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Report to the Congress

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FINANCIAL AUDIT

Federal Deposit Insurance Corporation's 1993 and 1992 Financial Statements

GAO

United States
General Accounting Office
Washington, D.C. 20548

Comptroller General
of the United States

B-253861

June 24, 1994

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 Bank Insurance Fund, the Savings Association Insurance Fund, and the Federal Savings and Loan Insurance Corporation (FSLIC) Resolution Fund for the years ended December 31, 1993 and 1992. These financial statements are the responsibility of the Federal Deposit Insurance Corporation (FDIC), the administrator of the three funds. This report also includes our opinion on FDIC's system of internal controls as of December 31, 1993. FDIC has made significant progress in addressing the internal control weaknesses we reported in 1992. However, a material weakness existed as of December 31, 1993, in FDIC's internal controls over its process for valuing failed institution assets. This report also discusses our evaluation of FDIC's compliance with laws and regulations during 1993.

In addition, this report includes our recommendations to improve FDIC's internal controls and discusses our concerns about the capitalization of the Savings Association Insurance Fund, the continued uncertainties surrounding the cost of financial institution failures, and improvements in the banking and savings association industries which have substantially accelerated the recapitalization of the Bank Insurance Fund and reduced the exposure of both the Bank Insurance Fund and the Savings Association Insurance Fund to losses from failed institutions. This report also discusses a $410 million reduction in the Bank Insurance Fund's estimated liability for troubled institutions, which FDIC reported on the fund's first quarter 1994 financial statements but which resulted from conditions as of December 31, 1993, and, therefore, more appropriately should have been reflected in the Bank Insurance Fund's financial statements as of December 31, 1993.

We conducted our audits pursuant to the provisions of section 17(d) of the Federal Deposit Insurance Act, as amended (12 U.S.C. 1827(d)), and in accordance with generally accepted government auditing standards.

We are sending copies of this report to the Acting Chairman of the Board of Directors of the Federal Deposit Insurance Corporation; the Chairman of the Board of Governors of the Federal Reserve System; the Comptroller of the Currency; the Acting Director of the Office of Thrift Supervision; 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; the Secretary of the Treasury; the Director of the Office of Management and Budget; and other interested parties.

This report was prepared under the direction of Robert W. Gramling, Director, Corporate Financial Audits. Other major contributors to this report are listed in appendix III.

Charles A. Bowsher
Comptroller General
of the United States

Contents

Abbreviations

BIF	Bank Insurance Fund
CFO	Chief Financial Officers Act
FDIC	Federal Deposit Insurance Corporation
FDICIA	Federal Deposit Insurance Corporation Improvement Act
FICO	Financing Corporation
FIRREA	Financial Institutions Reform, Recovery, and Enforcement Act
FRF	FSLIC Resolution Fund
FSLIC	Federal Savings and Loan Insurance Corporation
LAMIS	Liquidation Asset Management Information System
REFCORP	Resolution Funding Corporation
RTC	Resolution Trust Corporation
SAIF	Savings Association Insurance Fund

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To the Board of Directors
Federal Deposit Insurance Corporation

We have audited the statements of financial position as of December 31, 1993 and 1992, of the three funds administered by the Federal Deposit Insurance Corporation (FDIC), and the related statements of income and fund balance (accumulated deficit) and statements of cash flows for the years then ended. For these three funds—the Bank Insurance Fund (BIF), the Savings Association Insurance Fund (SAIF), and the Federal Savings and Loan Insurance Corporation (FSLIC) Resolution Fund (FRF)—we found that the financial statements, taken as a whole, were fairly stated as of December 31, 1993.

During our prior year's audits of the 1992 financial statements of the three funds,[1] we identified several significant weaknesses in FDIC's internal controls which adversely affected its ability to manage, liquidate, and report on the large volume of assets acquired from failed financial institutions. These weaknesses also affected FDIC's ability to accurately report transactions associated with BIF's and FRF's resolution and liquidation activity, and increased the risk of misappropriation of assets. We noted that this could add to the losses on failed institution assets being incurred by the funds. We also identified significant weaknesses in FDIC's time and attendance processing controls which increased the risk of inappropriate payroll expenditures and exposed SAIF to significant misapplication of payroll and other overhead expenditures. In addition to these weaknesses, which we considered material,[2] we identified other weaknesses in FDIC's internal controls which affected its ability to ensure that internal control objectives were achieved. We made a number of

[1]Financial Audit: Federal Deposit Insurance Corporation's 1992 and 1991 Financial Statements (GAO/AIMD-93-5, June 30, 1993) and Financial Audit: Federal Deposit Insurance Corporation's Internal Controls as of December 31, 1992 (GAO/AIMD-94-35, February 4, 1994).

