July 1996

FINANCIAL AUDIT

Resolution Trust Corporation’s 1995 and 1994 Financial Statements
To the President of the Senate and the Speaker of the House of Representatives

This report presents our opinions on the financial statements of the Resolution Trust Corporation (RTC) for the years ended December 31, 1995 and 1994. This report also presents our opinion on RTC management’s assertions regarding the effectiveness of its system of internal controls on December 31, 1995, and our evaluation of compliance with laws and regulations. We conducted our audits pursuant to the provisions of section 21A(k)(1) of the Federal Home Loan Bank Act (12 U.S.C. 1441a(k)(1)) and in accordance with generally accepted government auditing standards.

The report also discusses (1) an internal control weakness we identified, (2) the savings and loan crisis and the creation of RTC, (3) the completion of RTC’s mission, (4) RTC’s costs and funding, (5) RTC’s contracting, (6) the cost of resolving the savings and loan crisis, and (7) remaining fiscal implications of the crisis.

We are sending copies of this report to the Chairman and members of the Thrift Depositor Protection Oversight Board; the Chairman of the Board of Directors of the Federal Deposit Insurance Corporation; the Director of the Office of Management and Budget; the Chairmen and Ranking Minority Members of the Senate Committee on Governmental Affairs, the House Committee on Government Reform and Oversight, the Senate Committee on Banking, Housing and Urban Affairs, and the House Committee on Banking and Financial Services; and other interested parties.

This report was prepared under the direction of Robert W. Gramling, Director, Corporate Audits and Standards, who may be reached at (202) 512-9406 if you or your staff have any questions. Major contributors to this report are listed in appendix IV.

Charles A. Bowsher
Comptroller General
of the United States
## Abbreviations

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>FDIC</td>
<td>Federal Deposit Insurance Corporation</td>
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<tr>
<td>FICO</td>
<td>Financing Corporation</td>
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<tr>
<td>FIRREA</td>
<td>Financial Institutions Reform, Recovery, and Enforcement Act of 1989</td>
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<td>FMFIA</td>
<td>Federal Managers’ Financial Integrity Act of 1982</td>
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<td>FRF</td>
<td>FSLIC Resolution Fund</td>
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<td>FSLIC</td>
<td>Federal Savings and Loan Insurance Corporation</td>
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<td>REFCORP</td>
<td>Resolution Funding Corporation</td>
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<td>RTC</td>
<td>Resolution Trust Corporation</td>
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<td>SAIF</td>
<td>Savings Association Insurance Fund</td>
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To the Thrift Depositor Protection
Oversight Board

We have audited the Resolution Trust Corporation’s (RTC) statements of financial position as of December 31, 1995 and 1994, and the related statements of revenues, expenses, accumulated deficit, and cash flows for the years then ended as reported by the Federal Deposit Insurance Corporation (FDIC).¹ We found:

- RTC’s financial statements referred to above were reliable in all material respects.
- Although internal controls should be improved, RTC management fairly stated that internal controls in place on December 31, 1995, were effective in safeguarding assets from material loss, assuring material compliance with relevant laws and regulations, and assuring that there were no material misstatements in the financial statements.
- No reportable noncompliance with laws and regulations we tested.

The following section discusses each of the above conclusions in more detail. In addition, with the termination of RTC on December 31, 1995, an important phase of the savings and loan crisis has ended. Accordingly, the report also presents an historical perspective on the savings and loan crisis and RTC, the costs of the crisis, and remaining fiscal implications of the crisis.

Appendix I presents RTC’s financial statements. Appendix II presents RTC management’s report on internal controls. FDIC’s written comments on a draft of this report are included in appendix III. Major contributors to this report are included in appendix IV.

Opinion on Financial Statements

The financial statements including the accompanying notes present fairly, in all material respects, in accordance with generally accepted accounting principles, the Resolution Trust Corporation’s

- assets, liabilities, and equity;
- revenues, expenses, and accumulated deficit; and
- cash flows.

¹RTC’s final day of operation was December 31, 1995, and all of RTC’s assets and liabilities were transferred to the Federal Deposit Insurance Corporation’s FSLIC Resolution Fund. FDIC also assumed responsibility for RTC’s financial records and systems, and for preparing RTC’s final financial statements.
However, misstatements may nevertheless occur in other RTC-related financial information as a result of the internal control weakness described below.

Opinion on RTC Management’s Assertion About the Effectiveness of Internal Controls

We evaluated RTC management’s assertion about the effectiveness of its internal controls designed to

- safeguard assets against loss from unauthorized acquisition, use, or disposition;
- assure the execution of transactions in accordance with management’s authority and with laws and regulations that have a direct and material effect on the financial statements; and
- properly record, process, and summarize transactions to permit the preparation of reliable financial statements and to maintain accountability for assets.

RTC management fairly stated that those controls in place on December 31, 1995, provided reasonable assurance that losses, noncompliance, or misstatements material in relation to the financial statements would be prevented or detected on a timely basis. RTC management made this assertion, which is included in appendix II, based upon criteria established under the Federal Managers’ Financial Integrity Act of 1982 (FMFIA). RTC management, in making its assertion, recognized the need to improve internal controls. Our work also identified the need to improve internal controls, as described in the following section. The weakness in internal controls, although not considered a material weakness, represents a significant deficiency in the design or operation of internal controls which could have adversely affected RTC’s ability to fully meet the internal control objectives listed above.2

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2Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal controls that, in the auditor’s judgment, could adversely affect an entity’s ability to (1) safeguard assets against loss from unauthorized acquisition, use, or disposition, (2) ensure the execution of transactions in accordance with management’s authority and in accordance with laws and regulations, or (3) properly record, process, and summarize transactions to permit the preparation of financial statements and to maintain accountability for assets. A material weakness is a reportable condition in which the design or operation of the internal controls does not reduce to a relatively low level the risk that losses, noncompliance, or misstatements in amounts that would be material in relation to the financial statements may occur and not be detected within a timely period by employees in the normal course of their assigned duties. Reportable conditions which are not considered to be material nevertheless represent significant deficiencies in the design or operation of internal controls and need to be corrected by management.
RTC acted during 1995 to resolve the reportable condition related to the weaknesses in general controls over some computerized information systems identified in our audit of its 1994 financial statements. However, as reported by RTC, many of those corrective actions were not completed until late in 1995. In addition, our audit of RTC’s 1995 financial statements identified additional weaknesses related to general controls over its computerized systems such that this reportable condition continued to exist.

Because RTC relied on its computerized information systems extensively, both in its daily operations and in processing and reporting financial information, the effectiveness of general controls is a significant factor in ensuring the integrity and reliability of financial data. Because corrective actions for many of the general control weaknesses identified in our 1995 and 1994 audits were not implemented until late 1995 and early 1996, our audit found that general controls still did not provide adequate assurance that some of RTC data files and computer programs were fully protected from unauthorized access and modification.

In response to the weaknesses we identified, RTC and FDIC developed action plans to address the weaknesses. Prior to the completion of our audit work on June 7, 1996, FDIC reported that most of the corrective actions had been implemented, with those remaining scheduled for implementation by September 30, 1996. We plan to evaluate the effectiveness of the corrective actions as part of our 1996 audit of FDIC.

During 1995, RTC performed accounting and control procedures, such as reconciliations and manual comparisons, which would have detected material data integrity problems resulting from inadequate general controls. Without these procedures, weaknesses in the general controls would raise significant concern over the integrity of the information obtained from the affected systems.

Other less significant matters involving the internal control structure and its operation noted during our audit will be communicated separately to FDIC’s management, which assumed responsibility for RTC’s remaining assets and liabilities since RTC’s termination on December 31, 1995.

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3General controls are policies and procedures that apply to an entity’s overall effectiveness and security of operations which create the environment in which application controls and certain user controls operate. General controls include the organizational structure, operating procedures, software security features, system development and change control, and physical safeguards designed to ensure that only authorized changes are made to computer programs, that access to data is appropriately restricted, that back-up and recovery plans are adequate to ensure the continuity of essential operations, and that physical protection of facilities is provided.
Compliance With Laws and Regulations

Our tests for compliance with selected provisions of laws and regulations disclosed no instances of noncompliance that would be reportable under generally accepted government auditing standards. However, the objective of our audit was not to provide an opinion on the overall compliance with laws and regulations. Accordingly, we do not express such an opinion.

The Savings and Loan Crisis: Historical Perspective and Fiscal Implications

With the termination of RTC’s operations on December 31, 1995, a significant phase of the savings and loan crisis has ended. The following sections present an historical perspective on the savings and loan crisis and RTC’s role in resolving the crisis. Specifically, the information describes (1) background on the savings and loan crisis and the creation of RTC, (2) the completion of RTC’s mission, (3) RTC’s estimated costs and funding, (4) RTC’s controls over contracting, (5) the cost of resolving the savings and loan crisis, and (6) remaining fiscal implications of the crisis.

The Savings and Loan Crisis and RTC

During the 1980s, the savings and loan industry experienced severe financial losses because extremely high interest rates caused institutions to pay high rates on deposits and other funds while earning low yields on their long-term loan portfolios. During this period, regulators reduced capital standards and allowed the use of alternative accounting procedures to increase reported capital levels. While these conditions were occurring, institutions were allowed to diversify their investments into potentially more profitable, but risky, activities. The profitability of many of these activities depended heavily on continued inflation in real estate values to make them economically viable. In many cases, diversification was accompanied by inadequate internal controls and noncompliance with laws and regulations, thus further increasing the risk of these activities.

As a result of these factors, many institutions experienced substantial losses on their loans and investments, a condition that was made worse by an economic downturn. Faced with increasing losses, the industry’s insurance fund, the Federal Savings and Loan Insurance Corporation (FSLIC), began incurring losses in 1984. By the end of 1987, 505 savings and loan institutions were insolvent. The industry’s deteriorating financial condition overwhelmed the insurance fund which only 7 years earlier reported insurance reserves of $6.5 billion. In 1987, the Congress responded by creating the Financing Corporation (FICO) to provide financing to the FSLIC through the issuance of bonds. Through August 8, 1989, FICO provided $7.5 billion in financing to the FSLIC; however, the
insurance fund required far greater funding to deal with the industry’s problems.

In response to the worsening savings and loan crisis, the Congress enacted the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) on August 9, 1989. FIRREA abolished FSLIC and transferred its assets, liabilities, and operations to the newly-created FSLIC Resolution Fund (FRF) to be administered by the FDIC. In addition, FIRREA created a new insurance fund, the Savings Association Insurance Fund (SAIF).

FIRREA also created the RTC to resolve all troubled institutions placed into conservatorship or receivership from January 1, 1989, through June 30, 1995. RTC’s overall responsibilities included managing and disposing of receivership assets and recovering taxpayer funds. In 1993, the Resolution Trust Corporation Completion Act required RTC to cease its operations on or before December 31, 1995, and transfer any remaining assets and liabilities to the FSLIC Resolution Fund.

FIRREA provided RTC with a total of $50 billion in funding to resolve failed institutions and pay related expenses. FIRREA also established the Resolution Funding Corporation (REFCORP) to provide RTC with $30 billion of the $50 billion in funding through the issuance of bonds. However, funding provided to RTC by FIRREA was not sufficient and the Congress enacted subsequent legislation resulting in a total of $105 billion being made available to RTC to cover losses associated with resolutions.

