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Report to the Congress

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FINANCIAL AUDIT

Bank Insurance Fund's 1991 and 1990 Financial Statements

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Washington, D.C. 20548

Comptroller General
of the United States

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June 30, 1992

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

This report presents the results of our audit of the Bank Insurance Fund's financial statements for the years ended December 31, 1991 and 1990. The Bank Insurance Fund, the insurer of deposits for the banking industry, is administered by the Federal Deposit Insurance Corporation (FDIC). Our audit disclosed that the Fund's statements of financial position as of December 31, 1991 and 1990, and its related statements of income and fund balance and statements of cash flows for the years ended, present fairly, in all material respects, the financial position of the Bank Insurance Fund and the results of its operations and its cash flows.

However, significant uncertainties exist regarding general economic conditions and real estate markets. These uncertainties, which are largely beyond FDIC's control, could ultimately result in substantial reductions in the recovery value of failed bank assets held by the Fund and in substantial increases in costs from resolving future bank failures. In addition, material internal control weaknesses in FDIC's management information system for failed institution assets could further expose the Fund to losses from errors and irregularities that may not be detected in a timely manner.

We conducted our audits in accordance with generally accepted government auditing standards. Our reports on the Fund's internal control structure and its compliance with laws and regulations are also presented.

The Fund's December 31, 1991, financial statements reported a deficit fund balance of $7 billion, resulting from 4 consecutive years of net losses. FDIC expects a significant number of additional troubled banks to require resolution in the near future. The Federal Deposit Insurance Corporation Improvement Act of 1991 (Public Law 102-242) provided FDIC with increased authority to borrow funds to cover losses and working capital needs related to resolution activity. However, the degree to which this funding will be sufficient to deal with the Fund's exposure to troubled banks is subject to a number of uncertainties, including economic and market conditions, which could affect the Fund's ability to generate recoveries from sales of failed bank assets and the ultimate cost of resolving troubled banks.

We are sending copies of this report to the Chairman of the Board of Directors, Federal Deposit Insurance Corporation; the Director of the

Office of Management and Budget; the Secretary of the Treasury; the Chairman of the Board of Governors of the Federal Reserve System; the Acting Comptroller of the Currency; and the Chairmen and Ranking Minority Members of the Senate Committee on Banking, Housing and Urban Affairs and the House Committee on Banking, Finance and Urban Affairs.

Charles A. Bowsher
Comptroller General
of the United States

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Abbreviations

DACS	Division of Accounting and Corporate Services
FDIC	Federal Deposit Insurance Corporation
FFB	Federal Financing Bank
FSLIC	Federal Savings and Loan Insurance Corporation
FIRREA	Financial Institutions Reform, Recovery, and Enforcement Act of 1989
GCR	Gross Cash Recovery
LAMIS	Liquidation Asset Management Information System
RTC	Resolution Trust Corporation
SAIF	Savings Association Insurance Fund

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of the United States

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To the Board of Directors
Federal Deposit Insurance Corporation

We have audited the accompanying statements of financial position of the Bank Insurance Fund as of December 31, 1991 and 1990, and the related statements of income and fund balance and statements of cash flows for the years then ended. These financial statements are the responsibility of the management of the Federal Deposit Insurance Corporation (FDIC), the Fund's administrator. Our responsibility is to express an opinion on these financial statements based on our audits. In addition, we are reporting on our consideration of FDIC's internal control structure and on its compliance with laws and regulations as they relate to the Fund.

We conducted our audits in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management as well as evaluating the overall financial statements' presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Bank Insurance Fund as of December 31, 1991 and 1990, and the results of its operations and its cash flows for the years then ended, in conformity with generally accepted accounting principles. However, significant uncertainties regarding the value of real estate assets may ultimately result in substantial reductions in the recovery value of failed bank assets held by the Fund and in substantial increases in costs from resolving future bank failures.

The Fund's December 31, 1991, financial statements reported a deficit fund balance for the first time in the Fund's history. For the year ended December 31, 1991, the Fund reported a net loss of $11.1 billion, resulting in a fund deficit of $7 billion as of December 31, 1991. This deficit reflects the Fund's continued erosion through 4 consecutive years of net losses.

In 1991, problems facing the banking industry became increasingly concentrated in larger banks. The number of troubled banks at December 31, 1991, as represented by banks on FDIC's problem institution list, increased slightly from the previous year. However, total assets of these troubled banks increased by nearly 50 percent over the previous year, to over $600 billion. The failure of large banks can result in additional, significant losses to the Fund in future years, which could further increase the Fund's deficit.

Uncertainties Affect the Ultimate Recoveries From Receivership Assets

The Fund's December 31, 1991 and 1990 financial statements include $43.4 billion and $28.9 billion, respectively, in amounts the Fund advanced for resolving troubled banks, net of actual recoveries. These amounts are reported as receivables from bank resolutions on the Fund's financial statements. Funds to repay amounts advanced are generated from FDIC's management and liquidation of assets acquired from failed banks. Because the management and disposition of these assets generally will not generate amounts equal to the asset values as reflected on failed banks' financial records, FDIC establishes an allowance for losses against the receivables. The allowance for losses represents the difference between amounts advanced and the expected repayment, net of all estimated liquidation costs. As of December 31, 1991 and 1990, the allowance for losses equaled $22.4 billion and $16.6 billion, respectively.

FDIC maintains a management information system for assets in liquidation, which provides information on estimated recoveries from the management and sale of failed institution assets. These estimated recoveries are used to derive the allowance for losses. Because of material internal control weaknesses we identified in this system, we designed alternative audit procedures to test the reasonableness of the allowance for losses reported on the Fund's financial statements. These procedures, which consisted of analyzing FDIC's collection experience on failed bank assets to assess the reasonableness of the estimated recoveries on the Fund's existing asset inventory, provided us with reasonable assurance that the balance of net receivables from bank resolutions reported on the Fund's financial statements was fairly stated.

The estimates of future recoveries derived from historical collection experience, however, are subject to significant uncertainties. In recent years, economic conditions have adversely affected asset values, particularly real estate assets. Furthermore, the rapid growth in government-held assets and the significant volume of real estate assets now on the market, coupled with the significant discounts the Resolution Trust Corporation offers in an attempt to reduce its inventory of real estate assets, could materially affect FDIC's ability to generate future recoveries from asset sales for the Fund at rates comparable to those it experienced in the past.

As of December 31, 1991, the Fund, in its receivership capacity, held failed bank assets with a book value of $34.4 billion, an increase of nearly 200 percent from the $11.5 billion book value of failed bank assets the Fund held just 2 years ago. As more banks fail, the Fund's inventory of assets may continue to grow, increasing the Fund's exposure to unanticipated losses due to the existing uncertainties which may adversely affect FDIC's ultimate recovery on the disposition of these assets. Additionally, material internal control weaknesses in FDIC's management information system for assets in liquidation increase the Fund's risk of future exposure to losses resulting from errors and irregularities that may not be detected in a timely manner.

Uncertainties Affect the Fund's Ultimate Cost of Resolving Troubled Banks

The Fund's financial statements also reflect FDIC's estimate of the cost that the Fund will incur in resolving troubled banks that meet the criteria for loss recognition under generally accepted accounting principles. In 1990, FDIC used the equity position of a troubled institution as its basis for recognizing an estimated loss. Under these criteria, FDIC recorded an estimated loss of $7.7 billion on the Fund's December 31, 1990, financial statements for those banks determined to be equity insolvent.[1] The approach FDIC used in determining the Fund's estimated loss from troubled banks at December 31, 1990, was in accordance with existing accounting standards.

In 1991, FDIC revised its approach for determining what triggers the recognizing of estimated losses from troubled banks on the Fund's financial statements. In addition to including banks that are insolvent on an equity capital basis at year-end, FDIC recognized estimated losses on the Fund's financial statements for banks with positive equity capital at year-end whose financial conditions are such that FDIC believes it is more likely than not that the banks will require resolution in the near future.

[1]Equity insolvent banks are banks that reported negative equity capital on their quarterly financial reports filed with the regulators (call reports), and banks that reported positive equity capital on their quarterly call reports but whose reserves for loan losses, when compared to their level of nonperforming loans and loss reserves levels for similar banks in the same geographical region, were determined to be insufficient to cover the level of losses inherent in their loan portfolios. When these banks' reserves for loan losses were increased to reflect a more appropriate level to cover loan losses, their equity capital was depleted, resulting in their insolvency.