[2]A material weakness is a reportable condition in which the design or operation of the 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 promptly by employees in the normal course of their assigned duties. Reportable 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 laws and regulations, or (3) properly record, process, and summarize transactions to permit the preparation of financial statements. Reportable conditions which are not considered material nevertheless represent significant deficiencies in the design or operation of internal controls and need to be corrected by management.

recommendations to address each of the weaknesses identified in our 1992 audits.

In conducting our 1993 audits, we found that FDIC had made significant progress in addressing the internal control weaknesses we identified in our 1992 audits. FDIC's actions during 1993 fully resolved one weakness we considered material and resolved the other weaknesses to the extent that, while still significant conditions, we no longer consider them material. Also, FDIC's actions prior to year-end 1993 adequately addressed four of the six other weaknesses we identified during our 1992 audits. Additional actions FDIC took prior to the completion of our 1993 audits corrected one of the other two weaknesses.

While FDIC has acted aggressively to improve its system of internal controls, additional improvements are needed. Our 1993 audits identified a material weakness in FDIC's internal accounting controls over its process for estimating recoveries it will realize on the management and disposition of BIF's and FRF's inventory of failed institution assets. In addition, despite progress made by FDIC, we continued to identify weaknesses, though not material, in controls over FDIC's time and attendance processes and oversight of contracted asset servicing entities. We also continued to note weaknesses in computer security, although these weaknesses were corrected prior to the completion of our 1993 audits.

During our 1993 audits, we noted continued improvement in the condition of the nation's banking and savings institutions. These improvements have resulted in an acceleration of BIF's recapitalization and have reduced both BIF's and SAIF's exposure to significant losses from financial institution failures. We caution, however, that BIF's exposure to losses from past and future institution failures continues to be subject to significant uncertainties. In addition, SAIF is significantly undercapitalized, and building up SAIF's reserves through premium assessments of insured members is a slow process which can be affected by events impacting the savings association industry.

Summary of Results

The following section presents (1) our opinions on the 1993 financial statements of the three funds administered by FDIC, (2) our opinion on FDIC's internal controls as of December 31, 1993, as it relates to the three funds, (3) the results of our tests for compliance with significant provisions of selected laws and regulations, and (4) the responsibilities of

FDIC and the auditor with regard to the financial statements, internal controls, and compliance with laws and regulations.

Opinions on Financial Statements

In our opinion:

- The financial statements and accompanying notes of the Bank Insurance Fund present fairly, in all material respects, BIF's financial position as of December 31, 1993 and 1992, and the results of its operations and its cash flows for the years then ended, in conformity with generally accepted accounting principles.
- The financial statements and accompanying notes of the Savings Association Insurance Fund present fairly, in all material respects, SAIF's financial position as of December 31, 1993 and 1992, and the results of its operations and its cash flows for the years then ended, in conformity with generally accepted accounting principles.
- The financial statements and accompanying notes of the FSLIC Resolution Fund present fairly, in all material respects, FRF's financial position as of December 31, 1993 and 1992, and the results of its operations and its cash flows for the years then ended, in conformity with generally accepted accounting principles.

Opinion on Internal Controls

We evaluated whether FDIC's internal controls in effect on December 31, 1993, provided reasonable assurance that losses, noncompliance, or misstatements material in relation to the financial statements would be prevented or detected.

In our opinion, internal controls as of December 31, 1993, provided reasonable assurance that (1) assets of BIF, SAIF, and FRF were safeguarded against loss from unauthorized acquisition, use, or disposition, (2) transactions of SAIF were properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with generally accepted accounting principles, and (3) transactions of BIF, SAIF, and FRF were executed in accordance with significant provisions of selected laws and regulations.

However, in our opinion, because of the material weakness in FDIC's process for estimating recoveries on failed institution assets, internal controls as of December 31, 1993, did not provide reasonable assurance that transactions of BIF and FRF were properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with generally accepted accounting principles. Through substantive audit procedures, we were able to satisfy ourselves that this weakness did not have a material effect on the 1993 financial statements of the two funds.

Misstatements may nevertheless occur in other FDIC-reported financial information on BIF and FRF as a result of the material internal control weakness we identified. Also, significant uncertainties associated with the cost of past and future financial institution failures as discussed below and disclosed in the applicable notes to BIF's and FRF's financial statements may ultimately result in substantial changes in the recovery value of advances to receiverships and corporate-owned assets held by BIF and FRF.

