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BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

Examination Of The Federal Home Loan Bank Board's And Federal Savings And Loan Insurance Corporation's Financial Statements For The Years Ended December 31, 1983 And 1982

GAO examined the financial statements of the Federal Home Loan Bank Board and the Federal Savings and Loan Insurance Corporation for the years ended December 31, 1983 and 1982. The examinations were made in accordance with generally accepted government auditing standards.

In GAO's opinion, the financial statements present fairly the financial positions of the Board and Insurance Corporation as of December 31, 1983 and 1982, and the results of their operations and the changes in their financial positions for the years then ended, in conformity with generally accepted accounting principles.



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MAY 30, 1984

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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON D. C. 20548

May 30, 1984

B-206830

To the President of the Senate and the
Speaker of the House of Representatives

This report presents our opinion on the Federal Home Loan Bank Board's and the Federal Savings and Loan Insurance Corporation's financial statements for the years ended December 31, 1983 and 1982. We made our examinations pursuant to the provisions of 31 U.S.C. 9105 and in accordance with generally accepted government auditing standards. The Board supervises the activities of the Corporation; therefore, we included the Board's financial statements in our examination.

The Federal Home Loan Bank Board is an independent agency which formulates policies for and supervises the operation of the 12 Federal Home Loan Banks, the Federal Savings and Loan Insurance Corporation, and the system of federal savings and loan associations. The Federal Savings and Loan Insurance Corporation is a government corporation that insures the safety of savings in thrift and home financing institutions.

We are sending copies of this report to the Director of the Office of Management and Budget, the Secretary of the Treasury, and the Chairman of the Federal Home Loan Bank Board.

Charles A. Bowsher
Comptroller General
of the United States



COMPTROLLER GENERAL OF THE UNITED STATES

WASHINGTON D C 20548

May 30, 1984

B-206830

To the Board of Directors
Federal Home Loan Bank Board

We have examined the statements of condition of the Federal Home Loan Bank Board and the Federal Savings and Loan Insurance Corporation as of December 31, 1983 and 1982, and the related statements of income and expenses and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted government auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of the Federal Home Loan Bank Board and the Federal Savings and Loan Insurance Corporation as of December 31, 1983 and 1982, and the results of their operations and the changes in their financial positions for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

A handwritten signature in cursive script that reads "Charles A. Bowsher".

Comptroller General
of the United States

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REPORT ON INTERNAL ACCOUNTING CONTROLS
OF THE FEDERAL HOME LOAN BANK BOARD

As part of our examinations of the Federal Home Loan Bank Board's financial statements for the years ended December 31, 1983 and 1982, we made a study and evaluation of the system of internal accounting control to the extent we considered necessary to evaluate the system as required by generally accepted government auditing standards. This report pertains only to our study and evaluation of internal accounting controls for the year ended December 31, 1983. For the purpose of this report, we have classified the significant internal accounting controls in the following categories:

- assessments,
- expenditures,
- financial reporting, and
- payroll.

Our study included all of the control categories listed above except that we did not evaluate the accounting controls over financial reporting because it was more efficient to expand substantive audit tests. The purpose of our study and evaluation was to determine the nature, timing, and extent of the auditing procedures necessary for expressing an opinion on the Board's financial statements. Our study and evaluation were more limited than would be necessary to express an opinion on the system of internal accounting control taken as a whole or on any of the categories of controls identified above.

The management of the Federal Home Loan Bank Board is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any system of internal accounting control, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with the procedures may deteriorate.

Our study and evaluation made for the limited purpose described in the first paragraph would not necessarily disclose all material weaknesses in the system. Accordingly, we do not express an opinion on the system of internal accounting control of the Federal Home Loan Bank Board taken as a whole or on any of the categories of controls identified in the first paragraph. However, our study and evaluation disclosed no condition that we believe to be a material weakness.

REPORT ON THE FEDERAL HOME LOAN BANK BOARD'S
COMPLIANCE WITH LAWS AND REGULATIONS

We have examined the financial statements of the Federal Home Loan Bank Board for the years ended December 31, 1983 and 1982. Our examinations were made in accordance with generally accepted government auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures, including tests of compliance with laws and regulations, as we considered necessary in the circumstances. This report pertains only to our review of compliance with laws and regulations for the year ended December 31, 1983.