RTC’s Mission Substantially Completed

RTC closed 747 institutions with $402 billion in book value of assets when they entered the conservatorship phase. During conservatorship, assets were reduced by $162 billion to $240 billion through sales, collections, and

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4The funds needed to settle FSLIC’s remaining liabilities were provided from a variety of sources, including appropriations from the general fund of the Treasury (hereafter referred to as appropriations), industry assessments, and recoveries from asset sales.

5FIRREA created RTC to manage and resolve all troubled institutions that were previously insured by FSLIC and for which a conservator or receiver was appointed during the period January 1, 1989, through August 8, 1992. This period was extended to September 30, 1993, by the Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991. In December 1993, the period was again extended to a date not earlier than January 1, 1995, nor later than July 1, 1995 by the Resolution Trust Corporation Completion Act. The final date of June 30, 1995, was selected by the Chairperson of the Thrift Depositor Protection Oversight Board.

6The Resolution Trust Corporation Funding Act of 1991 provided an additional $30 billion. The Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991 provided $25 billion in December 1991, which was only available for obligation until April 1, 1992. In December 1993, the RTC Completion Act removed the April 1, 1992, deadline, thus making the balance of the $25 billion available to RTC for resolution activities.
other adjustments. In the receivership phase, assets were further reduced by $232 billion. Thus, at December 31, 1995, RTC assets in liquidation totaled approximately $8 billion. The remaining assets were transferred to the FSLIC Resolution Fund effective January 1, 1996.

RTC also fulfilled the government’s pledge to insured depositors by protecting 25 million depositor accounts. Of the $277 billion in liabilities at resolution, approximately $221 billion represented liabilities to depositors. At resolution, RTC generally transferred the deposit liabilities, along with the required funding, to one or more healthy acquiring institutions. During the receivership phase, RTC used asset recoveries to pay the remaining creditors, and to recover a portion of the amount it advanced to cover deposit liabilities.

Another important part of RTC’s activities included ensuring that as many thrift violators as possible were brought to justice and that funds were recovered on behalf of taxpayers. RTC investigated, initiated civil litigation, and made criminal referrals in cases involving former officers, directors, professionals, and others who played a role in the demise of failed institutions. Approximately $2.4 billion was recovered from professional liability claims, and $26 million was collected in criminal restitution.

RTC’s Estimated Costs and Funding

As of December 31, 1995, RTC estimated that the total cost for resolving the 747 failed institutions was $87.9 billion. These costs represent the difference between recoveries from receivership assets and the amounts advanced to pay depositors and other creditors of failed institutions plus the expenses associated with resolving institutions. As shown in table 1, $81.3 billion, or 92 percent, of RTC’s total estimated costs have already been realized through December 31, 1995, and therefore, are known. The estimated $6.6 billion remaining at December 31, 1995, represents expected future losses on remaining receivership and corporate assets. The ultimate recoveries on those assets are subject to uncertainties.
Losses of $72.2 billion were realized while institutions were in receivership and after termination. Receivership losses were realized when amounts realized from asset sales were not sufficient to repay the amounts advanced by RTC. For those institutions that were terminated, RTC realized further losses if it later sold assets for less than the price it paid when it purchased the assets from the receiverships at termination.

RTC borrowed working capital funds from the Federal Financing Bank (FFB) to provide funding for insured deposits and to replace high-cost borrowing of the failed institutions. In general, these funds were expected to be repaid with the proceeds from receivership asset sales, with any shortfall being covered by loss funding. Through December 31, 1995, RTC incurred $10.2 billion in interest expense on amounts borrowed from the FFB for working capital.

RTC’s administrative expenses represent overhead expenses not otherwise charged or billed back to receiverships. The portion of expenses billed back to receiverships is not included in RTC’s administrative expense total, but is included in the loss from receiverships. In addition, receiverships pay many other expenses directly which are also included in the losses from receiverships. The estimated $6.6 billion of future costs include expected losses from receiverships and terminations as well as estimated future administrative expenses.

In total, the Congress provided funding to cover $105 billion of losses and expenses associated with RTC’s resolution of failed institutions. As shown in table 2, after reducing the $105 billion available for RTC’s estimated losses of $87.9 billion, an estimated $17.1 billion in unused loss funds will remain.
Table 2: Estimated Unused Loss Funds After Completion of RTC’s Resolution Activities

<table>
<thead>
<tr>
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<th>Dollars in billions</th>
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<tbody>
<tr>
<td>Total loss funds provided</td>
<td>$105.0</td>
</tr>
<tr>
<td>Less: Total estimated loss funds</td>
<td>(87.9)</td>
</tr>
<tr>
<td><strong>Estimated unused loss funds</strong></td>
<td><strong>$17.1</strong></td>
</tr>
</tbody>
</table>

The final amount of unused loss funds will not be known with certainty until all remaining assets and liabilities are liquidated. Loss funds not used for RTC resolution activity are available until December 31, 1997, for losses incurred by the SAIF, if the conditions set forth in the Resolution Trust Corporation Completion Act are met. Also, according to the act, unused loss funds will be returned to the general fund of the Treasury.

Controls Over Contracting May Have Affected Receivership Recoveries

RTC used thousands of private contractors to manage and dispose of assets from failed thrifts, including activities such as collecting income and paying expenses. The estimated recoveries from receiverships included in RTC’s financial statements include the receipts collected and disbursements made by contractors that perform services for receiverships. As we previously reported, weak operating controls over contract issuance and contractor oversight may have affected the amounts RTC ultimately recovered from its receiverships. While we assess, as part of our financial statement audit, internal accounting controls over receivership receipts and disbursements, RTC’s operating controls over contract issuance and contractor oversight are not part of the scope of our audit. These operating controls were reviewed by RTC’s Inspector General and Office of Contract Oversight and Surveillance, as well as by GAO in other reviews.

RTC took various actions to improve the process of contract issuance and contractor oversight, and had placed increased emphasis on the process of

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7 The RTC Completion Act makes available to SAIF, during the 2-year period beginning on the date of RTC’s termination, any of the $18.3 billion in appropriated funds made available by the RTC Completion Act and not needed by RTC. However, prior to receiving such funds, FDIC must first certify, among other things, that SAIF cannot fund insurance losses through industry premium assessments or Treasury borrowings without adversely affecting the health of its member institutions and causing the government to incur greater losses.


closing out contracts to ensure that contractors have fulfilled all contractual responsibilities. However, results of audits conducted by RTC’s Inspector General and Office of Contract Oversight and Surveillance demonstrated that despite RTC’s actions to correct contracting problems, the effects of early neglect of contracting operations remained. These audits identified internal control problems with RTC’s auction contracts and with RTC’s general oversight of contractors. These audits also identified significant performance problems with contracts that were issued before many contracting reforms and improvements were implemented by RTC.

During 1995, RTC closed many contracts, pursued contract audit resolution, identified contracts necessary to accomplish the remaining workload after RTC’s termination, and processed contract modifications to transfer them to FDIC. However, estimated future recoveries from RTC receiverships remain vulnerable to the risks associated with early weaknesses in contractor oversight and performance. As a result of these operating weaknesses, RTC could not be sure that it has recovered all it should have recovered from its receiverships.

RTC’s costs for its responsibilities in resolving the savings and loan crisis represent only a portion of the total costs of the savings and loan crisis. The cost associated with FSLIC assistance and resolutions represents another sizable direct cost. In addition, the total cost includes indirect costs related to tax benefits granted in FSLIC assistance agreements.

RTC’s contracting manual states that a contract closeout includes, among other things, a determination by the contracting officer that (1) all deliverables, including reports, have been received by RTC and accepted, (2) final payment has been made, (3) all collections of funds due to RTC have been completed, (4) all financial documents are in the file, (5) all RTC property has been returned and accounted for, and (6) all RTC files have been returned.
Table 3: Estimated Direct and Indirect Costs of Resolving the Savings and Loan Crisis and Related Funding Sources

<table>
<thead>
<tr>
<th>Funding source</th>
<th>Total</th>
<th>Taxpayers</th>
<th>Private sources</th>
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</thead>
<tbody>
<tr>
<td><strong>Direct costs</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Resolution Trust Corporation</td>
<td>$ 87.9</td>
<td>$ 81.9</td>
<td>$ 6.0</td>
</tr>
<tr>
<td>FSLIC costs</td>
<td>64.7</td>
<td>42.7</td>
<td>22.0</td>
</tr>
<tr>
<td>Supervisory goodwill claims</td>
<td>___</td>
<td>___</td>
<td>___</td>
</tr>
<tr>
<td><strong>Total direct costs</strong></td>
<td>$152.6</td>
<td>$124.6</td>
<td>$28.0</td>
</tr>
<tr>
<td><strong>Indirect costs</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tax benefits under FSLIC assistance agreements</td>
<td>7.5</td>
<td>7.5</td>
<td>0.0</td>
</tr>
<tr>
<td><strong>Total indirect costs</strong></td>
<td>$ 7.5</td>
<td>$ 7.5</td>
<td>$ 0.0</td>
</tr>
<tr>
<td><strong>Total estimated direct and indirect costs</strong></td>
<td>$160.1</td>
<td>$132.1</td>
<td>$28.0</td>
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Note: Excluded from this table are the interest expenses associated with financing the direct costs of the crisis. See tables 4 and 5, and associated discussion for further information on interest expense.

Of the $160.1 billion in total direct and indirect costs, approximately $132.1 billion, or 83 percent was provided from taxpayer funding sources. The remaining $28.0 billion, or 17 percent was provided from industry assessments and other private sources. (See Figure 1.)
Direct Costs

As shown in table 3, the direct costs associated with resolving the savings and loans crisis include the cost of RTC resolutions, FSLIC activity, and supervisory goodwill claims. All of the funding for the estimated $152.6 billion in estimated costs related to FSLIC and RTC has been provided as of December 31, 1995. However, the cost of the claims is currently uncertain.

Resolution Trust Corporation

RTC resolved 747 failed institutions through June 30, 1995, when its authority to close failed thrifts expired. As of December 31, 1995, the total estimated losses associated with RTC’s resolved institutions is $87.9 billion. Taxpayer funding for RTC’s direct costs is estimated to be $81.9 billion, which is made up of $56.6 billion in appropriations and $25.3 billion related to the government’s responsibility attributable to the REFCORP.
transaction. The private sources of funding for RTC activity totaled $6.0 billion, consisting of $1.2 billion contributed to RTC from the Federal Home Loan Banks, and $4.8 billion from SAIF and the Federal Home Loan Banks to support the REFCORP transaction.

FSLIC Costs

As of December 31, 1995, the total estimated costs associated with FSLIC activity was $64.7 billion. The estimated cost includes expenses and liabilities arising from FSLIC assistance provided to acquirers of failed or failing savings and loan institutions and FSLIC resolution activity since January 1, 1986. Taxpayer funding for FSLIC’s costs consists of appropriations used by the FSLIC Resolution Fund and totaled $42.7 billion. The private sources of funding for the FSLIC costs include $13.8 billion from FSLIC capital and industry assessments and $8.2 billion provided by FICO.