In general, these banks with positive equity capital at year-end had minimal capital, excessive levels of problem assets, and earnings trends that, if continued, would lead to their insolvency in the near future. This approach is consistent with the loss recognition criteria we discussed in our report on the Fund's 1990 financial statements[2] and is within the latitude provided in the existing accounting standards regarding loss recognition. As of December 31, 1991, FDIC estimated, using its revised approach, that the Fund will incur costs of $16.3 billion for resolving troubled banks in the near future. As we disclosed in our report on the Fund's 1990 financial statements, if FDIC had applied this approach in 1990, $5.4 billion in additional estimated losses would have been recognized at that time, and the Fund would have had a deficit balance of $1.4 billion instead of the reported balance of $4.0 billion as of December 31, 1990.

As stated in note 11 to the financial statements, FDIC has estimated that troubled banks with combined assets ranging from $168 billion to $236 billion could fail in the next 2 years. FDIC estimates that the cost of resolving these banks could be between $25.8 billion and $35.3 billion, of which $16.3 billion has already been recorded on the Fund's 1991 financial statements for those banks that met FDIC's loss recognition criteria as of December 31, 1991. If the additional banks do fail, the Fund faces estimated costs beyond those already recognized on the financial statements of between $9.5 billion and $19.0 billion.

FDIC's loss estimates for troubled banks are primarily based on past resolution experience. Consequently, these estimates are subject to the same uncertainties as those affecting FDIC's estimates of future recoveries on the management and liquidation of assets acquired from previously failed banks. In addition, changes in economic conditions and fluctuations in interest rates can affect the timing of bank failures and the closing of these banks by regulators. Short-term profits due to the current low interest rates and gains from asset sales may delay the timing of a troubled bank's failure, but they do not necessarily eliminate the losses imbedded in the bank's asset portfolio. Sustained economic growth and improved real estate market conditions, coupled with banks' efforts to adequately recognize the extent of loan losses in their portfolios, dispose of poor quality assets, and meet capital requirements, are critical factors affecting a troubled bank's return to viability.

[2] Financial Audit: Bank Insurance Fund's 1990 and 1989 Financial Statements, (GAO/AFMD-92-24, November 12, 1991).

Adequacy of Funding for Resolving Troubled Banks Is Dependent on Future Events

The Federal Deposit Insurance Corporation Improvement Act of 1991 (Public Law 102-242), enacted December 19, 1991, provided FDIC with increased authority to borrow funds to cover both losses and working capital needs related to resolution activity. The FDIC Improvement Act increased FDIC's authority to borrow funds from the Treasury on behalf of the Bank Insurance Fund and the Savings Association Insurance Fund (SAIF)[3] to cover losses incurred in resolving troubled institutions to $30 billion. However, it also requires FDIC to recover these loss funds through premium assessments charged to insured institutions. In addition, FDIC may borrow funds for working capital, but the amount of its outstanding working capital borrowings is subject to a formula in the act that limits FDIC's total outstanding obligations. FDIC borrows working capital on behalf of the Fund from the Federal Financing Bank. Such borrowings are to be repaid primarily from the management and disposition of failed financial institution assets.

The adequacy of the funding the act provides to deal with the Fund's exposure to troubled banks is subject to a number of uncertainties. To the extent actual recoveries from the management and disposition of failed bank assets fall short of expectations, the ultimate cost of resolving these institutions will increase. If this occurs, the Fund may require additional loss funds to cover the shortfall. Furthermore, it is difficult to project the Fund's long term exposure to losses from troubled banks. While the $30 billion in loss funds appears to be sufficient based on FDIC's short-term projections of identifiable costs the Fund faces from troubled banks, any additional banks requiring resolution could result in the need for increased funding.

Future events in the thrift industry could also significantly affect the adequacy of the funding provided. Under the FDIC Improvement Act, FDIC is authorized to borrow $30 billion from the Treasury to cover losses incurred in resolving institutions insured by both the Bank Insurance Fund and SAIF. FIRREA also established RTC to resolve thrifts whose deposits had been insured by the Federal Savings and Loan Insurance Corporation (FSLIC) and that had been, or will be, placed into conservatorship or receivership from January 1, 1989, through August 8, 1992. The Resolution Trust Corporation Refinancing, Restructuring, and

[3]SAIF was established under the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) (Public Law 101-73) to insure the deposits of federally-insured savings associations (thrifts) and thrift deposits acquired by so-called "Oakar banks" under Section 5(d)(3) of the Federal Deposit Insurance Act. Through September 30, 1993, however, SAIF will share resolution responsibility with the Resolution Trust Corporation (RTC).

Improvement Act of 1991 (Public Law 102-233), enacted on December 12, 1991, extended RTC's resolution authority to thrifts placed into conservatorship or receivership through September 30, 1993. After this date, responsibility for resolving all federally-insured thrifts will be shifted to SAIF.[4]

Favorable interest rates could delay many thrift failures until after September 30, 1993. If the costs of resolving these institutions exceed SAIF's other available funding sources, FDIC could be forced to use some of the $30 billion in borrowing authority to cover SAIF's losses. Were this to occur, the funding the FDIC Improvement Act provides may not be sufficient to cover the exposure posed to both SAIF and the Bank Insurance Fund from their respective industries.

Additional Efforts to Recapitalize the Fund May Be Needed

The last 4 years have demonstrated how quickly unanticipated events can adversely impact the banking industry and ultimately deplete the reserves of the Fund. The Fund's dramatic decline from a high of $18.3 billion as of December 31, 1987, to its reported deficit of $7 billion as of December 31, 1991, illustrates the extent and swiftness in which rising numbers and costs of bank failures have depleted the Fund. At the time the Fund attained its highest level, the ratio of its reserves to insured deposits equaled approximately 1.10 percent. In the succeeding 4 years, as the Fund's reserve position declined by over $25 billion, the ratio of its reserve balance to insured deposits declined precipitously to a negative 0.36 percent as of December 31, 1991.

The FDIC Improvement Act contains provisions to recapitalize the Fund. It requires FDIC to set semiannual assessment rates for insured institutions that are sufficient to increase the Fund's ratio of its reserves to insured deposits to a designated ratio established by FIRREA of 1.25 percent no later than 1 year after setting the assessment rates, or in accordance with a recapitalization schedule established by FDIC. This schedule must specify, at semiannual intervals, target reserve ratios for the Fund, culminating in a ratio of reserves to insured deposits that is equal to the designated reserve ratio no later than 15 years after the date on which the schedule becomes effective. The FDIC Improvement Act also requires FDIC to implement a

[4]Any thrift requiring resolution after September 30, 1993, which had previously been under RTC conservatorship or receivership may be transferred back to RTC for resolution in accordance with the provisions of the Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991.

risk-based premium system by January 1, 1994. Under this system, insured institutions considered to pose a greater risk of loss to the Fund would be assessed at higher rates than stronger, well capitalized and managed institutions. The act permits FDIC to implement a transitional risk-based premium system prior to January 1, 1994.

FDIC recently issued a proposal for public comment to increase the semiannual assessment rates charged to insured institutions from the current rate of 23 cents per $100 of domestic deposits to 28 cents, effective January 1, 1993. This proposed rate increase is based on an analysis of the condition of the Fund and its ability to achieve the designated reserve ratio over the next 15 years. Concurrent with this proposal, FDIC proposed to shift to a risk-based premium system, also effective January 1, 1993. The initial assessment rates under the proposed risk-based premium system range from between 25 cents and 31 cents per $100 of domestic deposits and would vary from institution to institution based on the regulators' assessment of the institution's condition and health. If FDIC implements such a risk-based premium structure by January 1, 1993, it estimates that the proposed assessment rate of 28 cents per $100 of domestic deposits would become the average assessment rate FDIC would charge.

Even under the proposed assessment rate increase, there is considerable risk that the Fund will not achieve the designated reserve ratio within the maximum 15 year period allowed for in the FDIC Improvement Act. FDIC estimates that, with an assessment rate of 28 cents per $100 of domestic deposits, the probability of the Fund's reserves achieving the designated reserve ratio in 15 years is only 60 percent. Given the uncertainties discussed above that may ultimately impact asset recovery values, costs from future resolution activity, and the adequacy of the funding provided under the act, it is important to replenish the Fund's reserves as expeditiously as possible. As the last 4 years have shown, unexpected events such as economic downturns and their resulting impact on the banking industry can quickly deplete reserve levels once considered to be healthy. It is important that the Fund be recapitalized to avoid further borrowings from the taxpayers to finance losses from financial institution failures. This is consistent with previous positions we have taken regarding the need to recapitalize the Fund.[5]

Charles A. Bowsher
Comptroller General
of the United States

May 11, 1992

[5]Rebuilding the Bank Insurance Fund, (GAO/T-GGD-91-25, April 26, 1991).