In our opinion, the Federal Home Loan Bank Board complied with the terms and provisions of laws and regulations for the transactions tested that could have materially affected the Board's financial statements.

Nothing came to our attention in connection with our examination that caused us to believe that the Board was not in compliance with the terms and provisions of laws and regulations for those transactions not tested.

FEDERAL HOME LOAN BANK BOARD
COMPARATIVE STATEMENT OF CONDITION
DECEMBER 31, 1983 AND 1982

<u>Assets</u>	<u>1983</u>	<u>1982</u>
Cash with U. S. Treasury.....	\$ 1,216,273	\$ 1,040,136
Accounts Receivable	12,558,209	10,922,669
Land and Building (Note 1).....	46,079,996	46,763,917
Furniture, Fixtures and Equipment (Note 1)....	4,010,858	3,897,307
Other.....	<u>351,155</u>	<u>262,557</u>
Total Assets.....	\$ 64,216,491 =====	\$ 62,886,586 =====
 <u>Liabilities and Capital</u>		
Accounts Payable and Accrued Liabilities.....	\$ 6,634,407	\$ 5,975,488
Employees Accrued Annual Leave.....	<u>3,307,842</u>	<u>3,341,464</u>
Total Liabilities.....	<u>9,942,249</u>	<u>9,316,952</u>
Retained Earnings (Notes 4 & 5).....	9,689,962	8,985,354
Paid in Capital - FHLBB Quarters (Note 3).....	<u>44,584,280</u>	<u>44,584,280</u>
Total Capital (Notes 4 & 5).....	<u>54,274,242</u>	<u>53,569,634</u>
Total Liabilities and Capital.....	\$ 64,216,491 =====	\$ 62,886,586 =====

The accompanying notes are an integral part of these financial statements.

FEDERAL HOME LOAN BANK BOARD
COMPARATIVE STATEMENT OF INCOME AND EXPENSES
FOR THE YEARS ENDED DECEMBER 31, 1983 and 1982

	<u>1983</u>	<u>1982</u>
<u>Income</u>		
Examination Fees from Savings and Loan Institutions..	\$16,171,990	\$13,286,880
Assessments:		
Federal Home Loan Banks.....	11,196,442	9,879,993
Federal Savings and Loan Insurance Corporation..	30,276,418	36,446,645
Savings and Loan Institutions.....	8,395,488	2,613,909
Rent and Miscellaneous Other.....	2,242,709	2,168,351
Total Income.....	<u>68,283,047</u>	<u>64,395,778</u>
 <u>Expenses</u>		
Personnel Compensation.....	42,610,772	41,957,576
Personnel Benefits.....	5,040,114	3,980,474
Travel and Transportation.....	8,313,093	7,022,615
Rent, Communication, and Utilities.....	4,506,866	4,599,963
Depreciation:		
Furniture, Fixtures, and Equipment.....	714,478	667,318
Building.....	859,698	958,579
Building Maintenance and Other Services.....	5,533,418	5,565,163
Total Expenses.....	<u>67,578,439</u>	<u>64,751,688</u>
Net Income (Loss).....	\$ 704,608 *****	\$ (355,910) *****

The accompanying notes are an integral part of these financial statements.

FEDERAL HOME LOAN BANK BOARD
COMPARATIVE STATEMENT OF CHANGES IN FINANCIAL POSITION
FOR THE YEARS ENDED DECEMBER 31, 1983 AND 1982

	<u>1983</u>	<u>1982</u>
<u>Source of Funds</u>		
Net Income.....	\$ 704,608	\$ (355,910)
Adjustment for Non-cash items:		
Depreciation.....	1,574,176	1,625,897
Prior Year Adjustment (Note 4).....	-0-	304,926
Decrease in Paid in Capital (Note 3)	-0-	(415,720)
Decrease (increase) in:		
Accrued Annual Leave.....	(33,622)	70,334
Funds Provided From Operations.....	<u>2,245,162</u>	<u>1,229,527</u>
Increase (decrease) in:		
Accounts Payable and Accrued		
Liabilities.....	658,919	(371,851)
Total Funds Provided.....	<u>2,904,081</u>	<u>857,676</u>
<u>Application of Funds</u>		
Acquisition of:		
Capital Assets.....	1,003,806	1,439,558
Other Assets (decrease).....	88,598	(73,044)
Increase (decrease) in:		
Accounts Receivable.....	1,635,540	(285,726)
Total Funds Applied.....	<u>2,727,944</u>	<u>1,080,788</u>
Increase (decrease) in cash.....	\$ 176,137 =====	\$ (223,112) =====

The accompanying notes are an integral part of these financial statements.

