{According to one senior official, this practice allows the CFPB’s vendor more flexibility in selecting firms for fair lending analysis after task order issuance.} limiting the vendor’s ability to identify potential conflicts of interest in a timely manner. The CFPB first obtained a conflict of interest disclosure in January 2013, the same month it issued its fourth task order to the vendor. This disclosure listed three firms that could give rise to a possible conflict if the CFPB asked the vendor to perform any analysis related to those firms. OFLEO did not ask the vendor to perform work on any of these three firms. None of those three firms had been identified by the CFPB in previous task orders as firms that would or might require an analysis.

The agency issued nine additional task orders before receiving a second conflict of interest disclosure and the vendor’s first mitigation plan in February 2015.\footnote{Five of the nine task orders identified specific firms to be analyzed, and three identified 15 to 18 financial institutions that could require analysis. One of the nine task orders did not identify the firms on which the vendor was to conduct analysis.} The vendor’s second disclosure included eight financial institutions that could present a conflict. We noted that the CFPB included one of these eight firms on three task orders issued from September 2013 through September 2014. Because this firm was a client of the vendor’s starting in May 2013, the vendor should have disclosed this relationship at the issuance of each of these task orders so that the CFPB could avoid or mitigate any conflicts of interest. Instead, the vendor did not notify the CFPB of its relationship with the firm until submitting the February 2015 disclosure. Emails sent in April 2015 demonstrate that OFLEO took steps to follow up on the new disclosure. Although this firm was included in multiple task orders for potential analysis, OFLEO confirmed that the vendor never performed any work on the firm for the agency.

During the approximately 2-year interval between the vendor’s first and second conflict of interest disclosures, the lack of notice from the vendor about its business activities with firms supervised by the CFPB exposed the agency to the risk of actual conflicts of interest remaining undetected. Although we confirmed that the vendor did not perform work for the CFPB on the relevant firm, this situation and the lack of conflict of interest disclosures from the vendor from January 2013 through February 2015 highlight the importance of the agency actively enforcing the relevant contract provisions to anticipate, manage, and mitigate conflicts of interest. The agency issued three additional task orders from February 2015 through January 2016, obtaining a third conflict of interest disclosure and second mitigation plan in January 2016.

According to the contract, vendor disclosures must also include the vendor’s and any proposed or actual subcontractor’s or consultant’s past (up to 5 years) and current relationship to the firm that is the subject of the task order, or to any related entities of the firm. The CFPB first obtained documentation of the vendor’s prior work history in February 2015, after the agency issued 12 task orders. Figure 2 depicts a timeline of the task orders the CFPB issued and the conflict of interest disclosures and mitigation plans it obtained from the vendor.
The CFPB Did Not Consistently Require Its Vendor to Affirm That No Conflicts Exist

The CFPB did not consistently require the enforcement vendor to submit a statement in response to each task order affirming that the vendor had no conflicts of interest. The contract requires the enforcement vendor to identify and prepare a detailed written disclosure of conflicts prior to performing work under any new task order. In addition, some of the RTOP documents the CFPB issued require the vendor to issue a statement affirming that no conflicts of interest exist prior to performing work. However, the CFPB did not receive this affirmation for each task order that required one. We believe that not obtaining the vendor’s affirmation at the issuance of each task order inhibited conflict identification and mitigation. A senior official we interviewed agreed that requiring vendors to provide a response to each task order would improve the agency’s ability to identify conflicts of interest.

The CFPB First Obtained a Mitigation Plan From Its Enforcement Vendor in February 2015

As figure 2 shows, the CFPB obtained two mitigation plans from its enforcement vendor over the course of 16 task orders issued from July 2012 through January 2016. The agency first obtained a mitigation plan in February 2015, almost 3 years after the agency issued the first task order under the contract. The CFPB’s contract requires the vendor to submit a detailed written mitigation plan explaining any and all steps the vendor will undertake to avoid or mitigate conflicts of interest before performing any work under a new task order. The vendor submitted the same mitigation plan in January 2016.
Task Orders Did Not Always Identify Firms for Fair Lending Analysis

The CFPB can better facilitate conflict of interest identification and mitigation by ensuring that either task orders issued to the vendor or other documentation identify the firms for fair lending analysis. The CFPB’s contract with its fair lending vendor requires the vendor to identify and prepare a detailed written disclosure of conflicts of interest prior to performing work under a new task order. The agency’s issuance of two task orders that did not specify the financial institutions that the vendor may analyze does not facilitate accurate conflict of interest disclosures.