Also, because of inherent limitations in any system of internal controls, losses, noncompliance, or misstatements may nevertheless occur and not be detected. We also caution that projecting our favorable evaluation of certain controls 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 such controls may deteriorate.

Compliance With Laws and Regulations

Our tests for compliance with significant provisions of selected laws and regulations disclosed no material instances of noncompliance. With respect to laws and regulations that we tested, our limited tests would not necessarily detect all material instances of noncompliance. However, nothing came to our attention in the course of our work to indicate that material noncompliance with such provisions occurred.

Responsibilities of the Corporation and the Auditor

The management of FDIC is responsible for (1) preparing the financial statements of BIF, SAIF, and FRF in conformity with generally accepted accounting principles, (2) establishing and maintaining internal controls and systems to provide reasonable assurance that the internal control objectives previously mentioned are met, and (3) complying with applicable laws and regulations.

As the auditor of record, we are responsible for (1) obtaining reasonable assurance about whether the financial statements are free of material misstatement and presented fairly in conformity with generally accepted accounting principles, (2) obtaining reasonable assurance about whether relevant internal controls are in place and operating effectively, and

(3) testing compliance with significant provisions of selected laws and regulations.

Our audits were conducted in accordance with generally accepted government auditing standards. We believe our audits provide a reasonable basis for our opinions.

Discussed in the following sections are significant matters considered in performing our audits and forming our opinions. This report also discusses each of our conclusions in more detail. The scope and methodology of our audits is presented in appendix I.

Significant Matters

The following information is presented to highlight the condition and outlook of the banking and thrift industries and the insurance funds. We also discuss significant uncertainties that could affect the future financial condition of the insurance funds. Also, we discuss FDIC's significant progress in addressing internal control weaknesses we identified during our 1992 audits.

The Condition of FDIC-Insured Institutions Has Continued to Improve

The condition of FDIC-insured commercial banks improved significantly during 1993. Commercial banks posted record earnings of over $43.4 billion, an increase of 36 percent over the previous record of $32 billion set in 1992. The substantial improvements in the condition of commercial banks have been attributable primarily to continued favorable interest rates and significant improvements in asset quality. Both noncurrent loans and other real estate owned (repossessed collateral) have declined from a peak of 3.19 percent of total assets in mid-1991, to 1.61 percent of total assets at the end of 1993, the lowest level since 1986. Commercial banks have also realized large increases in noninterest income, which accounted for over 23 percent of total earnings in 1993. As a result of improved earnings and asset quality, commercial banks' equity capital increased to over 8 percent of total assets for the first time in 30 years.

The substantial improvement in the condition of FDIC-insured commercial banks has also been reflected in the continued reduction in the number of these banks identified by FDIC as problem institutions. At year-end 1993, 426 commercial banks, with total assets of $242 billion, were identified by FDIC as problem institutions, the lowest number since 1982. This represents a substantial decline from the 787 commercial banks, with total assets of $408 billion, which FDIC identified as problem institutions at year-end 1992. Similarly, bank failures have declined significantly. During 1993, 42 FDIC-insured commercial banks failed. In comparison, during 1992, 98 commercial banks failed. Commercial bank failures in 1993 represent the fewest since 1982, when 34 failed.

The condition of FDIC-insured savings institutions also continued to improve during 1993. Privately-held FDIC-insured savings institutions (those not under the government's control) earned $7 billion in 1993. This is the third consecutive year of positive earnings for savings institutions after four consecutive years of losses. Full-year net income and the average return on assets were the highest reported by savings institutions during the past 10 years, with nearly 95 percent of savings institutions reporting positive earnings for 1993. Positive earnings were attributable primarily to favorable interest rates and the decline in troubled assets. Troubled assets, such as noncurrent loans and leases and other real estate owned, declined to 2.1 percent of total industry assets in 1993 from 3.07 percent in 1992. As a result of improved earnings and asset quality, savings institutions' 1993 equity capital increased to 7.85 percent of total industry assets from 7.22 percent in 1992.

Continued improvements in the financial condition of FDIC-insured savings institutions has also resulted in a significant decline in the number and size of savings institutions identified by regulators as problem institutions. As of December 31, 1993, regulators identified 146 savings institutions, with assets totaling $92 billion, as problem institutions. In comparison, as of December 31, 1992, 276 savings institutions, with assets totaling $184 billion, were identified as problem institutions by the regulators.