Supervisory Goodwill Claims

An additional cost of the savings and loan crisis results from the federal government’s legal exposure related to supervisory goodwill and other forbearances from regulatory capital requirements granted to the acquirers of troubled savings and loan institutions in the 1980s. As of December 31, 1995, there were approximately 120 pending lawsuits which stem from legislation that resulted in the elimination of supervisory goodwill and other forbearances from regulatory capital. These lawsuits assert various legal claims including breach of contract or an uncompensated taking of property resulting from the FIRREA provisions regarding minimum capital requirements for thrifts and limitations as to the use of supervisory goodwill to meet minimum capital requirements. One case has resulted in a final judgment of $6 million against FDIC, which was paid by FRF.

On July 1, 1996, the United States Supreme Court concluded that the government is liable for damages in three other cases in which the changes

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11The REFCORP financing transaction is a hybrid transaction, supported by both taxpayer and private industry funding. REFCORP was established with the sole purpose of borrowing funds to finance savings and loan resolutions. A principal redemption fund was established using funds contributed by the Federal Home Loan Banks and SAIF. Annual interest expense on the REFCORP bonds is being paid mainly through appropriations, along with annual contributions from the Federal Home Loan Banks. REFCORP provided funding to RTC for resolution losses by issuing $30.0 billion of noncallable, 30- and 40-year bonds to the public. To calculate the taxpayer and private sources of funding related to the REFCORP transaction, we used the present value of the contributions made from taxpayer and private sources for both principal and interest payments.

12Calculation of costs begins in 1986 because FSLIC equity was depleted from a positive balance of $4.6 billion on January 1, 1986, to a negative balance of $6.3 billion at December 31, 1986.

13FICO was established with the sole purpose of borrowing funds to finance FSLIC’s costs. A principal redemption fund was established using funds contributed by the industry. The annual interest expense on these bonds is also being paid by the industry through insurance premium assessments. FICO provided funding for FSLIC-related costs by issuing $8.2 billion of noncallable, 30-year bonds to the public. FICO provided $7.5 billion to FSLIC and $0.7 billion to the FSLIC Resolution Fund.
in regulatory treatment required by FIRREA led the government to not honor its contractual obligations. However, because the lower courts had not determined the appropriate measure or amount of damages, the Supreme Court returned the cases to the Court of Federal Claims for further proceedings. Until the amounts of damages are determined by the court, the amount of additional cost from these three cases is uncertain. Further, with respect to the other pending cases, the outcome of each case and the amount of any possible damages will depend on the facts and circumstances, including the wording of agreements between thrift regulators and acquirers of troubled savings and loan institutions. Estimates of possible damages suggest that the additional costs associated with these claims may be in the billions. The Congressional Budget Office’s December 1995 update of its baseline budget projections increased its projection of future federal outlays for fiscal years 1997 through 2002 by $9 billion for possible payments of such claims.

Indirect Costs

As shown in table 3, the estimated cost of special tax benefits related to FSLIC assistance agreements represents an indirect cost of the savings and loan crisis. The estimated total cost for these tax benefits is $7.5 billion, which will be funded using taxpayer sources.

Acquiring institutions received various tax benefits associated with FSLIC assistance agreements. For instance, for tax purposes, assistance paid to an acquiring institution was considered nontaxable. In addition, in some cases, acquiring institutions could carry over certain losses and tax attributes of the acquired troubled institutions to reduce their own tax liability. The effect of these special tax benefits was to reduce the amount of FSLIC assistance payments required by an acquiring institution for a given transaction because of the value of tax benefits associated with the transaction. Thus, total assistance received by an acquiring institution consisted of both FSLIC payments and the value of these tax benefits.

Because these tax benefits represented a reduction in general Treasury receipts rather than direct costs to FSLIC, we are presenting tax benefits as indirect costs associated with FSLIC’s assistance transactions. Of the $7.5 billion in estimated tax benefits, $3.1 billion has been realized through December 31, 1995. The remaining $4.4 billion represents an estimate of the future tax benefits that could be realized by acquiring institutions in the future. However, the amount of future tax benefits depends greatly upon the future actions and profitability of the acquirers. For example, reduced or enhanced earnings, institutional acquisitions, and changes in
corporate control would all affect acquirers' taxable income or the amount of tax benefits allowed to offset such taxable income in the future. The current estimate of future tax benefits is based on assumptions which are currently deemed most likely to occur in the future. However, if conditions change, the amount of future estimated tax benefits realized could be substantially higher or lower than the estimated $4.4 billion.

Remaining Fiscal Implications of the Savings and Loan Crisis

Although most of the direct and indirect costs of the savings and loan crisis had been funded or provided for through December 31, 1995, significant fiscal implications remain as a result of the crisis. Substantial funds were borrowed through bonds specifically designed to provide funding for a portion of the direct costs. Both taxpayers and the industry are paying financing costs on those bonds. In addition, a significant portion of direct costs were paid from appropriations at a time when the federal government was operating with a sizable budget deficit. Therefore, it is arguable that additional borrowing was incurred. In view of these circumstances, we are presenting information on the known and estimated interest expense associated with financing the crisis because the future stream of payments associated with interest will have continuing fiscal implications for taxpayers and the savings and loan industry. An additional fiscal implication is that SAIF is currently undercapitalized and the savings and loan industry continues to pay high insurance premiums to build the fund.

FICO and REFCORP Bonds

In 1987, the Congress established FICO, which had the sole purpose of borrowing funds to provide financing to FSLIC. FICO provided funding for FSLIC-related costs by issuing $8.2 billion of noncallable, 30-year bonds to the public. In 1989, the Congress established REFCORP to borrow funds and provide funding to RTC. REFCORP provided funding to the RTC for resolution losses by issuing $30.0 billion of noncallable, 30- and 40-year bonds to the public. The annual interest expense on the $38.2 billion of bonds issued by FICO and REFCORP has and will continue to have a significant impact on taxpayers and the savings and loan industry. The annual FICO bond interest is funded from the industry’s insurance premiums and represents an increasing burden on the savings and loan industry. In addition, the government’s portion of annual interest expense on the REFCORP bonds will continue to require the use of increasingly scarce budgetary resources.

14An economic analysis of the costs of resolving the savings and loan crisis would present the amounts in present value terms. In present value terms, the amount borrowed is equal to the sum of interest costs plus debt repayment. While it is relevant to show interest payments to illustrate the remaining implications for the federal budget and the industry, adding the amount borrowed to the sum of interest payments would overstate the true economic cost of resolving the crisis.
Annual interest on the FICO bonds is $793 million and is currently being paid from industry assessments and interest earnings on FICO’s cash balances. The annual interest obligation on the FICO bonds will continue through the maturity of the bonds in the years 2017 through 2019. The total nominal amount of interest expense over the life of the FICO bonds will be $23.8 billion.

Annual interest expense on the REFCORP bonds is $2.6 billion. The Federal Home Loan Banks contribute $300 million annually to the payment of REFCORP interest expense, and the remaining $2.3 billion of annual interest expense is paid through appropriations. Annual interest expense will continue through the maturity of the REFCORP bonds in the years 2019, 2020, 2021, and 2030. The total nominal amount of interest expense over the life of the REFCORP bonds will be $88 billion.

The largest source of funding to pay the direct costs of the savings and loan crisis was provided by taxpayers as a result of legislation enacted to specifically deal with the crisis. This legislation was enacted during a period in which the federal government was financing—via deficit spending—a sizable portion of its regular, ongoing program activities and operations. Under these circumstances, it is arguable that substantial, incremental Treasury borrowing occurred in order to finance the taxpayer portion of the crisis.\(^{15}\)

To arrive at an amount for estimated future interest associated with appropriations, we made various simplifying assumptions. For purposes of estimating Treasury interest expense associated with resolving the savings and loan crisis, we assumed that the entire amount of appropriations used to pay direct costs was borrowed. Various other simplifying assumptions were made regarding interest rates and the financing period.\(^{16}\) We assumed that the $99.3 billion\(^{17}\) in appropriations for the FSLIC Resolution Fund and RTC was borrowed.

\(^{15}\) A budgetary measure of costs does not attribute general Treasury interest to programs because general federal receipts and borrowings are not tied to specific programs. From the perspective of the budget as a whole, the general funding sources, whether borrowing or revenue, are fungible.

\(^{16}\) This analysis rests on assumptions about inherently uncertain long-term fiscal and market behavior. Different assumptions could be made regarding interest rates, the mix of short-term versus long-term financing, the financing period and the portion financed with general receipts and borrowing.

\(^{17}\) We based our estimate of interest on the total appropriations for the FSLIC Resolution Fund and RTC, which were $42.7 billion and $56.6 billion, respectively. Total appropriations of $99.3 billion for FSLIC and RTC differ from the $124.6 billion in taxpayer costs presented in table 3. The difference of $25.3 billion represents the taxpayer share of the REFCORP transaction, which is the present value of the taxpayers’ share of future interest expense on the bonds issued by REFCORP. The $25.3 billion has been excluded from the calculation of estimated Treasury interest in order to avoid charging interest on interest expense.
Fund and the RTC would be financed for 30 years at 7 percent interest, with no future refinancing. Under these assumptions, approximately $209 billion in estimated interest payments would be needed over 30 years to cover the interest expense related to appropriations used to cover the direct costs of the crisis.

Table 4 presents the known and estimated interest expense components associated with the financing mechanisms used to provide funds for the direct costs of the savings and loan crisis.

<table>
<thead>
<tr>
<th>Table 4: Known and Estimated Interest Expense Related to the Savings and Loan Crisis</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Funding Source</strong></td>
</tr>
<tr>
<td>---------------------</td>
</tr>
<tr>
<td><strong>Known interest expense</strong></td>
</tr>
<tr>
<td>Interest expense on FICO bonds</td>
</tr>
<tr>
<td>Interest expense on REFCORP bonds</td>
</tr>
<tr>
<td><strong>Total known interest expense on bonds</strong></td>
</tr>
<tr>
<td><strong>Estimated interest expense</strong></td>
</tr>
<tr>
<td>Estimated interest expense on appropriations</td>
</tr>
<tr>
<td><strong>Total estimated interest expense on appropriations</strong></td>
</tr>
</tbody>
</table>

Future Financing Costs Associated With the Crisis

Significant resources will be needed in the future to pay the known annual interest expense on the FICO and REFCORP bonds as well as the estimated Treasury interest expense related to the crisis. As shown in table 5, $20.4 billion, or 18 percent of the total nominal interest expense on FICO and REFCORP bonds has been paid through December 31, 1995. The remaining $91.4 billion, or 82 percent, will be funded in the future.

Future interest expense of approximately $18 billion remains to be paid to cover the FICO bond interest. Currently, insurance premiums paid by certain SAIF-insured institutions are used to pay annual FICO bond interest expense. In 1995, the FICO interest expense represented about 69 percent of insurance premiums earned on SAIF’s FICO-assessable base. In recent years, the FICO-assessable base has been shrinking, thereby increasing the burden of the FICO interest expense relative to the size of the assessment.

---

18We used 7 percent because it represents a reasonable approximation of the average long-term and short-term rates during the years in which the appropriated funds were provided to FRF and RTC. A 30-year term was consistent with the majority of FICO and REFCORP financing terms.