Report on Internal Control Structure

We have audited the financial statements of the Bank Insurance Fund as of December 31, 1991 and 1990, and have issued our opinion thereon. This report pertains only to our consideration of the Federal Deposit Insurance Corporation's (FDIC) internal control structure as it relates to the Bank Insurance Fund for the calendar year ended December 31, 1991. The report on our consideration of the Corporation's internal control structure as it relates to the Fund for the calendar year ended December 31, 1990, is presented in GAO/AFMD-92-24, dated November 12, 1991.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. In planning and performing our audit, we considered the internal control structure of FDIC as it relates to the Fund in order to determine the auditing procedures needed for purposes of expressing our opinion on the financial statements and not to provide assurance on the internal control structure.

FDIC's management is responsible for establishing and maintaining an internal control structure over the Bank Insurance Fund. In fulfilling this responsibility, estimates and judgments by management are necessary to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles.

Because of the inherent limitations of any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the internal control structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For purposes of this report, we have classified FDIC's significant internal control structure policies and procedures, including those relevant to compliance with applicable laws and regulations, for the Fund into the following categories:

- assistance, consisting of the policies and procedures related to the Fund's efforts to provide financial assistance to open but troubled institutions and to liquidate closed financial institutions;
- estimated liabilities, consisting of the policies and procedures related to FDIC's development of estimates of future costs to be incurred arising from the failure of troubled financial institutions and ongoing corporate litigation;
- treasury, consisting of the policies and procedures related to cash balances, cash receipts, cash disbursements, and investing activity;
- assessments, consisting of the policies and procedures related to the Fund's levying, collecting, and accounting for insurance premiums charged to insured banks;
- expenditures, consisting of the policies and procedures related to the recognition of liabilities, expenses, and disbursements associated with borrowing from the Federal Financing Bank, payroll, property and buildings, and administrative expenses; and
- financial reporting, consisting of the policies and procedures related to the form, content, and preparation of the Fund's financial statements.

For each of the internal control structure categories listed above, we obtained an understanding of the design of the relevant policies and procedures and whether they have been placed in operation. Also, we assessed control risk. We performed limited tests of selected control procedures for each of the categories listed; however, we found it more efficient to rely primarily on substantive audit tests to determine if related financial statement balances and disclosures were fairly stated. For all categories, we performed audit tests to substantiate account balances associated with each control category. Such tests can also serve to identify weaknesses in the internal control structure.

Reportable Conditions

Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect an organization's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

There are two levels of reportable conditions—those that are considered material weaknesses,[6] which could affect the fair presentation of the financial statements, and those that, while not material to the financial statements, are significant matters which merit management's attention. We identified one condition involving FDIC's internal control structure and its operation which we consider to be a material weakness. This condition concerns significant deficiencies in the integrity of data maintained in FDIC's asset management information system. Through substantive testing and alternate auditing procedures, we satisfied ourselves that it did not have a material effect on the fair presentation of the Fund's 1991 financial statements. However, the existence of this condition greatly increases the risk that related balances may become materially misstated in the future if action is not taken to correct this problem. We also noted one matter that we consider to be a non-material reportable condition as defined above. This condition concerns lack of adherence to prescribed procedures over time and attendance accounting and reporting. In addition, we will be reporting separately upon other matters which, while less significant, we believe should nevertheless be brought to management's attention.

Weak Controls Over FDIC's Asset Management Information System Result in Data Integrity Problems

Controls to ensure the integrity of data in FDIC's primary system for estimating recoveries from the management and disposition of assets acquired from failed financial institutions are inadequate. The lack of effective maintenance and updating of data files within the system has resulted in a significant number of errors in system generated information on the estimated recoveries and related data on the condition of assets acquired from failed financial institutions. These errors, in turn, could result in material misstatements in the valuation allowance established against the Fund's reported balance of receivables from bank resolutions.

The Liquidation Asset Management Information System (LAMIS) is FDIC's primary system for managing assets acquired from failed financial institutions. It serves as a subsidiary system of the Fund's general ledger, which is maintained by FDIC's Financial Information System. LAMIS controls, accounts for, and reports upon the acquisition, management, and ultimate disposition of assets FDIC acquires through resolutions. LAMIS also

[6] A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

provides estimates of recoveries to be received from the management and disposition of these assets, known as the Gross Cash Recovery (GCR), to FDIC's Division of Accounting and Corporate Services (DACS). For assets with book values of $250,000 or more, the GCRs are estimated and input into LAMIS by responsible account officers. Assets with book values below $250,000 are assigned formula generated values by LAMIS based on historical collection experience with assets of similar status and type. DACS uses these estimates to derive the allowance for losses on the Fund's receivables from bank resolutions.

As of December 31, 1991, FDIC had approximately 136,000 assets with a total book value of $33 billion and a total GCR value of $23 billion recorded in LAMIS. The magnitude and nature of the information LAMIS processes and the manner in which it is used make the integrity of the data it generates critical to the accuracy of the Fund's financial statements and the management of the Fund's inventory of failed financial institution assets.

We conducted testing of information in LAMIS on estimated recoveries and related data on the condition of assets at four FDIC consolidated receivership offices representing all four FDIC regional offices. We selected a judgmental sample of assets and tested LAMIS information on their existence, classification, and valuation against asset file documentation. Our sample of assets selected included both assets with GCRs estimated by account officers (individually appraised assets) and assets with GCRs developed by LAMIS (formula appraised assets). Of the items tested, 61 were individually appraised and 113 were formula appraised.

Of the 61 individually appraised assets we selected for testing, file documentation for 16 (26 percent) did not support recorded GCR values. These included: (1) 11 assets with an aggregate GCR overstatement of about $2.4 million, (2) 2 assets with an aggregate GCR understatement of about $400,000, and (3) 3 assets for which we could not locate documentation in the asset files to support their GCR values, but whose LAMIS-recorded GCR value was about $187,000.

In addition, 2 assets remained recorded in LAMIS after they had been sold, 2 were double-counted and, for 1 asset, documentation in the asset file did not support the book value of the asset as reflected in LAMIS. These error rates are a matter of concern because individually appraised assets accounted for $28 billion (85 percent) of the $33 billion total book value and $21 billion (91 percent) of the $23 billion total GCR value of assets recorded in LAMIS as of December 31, 1991.

Of the 113 formula appraised assets we tested, file documentation did not support the recorded GCR for 33 (29 percent). Because formula driven GCR estimates are based on historical experience rather than actual individual assessment of an asset's value, we would expect some differences between the formula generated estimates of the recovery values for individual assets and those estimates that could be derived from documentation in the asset files, including both understatements and overstatements. Of the 33 exceptions found, files supporting 13 assets reflected values greater than those recorded in LAMIS, and files supporting 20 assets reflected values below those recorded in LAMIS.

However, the use of formula generated recovery estimates based on historical experience in a period of economic uncertainty carries with it the risk that asset values will become misstated due to the application of outdated formulas. In addition, use of formula generated estimates is also prone to other types of errors that can result in misstated asset recovery values. For example, in addition to the 33 errors identified above, we found 8 assets (7 percent) that were misclassified as to their asset type. As a result, LAMIS utilized an incorrect formula to generate a recovery value for these assets.

We also selected 45 asset files in three regions to determine if the assets were, in fact, recorded in LAMIS. Of these 45 files, 3 (7 percent) had not been recorded at the time of our audit.

FDIC's Office of the Inspector General conducted an audit of LAMIS between September 1991 and January 1992.[7] The results of this audit identified many of the same problems we identified in our audit, as well as a number of additional concerns. The Inspector General's audit, which was also conducted at four FDIC consolidated receivership offices, found that high error rates in LAMIS files compromised the accuracy of management and financial information generated by the system. Additionally, the Inspector General found that (1) LAMIS limitations and errors have eroded user confidence and reduced its effectiveness as an operational and management tool, (2) LAMIS security controls are weak, and (3) LAMIS responsibilities are not clearly defined.

The Inspector General reported that the pervasive data integrity problems that plague LAMIS are primarily due to erroneous data input and maintenance, rather than inaccurate calculations by the system itself.

[7]Information Systems Audit of LAMIS, (March 31, 1992).

These problems are traceable to a variety of causes, including inadequate training of system users, improper organization and content of physical asset files, data conversion and maintenance errors, inadequate review procedures, and a lack of centralized direction and control. Over time, these problems have been perpetuated and magnified by declining user interest in system maintenance as data quality has deteriorated and users have increasingly turned to alternate systems to serve their needs. The Inspector General concluded that the system of internal controls associated with LAMIS processing is inadequate and, by itself, cannot be relied upon to ensure accurate and timely processing and reporting of financial and management data. To correct these problems, the Inspector General recommended a number of actions addressing the (1) high error rates in LAMIS, (2) functional limitations and declining user confidence in the system, (3) weak security controls, and (4) lack of definition of responsibilities.