Strengthened Banking Industry Has Accelerated BIF's Recapitalization

The continued improvements in the condition of the banking industry have substantially accelerated the recapitalization of BIF. During 1993, BIF reported net income of $13.2 billion, the second consecutive year of positive results after four consecutive years of losses. This improvement resulted principally from insurance assessments and the reduction of reserves no longer considered necessary for insurance losses. The net income increased the fund balance from a $101 million deficit as of December 31, 1992, to a $13.1 billion positive balance, or about 0.69 percent of insured deposits as of December 31, 1993. FDIC currently projects that by 1996, BIF will achieve the ratio of reserves to insured deposits of 1.25 percent designated by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). This is 10 years earlier than anticipated by FDIC in its initial recapitalization schedule prepared in September 1992. Under the fund recapitalization requirements of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), FDIC was required to establish a recapitalization schedule for BIF to achieve the designated reserve ratio not later than 15 years after the schedule was implemented and to set insurance assessments in accordance with this schedule. However, if this goal is achieved sooner, as currently projected, FDIC will be able to significantly reduce assessment rates far earlier than had been anticipated.

SAIF Remains Significantly Undercapitalized

While the current condition of BIF is very positive, SAIF continues to be significantly undercapitalized. SAIF was created by FIRREA in 1989 without any initial capitalization. Over the past 4 years, assessments from SAIF-insured members have increased SAIF's fund balance to $1.2 billion as of December 31, 1993. Despite this growth, SAIF's ratio of reserves to estimated insured deposits as of December 31, 1993, was only 0.17 percent—substantially below the reserve ratio of 1.25 percent designated by FIRREA. FDIC's most recent projections indicate that SAIF will not achieve the designated 1.25 percent ratio of reserves to estimated insured deposits until the year 2004, when its fund balance is estimated to be about $7 billion.

The projected growth of SAIF's fund balance is based, in part, on the assumption that SAIF will not incur substantial losses from the failure of insured members. The Congress provided safeguards for this risk by enacting legislation to further strengthen SAIF. Specifically, FDICIA authorized FDIC to borrow up to $30 billion from the U.S. Treasury, on behalf of SAIF or BIF, to cover insurance losses.[3] Also, in December 1993, the Resolution Trust Corporation (RTC) Completion Act extended RTC's resolution responsibility through a date between January 1, 1995, and July 1, 1995.[4] The act also restored to RTC through December 31, 1995, $18.3 billion[5] to resolve troubled savings associations and provided that

[3]Through December 31, 1993, FDIC had borrowed no funds from the U.S. Treasury to cover insurance losses of either BIF or SAIF.

[4]RTC was responsible for assisting and resolving troubled SAIF members whose accounts had been insured by FSLIC and that had been placed in conservatorship or receivership from January 1, 1989, through September 30, 1993. The RTC Completion Act extended RTC's resolution responsibility and requires the chairperson of the Thrift Depositor Protection Oversight Board to select the actual date of termination. However, the date is to be no earlier than January 1, 1995, and no later than July 1, 1995.

[5]The act amended section 21A(i) of the Federal Home Loan Bank Act by removing the April 1, 1992, deadline for obligating $25 billion provided to RTC by Public Law 102-233 for resolution activity; through April 1, 1992, RTC had obligated $6.7 billion of the $25 billion.

any of these funds not used by RTC would become available for SAIF's insurance losses from December 31, 1995, through 1997. In addition, the act authorized up to $8 billion for insurance losses in fiscal years 1994 through 1998. However, as explained in the notes to SAIF's financial statements, both FDICIA and the RTC Completion Act contain certain requirements and restrictions regarding SAIF's access to and use of these funding sources. If these funds are not available to SAIF when needed, the impact of a single large institution failure could adversely affect SAIF's ability to achieve the designated reserve ratio within the currently projected period and may ultimately affect its solvency.

In addition, the future growth of SAIF's fund balance depends on the amount of assessments collected from insured members. However, from its inception through December 31, 1992, the share of industry assessments received by SAIF was minimal because FIRREA mandated that the Financing Corporation (FICO), the Resolution Funding Corporation (REFCORP), and FRF have prior claim on SAIF member assessments.[6] Beginning in 1993, only FICO continues to have prior claim on assessments from SAIF members, with SAIF receiving all remaining assessments. Each year, FICO receives approximately $800 million of SAIF member assessments to pay bond interest. In 1993, this amounted to approximately 46 percent of SAIF's gross assessment revenue. This claim and its impact on SAIF member assessments will continue until the year 2019, when FICO's bonds fully mature.