19Insurance premium assessments paid to SAIF for thrift deposits acquired by banks and deposits held by former thrifts that converted to bank charters cannot be used to pay FICO bond interest expense.
base, and calling into question the future ability of the FICO-assessable base to cover the annual FICO interest expense.\textsuperscript{20}

Future interest expense of approximately $73.4 billion remains to be paid on the REFCORP bonds. The Federal Home Loan Banks will continue to be responsible for paying $300 million each year toward the cost of REFCORP interest expense until the bonds mature. The remaining portion of the REFCORP bond interest expense will be paid with Treasury funds until the bonds mature in the years 2019, 2020, 2021, and 2030.

For purposes of analyzing the timing of estimated Treasury interest expense on funds provided to pay the direct costs, we estimated that approximately $176 billion of the $209 billion in estimated Treasury interest expense, shown in table 5, related to future periods.\textsuperscript{21} Under these assumptions, future estimated Treasury interest would represent a significant claim on future federal budgetary resources.

\begin{table}[h]
\centering
\begin{tabular}{lrrr}
\hline
\textbf{Table 5: Known and Estimated Interest Expense: Timing of Funding} \\
\hline

\textbf{Dollars in billions} & \textbf{Timing of Funding} \\
& & \textbf{Total} & \textbf{12/31/95} & \textbf{Future} \\
\hline
\textbf{Known interest expense} & & & & \\
Interest expense on FICO bonds & $23.8 & $5.8 & $18.0 \\
Interest expense on REFCORP bonds & 88.0 & 14.6 & 73.4 \\
\textbf{Total known interest expense on bonds} & $111.8 & $20.4 & $91.4 \\
\hline
\textbf{Estimated interest expense} & & & & \\
Estimated interest expense on appropriations & 209.0 & 33.0 & 176.0 \\
\textbf{Total estimated interest expense on appropriations} & $209.0 & $33.0 & $176.0 \\
\hline
\end{tabular}
\end{table}

Capitalizing SAIF

FIRREA created SAIF to insure deposits previously insured by the FSLIC, and set a designated reserve requirement of 1.25 percent of insured deposits. We consider the need to capitalizing SAIF a remaining fiscal implication of the crisis because insurance premiums that could have been used to capitalize SAIF were used to pay a portion of the direct costs of the crisis.\textsuperscript{22}

\textsuperscript{20}Deposit Insurance Funds: Analysis of Insurance Premium Disparity Between Banks and Thrifts (GAO/AIMD-95-84, March 3, 1995).

\textsuperscript{21}The breakout of estimated Treasury interest between the amount paid through December 31, 1995, and the future amount, was based on the assumption that borrowing generally corresponded with the transfer of appropriated funds to RTC and FRF.

\textsuperscript{22}The SAIF premiums used to resolve the savings and loan crisis are included in the $22 billion of funding from private sources used to pay FSLIC costs shown in table 3.
as well as annual interest expense on the FICO bonds. As a result, SAIF’s capitalization has been delayed, creating ongoing implications in terms of high deposit insurance premiums.

In order to be fully capitalized, SAIF would have needed $8.9 billion in reserves based on the level of insured deposits at December 31, 1995. However, at that date, SAIF had reserves of only $3.4 billion, $5.5 billion below the designated reserve amount of $8.9 billion.

Management is responsible for

• preparing annual financial statements in conformity with generally accepted accounting principles;
• establishing, maintaining, and assessing the internal control structure to provide reasonable assurance that the broad control objectives of FMFIA are met; and
• complying with applicable laws and regulations.

We are responsible for obtaining reasonable assurance about whether (1) the financial statements are free of material misstatement and presented fairly, in all material respects, in conformity with generally accepted accounting principles and (2) RTC management’s assertion about the effectiveness of internal controls is fairly stated in all material respects and is based upon the criteria established under FMFIA. We are also responsible for testing compliance with selected provisions of laws and regulations and for performing limited procedures with respect to certain other information appearing in the financial statements.

In order to fulfill these responsibilities, we

• examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
• assessed the accounting principles used and significant estimates made by management;
• evaluated the overall presentation of the financial statements;
• obtained an understanding of the internal control structure related to safeguarding assets, compliance with laws and regulations, including the execution of transactions in accordance with management authority and financial reporting;
• tested relevant internal controls over safeguarding, compliance, and financial reporting and evaluated management’s assertion about the effectiveness of internal controls; and
• tested compliance with selected provisions of the following laws and regulations:
  • section 21A of the Federal Home Loan Bank Act (12 U.S.C. 1441a) and

We did not evaluate all internal controls relevant to operating objectives as broadly defined by FFMIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to those controls necessary to achieve the objectives outlined in our opinion on RTC management’s assertion about the effectiveness of internal controls. Because of inherent limitations in any internal control structure, losses, noncompliance, or misstatements may nevertheless occur and not be detected. We also caution that projecting our evaluation to future periods is subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with controls may deteriorate.

With the termination of RTC on December 31, 1995, an important phase of the savings and loan crisis ended. To provide an historical perspective on RTC and its role in resolving the crisis, we obtained and reviewed background information and data from RTC and FDIC. In addition, we obtained and analyzed audited financial information from the following entities which had varying roles in resolving the savings and loan crisis: FSLIC, FICO, RTC, REFCORP, FSLIC Resolution Fund, and SAIF.

We conducted our audit from July 7, 1995, through June 7, 1996, in accordance with generally accepted government auditing standards.

FDIC Comments and Our Evaluation

FDIC provided written comments on a draft of this report because of its responsibility for RTC’s remaining assets and liabilities and its role in preparing RTC’s final financial statements. In FDIC’s comments, provided in appendix III, the Corporation’s Chief Financial Officer acknowledges the weaknesses in general controls over RTC’s computerized information systems and discusses the status of RTC and FDIC actions to correct them. We plan to evaluate the adequacy and effectiveness of those corrective actions as part of our audit of FDIC’s 1996 financial statements. The Chief
Financial Officer's comments also discuss FDIC's involvement in RTC's transition and FDIC's plans in assuming responsibility for closing out RTC's active and completed contracts.

Charles A. Bowsher
Comptroller General
of the United States

June 7, 1996
### Appendix I

## RTC’s Financial Statements

### Statements of Financial Position

<table>
<thead>
<tr>
<th>RESOLUTION TRUST CORPORATION</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>STATEMENTS OF FINANCIAL POSITION</strong></td>
<td><strong>December 31, 1995</strong></td>
<td><strong>December 31, 1994</strong></td>
</tr>
<tr>
<td><strong>ASSETS</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash (Note 3)</td>
<td>$1,251,278</td>
<td>$4,034,900</td>
</tr>
<tr>
<td>Net advances (Note 4, 6, 8 and 14)</td>
<td>1,334,505</td>
<td>2,963,704</td>
</tr>
<tr>
<td>Net subrogated claims (Note 5, 6, 8 and 14)</td>
<td>11,168,504</td>
<td>17,378,274</td>
</tr>
<tr>
<td>Net assets purchased by the Corporation (Note 6, 7 and 15)</td>
<td>458,834</td>
<td>235,097</td>
</tr>
<tr>
<td>Other assets</td>
<td>47,840</td>
<td>26,290</td>
</tr>
<tr>
<td><strong>TOTAL ASSETS (Note 14)</strong></td>
<td>$14,260,961</td>
<td>$24,638,265</td>
</tr>
<tr>
<td><strong>LIABILITIES</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts payable, accrued liabilities, and other (Note 16 and 17)</td>
<td>$216,021</td>
<td>$192,622</td>
</tr>
<tr>
<td>Notes payable and accrued interest (Note 9)</td>
<td>10,498,042</td>
<td>23,222,278</td>
</tr>
<tr>
<td>Estimated cost of unresolved cases (Note 6, 10 and 15)</td>
<td>0</td>
<td>410,517</td>
</tr>
<tr>
<td>Estimated losses from corporate litigation (Note 6 and 11)</td>
<td>136,636</td>
<td>199,030</td>
</tr>
<tr>
<td><strong>TOTAL LIABILITIES</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contingencies and commitments (Note 15)</td>
<td>10,850,699</td>
<td>24,024,447</td>
</tr>
<tr>
<td><strong>EQUITY</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contributed capital (Note 3)</td>
<td>60,058,924</td>
<td>59,526,884</td>
</tr>
<tr>
<td>Capital certificates</td>
<td>31,286,325</td>
<td>31,286,325</td>
</tr>
<tr>
<td>Accumulated deficit</td>
<td>(87,934,987)</td>
<td>(90,199,391)</td>
</tr>
<tr>
<td><strong>TOTAL EQUITY (Note 12)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>3,410,262</td>
<td>613,818</td>
</tr>
<tr>
<td><strong>TOTAL LIABILITIES AND EQUITY (Note 14)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>$14,260,961</td>
<td>$24,638,265</td>
</tr>
</tbody>
</table>

See accompanying notes
Appendix I
RTC's Financial Statements

Statements of Revenues, Expenses, and Accumulated Deficit

<table>
<thead>
<tr>
<th>RESOLUTION TRUST CORPORATION</th>
</tr>
</thead>
<tbody>
<tr>
<td>STATEMENTS OF REVENUES, EXPENSES AND ACCUMULATED DEFICIT</td>
</tr>
<tr>
<td>(Dollars in Thousands)</td>
</tr>
<tr>
<td>Year Ended December 31, 1995</td>
</tr>
<tr>
<td>-------------------------------</td>
</tr>
</tbody>
</table>

**REVENUES**
- Interest on advances and subrogated claims: $598,553 $853,396
- Other interest income: 28,716 8,696
- Other revenue (Note 3): 78,229 52,644
- **TOTAL REVENUES**: 705,498 914,736

**EXPENSES**
- Interest expense on notes issued by the Corporation: 932,480 1,100,133
- Interest expense on amounts due receiverships: 17,842 78,433
- Reduction in provision for losses (Note 6): (2,617,449) (1,138,118)
- Administrative operating and other expenses (Note 2, 14 and 17): 108,221 90,007
- **TOTAL EXPENSES**: (1,558,906) 130,455

**NET REVENUE**: 2,264,404 784,281

**ACCUMULATED DEFICIT, BEGINNING**: (90,199,391) (90,983,672)

**ACCUMULATED DEFICIT, ENDING (Note 12)**: (87,934,987) (90,199,391)

See accompanying notes.
## Statements of Cash Flows

**RESOLUTION TRUST CORPORATION**  
**STATEMENTS OF CASH FLOWS**  
*(Dollars in Thousands)*

<table>
<thead>
<tr>
<th>Year Ended December 31</th>
<th>Year Ended December 31</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995</td>
<td>1994</td>
</tr>
</tbody>
</table>

### CASH FLOWS FROM OPERATING ACTIVITIES:

- **Cash inflows from:**
  - Receipts from subrogated claims: $9,828,943
  - Repayments of advances and reimbursable expenditures: 2,578,302
  - Receipts of interest on advances and subrogated claims: 553,429
  - Receipts from asset liquidations: 131,515
  - Receipts from other operations: 185,293

- **Cash outflows for:**
  - Disbursements for subrogated claims: (1,375,341)
  - Disbursements for advances: (530,413)
  - Disbursements for reimbursable expenditures: (904,863)
  - Administrative operating and other expenditures: (115,229)
  - Interest paid on notes payable: (1,185,962)
  - Disbursements for asset liquidations: (45,942)

**Net Cash Provided by Operating Activities (Note 13):**  
9,119,732  
1,132,778

### CASH FLOWS FROM FINANCING ACTIVITIES:

- **Cash inflows from:**
  - Contributed capital: 567,400
  - Notes payable: 0

- **Cash outflows for:**
  - Repayment of notes payable, principal: (12,470,754)

**Net Cash Used by Financing Activities:**  
(11,903,354)  
(3,568,306)

**Net decrease in Cash:**  
(2,783,622)  
(2,435,528)

**CASH – BEGINNING:**  
4,034,900  
6,470,428

**CASH – ENDING:**  
$1,251,278  
$4,034,900

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*See accompanying notes*
Notes to Financial Statements

RESOLUTION TRUST CORPORATION
NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 1995 and 1994

1. Impact of Legislation:

The RTC, a Government Corporation, was created by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) to manage and resolve all troubled savings institutions that were previously insured by the Federal Savings and Loan Insurance Corporation (FSLIC) and for which a conservator or receiver was appointed during the period January 1, 1989 through August 8, 1992. This period was extended to September 30, 1993 by the Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991 and in December 1993, the period was extended to a date not earlier than January 1, 1995 nor later than July 1, 1995 by the Resolution Trust Corporation Completion Act of 1993. The final date of June 30, 1995 was selected by the Chairperson of the Thrift Depositor Protection (TDP) Oversight Board.