FEDERAL HOME LOAN BANK BOARD
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 1983 AND 1982

1. Summary of significant accounting policies:
 - a. Furniture, Fixtures and Equipment - These assets are at cost less accumulated depreciation of \$4,124,364 and \$3,436,909 at December 31, 1983 and 1982, respectively. Depreciation is computed on the straight-line method based on a 11 year useful life.
 - b. Land and Building - These assets are recorded at cost less accumulated depreciation for the building. Cost of land was \$10,165,227. Building costs at December 31, 1983 and 1982, were \$40,871,896 and \$40,696,119, less accumulated depreciation of \$4,957,127 and \$4,097,429, respectively. Depreciation for the building is computed on the straight-line method over 50 years.
 - c. The 1982 statement of changes in financial position was reclassified to be comparable to the 1983 format.
2. Related Party Transactions - The twelve District Federal Home Loan Banks (FHLBanks), together with their member institutions, comprise the FHLBank System. The FHLBank System is governed and regulated by the Federal Home Loan Bank Board (Bank Board) which is an independent federal agency in the executive branch of government. The Bank Board is the chartering and regulatory authority for the federal savings and loan associations and federal mutual savings banks. Further, the Bank Board, through the Federal Savings and Loan Insurance Corporation (FSLIC), governs the insurance of accounts in savings and loan associations and mutual savings banks. Bank Board expenses are met through assessments from the FHLBanks and the FSLIC and from member institutions for examinations. Accounts Receivable as of December 31, 1983 and 1982 for these assessments were: FHLBanks \$7,014,333 and \$6,065,539; FSLIC \$893,286 and \$2,106,059; and member institutions \$4,090,546 and \$2,312,365, respectively.
3. In 1974, the Board assessed the Federal Home Loan Banks \$40 million and, in 1977, another \$5 million for the total estimated cost to construct the Federal Home Loan Bank Board building located in Washington, D.C. Of the \$45 million assessed and classified as paid-in-capital, \$44,584,280 had been paid to the Board by the Banks. The General Services Administration has turned the building over to the Board. Therefore, the unpaid assessment of \$415,720 will not be required. Accordingly, the receivable was cancelled and paid-in-capital was reduced by this amount.

4. In October 1983, the Board implemented a new accounting system which enabled it to improve its practice of expensing some purchase orders before invoices had been received. Under its new system, the Board obligates purchase orders as they are issued and records expenses when invoices are received. In addition, the Board adjusted some 1982 expenses that had resulted from an inability to recognize inter-governmental billings in the year in which such expenses were incurred. The financial statements previously issued for 1982 have been restated as follows:

	<u>Previously Reported</u>	<u>Restated</u>
Other Assets	\$ 373,580	\$ 262,557
Accounts Payable and Accrued Liabilities	6,154,987	5,975,488
Retained Earnings	8,916,878	8,985,354
Building Maintenance and Other Services	5,328,713	5,565,163
Net (Loss)	(119,460)	(355,910)

5. The following is a summary of the Board's Capital:

	<u>1983</u>	<u>1982</u>
Retained Earnings at Beginning of Year		
As previously reported	\$8,916,878	\$9,036,338
Adjustments (Note 4)	68,476	304,926
As restated	<u>8,985,354</u>	<u>9,341,264</u>
Net Income (Loss)	704,608	(355,910)
Retained Earnings at End of Year	<u>9,689,962</u>	<u>8,985,354</u>
Paid-in-Capital at Beginning of Year	44,584,280	45,000,000
Assessment Cancellation (Note 3)	-0-	(415,720)
Paid-in-Capital at End of Year	<u>44,584,280</u>	<u>44,584,280</u>
Total Capital at End of Year	<u>\$54,274,242</u>	<u>\$53,569,634</u>

REPORT ON INTERNAL ACCOUNTING CONTROLS
OF THE FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION

As part of our examinations of the Federal Savings and Loan Insurance Corporation's financial statements for the years ended December 31, 1983 and 1982, we made a study and evaluation of the system of internal accounting control to the extent we considered necessary to evaluate the system as required by generally accepted government auditing standards. This report pertains only to our study and evaluation of internal accounting controls for the year ended December 31, 1983. For the purpose of this report, we have classified the significant internal accounting controls in the following categories:

- assistance to problem savings and loan associations,
- expenditures,
- financial reporting, and
- investments.