Until January 1, 1998, FDIC must set assessment rates at a level that will enable SAIF to achieve the designated reserve ratio within a reasonable period. After January 1, 1998, FDIC must set assessments for SAIF to meet the designated reserve ratio according to a 15-year schedule.[7] Once the ratio is met, FDIC can reduce the assessment rates charged to SAIF members. Since SAIF's fund balance is not projected to achieve the designated reserve ratio until the year 2004, FDIC anticipates that SAIF member assessment rates will be significantly higher than those projected

[6]FICO was established in 1987 to recapitalize FSLIC, and was given first claim on insurance assessments of SAIF members for payment of interest and custodial costs on its bonds. Although FICO no longer has authority to issue bonds, its claim to the insurance assessments will continue until the 30-year recapitalization bonds mature. In addition, REFCORP, established in 1989 to provide funding for RTC, was entitled to insurance assessments of SAIF members to finance payment of bond principal. REFCORP ceased all future bond issuances in early 1991 and therefore has no further claim to insurance assessments. Finally, FRF, established in 1989 to liquidate the assets and liabilities of the former FSLIC, was entitled, through December 31, 1992, to the insurance assessments not taken by FICO or REFCORP. Any remaining assessments belonged to SAIF.

[7]FDIC may extend the date specified in the schedule to a later date that it determines will, over time, maximize the amount of assessments received by SAIF, net of insurance losses incurred by SAIF.

for BIF members. FDIC predicts that BIF will achieve its designated reserve ratio 8 years earlier than SAIF, thus allowing FDIC to substantially reduce assessment rates for BIF members long before it can implement similar rate reductions for SAIF members. During this period, FDIC expects the average BIF assessment rate to range from 5 to 12 basis points (5 cents to 12 cents per $100 of deposits), compared to a projected average SAIF assessment of approximately 25 basis points.

Once SAIF reaches the designated reserve ratio, SAIF member assessment rates will continue to be significantly higher than those projected for BIF members because of the required future FICO payments, which equate to approximately 11 basis points. The SAIF Industry Advisory Committee[8] reported in March 1994 that this potentially wide disparity in the assessment rates charged to BIF and SAIF members could adversely affect SAIF members' ability to raise sufficient capital because of their competitive disadvantage with banks. This, in turn, could lead to failures of SAIF members which would result in a shrinking assessment base and less assessments available to fund future FICO payments and build SAIF's reserves to its designated ratio of reserves to estimated insured deposits. The SAIF Industry Advisory Committee recommended a merger of BIF and SAIF to resolve these concerns.

Uncertainties Affect the Cost of Past and Future Institution Failures

Estimates of the ultimate cost of past and potential failures are subject to significant uncertainties, such as future market conditions and changes in interest rates. FDIC's estimates of the costs of past resolutions depend, to a large degree, on the level of recoveries FDIC expects to realize on BIF's and FRF's inventory of failed institution assets. Similarly, estimates of future resolution costs encompass both FDIC's judgment concerning the likelihood of the failure of troubled institutions, and the expected cost of those that do fail, based on past resolution experience. Both the realizable value of assets acquired from previously failed institutions and the future viability of troubled institutions can be significantly affected by market conditions and interest rates.

The continued improvement in the condition of BIF-insured institutions allowed FDIC to reduce its estimate of the cost likely to be incurred by BIF in the resolution of troubled institutions by nearly $8 billion during 1993.

[8]The SAIF Industry Advisory Committee was created by FIRREA to advise the Congress on regulatory and other matters affecting financial institutions that are SAIF members. The committee is comprised of 12 representatives of SAIF members and 6 representatives of the public interest. The committee meets quarterly (or more frequently, if requested by the Congress), and reports to the Congress semiannually. FIRREA specified that the committee will cease to exist on August 9, 1999.

As of December 31, 1993, BIF's estimated liability for troubled institutions considered likely to fail, as reported on its financial statements, totaled $3 billion. In comparison, as of December 31, 1992, this estimate totaled $10.8 billion. However, the December 31, 1993, estimated liability does not include an additional $410 million reduction which FDIC estimated based upon continued financial improvement of certain institutions as reflected in 1993 year-end reports they filed with regulators. This additional reduction in BIF's exposure to troubled institutions reflects events which occurred during 1993 and, accordingly, should have been recognized in BIF's December 31, 1993, financial statements. However, FDIC reflected the reduction in BIF's March 31, 1994, quarterly financial statements. The effect of omitting this adjustment from BIF's 1993 financial statements is not considered material to the overall fair presentation of BIF's 1993 financial statements. However, it represents nearly 20 percent of BIF's net income for the 3 months ended March 31, 1994. Nevertheless, if the interest rate environment remains relatively stable and levels of problem assets continue to decline, the estimated liability for troubled institutions could be reduced further during 1994.