The activities of the RTC were subject to the general oversight of the Oversight Board, which was redesignated the TDP Oversight Board and increased in size by the 1991 Act. The TDP Oversight Board monitored the operations of the RTC, provided the RTC with general policy direction, and reviewed the RTC's performance. The seven members on the TDP Oversight Board included: the Secretary of the Treasury; the Chairperson of the Board of Governors of the Federal Reserve System; the Director of the Office of Thrift Supervision (OTS); the Chairperson of the Board of Directors of the Federal Deposit Insurance Corporation (FDIC); the Chief Executive Officer of the RTC; and two independent members appointed by the President, with the advice and consent of the Senate.

Under current law, the RTC terminated on December 31, 1995. All remaining assets and liabilities were transferred to the FSLIC Resolution Fund which is managed by the FDIC. Proceeds from the sale of such assets will be transferred to the Resolution Funding Corporation (REPCORP) for interest payments after satisfaction of any outstanding liabilities.

Source of Funds:

The RTC was funded from the following sources: 1) U.S. Treasury appropriations and borrowings; 2) a contribution from the Federal Home Loan Banks through REPCORP; 3) amounts borrowed by REPCORP which is authorized to issue long term debt securities; 4) the issuance of debt obligations and guarantees as permitted by the TDP Oversight Board; and 5) income earned on the assets of the RTC, proceeds from the sale of assets, and collections made on claims received by the RTC from receiverships.
Appendix I
RTC’s Financial Statements

The Secretary of the Treasury had contributed capital of $60.1 billion to the RTC as of December 31, 1995. $18.8 billion of which was authorized by FIRREA, $30 billion of which was authorized by the Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991, $6.7 billion of which related to the Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991, and $4.6 billion of which related to the Resolution Trust Corporation Completion Act of 1993 (see Note 12). The legislation signed in December 1991 authorized the Secretary of the Treasury to provide an additional $25 billion in capital to the RTC for its operations through March 31, 1992. These funds were received in January 1992. In April, 1992, the RTC returned $18.3 billion to the Treasury which represented funds not committed by the March 31, 1992 deadline.

In December 1993, the Resolution Trust Corporation Completion Act authorized funding of the $18.3 billion which had been returned to Treasury in 1992. Expenditure of funds in excess of $10 billion required certification by the Secretary of the Treasury that certain statutory requirements had been met. In January 1994, the TDP Oversight Board received $10 billion in funds, of which $4 billion was forwarded to the RTC. In October 1995, an additional $556 million was forwarded to the RTC.

The RTC had also issued capital certificates of $31.3 billion to REFCORP as of December 31, 1995 (see Note 12). FIRREA prohibited the payment of dividends on any of these capital certificates. The RTC was also authorized to borrow directly from the Treasury an amount not to exceed in the aggregate $5.0 billion. There had been no draws against these authorized borrowings through the end of 1995.

2. Summary of Significant Accounting Policies:

General. These statements pertain to the financial position, results of operations and cash flows of the RTC, and are presented in accordance with generally accepted accounting principles. These statements do not include the reporting of assets and liabilities of closed thrifts for which the RTC acted as receiver/liquidating agent or of thrifts in conservatorship for which the RTC acted as managing agent. However, these statements do reflect the RTC’s transactions with these thrifts. See Note 14 for more detailed information.

Use of Estimates. The preparation of financial statements in conformity with generally accepted accounting principles required management to make estimates and assumptions that affected the amounts reported in the financial statements and notes. The use of estimates and assumptions have been disclosed throughout the notes, where applicable. Actual results could differ from those estimates.

Allowance for Losses on Advances. The RTC recognized an estimated loss on advances. The allowance for losses represented the difference between amounts advanced to conservatorships or receiverships and expected repayments.

Allowance for Losses on Subrogated Claims. The RTC recorded as assets the amounts disbursed for assisting and closing thrifts, primarily the amounts for insured deposit liabilities. An allowance for losses was established against subrogated claims representing the difference between the amounts disbursed and the expected repayments. The allowance was based on the estimated cash recoveries from the assets of the assisted or failed thrifts, net of estimated asset liquidation and overhead expenses, including interest costs.

Estimated Cost of Unresolved Cases. The RTC recorded the estimated losses related to thrifts in conservatorship and those identified in the regulatory process as probable to fail on or before June 30, 1995.
Appendix I
RTC’s Financial Statements

Litigation Losses. The RTC recognized an estimated loss for litigation against it in its Corporate, conservatorship and receivership capacities. The RTC Legal Division recommended these estimated losses on a case-by-case basis.

Due to Receiverships - Assets Sold. The RTC established a contra asset account to record the amount payable to receiverships for the purchase price of receivership assets sold to acquiring institutions in resolution transactions. This was done in lieu of the receivership receiving the cash proceeds from the sale of its assets. This contra account offsets the balance due from the receiverships for subrogated claims. The amounts that exceeded the expected recovery of subrogated claims due from the receiverships were recorded as a liability entitled “Due to receiverships.” The RTC accrued interest on the total of the contra asset and liability accounts.

National Judgments, Deficiencies and Charge-offs Joint Venture Program. The RTC purchased assets from receiverships, conservatorships, and their subsidiaries to facilitate the sale and/or transfer of selected assets to several Joint Ventures in which the RTC retained a financial interest.

Allocation of Common Expenses. The RTC shared certain administrative operating expenses with FDIC’s Bank Insurance Fund, FSLIC Resolution Fund, and Savings Association Insurance Fund. The administrative operating expenses included allocated personnel, administrative, and other overhead expenses.

Allocation of Corporate Expenses. The RTC recovered costs incurred by the Corporation in support of liquidation/receivership activities, including a portion of administrative expenses. These costs were billed to individual receiverships with the offsetting credits reducing the Corporation’s “Administrative operating and other expenses.”

Depreciation. The cost of furniture, fixtures, equipment and other fixed assets was expensed at the time of acquisition and was reported as “Administrative operating and other expenses.” Although this policy was a departure from generally accepted accounting principles, the financial impact was not material to the RTC’s financial statements.

Cash Equivalents. The RTC considered cash equivalents to be short-term, highly liquid investments with original maturities of three months or less. As of December 31, 1995 and 1994, the RTC did not have any cash equivalents.

Fair Value of Financial Instruments. The balances of financial instruments included in the RTC’s Statement of Financial Position approximated their estimated fair values. The values of “Net advances” and “Net subrogated claims” were based on the discounted net cash flows expected to be received from those instruments. The frequent repricing of the balances of “Due to receiverships” and the short-term nature of “Notes payable” resulted in face amounts of such instruments which approximated their fair values.

3. Office of Inspector General:

FIRREA established an Inspector General of the Corporation and authorized to be appropriated such sums as may be necessary for the operation of the Office of Inspector General (OIG). All financial transactions related to the OIG were included in the Corporation’s financial statements.

The OIG received $152.3 million of appropriated funds from the U.S. Treasury since it was established of which $11.4 million related to the Government’s Fiscal Year (FY) 1996 and $32.0 million related to FY 1995. These funds were used to finance the activities of the OIG. Restricted
Appendix I
RTC's Financial Statements


Reductions to the OIG appropriated funds resulting from obligations were recorded as "Other revenue." Accordingly, the OIG appropriated funds were reduced by $35,361,109 and $29,108,773 during 1995 and 1994, respectively, and recorded as "Other revenue."

Disbursements of the OIG appropriated funds for expenditures were recorded as "Administrative operating and other expenses." These disbursements totalled $28,450,696 during 1995 and $32,000,098 during 1994. As of December 31, 1995 and 1994, the unobligated OIG appropriation balances included in "Contributed capital" were $17.7 million and $41.7 million, respectively.

4. Net Advances (in thousands):

The RTC made advances to receiverships and conservatorships. Advances were made to conservatorships to provide funds for liquidity needs and to reduce the cost of funds, and to receiverships to provide working capital. The advances generally were either secured by the assets of the conservatorship or receivership at the time the advances were made or had the highest priority of unsecured claims. The Corporation accrued interest on these advances which was included in the Statements of Revenues, Expenses and Accumulated Deficit. The Corporation expected repayment of these advances, including interest, before any subrogated claims were paid by receiverships. The advances carried a floating rate of interest based upon the 13-week Treasury Bill rate. Interest rates charged during 1995 ranged between 5.30% and 6.29%, and between 3.27% and 6.25% in 1994. At December 31, 1995 and 1994, the interest rates on advances were 5.30% and 5.91%, respectively.

<table>
<thead>
<tr>
<th>December 31,</th>
<th>1995</th>
<th>1994</th>
</tr>
</thead>
<tbody>
<tr>
<td>Advances to conservatorships/others</td>
<td>$46,055</td>
<td>$81,089</td>
</tr>
<tr>
<td>Advances to receiverships</td>
<td>6,810,741</td>
<td>8,084,024</td>
</tr>
<tr>
<td>Reimbursements due from receiverships and conservatorships</td>
<td>152,273</td>
<td>130,031</td>
</tr>
<tr>
<td>Accrued interest</td>
<td>253,993</td>
<td>154,140</td>
</tr>
<tr>
<td>Write-offs at termination - advances (Note 6 and 7)</td>
<td>(142,076)</td>
<td>(20,489)</td>
</tr>
<tr>
<td>Allowance for losses on receivership advances (Note 6)</td>
<td>(5,786,481)</td>
<td>(5,434,002)</td>
</tr>
<tr>
<td>Allowance for losses on conservatorship advances (Note 6)</td>
<td>0</td>
<td>(31,089)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$1,334,505</strong></td>
<td><strong>$2,963,704</strong></td>
</tr>
</tbody>
</table>

Reimbursements due from receiverships and conservatorships represented operating expenses paid by the RTC on behalf of the receiverships and conservatorships for which repayment was expected in full. Interest was not accrued on these reimbursements.