One official we interviewed stated that when a task order does not include specific firms for analysis, the process to ensure that no conflicts of interest exist as work is conducted under the task order takes on additional significance. The same official is confident that OFLEO has been properly mitigating the risk of potential conflicts of interest but stated that the CFPB should clarify the process and the various responsibilities for managing conflicts of interest. The agency’s current approach exposes the agency to reputational risk, because neither vendors nor the agency can reliably identify potential conflicts of interest at the time the task order is issued.

Unclear Roles and Responsibilities Contributed to Challenges in Managing Potential Conflicts of Interest

Because the CFPB has not consistently established conflict of interest documentation requirements, the enforcement vendor for the contract we reviewed has not strictly complied with relevant contract provisions. Lack of clarity about roles and responsibilities for identifying and mitigating potential conflicts of interest between vendors and firms undergoing analysis may have contributed to this situation. OFLEO and Procurement Office employees had differing views concerning who is responsible for identifying and mitigating conflicts of interest.

The FAR assigns responsibility to the contracting officer for identifying, avoiding, or mitigating significant potential conflicts of interest. Similarly, CFPB task orders specifying the work to be performed also state that the contracting officer in the Procurement Office is responsible for determining whether a contractor’s mitigation plan is acceptable. CFPB designation letters to the CORs in program offices, however, assign responsibility to the CORs for reporting suspected conflicts of interest. Further, according to FAI standards, CORs are responsible for identifying, and in certain cases mitigating, conflicts of interest.

Two OFLEO employees stated that rather than CORs focusing on potential conflicts of interest, their responsibilities are more administrative in nature, such as paying vendor invoices. This confusion reflects a lack of clear roles and responsibilities for identifying and mitigating potential conflicts of interest. We also spoke with OFLEO officials who identified multiple positions that share the responsibility for mitigating conflicts of interest, including positions in OFLEO and in the Procurement Office. We found that there is no CFPB policy, however, outlining the specific conflict of interest responsibilities of the program offices and the Procurement Office.
Several officials noted that the CORs’ primary job responsibilities are in their respective program offices and that serving as a COR is an additional duty. One OFLEO official said that the office does not hire staff with the expectation that they have contracting or procurement experience, and that OFLEO typically focuses on the execution of its mission rather than the operational or administrative aspects of contract management. This official also stated that there are no guidelines that explicitly outline the roles and responsibilities of the various positions involved in contracting. We heard conflicting information from various CFPB employees on which divisions or positions are responsible for identifying and mitigating potential conflicts of interest. As a result, the CFPB may not appropriately identify and mitigate possible conflicts of interest, potentially exposing the agency to reputational and operational risk.

Summary

The CFPB did not actively enforce its conflict of interest disclosure and mitigation requirements, potentially exposing the agency to the risk of a possible conflict remaining undetected and unmitigated. During our review, we identified one firm that was included on certain 2013 and 2014 task orders for potential fair lending analysis but that was only included in the vendor’s February 2015 conflict of interest disclosure. The vendor later notified the CFPB that it began working on a matter for this firm in May 2013. While we confirmed that the vendor did not perform work for the CFPB on this firm, this finding highlights the importance of the agency executing its expected control practices to ensure the vendor does not perform work on a firm when an appearance issue or actual conflict exists. We found that inconsistent documentation requirements and unclear roles and responsibilities contributed to these lapses.

Management Actions Taken

Before the issuance of our report, the agency finalized a conflicts of interest policy and procedures for staff managing contracting activities with vendors. The policy helps to clarify the roles and responsibilities among CFPB divisions for identifying and mitigating conflicts of interest and establishes documentation requirements for (1) all vendor communications regarding conflicts of interest and (2) decisions on conflict of interest–related matters. The policy also requires all contract solicitations, purchase orders, RTOPs, contracts, and other contract documents for service support contracts above a certain dollar threshold to include a standard conflict of interest clause. As a result, vendors must attest to whether they are aware of facts that create an actual conflict, a potential conflict, or the appearance of a conflict.

We also learned that the Procurement Office is in the process of hiring full-time CORs to assess the CFPB’s current contract management processes and make recommendations for improvements. After the CORs complete their initial assessments of existing practices, they may assist program office–level CORs in their management of contracts. We believe that this approach may address an issue we identified, particularly if the full-time CORs help to clarify the division of responsibilities across the CFPB for managing potential conflicts of interest.
Recommendations

We recommend that the Assistant Director for Procurement, in conjunction with the Associate Director of SEFL,

1. Update policies and procedures as they relate to identifying and mitigating potential or actual conflicts of interest, to
   a. clarify division-specific and job-specific roles and responsibilities for managing contracts.
   b. reinforce documentation requirements throughout the contract.