Significant uncertainties also affect the receivables from bank or thrift resolutions and investments in corporate-owned assets reported on the financial statements of BIF and FRF. These amounts represent funds advanced to resolve previously failed institutions or to purchase assets of terminated receiverships. As of December 31, 1993, BIF's and FRF's financial statements included $14.4 billion and $2.8 billion, respectively, of such advances, net of an allowance for losses. These advances are repaid from collections from the management and disposition of failed institution assets. The allowance for losses represents the difference between amounts advanced and the expected repayment, based on estimates of recoveries to be received from the management and liquidation of the failed institution assets, net of all estimated liquidation costs. In the event of a deterioration in economic conditions, the marketability of these assets could be adversely affected, as could the ability of the responsible debtors to repay their outstanding loans. Should this occur, actual recoveries on these assets could be significantly less than current estimates.

Significant Progress on 1992 Audit Recommendations

In our reports on the results of our 1992 audits of FDIC's financial statements, we identified material weaknesses in FDIC's internal accounting controls over (1) contractors engaged to service and liquidate failed bank assets, (2) data maintained in FDIC's asset management information system and reconciliations between this system and FDIC's general ledger system, (3) reconciliations between FDIC's primary performing commercial and residential loan servicer's systems and FDIC's asset management and general ledger systems, and (4) FDIC's time and attendance reporting process. The weaknesses in FDIC's internal accounting controls over its management and liquidation of failed institution assets adversely affected its ability to safeguard these assets against loss from unauthorized acquisition, use, or disposition and ensure that transactions associated with asset servicing and disposition activities were properly accounted for and reported on BIF's and FRF's financial statements. Also, the weaknesses in internal accounting controls over FDIC's time and attendance reporting process adversely affected its ability to ensure that established policies and procedures were adhered to or that payroll and other related expenses were properly allocated among the three funds.

During 1993, FDIC implemented a number of our recommendations to address these weaknesses. FDIC's actions during the year fully resolved one weakness we deemed material and resolved the other weaknesses to the extent that, while still significant conditions during 1993, we no longer consider them material weaknesses. Specifically, FDIC:

- Developed a computerized report to identify differences between the systems of its performing commercial and residential loan servicer and FDIC's asset management information and general ledger systems. As a result of this automation, FDIC can more efficiently use its resources in identifying and resolving the reconciling items associated with the differences between these systems.
- Progressed in identifying and resolving differences between book values of receivership and corporate-owned assets recorded in its financial information and asset management information systems. While some consolidated receivership offices continue to experience differences in reported asset book values between the two systems, these differences are not considered material in the aggregate. In addition, FDIC progressed in maintaining and updating system data files to reflect current information affecting the condition and potential recoveries on assets in liquidation.
- Increased the number of personnel under its Contractor Accounting Oversight Group and assigned to them the responsibility for reconciling monthly the reported asset pool balances between contracted asset servicers' records and FDIC's general ledger control accounts. It also distributed to the servicers' internal audit departments a list of critical audit areas that should be addressed through internal audits each year. In addition, it established a policy requiring the servicers to adopt FDIC's

procedures for calculating recovery estimates on serviced assets. While weaknesses still exist in reconciling the serviced asset pool balances to FDIC's general ledger system and performing audit procedures on critical servicer functions, the affect of these weaknesses is no longer considered material.

- Revised its Time and Attendance Reporting Directive and issued other related guidance to (1) require separation of the timekeeping, data input, and reconciliation functions, (2) emphasize the importance of charging time to the proper fund, (3) address the proper use of the common services fund, and (4) ensure review of time and attendance reports. While FDIC improved time and attendance reporting guidance enough that we no longer consider this weakness material, additional action is needed to ensure consistent adherence to the revised procedures.

In addition to the material weaknesses discussed above, our reports on our 1992 audits also noted other reportable conditions which affected FDIC's ability to ensure that internal control objectives were achieved. These involved weaknesses in FDIC's controls over (1) access to computerized information systems' hardware and software, (2) cash receipts at some consolidated receivership sites, (3) accounting methodologies used by certain asset servicers, (4) recording assessment revenue due SAIF, (5) recording exit fee transactions, and (6) authorization of adjustments to the financial statements. We reported that these weaknesses, though not material, impaired the ability of FDIC's system of internal accounting controls to ensure accurate reporting of financial transactions and proper safeguarding of assets, and we made several recommendations to correct them.