5. Net Subrogated Claims (in thousands):

Subrogated claims represented disbursements made by the RTC primarily for deposit liabilities. The Corporation recognized an estimated loss on these subrogated claims. These estimates were based in part on a statistical sampling of receivership assets subject to a sampling error of plus or minus $0.3 billion with a 95 percent confidence interval.
Appendix I
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The value of assets under RTC management could be lower (or higher) than projected because general economic conditions, interest rates and real estate markets could change. Because of these uncertainties, it is reasonably possible that the actual losses could be higher (or lower) than the current “Allowance for losses on subrogated claims.”

 Receiverships frequently sold a portion of their assets to institutions acquiring their deposit liabilities. In lieu of the receiverships receiving cash for the sale, the purchase price of the assets sold was recorded by the receivership as a receivable and by the RTC in a contra asset account entitled “Due to receiverships - assets sold.” This account was offset against subrogated claims expected to be collected from the receivership. The portion of the contra asset account, if any, in excess of expected subrogated claim recoveries was recorded as a liability entitled “Due to receiverships.” The RTC accrued interest payable to the receiverships on the total of the contra asset and liability accounts. The rates used by the RTC to accrue interest were based upon the Chicago FHLB Daily Investment Deposit Rates. Interest rates paid during 1995 ranged between 5.17% and 6.21%, and between 2.73% and 5.91% in 1994. At October 31, 1995 and December 31, 1994, the interest rates paid on these accounts were 5.77% and 5.90%, respectively.

December 31, 1995 1994
Subrogated claims $224,281,715 $222,450,889
Recovery of subrogated claims (140,419,527) (129,042,815)
Claims of depositors pending and unpaid 6,956 10,905
Due to receiverships - assets sold (3,196) (716,196)
Write-offs at termination - subrogated claims (Note 6 and 7) (5,899,585) (1,084,425)
Allowance for losses on subrogated claims (Note 6) (66,797,859) (73,340,074)

$11,168,504 $17,378,274

6. Changes in Allowance for Losses (in thousands):

<table>
<thead>
<tr>
<th></th>
<th>Allowance for losses on subrogated claims (Note 5)</th>
<th>Allowance for losses on advances (Note 4)</th>
<th>Allowance for losses on corp assets (Note 7)</th>
<th>Estimated cost of unresolved cases (Note 10)</th>
<th>Estimated losses from corporate litigation (Note 11)</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance, Dec 31, 1993</td>
<td>$568,667,882</td>
<td>$4,967,864</td>
<td>$16,250</td>
<td>$80,097,831</td>
<td>$1,518,333</td>
<td>$81,921,480</td>
</tr>
<tr>
<td>Provisions (reductions)</td>
<td>(314,343)</td>
<td>(1,674)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Write-offs at termination (Note 7)</td>
<td>(1,344,850)</td>
<td>(16,674)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Cost of resolutions</td>
<td>6,331,485</td>
<td>-</td>
<td>(6,331,485)</td>
<td></td>
<td>-</td>
<td>0</td>
</tr>
<tr>
<td>Balance, Dec 31, 1994</td>
<td>73,340,074</td>
<td>5,465,091</td>
<td>7,126</td>
<td>410,517</td>
<td>109,030</td>
<td>79,421,838</td>
</tr>
<tr>
<td>Provisions (reductions)</td>
<td>(2,968,056)</td>
<td>442,976</td>
<td>54,438</td>
<td>(68,626)</td>
<td>(6,294)</td>
<td>(2,602,562)</td>
</tr>
<tr>
<td>Write-offs at termination (Note 7)</td>
<td>(3,915,150)</td>
<td>(121,586)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>(4,036,736)</td>
</tr>
<tr>
<td>Cost of resolutions</td>
<td>341,891</td>
<td>-</td>
<td>(341,891)</td>
<td></td>
<td>-</td>
<td>0</td>
</tr>
<tr>
<td>Balance, Dec 31, 1995</td>
<td>566,797,859</td>
<td>5,780,481</td>
<td>61,564</td>
<td>-</td>
<td>-</td>
<td>58,752,480</td>
</tr>
</tbody>
</table>
Appendix I
RTC's Financial Statements

The "Allowance for losses on subrogated claims" included future interest costs and overhead expenses. Total "reductions" in loss allowances contained the offset of net interest costs incurred in the current period that were previously included in provisions. "Cost of resolutions" represented amounts transferred from "Estimated cost of unresolved cases" to "Allowance for losses on subrogated claims" as a result of case resolutions in each year.

7. Net Assets Purchased by the Corporation (in thousands):

In order to pay a final dividend to the receiverships' creditors and to expedite the process of legally terminating the receivership entities, the RTC purchased the remaining assets of selected receiverships. As of December 31, 1993, the RTC had purchased assets from 301 receiverships for $687 million (assets from 161 receiverships for $295 million at December 31, 1994). Upon termination, the RTC realized a loss on advances and subrogated claims that was previously included in the respective allowances and recognized in the provision for losses in a prior year. Additionally, as of December 31, 1995, the RTC had purchased assets from receiverships, conservatorships, and their subsidiaries for $133 million to facilitate the sale and/or transfer of selected assets to several Joint Ventures in which the RTC retained a financial interest.

<table>
<thead>
<tr>
<th>December 31</th>
<th>1995</th>
<th>1994</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets in liquidation purchased</td>
<td>$820,341</td>
<td>$396,377</td>
</tr>
<tr>
<td>Sales, collections and adjustments</td>
<td>(299,943)</td>
<td>(154,154)</td>
</tr>
<tr>
<td>Allowance for losses on corporate assets (Note 6)</td>
<td>(61,584)</td>
<td>(7,126)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$458,834</strong></td>
<td><strong>$235,097</strong></td>
</tr>
</tbody>
</table>

Assets purchased included mortgage loans backed by 1-4 family homes, multi-family dwellings or commercial real estate; consumer loans; real estate; and other assets including receivership interests in credit enhancement reserve funds created when receiverships participated in RTC loan securitizations.

8. Concentration of Credit Risk:

The RTC had receivables from conservatorships and receiverships located throughout the United States which were experiencing problems with both loans and real estate. Their ability to make repayments to the RTC was largely influenced by the economy of the area in which they were located. The gross balance of these receivables at December 31, 1995 was $91.1 billion (against which $78.6 billion of reserves and contra assets had been recorded). Of the total receivables, $26.3 billion was attributable to institutions located in Texas, $13.8 billion was attributable to institutions located in California, $6.5 billion was attributable to institutions located in Florida and $5.7 billion was attributable to institutions located in Arizona.

9. Notes Payable and Accrued Interest:

Working capital was made available to the RTC under an agreement between the RTC and the Federal Financing Bank to fund the resolution of thrifts and for use in the RTC's high-cost funds replacement and emergency liquidity programs. The outstanding notes matured at the end of each calendar quarter, at which time they were generally refinanced at similar terms. Payments on the
note balance were also made during each calendar quarter. The notes payable carried a floating rate of interest established by the Federal Financing Bank and ranged between 6.01% and 5.52% during 1995 and between 3.17% and 5.03% in 1994. As of December 31, 1995 and 1994, the RTC had $10.5 billion and $23.2 billion, respectively, in borrowings and accrued interest outstanding from the Federal Financing Bank. These borrowings, approved by the TDP Oversight Board, were within the limitations imposed under FIRREA.

10. Estimated Cost of Unresolved Cases:

The RTC had no liability at December 31, 1995 for the anticipated costs of resolving troubled institutions ($411 million at December 31, 1994) (see Note 6). June 30, 1995 was the last date the RTC could have been appointed Conservator. All conservatorships had been resolved as of that date.

11. Estimated Losses from Corporate Litigation:

As of December 31, 1995, the RTC had been named in over a thousand lawsuits while serving in its Corporate, conservatorship or receivership capacities. It was not possible to predict the outcome for all of the various actions. An allowance for loss totalling $136.6 million had been established as of December 31, 1995 for the 31 actions that management felt were probable to result in a significant loss ($199.0 million at December 31, 1994 for 57 actions) (see Note 6). Additionally, the Corporation could possibly incur further losses of up to $347.7 million from other pending lawsuits and other yet unasserted claims.

12. Changes in Equity (in thousands):

<table>
<thead>
<tr>
<th></th>
<th>Contributed Capital</th>
<th>Capital Certificates</th>
<th>Accumulated Deficit</th>
<th>Total Equity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance, Dec 31, 1993</td>
<td>$55,523,993</td>
<td>$31,286,325</td>
<td>$(90,983,672)</td>
<td>$(4,173,354)</td>
</tr>
<tr>
<td>1994 Net revenue</td>
<td>-</td>
<td>-</td>
<td>784,281</td>
<td>784,281</td>
</tr>
<tr>
<td>Resolution Trust Corporation Completion Act of 1993</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>4,000,000</td>
</tr>
<tr>
<td>FY 95 OIG appropriation</td>
<td>32,000</td>
<td>-</td>
<td>-</td>
<td>32,000</td>
</tr>
<tr>
<td>1994 Obligated OIG funds</td>
<td>(29,109)</td>
<td>-</td>
<td>-</td>
<td>(29,109)</td>
</tr>
<tr>
<td>Balance, Dec 31, 1994</td>
<td>59,526,884</td>
<td>31,286,325</td>
<td>(90,199,391)</td>
<td>613,818</td>
</tr>
<tr>
<td>1995 Net revenue</td>
<td>-</td>
<td>-</td>
<td>2,264,404</td>
<td>2,264,404</td>
</tr>
<tr>
<td>Resolution Trust Corporation Completion Act of 1993</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>556,000</td>
</tr>
<tr>
<td>FY 96 OIG appropriation</td>
<td>11,400</td>
<td>-</td>
<td>-</td>
<td>11,400</td>
</tr>
<tr>
<td>1995 Obligated OIG funds</td>
<td>(35,360)</td>
<td>-</td>
<td>-</td>
<td>(35,360)</td>
</tr>
<tr>
<td>Balance, Dec 31, 1995</td>
<td>$60,058,924</td>
<td>$31,286,325</td>
<td>$(87,934,987)</td>
<td>$3,410,262</td>
</tr>
</tbody>
</table>
Appendix I
RTC's Financial Statements


Reconciliation of net revenue to net cash provided by operating activities:

<table>
<thead>
<tr>
<th></th>
<th>For the Year Ended December 31,</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1995</td>
</tr>
<tr>
<td>Net Revenue</td>
<td>$ 2,264,404</td>
</tr>
<tr>
<td>Reduction in provision for losses</td>
<td>(2,617,449)</td>
</tr>
<tr>
<td>Interest expense financed as additional notes payable</td>
<td>-0-</td>
</tr>
<tr>
<td>Increase (decrease) in accrued interest on notes payable</td>
<td>(253,482)</td>
</tr>
<tr>
<td>Increase in accrued interest on amounts due to receiversonships</td>
<td>17,842</td>
</tr>
<tr>
<td>(Increase) decrease in accrued interest due from advances and subrogated claims</td>
<td>133,204</td>
</tr>
<tr>
<td>Receipts from subrogated claims</td>
<td>9,828,943</td>
</tr>
<tr>
<td>Repayments of advances and reimbursable expenditures</td>
<td>2,578,302</td>
</tr>
<tr>
<td>Receipts from asset liquidations</td>
<td>131,515</td>
</tr>
<tr>
<td>Increase in accounts payable, accrued liabilities and other liabilities above</td>
<td>119,201</td>
</tr>
<tr>
<td>(Increase) decrease in reimbursable portion of liabilities above</td>
<td>20,756</td>
</tr>
<tr>
<td>Disbursements for advances</td>
<td>(530,413)</td>
</tr>
<tr>
<td>Disbursements for subrogated claims</td>
<td>(1,375,341)</td>
</tr>
<tr>
<td>Disbursements for reimbursable expenditures</td>
<td>(904,863)</td>
</tr>
<tr>
<td>Disbursements for asset liquidations</td>
<td>(45,942)</td>
</tr>
<tr>
<td>OIG income recognized</td>
<td>(33,360)</td>
</tr>
<tr>
<td>Interest accrued on subrogated claims</td>
<td>(175,687)</td>
</tr>
<tr>
<td>Other non-cash (income) expenses (net)</td>
<td>(36,111)</td>
</tr>
<tr>
<td>(Increase) decrease in other assets</td>
<td>213</td>
</tr>
<tr>
<td><strong>Net cash provided by operating activities</strong></td>
<td><strong>$ 9,119,732</strong></td>
</tr>
</tbody>
</table>

Noncash transactions incurred from thrift assistance and failures:

- $341,891 and $633,485 were reclassified from "Estimated cost of unresolved cases" to "Allowance for losses on subrogated claims" during 1995 and 1994, respectively, due to the resolution of 3 cases in 1995 and 64 cases in 1994.