Our study included all of the control categories listed above except that we did not evaluate the accounting controls over assistance to problem savings and loan associations and financial reporting because it was more efficient to expand substantive audit tests. The purpose of our study and evaluation was to determine the nature, timing, and extent of the auditing procedures necessary for expressing an opinion on the Board's financial statements. Our study and evaluation were more limited than would be necessary to express an opinion on the system of internal accounting control taken as a whole or on any of the categories of controls identified above.

The management of the Federal Savings and Loan Insurance Corporation is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgements by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any system of internal accounting control, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with the procedures may deteriorate.

Our study and evaluation made for the limited purpose described in the first paragraph would not necessarily disclose all material weaknesses in the system. Accordingly, we do not express an opinion on the system of internal accounting control of the Federal Savings and Loan Insurance Corporation taken as a whole or on any of the categories of controls identified in the first paragraph. However, our study and evaluation disclosed no condition that we believe to be a material weakness.

REPORT ON THE FEDERAL SAVINGS AND LOAN INSURANCE
CORPORATION'S COMPLIANCE WITH LAWS AND REGULATIONS

We have examined the financial statements of the Federal Savings and Loan Insurance Corporation for the years ended December 31, 1983 and 1982. Our examinations were made in accordance with generally accepted government auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures, including tests of compliance with laws and regulations, as we considered necessary in the circumstances. This report pertains only to our review of compliance with laws and regulations for the year ended December 31, 1983.

In our opinion, the Federal Savings and Loan Insurance Corporation complied with the terms and provisions of laws and regulations for the transactions tested that could have materially affected the Corporation's financial statements.

Nothing came to our attention in connection with our examination that caused us to believe that the Corporation was not in compliance with the terms and provisions of laws and regulations for those transactions not tested.

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION
COMPARATIVE STATEMENT OF CONDITION
DECEMBER 31, 1983 AND 1982

	<u>1983</u>	<u>1982</u>
<u>Assets</u>		
Cash.....	\$ 1,160,313	\$ 202,632
Accounts Receivable.....	46,336,719	22,941,411
Investments (Notes 1 and 2).....	6,799,195,381	6,378,530,259
Interest Receivable on Investments.....	70,840,669	82,422,387
Loans to Insured Institutions.....	208,749,278	338,142,476
Interest Receivable on Loans to Insured Institutions.....	3,433,918	8,280,094
Subrogated Accounts in Insured Institutions	351,876,053	98,448,431
Less Allowance for Possible Future Losses (Note 3).....	108,800,000	-0-
Net Subrogated Accounts	<u>243,076,053</u>	<u>98,448,431</u>
Income Capital and Net Worth Certificates.....	850,100,000	441,800,000
Dividends Receivable on Net Worth Certificates.....	260,572	-0-
Less Allowance for Possible Future Losses.....	101,500,000	169,900,000
Net Certificates (Note 5).....	<u>748,860,572</u>	<u>271,900,000</u>
Mortgage Loans and Other Assets.....	253,277,765	375,417,897
Less Allowance for Possible Future Losses.....	27,638,989	40,440,587
Net Mortgage Loans and Other Assets (Note 1).....	<u>225,638,776</u>	<u>334,977,310</u>
Total Assets	<u>\$ 8,347,291,679</u>	<u>\$ 7,535,845,000</u>
<u>Liabilities and Reserves</u>		
Accounts Payable and Other Liabilities.....	\$ 33,358,958	\$ 25,381,027
Notes Payable to Insured Institutions (Note 6).....	842,603,148	456,503,030
Accrued Interest on Notes Payable.....	38,325,995	17,759,695
Allowance for Possible Future Losses Under		
Contribution Agreements (Note 4).....	1,007,582,054	705,358,127
Primary Reserve (Note 7 & 10).....	5,764,260,686	5,717,193,460
Secondary Reserve (Note 7).....	<u>661,160,838</u>	<u>613,649,650</u>
Total Liabilities and Reserves.....	<u>\$ 8,347,291,679</u>	<u>\$ 7,535,845,000</u>

The accompanying notes are an integral part of these financial statements.