During 1993, FDIC acted to address these weaknesses. For four of the six weaknesses, FDIC's actions addressed our concerns to the extent that, as of December 31, 1993, we no longer considered them to be reportable conditions. Specifically, FDIC:

- Adopted uniform procedures for processing and reconciling cash receipts at its consolidated receivership offices. Because FDIC is in the process of merging certain consolidated receivership offices as part of its downsizing efforts, continued monitoring of these new procedures is particularly important in view of the anticipated increase in activity at key offices.
- Established a systematic ongoing process for conducting audits of assessments due SAIF. This process, if implemented as designed, can be an effective internal control. However, if the full potential of this control is to be realized, FDIC will need to ensure that (1) these audits encompass all

institutions owing material levels of assessments to SAIF and (2) any resulting material audit adjustments are reflected in the proper accounting period, consistent with generally accepted accounting principles.

- Improved its process for reconciling exit fee reports. During 1993, this improved reconciliation successfully identified material discrepancies, and all adjustments arising out of audits of exit fees were properly recorded in the general ledger.
- Developed written procedures governing the processing of financial reporting adjustments. The requirements of these procedures, if adhered to, appear adequate to address the concerns we reported during our 1992 audits.

However, FDIC's actions during 1993 did not fully correct the weaknesses we identified in its internal controls over access to computerized information systems software and hardware and accounting methodologies used by certain asset servicers. Thus, we continue to consider these weaknesses reportable conditions as of December 31, 1993. However, actions to strengthen controls over computer security, which FDIC took before the completion of our audits, if adhered to, should correct this weakness. These actions are discussed in a later section of this report.

Material Internal Control Weakness Exists in Asset Recovery Estimation Process

During our 1993 audits, we identified a material weakness in FDIC's internal accounting controls over its process for estimating recoveries it will realize on the management and disposition of BIF's and FRF's inventory of failed institution assets. These estimates form the basis for establishing BIF's and FRF's allowance for losses on their respective balances of subrogated claims and investment in corporate-owned assets. Specifically, internal accounting controls are not adequate to ensure that consistent and sound methodologies are used to estimate recoveries on failed institution assets. Also, internal controls are not effective in ensuring that proper documentation is maintained to support recovery estimates.

Although we were able to satisfy ourselves that this weakness did not have a material effect on the 1993 financial statements of the funds, this weakness could result in material misstatements in future financial statements and other financial information if not corrected by FDIC. The magnitude of these misstatements could be further exacerbated when FDIC assumes responsibility for managing and disposing of failed institution assets transferred from RTC when it terminates its asset disposition operations. RTC is currently scheduled to terminate its operations and transfer any remaining receivership assets to FDIC no later than December 31, 1995.

FDIC uses the Liquidation Asset Management Information System (LAMIS) to assist in managing assets of failed institutions that are primarily serviced internally by FDIC personnel. FDIC also contracts with private entities to service large pools of receivership and corporate-owned assets from failed banks resolved by BIF. As of December 31, 1993, BIF and FRF held failed institution assets with a book value of $25 billion and $2.7 billion, respectively. Estimates of recoveries from the management and disposition of these assets are used to determine the allowance for losses on BIF's and FRF's balances of subrogated claims and investments in corporate-owned assets. To ensure the reliability of the aggregate estimated recovery on BIF's and FRF's inventories of failed institution assets, consistent and sound methodologies should be used to develop asset recovery estimates and adequate documentation should be maintained to support them.

During 1993, we found that both FDIC and servicer personnel used inconsistent and unsupported methodologies for estimating recoveries on assets with similar liquidation strategies. Also, the methods for developing the estimates did not always result in recovery estimates which represented the net realizable value of these assets. These weaknesses result in estimates that lose their comparability, diminishing FDIC's ability to accurately report on these assets.

We found:

- For anticipated loan restructurings and performing loans, most servicers' personnel included in recovery estimates interest income anticipated for the duration of either the loan or the servicing contract. In contrast, FDIC personnel did not include in their estimates any interest income for anticipated loan restructurings and limited anticipated interest income for performing loans to 1 year.
- For nonperforming loans which are expected to be foreclosed, recovery estimates prepared by servicers' personnel included operating income associated with the loans' underlying collateral, even though FDIC's legal right to rental income had not yet been established. For similar assets serviced by FDIC personnel, operating income was not included in estimating recoveries until the foreclosure actually occurred or FDIC's legal right to the rental income was established.