Because of the weaknesses we identified and those reported by the Inspector General, we were unable to rely upon the data generated by LAMIS as a basis for estimates of future recoveries. As an alternate auditing procedure, we conducted an analysis of FDIC's actual experience in collections from the management and disposition of assets acquired from failed financial institutions. The purpose of this analysis was to assess the reasonableness of the aggregate recovery estimates and, consequently, the valuation of the assets in the Fund's asset inventory. Through this analysis, we were able to obtain reasonable assurance that FDIC's estimates of future collections were reasonable as of December 31, 1991. However, there remains a significant risk of material misstatement in the future if the weaknesses identified by our work and the work of the Inspector General are not corrected.

FDIC Is Not Adhering to Its Time and Attendance Accounting and Reporting Procedures

FDIC is not consistently adhering to its procedures over the time and attendance accounting and reporting process. Because FDIC allocates payroll expenses among the several funds it administers, lack of adherence to procedures over the time and attendance accounting and reporting process could lead to incorrect allocations among the funds and, consequently, to misstatements in each fund's payroll expense.

FDIC is responsible for administering and separately accounting for the Bank Insurance Fund, the Savings Association Insurance Fund (SAIF), and the FSLIC Resolution Fund. FDIC allocates overhead expenses, including payroll expenses, among these three funds based on the percentage of time employees report having worked on activities pertaining to a particular fund. FDIC employees are responsible for determining and documenting on their time cards the hours worked on each fund.

We statistically selected 60 time cards from the first 9 months of 1991 and examined the time cards for evidence of proper signatures and agreement with various payroll reports. We also reviewed the time cards and related payroll reports for conformance with FDIC's Time and Attendance Reporting Directive. Our review disclosed significant weaknesses over FDIC's time and attendance reporting process including (1) payroll reports missing and/or not signed by the supervisor, (2) time card data changed by timekeepers without the approval of the employee or the employee's supervisor, (3) payroll reports not reconciled to time cards, and (4) employees not being provided time and attendance reports documenting their time card data that had been input into the payroll system.

The Bank Insurance Fund's 1991 payroll expenses are not material to the financial statements of the Fund taken as a whole. However, since FDIC employees perform functions for all three funds and are responsible for allocating their time charges to the proper fund, it is essential that FDIC implement the necessary procedures and controls to ensure employees' time charges are valid and to decrease the likelihood that payroll expenses are charged to the wrong fund. In the report on our study of the internal control structure of SAIF for the calendar year ended December 31, 1991 (GAO/AFMD-92-72), we recommended that FDIC enforce the policies and procedures contained in its Time and Attendance Reporting Directive to ensure that employees' time charges are valid and to decrease the likelihood that payroll expenses are charged to the wrong fund.

Conclusion

Through substantive testing and alternate auditing procedures, we were able to obtain reasonable assurance that the financial statement balances affected by the material weakness identified above were fairly stated as of, and for the year ended, December 31, 1991. We believe such procedures, if implemented, would enable FDIC to verify the reasonableness of the aggregate estimates of cash recoveries on the Fund's existing inventory of failed bank assets. However, the existence of this material weakness significantly increases the risk that related balances may become materially misstated in the future if problems affecting the integrity of the data provided by FDIC's asset management system are not corrected.

Recommendations

In addition to the actions recommended by the Inspector General to address the weaknesses in FDIC's asset management system, we recommend that the Chairman of the FDIC direct the heads of the Division of Accounting and Corporate Services and Division of Liquidation to

- conduct, on a quarterly basis, an analysis of collection experience as a compensating control for evaluating the reasonableness of aggregate loss reserves on an ongoing basis and
- implement procedures to ensure that the estimated recovery values of all assets acquired from failed financial institutions are promptly and continually updated to reflect current events, such as actual appraisal results, and asset sales.

Agency Comments

We discussed our findings with the FDIC Chairman and other officials, who acknowledged that weaknesses exist in controls over the integrity of data maintained in the FDIC asset management information system. FDIC officials told us that they intend to implement our recommendation to conduct a quarterly analysis of collection experience to assist them in evaluating the reasonableness of the Fund's loss reserves. FDIC officials also stated that FDIC has established operating procedures to verify, on a quarterly basis, the accuracy of certain large adjustments to the allowance for losses based on cash recovery estimates generated from LAMIS. They said that these measures should provide better assurance that the information in LAMIS is periodically reviewed and updated to reflect current events.

While these are useful procedures, we are concerned that limiting the quarterly review of recovery estimates to large adjustments to the allowance for losses may fail to identify significant adjustments to asset carrying values in LAMIS that may be required based on recent events. We believe FDIC's procedures should ensure that all assets are properly valued to reflect the effects of recent events on their ultimate recovery.

Report on Compliance With Laws and Regulations

We have audited the financial statements of the Bank Insurance Fund as of December 31, 1991 and 1990, and have issued our opinion thereon. This report pertains only to our review of the Federal Deposit Insurance Corporation's (FDIC) compliance with laws and regulations as they relate to the Bank Insurance Fund for the year ended December 31, 1991. Our report on FDIC's compliance with laws and regulations for the year ended December 31, 1990, is presented in GAO/AFMD-92-24, dated November 12, 1991.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

FDIC's management is responsible for compliance with laws and regulations applicable to the Bank Insurance Fund. As part of obtaining reasonable assurance as to whether the financial statements were free of material misstatements, we selected and tested transactions and records to verify FDIC's compliance with certain provisions of the Federal Deposit Insurance Act, as amended (12 U.S.C. 1811 et. seq.) which, if not complied with, could have a material effect on the Bank Insurance Fund's financial statements. These provisions included those relating to (1) assessment rates (12 U.S.C. 1817(b)(1)(C)), (2) investment of amounts held by the Fund (12 U.S.C. 1823(a)(1)), and (3) issuance and sale of obligations to the Federal Financing Bank (12 U.S.C. 1824(b)).

However, it should be noted that our objective was not to provide an opinion on the overall compliance with such provisions. Accordingly, we do not express such an opinion. Also, because of the limited purpose for which our tests of compliance were made, the laws and regulations tested did not cover all legal requirements with which FDIC must comply.

The results of our tests indicate that, with respect to the transactions tested, FDIC complied, in all material respects, with those provisions of laws and regulations that could have a material effect on the Fund's financial statements. With respect to transactions not tested, nothing came to our attention that caused us to believe that FDIC had not complied, in all material respects, with those provisions.

Financial Statements

Statements of Financial Position

(dollars in thousands)

	December 31 1991	December 31 1990
Assets		
Cash and cash equivalents (Note 3)	$ 1,770,016	$ 1,122,179
Investment in U.S. Treasury obligations, net (Note 4)	3,302,861	5,649,222
Accrued interest receivable on investments and other assets	163,986	196,795
Net receivables from bank resolutions (Note 5)	21,014,834	12,935,346
Property and buildings (Note 7)	163,466	145,218
	$26,415,163	**$20,048,760**
Liabilities and the Fund Balance		
Accounts payable, accrued and other liabilities	83,835	87,942
Notes Payable - Federal Financing Bank borrowings (Note 8)	10,745,964	-0-
Liabilities incurred from bank resolutions (Note 9)	6,106,324	8,079,396
Estimated Liabilities for: (Note 11)		
Unresolved cases	16,345,871	7,685,033
Litigation losses	161,111	151,903
Total Liabilities	33,443,105	16,004,274
Fund Balance	(7,027,942)	4,044,486
	$26,415,163	**$20,048,760**

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

Statements of Income and the Fund Balance

(dollars in thousands)

	For the Year Ended December 31	
	1991	1990
Revenue		
Assessments earned (Note 12)	$ 5,160,486	$ 2,855,263
Interest on U.S. Treasury obligations	471,072	855,252
Other revenue	158,409	147,079
	5,789,967	3,857,594
Expenses and Losses		
Administrative expenses	284,147	219,581
Provision for insurance losses - Actual (Note 6)	49,192	4,448,055
Provision for insurance losses - Unresolved (Note 6)	15,427,000	7,685,033
Interest and other insurance expenses (Note 13)	1,102,056	669,962
	16,862,395	13,022,631
Net (Loss)	(11,072,428)	(9,165,037)
Fund Balance - Beginning	4,044,486	13,209,523
Fund Balance - Ending	$(7,027,942)	$ 4,044,486

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

Statements of Cash Flows

(dollars in thousands)