- "Due to receiverships - assets sold" decreased by $66,418 and $1,020,715 in 1995 and 1994, respectively, with offsetting decreases of $62,462 and $900,923 to "Advances to receiverships" and of $3,956 and $119,782 to "Accrued interest" to repay receivership advances and related interest.

- No interest expense was financed through increases in notes payable in 1995 and 1994.
Appendix I
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- "Recovery of subrogated claims" increased by $1,331,609 and $4,406,990 during 1995 and 1994, respectively, with an offsetting decrease in "Due to receiverships - assets sold", to record liquidating dividends declared by receiverships.

- 'Subrogated claims' increased by $279,596 and $4,060,927 in 1995 and 1994, respectively, resulting from resolution activity with an offsetting increase in "Due to receiverships - assets sold."

- "Due to receiverships" decreased by $2,062 and $11,334 in 1995 and 1994, respectively, with the offset to "Due to receiverships - assets sold" (a component of "Net subrogated claims") for amounts exceeding the expected recovery of subrogated claims due from the receiverships.

- 'Reimbursements due from receiverships and conservatorships' decreased by $59,086 and $130,573 during 1995 and 1994, respectively, with an offsetting decrease to "Due to receiverships - assets sold."

- "Due to receiverships - assets sold" increased by $391,706 and $123,670 in 1995 and 1994, respectively, with an offsetting increase to "Net assets purchased by the Corporation" relating to the purchase of receivership assets by the Corporation.

14. Related Party Transactions:

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 established the RTC to manage and resolve failed savings institutions that were formerly insured by the FSLIC and for which a receiver or conservator was appointed after January 1, 1989. At December 31, 1995, there were 747 institutions with $20.5 billion of assets for which the RTC had been appointed conservator or receiver (745 institutions with $40.5 billion of assets at December 31, 1994).

In its fiduciary capacity as receiver or conservator, the RTC had substantial control over the operations of the institutions placed in receivership or conservatorship by the OTS. The RTC, as receiver or conservator, had ultimate authority in the day-to-day operations, including the timing and methods of the disposal of the institutions' assets in an effort to maximize returns on such assets.

The RTC did not include the assets and liabilities of the receiverships and conservatorships in its financial statements. However, certain transactions with these institutions, including advances to and receivables from the institutions, as well as interest paid or received on such items, were included in the RTC's financial records. At December 31, 1995, the net balances of advances and subrogated claims were $1.3 billion and $11.2 billion (net of "Due to receiverships - assets sold" of $3.2 million), respectively. The RTC owed $3.2 million to receiverships at December 31, 1995 resulting from resolution transactions (see Note 5). Interest income earned on advances and subrogated claims was $599 million during the year ended December 31, 1995 and interest expense on amounts due receiverships was $18 million. At December 31, 1994, the net balances of advances and subrogated claims were $3.0 billion and $17.4 billion (net of "Due to receiverships - assets sold" of $0.7 billion), respectively. Total amounts due receiverships were $0.7 billion, including the liability account of $2 million. Interest income on advances and subrogated claims was $853 million during the year ended December 31, 1994 and interest expense on amounts due receiverships was $78 million.
RTC receiverships and conservatorships were holders of limited partnership equity interests as a result of various RTC sales programs which included the National Land Fund, Multiple Investor Funds, N-Series and S-Series programs. Through 1995, the RTC sold $8.1 billion of loans through these programs ($7.1 billion through 1994).

The RTC funded the activities of the TDP Oversight Board based on its fiscal year budgets. The amounts funded in 1995 and 1994 were $0 and $5.2 million, respectively. These amounts were subject to the Corporation’s policy of allocating corporate expenses to the receiverships.

"Administrative operating and other expenses" for the Corporation were $108.2 million and $90.0 million for the years ended December 31, 1995 and 1994, respectively (total costs of $729.1 million and $484.3 million less $620.9 million and $758.3 million billed back to receiverships during 1995 and 1994, respectively). The Corporation assumed the costs of administrative expenses for the assets purchased from receiverships in the termination process since they were managed by the Corporation (see Note 7).

15. Contingencies and Commitments:

Securitization Credit Reserves:

Through 1995, the RTC sold through its mortgage-backed securities securitization program $42.4 billion of receivership, conservatorship and Corporate loans ($39.2 billion through 1994). The loans sold were secured by various types of real estate including 1-4 family homes, multi-family dwellings and commercial real estate. Each securitization transaction was accomplished through the creation of a trust, which purchased the loans to be securitized from one or more institutions for which the Corporation acted as a receiver or conservator or purchased loans owned by the Corporation. The loans in each trust were pooled and stratified and the resulting cash flow was directed into a number of different classes of pass-through certificates. The regular pass-through certificates were sold to the public through licensed brokerage houses. RTC and its receiverships and conservatorships retained residual pass-through certificates which were entitled to any remaining cash flows from the trust after obligations to regular pass-through holders had been met.

To increase the likelihood of full and timely distributions of interest and principal to the holders of the regular pass-through certificates, and thus the marketability of such certificates, a portion of the proceeds from the sale of the certificates was placed in credit enhancement reserve funds (reserve funds) to cover future credit losses with respect to the loans underlying the certificates. The reserve funds’ structure limited the receiverships’, conservatorships’ or Corporation’s exposure from credit losses on loans sold through the RTC securitization program to the balance of the reserve funds. The initial balances of the reserve funds were determined by independent rating agencies and were subsequently reduced for claims paid and recovered reserves. Through December 1995, the amount of claims paid was approximately 12% of the initial reserve funds. At December 31, 1995 and 1994, reserve funds related to the RTC securitization program totalled $6.8 billion and $6.9 billion, respectively. RTC management expected to recover a substantial portion of the reserve funds over time. In 1995 and 1994, the RTC estimated Corporate losses related to the receiverships’ reserve funds as part of the RTC’s allowances for losses. In 1994, the RTC also estimated Corporate losses related to conservatorships’ reserve funds as part of the RTC’s “Estimated cost of unresolved cases.” As of December 31, 1995, the RTC included $1.1 billion in these provisions to cover future estimated losses on the reserve funds ($1.7 billion as of December 31, 1994). As of December 31, 1995, the provisions were offset by $0.8 billion, the market value of the residual pass-through certificates ($0.6 billion as of December 31, 1994).
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Representations and Warranties:

The RTC provided guarantees, representations and warranties on approximately $103 billion in unpaid principal balance of loans sold and approximately $163 billion in unpaid principal balance of loans under servicing right contracts which had been sold. In general, the guarantees, representations and warranties on loans sold primarily related to the completeness and accuracy of loan documentation, the quality of the underwriting standards used, the accuracy of the delinquency status when sold, and the conformity of the loans with characteristics of the pool in which they were sold. The representations and warranties made in connection with the sale of servicing rights were limited to the responsibilities of acting as a servicer of the loans.

For loans which were sold through the securitization program or for which the sales terms provided corporate guarantees, the receiverships and conservatorships which sold the loans had established escrow accounts containing a portion of the sales proceeds to honor any obligations that might arise from the guarantees, representations and warranties.

Future losses on representations and warranties could significantly increase or decrease over the remaining life of the loans that were sold, which could be as long as twenty years. In 1995 and 1994, the RTC estimated Corporate losses related to the receiverships' representations and warranties claims as part of the RTC's allowances for losses. In 1994, the RTC estimated Corporate losses related to the conservatorships' representations and warranties claims as part of the RTC's "Estimated cost of unresolved cases." In both years, the Corporation also established a liability for the estimate of losses related to representations and warranties claims associated with loan sales that involved corporate purchased assets. As of December 31, 1995, the RTC included $810 million in these provisions to cover the estimated costs of representations and warranties claims ($1.2 billion as of December 31, 1994).

Letters of Credit:

The RTC had adopted special policies for outstanding RTC conservatorship and receivership collateralized letters of credit. These policies enabled the RTC to minimize the impact of its actions on capital markets. In most cases, these letters of credit were used to guarantee tax-exempt bonds issued by state and local housing authorities or other public agencies to finance housing projects for low and moderate income individuals or families. As of December 31, 1995, the RTC had issued a commitment to honor $413 million of these letters of credit. The Corporation had also established a liability for the estimate of losses related to letters of credit in the amount of $142 million.

Affordable Housing Program:

As part of its Affordable Housing Program, RTC management had committed to expend up to $6 million to pay reasonable and customary commitment fees to various state and local housing authorities who, in turn, assisted in providing financing to low and moderate income families. Under that program, the RTC worked with state and local housing finance agencies to secure commitments of Mortgage Revenue Bond and Mortgage Credit Certificate funds which were lent to qualifying families to enable them to purchase properties from the RTC. As of April 15, 1994, all commitments had expired and the Mortgage Revenue Bond program closed. As of December 31, 1995, $2.1 million remained unexpended. No substantial recoveries were anticipated from the program.
Rental Expense:

The RTC leased office space at several locations to accommodate its staff. As of December 31, 1995, these offices included: (1) Washington, D.C. Headquarters offices, (2) six megasite offices, and (3) one satellite office located throughout the country. Additional satellite offices had been closed, but the RTC remained obligated for the remainder of their lease terms pending negotiations for lease buyouts or subleases. These obligations totaled $0.2 million. The RTC's rental expense for 1995 and 1994 totaled $45.5 million and $49.8 million, respectively. The RTC's total contractual obligations under lease agreements for office space were approximately $61.3 million. These agreements often contained escalation clauses which could result in adjustments to rental fees for future years. The minimum yearly rental expense for all locations was as follows (in thousands):

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$21,661</td>
<td>$6,616</td>
<td>$7,069</td>
<td>$7,069</td>
<td>$7,069</td>
<td>$11,782</td>
</tr>
</tbody>
</table>

Lease obligations for 1997 and beyond were exclusively for the RTC headquarters building in Washington, D.C. This lease was entered into by the now defunct FSLIC in 1987. At RTC's termination on December 31, 1995, all of the RTC's debts, obligations and assets, including the above lease obligations, were transferred to the FSLIC Resolution Fund which is managed by the FDIC.