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION
COMPARATIVE STATEMENT OF INCOME AND EXPENSE
FOR THE YEARS ENDED DECEMBER 31, 1983 AND 1982

	<u>1983</u>	<u>1982</u>
<u>Income</u>		
Insurance Premiums (Note 1).....	\$ 508,491,095	\$ 426,988,298
Interest on Investments.....	604,655,968	591,278,444
Interest on Loans to Insured Institutions....	20,200,094	33,982,328
Income on Mortgage Loans.....	28,194,774	24,183,608
Other Income	<u>931,050</u>	<u>1,351,148</u>
Total Income.....	<u>1,162,472,981</u>	<u>1,077,783,826</u>
<u>Expenses</u>		
Administrative Expenses.....	1,076,727	1,013,549
Net Loss on Sale of Securities	17,887,091	306,253
Services Rendered by The Federal Home Loan Bank Board (Note 8).....	30,276,417	36,446,645
Insurance Settlement and Other Expenses.....	83,590,983	41,842,674
Provision for Possible Future Losses:		
Contribution Agreements (Note 4).....	895,178,263	596,718,914
Mortgage Loans and Other Assets.....	5,000,000	56,883,388
Certificates.....	(68,400,000)	169,900,000
Subrogated Accounts (Net)(Note 3).....	<u>103,038,249</u>	<u>-0-</u>
Total Expenses.....	<u>1,067,647,730</u>	<u>903,111,423</u>
<u>Net Income from Operations</u>	<u>\$ 94,825,251</u>	<u>\$ 174,672,403</u>
Interest Applied to the Secondary Reserve (Note 7).....	<u>47,758,026</u>	<u>50,189,475</u>
<u>Net Income</u>	<u>\$ 47,067,225</u> =====	<u>\$ 124,482,928</u> =====

The accompanying notes are an integral part of these financial statements.

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION
STATEMENT OF CHANGES IN FINANCIAL POSITION
FOR THE YEARS ENDED DECEMBER 31, 1983 AND 1982

<u>Source of Funds:</u>	<u>1983</u>	<u>1982</u>
Net Income.....	\$ 47,067,225	\$ 124,482,928
Add (deduct) Items not Requiring, or Generating Cash:		
Depreciation of F&E.....	16,559	12,903
Provision for Losses on:		
Mortgage Loans.....	5,000,000	56,883,388
Certificates.....	(68,400,000)	169,900,000
Contributions.....	895,178,263	596,718,914
Subrogated Accounts.....	108,800,000	-0-
Return on Secondary Reserve.....	47,758,026	50,189,475
Transfer from Secondary Reserve.....	(189,802)	(35,691,577)
Amortization Income.....	(96,597,810)	(32,068,507)
Funds Provided from Operations.....	<u>938,632,461</u>	<u>930,427,524</u>
Increase (decrease) in:		
Notes Payable and Accrued Interest.....	406,666,414	387,530,427
Accounts Payable & Other Liabilities.....	7,977,931	(11,256,550)
Decrease in:		
Loans to Insured Institutions and Interest Receivable.....	134,239,374	43,567,946
Mortgage Loans & Other Assets.....	<u>105,807,758</u>	<u>43,271,567</u>
Total.....	<u>\$1,593,323,938</u>	<u>\$1,393,540,914</u>
 <u>Application of Funds:</u>		
Increase in:		
Subrogated Accounts.....	\$ 253,427,622	\$ 30,217,609
Income Capital & Net Worth Certificates.....	408,300,000	357,800,000
Investments and Interest Receivable.....	313,971,377	503,537,254
Accounts and Dividends Receivable.....	23,655,880	232,339
Amount Paid Under Contribution Agreements....	592,954,336	503,877,673
Refund of Secondary Reserve.....	<u>57,042</u>	<u>109,619</u>
Total.....	<u>\$1,592,366,257</u>	<u>\$1,395,774,494</u>
Increase (decrease) in Cash.....	\$ 957,681	\$ (2,233,580)
	=====	=====

The accompanying notes are an integral part of these financial statements.