2. Develop a strategy to ensure that CORs have the required support to effectively identify and mitigate conflicts of interest.

3. Require that vendors submit a written response to each task order disclosing potential conflicts of interest or affirming that no conflicts of interest exist.

4. Determine an approach for specifying to vendors the firm or firms that may be subject to analysis at the issuance of each task order.

Management’s Response

In its response to our draft report, the CFPB concurs with recommendations 1, 2, 3, and 4. The agency notes that on January 4, 2017, the Office of the Chief Procurement Officer finalized a new policy that seeks to distinguish division-specific and job-specific roles and responsibilities for managing conflicts, reinforce documentation requirements, and require vendors to submit a written response to each task order disclosing potential conflicts or affirming that none exist. The agency also notes that it has recently hired five COR advisors who are available to assist CORs in meeting their responsibilities in managing contracts. Finally, the agency states that it will specify the firm or firms relevant to the scope of work at the issuance of each task order.

OIG Comment

We have reviewed documentation associated with the actions taken by the CFPB to address recommendations 1, 2, and 3. We believe that the agency has taken sufficient action to close these three recommendations. With respect to recommendation 4, the actions described by the CFPB appear to be responsive to the recommendation. We plan to follow up on the CFPB’s actions to ensure that recommendation 4 is fully addressed.
During our review period, the CFPB used both internal and external resources to perform fair lending enforcement analysis. Prior to awarding the initial contract for fair lending enforcement analysis and expert witness services, the CFPB did not formally evaluate the potential benefits and drawbacks of performing the work internally. Instead, during the agency’s formal Investment Review Board process to review the initial contract, it only considered either contracting the work out or not performing it at all. In addition, the CFPB requires program offices to complete a service contract code (SCC) determination worksheet for all new service contracts that assesses whether the work is inherently governmental. In completing this worksheet, the agency categorized the work to be performed by a fair lending enforcement vendor as “closely associated with inherently governmental functions,” because its attorneys use the vendor’s work product with other analyses to decide whether or how to pursue enforcement actions for fair lending violations. According to the SCC determination worksheet, agencies should perform such work internally to the maximum extent practicable. We believe that performing the analyses in-house would be the most effective way to mitigate the conflict of interest risk associated with this contract. According to the CFPB, it has performed this work internally in some matters, including an instance in which a vendor identified a potential appearance of a conflict. As of December 2016, however, the agency continues to engage external resources to perform fair lending enforcement analysis.

**The CFPB’s Investment Review Board Process Did Not Formally Consider Performing Fair Lending Enforcement Work Internally**

The information presented to the Investment Review Board in support of the CFPB’s investment in fair lending enforcement work included an analysis of alternatives to contracting the work out to a vendor. The alternatives presented did not include performing the work in-house. By contrast, the agency did consider performing the work internally during the formal review process for its investment in fair lending analysis for supervision activities.

15. The CFPB Investment Review Board is an executive advisory board body chaired by the Chief Financial Officer. The Investment Review Board must review and approve all CFPB investments above $500,000, unless they are deemed an “ongoing operating expense” by the Chair.

16. Before a procurement action for services is initiated, the relevant CFPB program office is required to submit an SCC determination worksheet to the Procurement Office and the Office of Human Capital. The Chief Human Capital Officer must then sign off on the procurement, ensuring that the action does not involve an inherently governmental function.
Transitioning More Fair Lending Enforcement Work In-House Would Reduce the Risk Associated With Potential Vendor Conflicts of Interest

The CFPB’s SCC determination worksheet stipulates that if a vendor performs work, as in the case of fair lending enforcement analysis, the CFPB must certify that the agency has sufficient internal capacity to oversee and manage the vendor’s activities and maintain control of its mission and operations. The CFPB must also certify that it has considered proper workforce balancing when fulfilling those requirements. Finally, it must attach a written analysis showing how it arrived at the decision to code the contract as “closely associated with inherently governmental functions.” This analysis should detail how the agency will maintain sufficient internal capability to oversee and manage contractor activities and maintain control of its mission and operations, including how the agency will avoid or mitigate conflicts of interest.

The CFPB did submit a written analysis with the SCC determination worksheet associated with the fair lending enforcement contract we reviewed; however, it did not address some of the applicable requirements. For example, the written analysis did not include a plan for addressing the responsibilities cited in the SCC determination worksheet, including the mitigation of potential conflicts of interest.