	For the Year Ended December 31	
	1991	**1990**
Cash Flows From Operating Activities		
Cash inflows from:		
Assessments	$ 5,163,249	$ 2,851,561
Interest on U.S. Treasury obligations	600,748	1,019,085
Recoveries from bank resolutions	7,880,293	2,700,099
Miscellaneous receipts	30,717	51,518
Cash outflows for:		
Administrative expenses	340,550	218,214
Disbursements for bank resolutions	22,902,196	9,834,529
Interest paid on indebtedness incurred from bank resolutions	259,294	309,031
Net Cash Used by Operating Activities	**(9,827,033)**	**(3,739,511)**
Cash Flows From Investing Activities		
Cash inflows from:		
Maturity and sale of U.S. Treasury obligations	2,299,319	3,199,544
Gain on sale of U.S. Treasury obligations	3,806	6,143
Cash outflows for:		
Property and buildings	20,916	48,932
Net Cash Provided by Investing Activities	**2,282,209**	**3,156,755**
Cash Flows From Financing Activities		
Cash inflows from:		
Federal Financing Bank borrowings	10,607,000	-0-
Cash outflows for:		
Payments of indebtedness incurred from bank resolutions	2,414,339	3,088,710
Cash Provided (Used) by Financing Activities	**8,192,661**	**(3,088,710)**
Net Increase (Decrease) in Cash and Cash Equivalents	**647,837**	**(3,671,466)**
Cash and Cash Equivalents - Beginning	**1,122,179**	**4,793,645**
Cash and Cash Equivalents - Ending	**$ 1,770,016**	**$ 1,122,179**

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

Notes to the Financial Statements

DECEMBER 31, 1991 and 1990

1. Legislative History and Reform

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) was enacted to reform, recapitalize and consolidate the federal deposit insurance system. FIRREA designated the Federal Deposit Insurance Corporation (FDIC) as administrator of the Bank Insurance Fund (BIF), which insures the deposits of all BIF-member institutions (normally commercial banks) and the Savings Association Insurance Fund (SAIF), which insures the deposits of all SAIF-member institutions (normally thrifts). Both insurance funds are maintained separately to carry out their respective mandates. The FDIC also administers the FSLIC Resolution Fund (FRF), which is responsible for winding up the affairs of the former Federal Savings and Loan Insurance Corporation (FSLIC).

The Omnibus Budget Reconciliation Act of 1990 removed caps on assessment rate increases and allowed for semiannual rate increases. In addition, this Act permitted the FDIC, on behalf of the BIF and the SAIF, to borrow from the Federal Financing Bank (FFB) under terms and conditions determined by the FFB.

The Federal Deposit Insurance Corporation Improvement Act of 1991 (1991 Act) was enacted to further strengthen the FDIC. The FDIC's authority to borrow from the U.S. Treasury was increased from $5 billion to $30 billion. However, the FDIC cannot incur any additional obligation for the BIF or the SAIF if the amount of obligations in the respective Fund would exceed the sum of: 1) its cash and cash equivalents; 2) the amount equal to 90 percent of the fair-market value of its other assets; and 3) its portion of the total amount authorized to be borrowed from the U.S. Treasury (excluding FFB borrowings).

As required by the 1991 Act, U.S. Treasury borrowings are to be repaid from assessment revenues. The FDIC must provide the U.S. Treasury a repayment schedule demonstrating that assessment revenues are adequate to repay principal and interest due. In addition, the FDIC now has authority to increase assessment rates more frequently than semiannually and impose emergency special assessments as necessary to ensure that funds are available for these payments.

Other provisions of the 1991 Act require the FDIC to strengthen the banking industry with improved capital standards and regulatory controls, implement a risk-based assessment system and limit insurance coverage for uninsured liabilities. The FDIC must also resolve troubled institutions in a manner that will result in the least possible cost to the deposit insurance funds and provide a schedule for bringing the reserves in the insurance funds to 1.25 percent of insured deposits.

2. Summary of Significant Accounting Policies

General. These financial statements pertain to the financial position, results of operations and cash flows of the BIF. These statements do not include reporting for assets and liabilities of closed banks for which the BIF acts as receiver or liquidating agent. Periodic and final accountability reports of the BIF's activities as receiver or liquidating agent are furnished to courts, supervisory authorities and others as required.

U.S. Treasury Obligations. Securities are intended to be held to maturity and are shown at amortized cost, which is the purchase price of securities less the amortized premium or plus the accreted discount. Such amortizations and accretions are computed on a daily basis from the date of acquisition to the date of maturity. Interest is calculated on a daily basis and recorded monthly using the constant yield method.

Allowance for Loss on Receivables from Bank Resolutions. A receivable and an associated estimated allowance for loss are established for funds advanced for assisting and closing banks. The allowance for loss represents the difference between the funds advanced and the expected repayment. The latter is based on the estimated cash recoveries from the assets of assisted or failed banks, net of all estimated liquidation costs. Estimated cash recoveries also include dividends and gains on sales from equity instruments acquired in assistance agreements (the proceeds of which are deferred pending final settlement of the assistance transaction).

Escrowed Funds from Resolution Transactions. In various resolution transactions, the BIF pays the acquirer the difference between failed bank liabilities assumed and assets purchased, plus or minus any premium or discount. The BIF considers the amount of the deduction for assets purchased to be funds held on behalf of the receivership. The funds will remain in escrow and accrue interest until such time as the receivership uses the funds to: 1) repurchase assets under asset put options; 2) pay preferred and secured claims; 3) pay receivership expenses; or 4) pay dividends.

Litigation Losses. The BIF accrues, as a charge to current period operations, an estimate of loss from litigation against the BIF in both its corporate and receivership capacities. The FDIC Legal Division recommends these estimates on a case-by-case basis.

Receivership Administration. The BIF is responsible for controlling and disposing of the assets of failed institutions in an orderly and efficient manner. The assets, and the claims against those assets, are accounted for separately to ensure that liquidation proceeds are distributed in accordance with applicable laws and regulations. Costs and expenses related to specific receiverships are charged directly to those receiverships. The BIF also recovers indirect liquidation expenses from the receiverships.

Cost Allocations Among Funds. Operating expenses (including personnel, administrative and other indirect expenses) not directly charged to each Fund under the FDIC's management are allocated on the basis of the relative degree to which the expenses were incurred by the Funds.

Depreciation. The Washington office buildings and the L. William Seidman Center in Arlington, Virginia, are depreciated on a straight-line basis over a 50-year estimated life. The San Francisco condominium offices are depreciated on a straight-line basis over a 35-year estimated life. The BIF expenses its share of furniture, fixtures and equipment at the time of acquisition because of their immaterial amounts.

Reclassifications. Reclassifications have been made in the 1990 Financial Statements to conform to the presentation used in 1991.

Related Parties. The nature of related parties and a description of related party transactions are disclosed throughout the financial statements and footnotes.

Restatement. Beginning in 1991, management has changed certain accounting presentations to more appropriately reflect financial position and cash flows. Accordingly, the following changes have affected both the Statement of Financial Position and the Statement of Cash Flows: 1) Cash and Cash Equivalents and Liabilities Incurred from Bank Resolutions for 1990 have been restated to reflect the offset of certain amounts previously included with liabilities; and 2) Net Receivables from Bank Resolutions and Liabilities Incurred from Bank Resolutions for 1990 have been restated to include capital instruments previously presented as off-balance sheet financial instruments.

3. Cash and Cash Equivalents

The BIF considers cash equivalents to be short-term, highly liquid investments with original maturities of three months or less. In 1991, cash restrictions included $8,176,000 for health insurance payable and $1,084,000 for funds held in trust. In 1990, there was a cash restriction represented by funds held in trust totaling $146,425,000. The funds related to a litigation settlement on the sale to Citicorp of the Delaware Bridge Bank (the credit card subsidiary of First RepublicBank of Texas). Those funds were released in July of 1991. Cash and cash equivalents as of December 31 consisted of the following (in thousands of dollars):

	1991	1990
Cash	$ 299,311	$ 467,033
Cash equivalents	1,470,705	655,146
	$ 1,770,016	**$ 1,122,179**

Cash and cash equivalents for 1990 have been restated to conform to the presentation used in 1991, and resulted in a decrease of $94,006,000 in the 1990 cash and cash equivalent line item.