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION
 NOTES TO FINANCIAL STATEMENTS, DECEMBER 31, 1983 AND 1982

1. Summary of significant accounting policies:

- a) Investments - Investment securities are stated at cost, adjusted for amortization of premiums and accretion of discounts. Such amortization and accretion are computed on the level yield method at rates based upon the lives of the related securities. Both amortization and accretions are recognized as an adjustment to Interest on Investments.
- b) Furniture and Equipment - These assets are stated at cost less accumulated depreciation. Depreciation is computed on the straight-line method over 11 years. The net balance of this account is insignificant and is included in Other Assets.
- c) Income Recognition - Insurance Premium Income is recognized as earned when member institutions are assessed.
- d) The 1982 Statement of Changes in Financial Position was reclassified to be comparable to the 1983 format.
- e) Generally the Provision for Possible Future Losses is recorded when a default prevention action is taken.

2. Investments - The Investments at December 31, 1983 and 1982 are:

	1983		1982	
	<u>Book Value</u>	<u>Market Value</u>	<u>Book Value</u>	<u>Market Value</u>
	(in thousands)		(in thousands)	
U.S. Treasury Obligations	\$ 5,927,154	\$ 5,548,621	\$ 5,257,882	\$ 4,961,138
Federal Agency Obligations	863,023	796,708	1,087,280	1,077,406
Other Investments	9,018	6,096	33,368	28,706
Total	<u>\$ 6,799,195</u>	<u>\$ 6,351,425</u>	<u>\$ 6,378,530</u>	<u>\$ 6,067,250</u>
	*****	*****	*****	*****

3. As required by Statute, the FSLIC liquidates institutions only when there is no default prevention measure that would be less costly than liquidation. In these cases, FSLIC settles insurance claims either by cash payout of insured accounts or by transferring insured accounts to another insured institution. In either case insurance payment is made in exchange for the account holder's claim against the assets of the defaulted institution. Subrogated Accounts represent the total of these outstanding claims. An Allowance for Possible Future Losses on Subrogated Accounts has been established in the amount of \$108,800,000 at December 31, 1983. The related provision of \$103,038,249 is the net amount of the loss allowance less \$5,761,751 in discounts earned on subrogated accounts required during 1983. As of December 31, 1982, no allowance for losses had been established.

4. The FSLIC makes contribution agreements to prevent default of an insured institution. Under some of these agreements the Corporation agrees to make, or commits itself to make, certain contributions over time. The changes in the Allowance for Possible Future Losses Under Contribution Agreements for the years ended December 31, 1983 and 1982 are:

	<u>1983</u>	<u>1982</u>
	(in thousands)	
Allowance for Possible Future Losses:		
Balance, Beginning of Year	\$ 705,358	\$ 612,517
Add: Provision Charged to Expense	895,178	596,719
Less: Contributions Paid	<u>592,954</u>	<u>503,878</u>
Balance, End of Year	\$ <u>1,007,582</u>	\$ <u>705,358</u>
	=====	=====

5. Since 1981 the FSLIC has purchased Income Capital Certificates (ICC's) from insured institutions. The FSLIC records the ICC's at cost. The ICC's earn annual income payments based on the United States Treasury Bill rates. The annual income payments and principal are redeemable upon the issuing institution having profitable operations and attaining a specified net worth level. The changes in the ICC's for the years ended December 31, 1983 and 1982 are:

	<u>1983</u>	<u>1982</u>
	(in thousands)	
Balance Beginning of Year	\$ 404,300	\$ 84,000
Add: Net Purchases During Year	<u>368,900</u>	<u>320,300</u>
	773,200	404,300
Less: Allowance for Possible Future Losses	<u>92,750</u>	<u>151,150</u>
Balance, End of Year	\$ <u>680,450</u>	\$ <u>253,150</u>
	=====	=====

In addition, since 1982 the FSLIC has purchased Net Worth Certificates (NWC's) from insured institutions as part of its default prevention activities. NWC's earn annual income payments based on the cost of Federal Home Loan Bank System Obligations plus 1/4 of one percent. Annual income and principal payments are redeemable upon the issuing

5. (Con't)

institution having profitable operations and attaining a specified net worth level. Such payments have been accrued for institutions meeting these requirements. The changes in the NWC's for the years ended December 31, 1983 and 1982 are:

	<u>1983</u>	<u>1982</u>
	(in thousands)	
Balance, Beginning of Year	\$ 37,500	\$ -0-
Add: Purchases During Year	39,400	37,500
Dividends Receivable	261	-0-
	<u>77,161</u>	<u>37,500</u>
Less: Allowance for Possible Future Losses	8,750	18,750
Balance, End of Year	<u>\$ 68,411</u>	<u>\$ 18,750</u>
	=====	=====