After initially contracting out some fair lending supervision analysis work, the agency has successfully transitioned all this work in-house and currently performs the work without assistance from vendors. The agency also has used in-house resources for some of its fair lending enforcement matters. During interviews with CFPB employees and senior officials, we discussed the possibility of a similar transition for more of the enforcement work that is currently outsourced. According to one CFPB official, transitioning the supervision work in-house entirely removed the risk associated with potential conflicts of interest between external parties and brought the added benefit of strengthening ties across CFPB divisions. The official stated that it is reasonable to assume that transitioning more of the enforcement work in-house would yield similar benefits. Another CFPB official stated that performing additional enforcement analysis internally would provide more opportunity for intra-agency collaboration through informal interactions among CFPB employees.

We discussed with CFPB officials the resource considerations associated with transitioning more of this work internally. According to officials in RMR, the division’s Office of Research has the capability but is not adequately staffed to perform the fair lending enforcement analysis currently performed externally. A CFPB official estimated that the agency would need to hire four or five additional economists and additional support staff to perform the enforcement analysis work internally and that the transition could take up to 2 years.

Although several officials acknowledged the potential benefits of performing more of the work internally, some raised concerns and cautioned against transitioning all such analysis in-house. Notably, multiple officials stated that engaging with vendors on an as-needed basis may provide the CFPB with more staffing flexibility. CFPB officials also noted that a vendor the agency has engaged is a recognized expert in the field of fair lending analysis and that the CFPB may have difficulty hiring and retaining people with such expertise. One official emphasized the benefit of engaging with a vendor that also performs work for some of the financial institutions that the CFPB supervises, stating that this practice provides the CFPB with valuable insights into industry perspective on enforcement matters. Further, several
officials noted that vendors may be best suited to serve as expert witnesses during any fair lending litigation.

We concur that the CFPB should consider the importance of resource flexibility and the expertise provided by a vendor when considering whether to transition more of the fair lending enforcement analysis in-house. However, as discussed in this report, using external resources to conduct fair lending enforcement analysis presents a risk of possible conflicts arising. In light of the control weaknesses previously noted in this report, we believe that the CFPB should evaluate the potential benefits and costs of transitioning more of the fair lending enforcement analysis work in-house.

**Recommendation**

We recommend that the Associate Director of RMR, in conjunction with the Associate Director of SEFL,

5. Evaluate the potential costs and benefits of performing more of the fair lending enforcement analysis internally.

**Management’s Response**

In its response to our draft report, the CFPB concurs with recommendation 5. According to the agency, it will evaluate the potential costs and benefits of performing more fair lending enforcement analysis internally.

**OIG Comment**

The actions described by the CFPB appear to be responsive to the recommendation. We plan to follow up on the CFPB’s actions to ensure that recommendation 5 is fully addressed.
After reviewing initial documentation associated with all CFPB fair lending contracts from the CFPB’s inception in July 2011 through January 2016, we decided to narrow our scope to focus on a specific contract for fair lending enforcement analysis and expert witness services. Because we focused on one contract pertaining to fair lending analysis, our findings may not be applicable to all CFPB contracting practices. We reference the CFPB’s practices more broadly in this report where our findings and recommendations pertain to multiple CFPB divisions.

In addition to this evaluation, the OIG is currently auditing the CFPB’s contract solicitation, selection, and award process. That audit focuses on assessing the CFPB’s compliance with the FAR and CFPB policy, as well as the effectiveness of the CFPB’s internal controls related to its contract solicitation, selection, and award processes. It includes a review of sole-source contracts awarded by the CFPB, such as the fair lending enforcement contract reviewed in this report. To minimize the duplication of efforts, we focused this evaluation on the CFPB’s management of potential conflicts of interest related to a fair lending enforcement vendor after contract award.

To accomplish our objective, we reviewed all contracts and task orders that the CFPB entered into for fair lending enforcement analysis from June 2012 through January 2016. This included a review of supplemental documentation, such as conflict of interest disclosures and mitigation plans from vendors that submitted proposals to the CFPB. Our evaluation also entailed reviewing applicable policies, procedures, and agency practices; meeting with CFPB employees and officials; reviewing vendor contracts; and reviewing documentation associated with the CFPB’s fair lending analyses and determinations.

We also reviewed correspondence between OFLEO and its vendor related to conflicts of interest. In addition, we interviewed senior officials from OFLEO and RMR as well as CFPB employees involved in the contracting process, including CORs, a contracting officer, and a project manager. We also interviewed executives from the CFPB’s vendor to obtain their insight on the CFPB’s mitigation of potential conflicts of interest related to its fair lending work.