4. U.S. Treasury Obligations

All cash received by the BIF is invested in U.S. Treasury obligations unless the cash is: 1) to defray operating expenses; 2) for outlays related to assistance to banks and liquidation activities; or 3) invested in short-term, highly liquid investments. The BIF investment portfolio as of December 31 consisted of the following (in thousands of dollars):

1991

Maturity	Description	Yield to Maturity at Market	Book Value	Market Value	Face Value
Less than one year	U.S. Treasury Bills, Notes & Bonds	4.07%	$1,619,709	$1,647,748	$1,600,000
1-3 years	U.S. Treasury Notes & Bonds	4.52%	1,683,152	1,765,410	1,700,000
			$3,302,861	**$3,413,158**	**$3,300,000**

1990

Maturity	Description	Yield to Maturity at Market	Book Value	Market Value	Face Value
Less than one year	U.S. Treasury Bills, Notes & Bonds	6.92%	$1,711,922	$1,714,568	$1,700,000
1-3 years	U.S. Treasury Notes & Bonds	7.23%	3,937,300	3,970,721	3,900,000
			$5,649,222	**$5,685,289**	**$5,600,000**

The unamortized premium, net of unaccreted discount, for 1991 and 1990 was $2,861,000 and $49,222,000, respectively. The amortized premium, net of accreted discount, for 1991 and 1990 was $47,042,000 and $76,594,000, respectively.

5. Net Receivables from Bank Resolutions

The FDIC resolution process can take various forms. Open bank assistance and assisted merger resolutions result in contractual agreements to provide ongoing assistance which allows banking operations to continue. Closed bank resolutions occur when the failing bank is closed by its chartering authority.

Net Receivables from Bank Resolutions as of December 31 consisted of the following (in thousands of dollars):

	1991	1990
Receivables from Open Banks:		
Open banks	$ 1,361,054	$ 1,724,163
Capital instruments	73,500	179,488
Notes receivable	181,500	186,000
Accrued interest receivable	6,876	7,777
Allowance for losses	(1,198,946)	(1,207,158)
	423,984	**890,270**
Receivables from Closed Banks:		
Loans and related assets	1,654,632	1,741,275
Resolution transactions (1)	38,737,855	26,063,367
Depositors' claims unpaid	10,765	509,363
Corporate purchase transactions	2,999,141	623,174
Deferred settlements (2)	(403,901)	(298,992)
Allowance for losses	(22,407,642)	(16,593,111)
	20,590,850	**12,045,076**
	$ 21,014,834	**$ 12,935,346**

(1) Includes $21 million due from SAIF for Southeast Bank, N.A., Miami, Florida, transaction, September 19, 1991

(2) Includes Continental Bank, Chicago, Illinois, transaction, September 26, 1984

As stated in Note 2, the allowance for loss on receivables from bank resolutions represents the difference between amounts advanced and the expected repayment, based upon the estimated cash recoveries from the assets of the assisted or failed bank, net of all estimated liquidation costs.

As of December 31, 1991 and 1990, the BIF, in its receivership capacity, held assets of $43.2 billion and $23.7 billion, respectively. The estimated cash recoveries from the sale of these assets (excluding cash and miscellaneous receivable of $8.9 billion) are regularly evaluated, but remain subject to uncertainties because of changing economic conditions affecting real estate assets now in the marketplace. These factors could reduce the BIF's actual recoveries upon the sale of these assets from the level of recoveries currently estimated.

Receivables from open banks include amounts outstanding to qualified institutions under the Capital Instrument Program. This program, which was established at the FDIC by authorization of the Garn-St Germain Depository Institutions Act of 1982, was extended through October 13, 1991, by the Competitive Equality Banking Act of 1987 (authority for this program has not been extended). Under this program, the BIF would purchase a qualified institution's capital instrument, such as Net Worth Certificates and Income Capital Certificates. The BIF would issue, in a non-cash exchange, its non-negotiable promissory note of equal value. The total assistance outstanding to qualified institutions as of December 31, 1991 and 1990 is $73,500,000 and $179,488,000, respectively.

6. Analysis of Changes in Allowance for Losses and Estimated Liabilities

The Provision for Loss transactions include estimates of loss for bank resolutions occurring during the year for which an estimated loss had not been previously established. It also includes loss adjustments for bank resolutions that occurred in prior periods.

Transfers consist of bank resolutions that occurred during the year for which an estimated cost had already been recognized in a previous period. Terminations represent any final adjustments to the estimated cost figures for those bank resolutions that have been completed and for which the receivership has been removed from the books of the BIF.

The Analysis of Changes in Allowance for Losses and Estimated Liabilities as of December 31 consisted of the following (in millions of dollars):

		Provision for Insurance Losses					
Allowance for Losses	Beginning Balance 01/01/91	Current Year	Prior Year	Total	Net Cash Payments	Transfers/ Adjust/Term.	Ending Balance 12/31/91
Operating Banks	$ 1,207	$ 1	$ 130	$ 131	$ (7)	$ (132)	$ 1,199
Closed Banks:							
Loans and related assets	1,120	-0-	37	37	-0-	-0-	1,157
Resolution transactions	15,067	747	(1,018)	(268)	-0-	5,793	20,592
Corporate purchases	407	-0-	258	258	-0-	(6)	659
Operating/Closed Banks	17,801	748	(590)	158	(7)	5,655	23,807
Estimated Liabilities:							
Assistance agreements	916	(132)	14	(118)	(1,102)	502	198
Litigation losses	152	-0-	9	9	-0-	-0-	161
Estimated Liabilities	1,068	(132)	23	(109)	(1,102)	502	359
Total Allowance/Estimated Liabilities Failed Banks	18,869	616	(567)	49	(1,109)	6,157	23,966
Estimated liabilities:							
Unresolved cases	7,685	15,427	-0-	15,427	-0-	(6,766)	16,346
Total Allowances/ Estimated Liabilities	$ 26,554	$ 16,043	$ (567)	$ 15,476	$ (1,109)	$ (609)	$ 40,312

6. Analysis of Changes in Allowance for Losses and Estimated Liabilities (continued)

Allowance for Losses	Beginning Balance 01/01/90	Provision for Insurance Losses Current Year	Prior Year	Total	Net Cash Payments	Transfers/ Adjust/Term.	Ending Balance 12/31/90
Operating Banks	$ 1,158	$ 2	$ 86	$ 88	$ 6	$ (45)	$ 1,207
Bridge Banks	1,750	-0-	-0-	-0-	-0-	(1,750)	-0-
Closed Banks:							
Loans and related assets	1,058	-0-	62	62	-0-	-0-	1,120
Resolution transactions	10,892	2,798	609	3,407	-0-	768	15,067
Corporate purchases	223	-0-	146	146	-0-	39	407
Operating/Bridge/ Closed Banks	15,081	2,800	902	3,702	6	(988)	17,801
Estimated Liabilities:							
Assistance agreements	2,730	-0-	716	716	(1,511)	(1,019)	916
Litigation Losses	122	-0-	30	30	-0-	-0-	152
Estimated Liabilities	2,852	-0-	746	746	(1,511)	(1,019)	1,068
Total Allowance/Estimated Liabilities Failed Banks	17,933	2,800	1,648	4,448	(1,505)	(2,007)	18,869
Estimated liabilities: Unresolved cases	1,095	7,685	-0-	7,685	-0-	(1,095)	7,685
Total Allowance/Estimated Liabilities	$19,028	$10,485	$1,648	$12,133	$(1,505)	$(3,102)	$26,554

7. Property and Buildings

Property and Buildings as of December 31 consisted of the following (in thousands of dollars):

	1991	1990
Land	$ 29,631	$ 32,024
Office buildings	149,790	126,481
Accumulated depreciation	(15,955)	(13,287)
	$163,466	$ 145,218

The 1991 net increase of $20,916,000 for land and buildings represents disbursements for completion of the L. William Seidman Center. The $2.4 million decrease in land is a reclassification of capitalized expenditures from land to buildings.

8. Note Payable - Federal Financing Bank (FFB) Borrowings

The FDIC was authorized to borrow from the FFB under the Omnibus Budget Reconciliation Act of 1990. On January 8, 1991, the FDIC and the FFB entered into a Note Purchase Agreement, renewable annually, permitting the FDIC to borrow for financing requirements. Funds borrowed will be recovered and repaid to the FFB through the liquidation of assets from failed institutions.

The terms of the note provide for quarterly renewal and rollover of borrowing, and require estimates of subsequent quarter financing needs. Periodic advances are drawn on the note as needed. Interest rates are based on the U.S. Treasury bill auction rate in effect during the quarter plus 12.5 basis points. Interest is expensed monthly and is payable quarterly. The FDIC may elect to repay any portion of the outstanding principal amount at any time consistent with the terms of the note.

As of December 31, 1991, FFB borrowings and accrued interest were $10,619,954,000 and $126,010,000, respectively. On January 2, 1992, the scheduled maturity date, the outstanding note balance was rolled over into a new borrowing that provides a borrowing authority up to $20 billion. The effective interest rates applicable for the outstanding borrowing ranged from 4.7 percent to 5.4 percent.