6. The FSLIC has issued negotiable notes to purchase ICC's and promissory notes to purchase NWC's in the amount of \$776,900,000. Variable interest is paid semiannually based on the cost of Federal Home Loan Bank System Obligations or the average auction yield for United States Treasury Notes with maturities from 5 - 10 years. In addition to issuing notes to purchase ICC's and NWC's, the FSLIC has also issued other negotiable notes to carry out its default prevention activities in the amount of \$65,703,148.
7. The FSLIC's total reserves available for losses consist of the Primary and Secondary Reserves. The Secondary Reserve is the equity of certain institutions in FSLIC based on premium prepayments and related interest not yet paid to these institutions. It is available for losses, but may also be paid back to the institutions depending on FSLIC's financial condition and management's anticipation of losses. Interest is credited to the Secondary Reserve based on the yield of FSLIC's investment portfolio. The Primary Reserve is the cumulative net income of the FSLIC since its inception less the interest applied to the Secondary Reserve.
8. Related Party Transactions - The Federal Home Loan Bank Board is an independent federal agency in the executive branch of government and governs the Federal Savings and Loan Insurance Corporation (FSLIC). The Bank Board assesses the FSLIC for services rendered. The principal function of the FSLIC is to insure accounts in savings and loan associations and federal mutual savings banks. In addition, the FSLIC may guarantee repayment of FHLBank advances that were made to certain insured institutions from time to time in its default prevention activities. These guarantees are

8. (Con't.)

typically granted on a short-term basis, generally covering advances that are totally secured. The amount of these advances as of December 31, 1983, totaled \$ 558.5 million, and \$523.5 million at December 31, 1982. The FSLIC considers the likelihood of ever incurring losses under these arrangements to be very remote. In the unlikely event that it would be called upon to honor these guarantees, the FSLIC would have claim against any assets pledged as collateral to secure such advances.

9. During 1983 the FSLIC changed its method of amortization of GNMA premiums and discounts from the sum of the years digits to the level yield method. In addition, a new accounting system was implemented which enabled it to improve the long-standing accounting practice of expensing some purchase orders before invoices had been received. Under the new system, purchase orders are obligated when issued and invoices are expensed when received. Furthermore, accrued interest on notes payable is reported as a separate line item in the 1983 financial statements. In 1982 it was classified as part of accounts payable and other liabilities. The financial statements previously issued for 1982 have been restated as follows:

	<u>Previously Reported</u>	<u>Restated</u>
Investments	\$6,354,939,104	\$6,378,530,259
Accounts Payable and Other Liabilities	43,073,295	25,381,027
Accrued Interest on Notes Payable	-0-	17,759,699
Primary Reserve	5,693,669,737	5,717,193,461
Interest on Investments	603,591,599	591,278,444
Insurance Settlement and Other Expenses	41,775,243	41,842,674
Net Income	136,863,514	124,482,928

10. The following is a summary of the FSLIC's Primary Reserve:

	<u>1983</u>	<u>1982</u>
Primary Reserve at Beginning of Year		
As Previously Reported	\$ 5,693,669,737	\$ 5,556,806,223
Prior Period Adjustments	23,523,724	35,904,310
As Restated	<u>5,717,193,461</u>	<u>5,592,710,533</u>
Net Income	47,067,225	124,482,928
Primary Reserve at End of Year	<u>\$ 5,764,260,686</u> =====	<u>\$ 5,717,193,461</u> =====

11. Subsequent Event - On January 20, 1984, the FSLIC executed contribution agreements to facilitate the rehabilitation of certain institutions. These agreements will necessitate the cancelling of \$125,500,000 in Income Capital Certificates and \$102,500,000 in Notes Payable to Purchase Income Capital Certificates. The remaining \$23,000,000 will be applied against Allowance for Possible Future Losses Under Contributions.
12. Given the state of the economy and present condition of the industry, it is possible that FSLIC could sustain additional losses in subsequent accounting periods due to its default prevention actions. Because many of the causes for default are beyond management's control, the amount of these losses cannot be determined. However, the Corporation believes that its resources, including the right to increase insurance premiums, are sufficient to absorb any such losses over the foreseeable future.

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