Based on our review of conflict of interest disclosures and task orders issued as of January 2016, in addition to testimonial statements, we did not identify any actual conflicts of interest. In our comparison of the firms listed on the CFPB’s task orders and the firms listed on the enforcement vendor’s conflict of interest disclosures, we identified one firm that may have presented a potential conflict of interest. We confirmed with the CFPB that the enforcement vendor never performed any work for the CFPB related to this firm. Our scope did not include identifying potential or actual conflicts of interest related to the CFPB’s fair lending supervision contracts.
We conducted our fieldwork from March 2016 through August 2016. We performed our evaluation in accordance with the *Quality Standards for Inspection and Evaluation* issued in January 2012 by the Council of the Inspectors General on Integrity and Efficiency.
Appendix B
Management’s Response

March 10, 2017
Ms. Melissa Heist
Associate Inspector General for Audits and Evaluations
Board of Governors of the Federal Reserve System
Consumer Financial Protection Bureau
20th and Constitution Avenue
Washington, DC 20551

Dear Ms. Heist,

Thank you for the opportunity to review and comment on the Office of the Inspector General’s draft report “The CFPB Can Strengthen Its Controls for Managing Conflicts of Interest Related to Vendor Activities.”

We thank the OIG for conducting a thorough and detailed evaluation of the Bureau’s fair lending enforcement analyses contracts for potential conflicts of interest. The OIG did not identify any conflicts of interest as to the contracts it reviewed. The Bureau is committed to improving our internal procedures in order to ensure continuing avoidance of conflicts of interest and compliance with conflict of interest contracting guidelines. We have reviewed the report and concur with the draft recommendations.

Thank you again for your review. We provide the following comments for each recommendation.

Sincerely,
David Silberman
Acting Deputy Director, and
Associate Director,
Division of Research,
Markets and Regulations

David P. Gragan
Chief Procurement Officer and
Assistant Director, Office of the Chief Procurement Officer

c consumerfinance.gov
Recommendation 1. Update policies and procedures as they relate to identifying and mitigating potential or actual conflicts of interest, to
   a. clarify division-specific and job-specific roles and responsibilities for managing contracts;
   b. reinforce documentation requirements throughout the contract.

Recommendation 2. Develop a strategy to ensure that the contracting officer’s representatives have the required support to effectively identify and mitigate conflicts of interest.

Recommendation 3. Require that vendors submit a written response to each task order disclosing potential conflicts of interest or affirming that no conflicts of interest exist.

We concur with these recommendations. On January 4, 2017, the Office of the Chief Procurement Officer finalized a new CFPB policy entitled, ‘Conflicts of Interest Policy and Procedures for Contractors,’ (the “policy”), to ensure that: standardized Organizational Conflicts of Interest (OCI) contract clause language is included in all new CFPB solicitations and contracts for service support acquisitions; CFPB employees involved with contractors and acquisition functions are aware of the requirements for preventing, identifying, and reporting actual or potential OCIs; Contracting Officers are consulted as early in the process as possible in order to evaluate potential OCIs, and to avoid, neutralize, and/or mitigate OCIs; and that CFPB has an organization-wide culture of OCI awareness.

Specifically, the policy addresses Recommendation 1 a on clarifying division-specific and job-specific roles and responsibilities for managing conflicts in Sections III, IV and V, and directly distinguishes the roles for CFPB’s Contracting Officers (CO) and Contracting Officer’s Representatives (COR) with regard to OCI identification and mitigation in Section VI. The policy addresses Recommendation 1 b on reinforcing documentation requirements throughout the contract in Sections III, IV, V and VI. The policy addresses Recommendation 2 in Section VI and Recommendation 3 in Section IV.

With regard to Recommendation 2, the Bureau also provides support to CORs by the recent hires of five COR Advisors, who are available to assist CORs in meeting their responsibilities in managing the Bureau’s contracts. The Bureau also began holding monthly COR meetings in September 2011 to discuss acquisition topics in depth, including addressing OCI, and is in the process of revising the Desk Guide for CORs and Invoice Approvers, a reference that explains roles, responsibilities and resources for CORs. The new COR Advisors have already trained COR staff on the OCI policy and are updating the Desk Guide to include processes on handling OCI. The revised Desk Guide is expected to be issued in April, 2017.

Recommendation 4. Determine an approach for specifying to vendors the firm or firms that may be subject to analysis at the issuance of each task order.

We concur with this recommendation. The Division of Supervision, Enforcement, and Fair Lending, in coordination with the Office of the Chief Procurement Officer, will specify to vendors the firm or firms relevant to the scope of work at the issuance of each task order.

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Recommendation 5. Evaluate the potential costs and benefits of performing more of the fair lending enforcement analysis internally.

We concur with this recommendation. The Division of Research, Markets, and Regulations and the Division of Supervision, Enforcement, and Fair Lending will evaluate the potential costs and benefits of performing more fair lending enforcement analysis internally.
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