9. Liabilities Incurred from Bank Resolutions

Liabilities incurred from bank resolutions as of December 31 consisted of the following (in thousands of dollars):

	1991	1990
Escrowed funds from resolution transactions	$ 5,606,910	$ 3,673,279
Funds held in trust	1,084	146,425
Depositors' claims unpaid	10,765	509,363
Notes indebtedness	153,194	2,768,243
Estimated liabilities for assistance agreements	298,171	916,080
Accrued interest/other liabilities	36,200	66,006
	$ 6,106,324	**$ 8,079,396**

Maturities of these liabilities for the next five years are as follows (in thousands of dollars):

1992	1993	1994	1995	1996
$5,925,987	$29,652	$19,446	$9,566	$121,673

10. Resolution of Large Failed Bank Transactions

On-Balance Sheet Separate Asset Pools. The FDIC structured several large 1991 resolutions by negotiating Purchase and Assumption agreements between the acquiring institution and the FDIC as receiver that provided for the repurchase of classified assets by the receiver. These assets are owned by the receiver, but are managed and liquidated by the acquirer with oversight from the FDIC through the administration of a service agreement. The initial pool balance may be increased by subsequent transfers of assets (putbacks) to the FDIC over a two or three year period depending on the agreement. In addition, two transactions contain loss sharing components in which the acquirer and the FDIC as receiver share in credit losses on pool assets. One transaction involves two banking subsidiaries of Southeast Banking Corporation, Miami, Florida, that was closed on September 19, 1991. The other involves Connecticut Savings Bank, New Haven, Connecticut, that was closed on November 14, 1991.

Off-Balance Sheet Separate Asset Pools. The FDIC has negotiated several large transactions where problem assets are purchased by an acquiring institution under an agreement that calls for the FDIC to absorb credit losses and to pay related costs for funding and administration plus an incentive fee. Estimated total transaction costs for institutions involving separate asset pools include estimated costs for credit losses on all pool assets as well as funding, administration and incentives. In addition, the FDIC has a loss-sharing arrangement relating to Maine Savings Bank, Portland, Maine, closed February 1, 1991. This arrangement calls for the establishment of a deferred settlement account on the records of Fleet Bank of Maine, Portland, Maine, the acquiring institution, to which gains or losses on the final disposition of pool assets are posted. At termination of the asset pool, the FDIC pays the assuming bank the aggregate of net losses over net gains, if any.

In addition to the above costs, for which the receiver has a claim against the assets of the receivership, the FDIC incurs an interest cost on borrowing for these and other resolution transactions. Funds are borrowed from the FFB to acquire and carry assets of failed banks until they are liquidated. Interest expense on the borrowings is reflected as a period expense and not as part of the cost resulting from bank failures. In prior years the FDIC used its own cash and therefore incurred an "opportunity cost" through reduced income.

Shown below are the problem assets handled in these transactions, actual and estimated additional asset putbacks, the total volume of assets for which the FDIC remains at risk and the estimated cost of these transactions, which includes credit losses, carrying costs and administrative and incentive fee expenses (in millions of dollars):

	Date of Failure	Initial Pool Balance	Actual and Estimated Putbacks	Estimated Total Assets at Risk	Remaining Assets at Risk 12-31-91	Estimated Transaction Cost
On-Balance Sheet Pools						
First RepublicBank (a) Dallas, TX (41 banks)	07/29/88	$ 9,132	$ 2,163	$11,295	$ 2,533	$ 3,600
Bank of New England Boston, MA	01/06/91	6,380	1,450	7,830	6,552	1,034
Goldome Buffalo, NY	05/31/91	1,624	196	1,820	1,756	1,025
Southeast Bank (b) Miami/West Pensacola, FL (2 banks)	09/19/91	641	2,195	2,836	2,801	178
Bridgeport Group, Bridgeport, CT (2 banks)	08/09/91	666	785	1,451	1,451	736
New Hampshire Plan New Hampshire (7 banks)	10/10/91	1,060	298	1,358	1,358	960
Connecticut Savings New Haven, CT	11/14/91	337	-0-	337	337	112
Off-Balance Sheet Pools						
MCorp Dallas, TX (20 banks)	03/28/89	3,388	818	4,206	1,034	2,869
Texas American Bancshares Dallas, TX (24 banks)	07/20/89	1,249	267	1,516	383	1,039
Maine Savings Bank Portland, ME	02/01/91	$ 361	$ 124	$ 485	$ 485	$ 215

(a) This was an off-balance sheet pool prior to the 1991 repurchase of assets.
(b) Estimated transaction cost includes $21 million that is the responsibility of the SAIF (see Note 5).

11. Estimated Liabilities for Unresolved Cases

Unresolved Cases. In 1990, the BIF recorded as a contingent liability on its financial statements an estimated loss for its probable cost for banks that have not yet failed, but the regulatory process had identified as either equity insolvent or in-substance equity insolvent. The FDIC relied on this finding regarding solvency as the determining factor in defining the existence of the "accountable event" that triggers loss recognition under generally accepted accounting principles.

In 1991, the FDIC has taken a new view of what constitutes an accountable event for purposes of recognizing an estimated loss for future bank failures. Specifically, the FDIC has expanded its concept of banks considered to be in-substance insolvent for 1991 to include those that are solvent at year end, but which have adverse financial trends and, absent some favorable event (such as obtaining additional capital or a merger), will probably become equity deficient in 1992 or thereafter.

As with any of its contingent liabilities, the FDIC cannot predict the timing of events with reasonable accuracy. Yet, the FDIC recognizes these liabilities and a corresponding reduction in the Fund Balance in the period in which they are deemed probable and reasonably estimable. It should be noted, however, that future assessment revenues will be available to the BIF to recover some or all of these losses, and that their amounts have not been reflected as a reduction in the losses.

Liabilities for unresolved cases as of December 31, 1991 and 1990, using the definition of in-substance equity insolvent employed in 1990, were $7.8 billion and $7.7 billion respectively. Additional losses of $7.7 billion were recorded in 1991 using the expanded concept. The estimated costs for these probable bank failures are derived in part from estimates of recoveries from the sale of the assets of these banks. As such, they are subject to the same uncertainties as those affecting the BIF's net receivables from bank resolutions (see Note 5). This could understate the ultimate costs to the BIF from probable bank failures.

The FDIC estimates that 375 banks with combined assets ranging from $168 billion to $236 billion could fail in 1992 and 1993. These institutions are experiencing the effects of softening real estate markets and weakening state economies. The BIF's resolution costs of these institutions are estimated to range from $25.8 billion to $35.3 billion, of which $16.3 billion already has been recognized as a cost. The farther into the future projections of bank solvency are made, the greater the uncertainty of which banks will fail and the magnitude of the loss associated with those failures. The accuracy of these estimates will depend largely on future economic conditions, particularly in real estate markets and in the volume of real estate held by the federal government, and the resulting impact on the financial performance of banks and bank borrowers.

Litigation Losses. During a 1992 first quarter review, the FDIC Legal Division has determined that the estimated liability for unresolved legal cases could result in litigation losses as high as $330 million. This exceeds the amount recorded for 1991 as estimated liabilities for litigation losses by $169 million.

12. Assessments

The FDI Act authorizes the FDIC to set assessment rates for the BIF members semiannually, to be applied against a member's average assessment base. The assessment rate for the first semiannual period for calendar year 1991 was 0.195 percent (19.5 cents per $100 of domestic deposits). The FDIC Board of Directors approved an increase in the assessment rate to 0.230 percent (23 cents per $100 of domestic deposits) for the second semiannual period of 1991 and thereafter.

The FDI Act, as amended by the 1991 Act, authorizes the FDIC to increase assessment rates for BIF-member institutions as needed to ensure that funds are available to satisfy BIF obligations. Also, the 1991 Act requires the FDIC to provide a recapitalization schedule, not to exceed 15 years, that outlines projected semiannual assessment rate increases and interim targeted reserve ratios until the designated reserve ratio of 1.25 percent of insured deposits is achieved.

13. Interest and Other Insurance Expenses

The FDIC incurs interest expense on its note obligations, escrowed funds and FFB borrowings. Other insurance expenses are incurred by the BIF as a result of: 1) paying insured depositors in closed bank payoff activity, including funding "bridge bank" operations; 2) administering and liquidating assets purchased in a corporate capacity; and 3) administering assistance transactions.