16. Pension Plan and Accrued Annual Leave:

The FDIC eligible employees assigned to the RTC were covered by the Civil Service Retirement System and the Federal Employees Retirement System. Employer contributions provided by the RTC for all eligible employees for the years ended December 31, 1995 and 1994 were approximately $16.1 million and $18.4 million, respectively.

Although the RTC contributed a portion of pension benefits for eligible employees and made the necessary payroll withholdings from them, the RTC did not account for the assets of either of these retirement funds and did not have actuarial data with respect to accumulated plan benefits or the unfunded liability relative to its eligible employees. These amounts were reported by the U.S. Office of Personnel Management (OPM) and were not allocated to the individual employers. OPM also accounted for Federal health and life insurance programs for those RTC retired eligible employees who had selected Federal government sponsored plans.

The RTC's liability to employees for accrued annual leave was approximately $23.1 million at December 31, 1995, and $24.8 million at December 31, 1994.

17. Health, Dental and Life Insurance Plans for Retirees:

The RTC, through its association with the FDIC, provided certain health, dental and life insurance coverage for its eligible retirees, the retirees' beneficiaries and covered dependents. Eligible retirees were those who had elected the FDIC's health and/or life insurance programs and were entitled to an immediate annuity (dental coverage was automatic at retirement). The health insurance coverage was a comprehensive fee-for-service program, with hospital coverage and a major medical wraparound. These employee plans will continue under FDIC management.
Corporate contributions for retirees were the same as those for active employees. Premiums were paid to the FDIC, where they were held until plan fixed costs and expenses were paid. The life insurance program provided for basic coverage at no cost and allowed converting optional coverages to direct-pay plans. The cost of providing this benefit was not separable from the cost of providing benefits for active employees, as the charge for retirees was built into rates for active employees.

The RTC recorded charges of $8.5 million and $6.9 million for the current periodic cost, for 1995 and 1994, respectively. All amounts had been reflected in the "Administrative operating and other expenses" line of the Statements of Revenues, Expenses and Accumulated Deficit.

The net periodic postretirement benefit cost for 1995 and 1994 included the following components (in millions):

<table>
<thead>
<tr>
<th>Component</th>
<th>1995</th>
<th>1994</th>
</tr>
</thead>
<tbody>
<tr>
<td>Service cost, benefits attributed to employee service during the year</td>
<td>$7.2</td>
<td>$7.2</td>
</tr>
<tr>
<td>Interest cost on accumulated postretirement benefit obligations</td>
<td>4.7</td>
<td>4.1</td>
</tr>
<tr>
<td>Net amortization and deferral</td>
<td>(1.1)</td>
<td>(1.4)</td>
</tr>
<tr>
<td>Return on plan assets</td>
<td>(2.3)</td>
<td>(3.0)</td>
</tr>
<tr>
<td>Net periodic postretirement benefit cost</td>
<td>$8.5</td>
<td>$6.9</td>
</tr>
</tbody>
</table>

The RTC, as a government corporation terminated on December 31, 1995, had decided, in conjunction with the FDIC, that the liability for postretirement benefits for eligible employees assigned to the RTC would be recorded on the books of the FDIC. The RTC paid the FDIC an amount equal to the RTC’s obligation. In return, the FDIC agreed to pay the costs associated with postretirement benefits due to eligible employees assigned to the RTC upon their retirement. As of December 31, 1995, the RTC had included as a current liability on its Statement of Financial Position an amount equal to $14.2 million for a revised 1995 net periodic postretirement cost ($6.1 million as of December 31, 1994).

The discount rate used in the calculation of the postretirement benefit obligation was 6.0% in 1995 (6.0% in 1994). The assumed medical inflation trend in 1995 was 12.0% (12.5% in 1994), decreasing to an ultimate rate of 8.0% in 1999 and remaining at that level thereafter. The dental cost trend rate in 1995 and thereafter was 8.0%. Both the assumed discount rate and health care cost trend rates had a significant effect on the amount of the obligation and periodic cost reported.

If the health care cost trend rate was increased one percent, the accumulated postretirement benefit obligation for health care benefits as of December 31, 1995 would have increased $21.9 million, or 25.5% ($15.3 million, or 26.2% as of December 31, 1994). Additionally, a one percent increase would have increased the aggregate service and interest costs of the 1995 net periodic postretirement health care benefit cost by $3.8 million, or 29.3% ($2.9 million, or 29.9% of the 1994 cost).
Management’s Report on Internal Controls

Corporate Internal Control Objectives

The Resolution Trust Corporation (RTC) maintained an internal control system which provided reasonable assurance that:

- assets are safeguarded against loss from unauthorized acquisition, use or disposition;
- transactions are executed in accordance with management’s authority and with laws and regulations; and
- transactions are properly recorded, processed, and summarized in accordance with generally accepted accounting principles and to maintain accountability for assets.

The internal control system established by RTC included a documented organizational structure, division of responsibility, and established policies and procedures. The corporate policy set a positive tone for the organization and is intended to influence the control consciousness of RTC personnel.

During 1995, the Corporation’s objectives were to build on past successes by managing and maintaining its existing programs, by continuing to aggressively pursue its internal control and review activity and to develop control plans related to RTC’s downsizing and transition of its functions to the Federal Deposit Insurance Corporation (FDIC) in a manner that preserves accountability and fiscal integrity.

Management’s Assertion

Management acknowledges its responsibility for establishing and maintaining an effective system of internal control. During the year, management evaluated the Corporation’s internal control system to determine whether it achieved its objectives. The
evaluation was based on the control criteria established under Federal Managers Fiscal Integrity Act, federal directives and applicable policy statements of the Thrift Depositors Protection Oversight Board. Based on that evaluation, management believes that the Corporation's internal control system as of December 31, 1995, was effective in safeguarding material assets against loss from unauthorized acquisition, use, or disposition; assuring the execution of transactions in accordance with management's authority and applicable laws and regulations; and assuring that there were no material financial misstatements.

There are, however, inherent limitations in the effectiveness of any internal control system, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even the most effective internal control system can provide only reasonable assurance with respect to safeguarding of assets against unauthorized acquisition, use or disposition, compliance with laws and regulations, and preparation of financial reports. Furthermore, the effectiveness of an internal control system can change with circumstances.

It should be noted that, notwithstanding management's overall conclusion on the adequacy of RTC's system of internal control, high risk areas and control weaknesses were identified and disclosed through internal control reviews undertaken and audits conducted by external entities in 1995. However, management does not consider the high risk areas and control weaknesses disclosed to be material in relation to the administrative functions or to the financial records relative to the Corporation's operations. Through December 31, 1995, known high risk areas and significant control weaknesses, along with the status of corrective actions taken or proposed, were disclosed in the Corporation's 1995 Internal Control Report to the TDPOB dated December 31, 1995.

Donna H. Cunningham
FDIC’s Comments

FDIC
Federal Deposit Insurance Corporation
550 17th Street, N.W. Washington, D.C. 20429-9360

Deputy to the Chairman for Finance and Chief Financial Officer

June 25, 1996

Gene L. Dodaro
Assistant Comptroller General
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Dodaro:

We appreciate the opportunity to respond to the General Accounting Office (GAO) report on its audits of the 1995 and 1994 financial statements of the Resolution Trust Corporation (RTC). In accordance with statute, the RTC terminated on December 31, 1995, and its remaining assets and liabilities were transferred to the FSLIC Resolution Fund (FRF), managed by the FDIC. The FDIC has, therefore, assumed responsibility for the RTC’s remaining workload.

In that regard, we note that the GAO has concluded that the RTC’s financial statements are fairly presented in all material respects and that RTC management fairly stated that the RTC’s system of internal controls provides reasonable assurance that losses, non-compliance, or misstatements material in relation to the financial statements would be prevented or detected on a timely basis. Additionally, we note that the GAO found no reportable instances of non-compliance with laws or regulations during the course of the audit.

THE SAVINGS AND LOAN CRISIS: HISTORICAL PERSPECTIVE AND FISCAL IMPLICATIONS

We commend the GAO for its discussion of the savings and loan crisis. The discussion is a concise and accurate account of the history, costs, and ongoing fiscal implications of the crisis and will serve as a valuable resource.

TRANSITION OF THE RTC TO THE FDIC

The FDIC worked with the RTC during 1994 and 1995 through its participation on the FDIC/RTC Transition Task Force to ensure the smooth transition of RTC operations, personnel, and assets to the FDIC. In addition, the FDIC is implementing numerous RTC systems and “best practices” recommended by the Task Force.

As part of its ongoing responsibility for residual RTC work, the FDIC will be addressing the concerns identified by the GAO in its report. These include the reportable condition relating to computerized information system controls as well as the concerns expressed about controls over RTC contracting and their possible impact on receivership recoveries.
DISCUSSION OF THE COMPUTERIZED INFORMATION SYSTEM CONTROLS REPORTABLE CONDITION IDENTIFIED IN THE GAO'S 1994 AND 1995 FINANCIAL STATEMENT AUDITS

The RTC reported to the GAO that corrective actions for many of the computerized information system internal control weaknesses identified in the 1994 audit were completed late in 1995. However, the GAO identified additional weaknesses relating to general controls over the RTC’s computerized systems during the 1995 audit.

Effective June 25, 1995, the FDIC began providing information resource management (IRM) services to the RTC pursuant to the terms of a “Letter of Agreement”, which provided for the continued separation of RTC systems and IRM support until termination of the RTC on December 31, 1995. Most of the general control weaknesses that the GAO identified were addressed late in 1995 and early in 1996. FDIC management plans to implement corrective actions for the remaining two control weaknesses by September 30, 1996. To ensure final resolution, FDIC staff will monitor the completion and progress of the corrective actions.

CONTROLS OVER CONTRACTING

The GAO report notes that although the RTC took numerous actions in recent years to improve controls over its contracting activities, the effects of the RTC’s early neglect of its contracting operations remained, particularly for contracts issued prior to the implementation of RTC contracting reforms and improvements. The result was that the RTC could not be sure that it had recovered all that it should have recovered from its receivables.

A large number of active RTC contracts were transferred to the FDIC on December 31, 1995, and the FDIC has assumed responsibility for closing out and resolving open audit issues for a much larger number of completed RTC contracts. During 1995, the RTC intensified its efforts to close out completed contracts and to resolve open contract audit issues. The FDIC and the RTC also worked together through the transition process to identify RTC contracts that would be needed to accomplish remaining RTC work after the RTC’s termination, and the RTC modified those contracts during late 1995 to enable their transfer to the FDIC.

In assuming responsibility for the RTC’s remaining contracting work, the FDIC will make its best efforts to recover any funds due under these contracts, recognizing the limitations that may exist because of the factors cited in the GAO report.

Please contact me if any further assistance may be provided by this office.

Sincerely,

William A. Longbrake
Deputy to the Chairman for Finance
and Chief Financial Officer
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Resolution Trust Corporation: Evaluations Needed to Identify the Most Effective Land Sales Methods (GAO/GGD-95-43, April 13, 1995)


Resolution Trust Corporation: Management Improvements Reduce Risk But Transition Challenges Remain (GAO/T-GGD-95-188, June 20, 1995)

Inspectors General: Mandated Studies to Review Costly Bank and Thrift Failures (GAO/GGD-95-126, July 31, 1995)

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