Interest and other insurance expenses as of December 31 consisted of the following (in thousands of dollars):

	1991	1990
Interest Expense for:		
Notes payable	$ 12,282	$ 94,453
Escrowed funds from resolution transactions	664,102	313,073
FFB borrowings	237,853	-0-
	914,237	**407,526**
Insurance Expense for:		
Resolution Transactions	2,895	16,704
Corporate Purchases	55,226	43,472
Assistance Transactions	129,698	202,260
	187,819	**262,436**
	$ 1,102,056	**$ 669,962**

14. Pension Benefits, Savings Plans and Accrued Annual Leave

Eligible FDIC employees (i.e., all permanent and temporary employees with appointments exceeding one year) are covered by either the Civil Service Retirement System (CSRS) or the Federal Employee Retirement System (FERS). The CSRS is a defined benefit plan integrated with the Social Security System in certain cases. Plan benefits are determined on the basis of years of creditable service and compensation levels. The CSRS-covered employees can also participate in a federally sponsored tax-deferred savings plan available to provide additional retirement benefits. The FERS is a three-part plan consisting of a basic defined benefit plan that provides benefits based on years of creditable service and compensation levels, Social Security benefits and a tax-deferred savings plan. Further, automatic and matching employer contributions are provided up to specified amounts under the FERS. Eligible employees may participate in an FDIC sponsored tax-deferred savings plan with matching contributions. The BIF pays the related employer-portion of the costs.

The BIF's allocated share of pension benefits and savings plans expenses as of December 31 consisted of the following (in thousands of dollars):

	1991	**1990**
Civil Service Retirement System	$ 6,622	$ 6,284
Federal Employee Retirement System (Basic Benefit)	15,667	10,573
FDIC Savings Plan	7,308	5,697
Federal Thrift Savings Plan	3,838	2,181
	$ 33,435	**$ 24,735**

The liability to employees for accrued annual leave is approximately $20,444,000 and $17,062,000 at December 31, 1991 and 1990, respectively.

Although the BIF contributes a portion of pension benefits for eligible employees, it does not account for the assets of either retirement system, nor does it have actuarial data with respect to accumulated plan benefits or the unfunded liability relative to eligible employees. These amounts are reported and accounted for by the U.S. Office of Personnel Management.

15. FDIC Health, Dental and Life Insurance Plans for Retirees

The FDIC provides certain health, dental and life insurance coverage for its eligible retirees. Eligible retirees are those who have elected the FDIC's health and/or life insurance program and are entitled to an immediate annuity. The health insurance coverage is a comprehensive fee-for-service program underwritten by Blue Cross/Blue Shield of the National Capital Area, with hospital coverage and a major medical wrap-around. The dental care is underwritten by Connecticut General Insurance Company. The FDIC makes the same contributions for retirees as those for active employees. The FDIC benefit programs are fully insured. Effective January 1, 1991, the funding mechanism was changed to a "minimum premium funding arrangement." Fixed costs and expenses for incurred claims are paid as incurred. Premiums are deposited for IBNR (incurred but not reported) claims and held by the Corporation.

The life insurance program is underwritten by Metropolitan Life Insurance Company. The program provides for basic coverage at no cost and allows converting optional coverages to direct-pay plans with Metropolitan Life. The FDIC does not make any contributions towards an annuitants' basic life insurance coverage; this charge is built into rates for active employees.

The BIF's allocated share of retiree benefits provided as of December 31 are as follows (in thousands of dollars):

	1991	1990
Health premiums paid	$ 573	$ 434
Dental premiums paid	30	36

The FASB has issued Statement of Financial Accounting Standards No. 106 (Employers' Accounting for Postretirement Benefits Other Than Pensions), which the FDIC is required to adopt by 1993. The standard requires companies to recognize postretirement benefits during the years employees are working and earning benefits for retirement. Resulting estimated expenses will be allocated to the BIF based on the relative degree to which expenses were incurred. Although the impact of the FDIC's adoption of the standard cannot reasonably be estimated at this time, the standard may increase reported administrative costs and expenses of the BIF.

16. Commitments

Leases. Lease agreement commitments for the BIF office space are $87,841,381 for future years. The agreements contain escalation clauses resulting in adjustments, usually on an annual basis. The BIF recognized leased space expense of $37,294,000 and $31,284,000 for the years ended December 31, 1991 and 1990, respectively.

The BIF's allocated share of leased space fees for future years, which are committed per contractual agreement, are as follows (in thousands of dollars):

1992	1993	1994	1995	1996
$25,968	$22,823	$19,028	$13,029	$6,993

Asset Putbacks. Upon resolution of a failed bank, the assets are placed into receivership and may be sold to an acquirer under an agreement that certain assets may be "put back" or resold to the receivership at the recognized book value within a defined period of time. It is possible that the BIF could be called upon to fund the purchase of any or all of the "unexpired puts" at any time prior to expiration. The FDIC's estimate of the volume of assets that are subject to put under existing agreements is $5.2 billion including $1.3 billion from the April sale of the Bank of New England franchise to Fleet/Norstar and $2 billion from the Southeast Bank assistance transaction. The total amount that will be repurchased and the losses resulting from these acquisitions is not reasonably estimable at December 31, 1991.

17. Concentration of Credit Risk

The BIF is counterparty to a group of financial instruments with entities located throughout regions of the United States experiencing problems in both loans and real estate. The BIF's maximum exposure to possible accounting loss, should each counterparty to these instruments fail to perform and any underlying assets prove to be of no value, is shown as follows (in millions of dollars):

December 31, 1991

	South-East	South-West	North-East	Mid-West	Central	West	Total
Net receivables from bank resolutions	$ 3,549	$ 1,815	$12,394	$ 16	$ 369	$ 532	$18,675
Corporate purchases (net)	6	2,140	111	-0-	36	47	2,340
Asset putback agreements (off-balance sheet)	2,106	-0-	3,053	-0-	-0-	-0-	5,159
Total	**$ 5,661**	**$ 3,955**	**$15,558**	**$ 16**	**$ 405**	**$ 579**	**$ 26,174**

18. Supplementary Information Relating to the Statements of Cash Flows

Reconciliation of net loss to net cash used by operating activities for the year ended December 31 (in thousands of dollars):

	1991	1990
Net (Loss)	$(11,072,427)	$(9,165,037)
Adjustments to reconcile net loss to net cash used by operating activities:		
Provision for insurance losses	15,476,192	12,133,088
Amortization of U.S. Treasury obligations	47,042	76,594
Interest on Federal Financing Bank borrowings	126,010	-0-
Gain on sale of U.S. Treasury obligations	(3,806)	(6,143)
Depreciation expense	2,667	765
Decrease in assessment receivable	630	1,387
Increase (decrease) in accounts payable, accrued and other liabilities	(9,845)	31,359
Decrease in accrued interest receivable on investments and other assets	188,658	20,159
Disbursements for bank resolutions not impacting income	(14,861,031)	(7,166,372)
Accrual of assets and liabilities from bank resolutions	278,877	334,689
Net cash used by operating activities	**$(9,827,033)**	**$(3,739,511)**

The non-cash financing activity for the year ending December 31, 1991 included: 1) a write-down of a note payable totaling $92,261,000 resulting from the repurchase of stock owned by the Corporation and 2) an increase to notes payable of $12,954,181 resulting from the rollover of accrued interest on borrowings from the FFB.

In 1990, there was an increase of $2.1 billion in net receivables from bank resolutions and a reciprocal increase in liabilities incurred from bank resolutions. These transactions were for notes issued and for the establishment of valuation allowances for failed banks previously presented as unresolved contingent liabilities.

As stated in the Summary of Significant Accounting Policies (See Note 2, Escrowed Funds from Resolution Transactions), the BIF pays the acquirer the difference between failed bank liabilities assumed and assets purchased, plus or minus any premium or discount. The BIF considers the assets purchased portion of this transaction to be a non-cash adjustment. Accordingly, for Cash Flow Statement presentation, cash outflows for bank resolutions excludes $4.9 billion in 1991 and $3.3 billion in 1990 for assets purchased.

19. Subsequent Events

CrossLand Savings Bank, FSB, New York, New York

On January 24, 1992, CrossLand Savings Bank was closed by the Office of Thrift Supervision (OTS) and the FDIC was appointed receiver. The receiver organized a new assuming savings bank (CrossLand Federal Savings Bank) and the charter was approved by the OTS. The OTS appointed the FDIC as conservator of the assuming bank, which acquired virtually all of the assets, deposits and certain non-deposit liabilities of the failed bank. In 1991, the BIF recorded an estimated loss of $1.1 billion for this transaction.

Dollar Dry Dock Savings Bank, White Plains, New York

On February 21, 1992, Dollar Dry Dock was declared insolvent by the state chartering authority and subsequently closed and the FDIC was appointed receiver. The FDIC approved the sale of the failed institution to Emigrant Savings Bank of New York. The BIF recorded an estimated loss of $600 million for this transaction.

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