- For assets with similar liquidation strategies, certain FDIC and servicers' account officers applied across-the-board discounts to appraised values in estimating recoveries, while other account officers estimated recoveries at 100 percent of appraised value. Similarly, for assets to be disposed of through bulk sales, certain account officers discounted appraised values of these assets, some used 100 percent of the appraised value, and others used FDIC's minimum acceptable price assigned to the assets in estimating recoveries.
- For failed institution assets constituting investments in subsidiaries, account officers at one servicer estimated recoveries based on the net cash flow to FDIC that was expected from subsidiary dividends, while account officers at another servicer estimated recoveries based on the expected return on specific subsidiary assets without deducting subsidiary liabilities.
- For assets whose recoveries are estimated based on predetermined formulas,[9] the personnel of one servicing entity applied the recovery formulas against the adjusted pool value of the serviced assets.[10] In contrast, FDIC and other servicing entity personnel followed the guidance in FDIC's Credit Manual, which instructs account officers to apply the predetermined recovery formulas to the assets' book values. The adjusted pool value is generally less than book value because interest income and other income collected on these assets are deducted from the assets' principal balance.
- For assets whose estimated recoveries are based on payment streams that extend for several years, these cash flows were not discounted to their net present value. Assets with large balloon payments, assets recently or currently in the process of being restructured, and assets which are not easily liquidated often have large payment streams beyond 1 year. The differences between the estimated recoveries calculated by FDIC and servicer personnel on a gross basis and the net present value of these recoveries could be substantial.

During our 1992 audits, we found that estimates of recoveries on failed institution assets were not always supported by documentation in asset files maintained by FDIC and servicer personnel. This weakness increases the risk that estimates of recoveries may not be reasonable and based on

[9]For assets with book values of $250,000 or more and for all judgments, subsidiaries, claims, and restitutions, account officers assigned to manage and liquidate the assets are responsible for preparing complete and accurate recovery estimates for each asset. For those assets with book values less than $250,000, recoveries are calculated using recovery rates contained in FDIC's Credit Manual.

[10]Adjusted pool balance represents the principal balance of the asset, net of specific reserves, as reflected on the accounting records of the relevant failed bank or assuming bank less all subsequent collections, such as principal, interest, and other income.

the most current information available. While FDIC has made some progress in addressing these weaknesses, we found similar documentation deficiencies during our 1993 audits. In addition, methodologies used to estimate asset recoveries were not always supported by historical or other evidential data. We found:

- For assets whose recoveries are based on discounted appraised values, neither FDIC or servicing personnel could provide any data or analysis to support these discounts.
- For assets whose recoveries are calculated by predetermined formulas, FDIC was unable to provide an analysis of historical data to support the recovery rates. In addition, FDIC did not consider the appraised value of the underlying collateral in calculating recoveries for these assets even though FDIC requires at least one current appraisal (less than 1 year old) for property pledged as collateral except when the collateral value is less than $25,000. Using book values, rather than available appraised values, as a basis for determining recoveries does not consider changes in recoveries that would occur due to changing economic conditions.

The use of inconsistent and unsupported methodologies in determining recovery estimates on failed institution assets is largely due to the lack of comprehensive procedures for estimating recoveries. Although FDIC's Credit Manual provides some illustrations on estimating asset recoveries, the guidance and examples provided are not comprehensive enough to consider the numerous liquidation strategies that account officers may use. For a given asset, the Credit Manual does not specifically instruct account officers to base the recovery estimate on the liquidation strategy being pursued. Further, the guidance available in the Credit Manual is often vague and subject to different interpretations by the various user groups.

The weaknesses in FDIC's internal controls over its asset recovery estimation process have resulted in a significant number of errors in asset recovery estimates. We found that for 714 failed institution assets we reviewed, FDIC's recovery estimates were misstated for 372 (52 percent). Because some errors understated recovery estimates while other errors overstated them, the net aggregate effect of these errors did not result in a material misstatement of BIF's or FRF's financial statements as of December 31, 1993. However, these weaknesses could result in material misstatements if not corrected.

Reportable Conditions

Although FDIC made significant progress during 1993 in addressing the internal control weaknesses identified in our 1992 audits, certain internal control deficiencies still existed in the following areas during 1993 to the point that we consider them reportable conditions.

1. During 1993, FDIC acted to address the weaknesses we identified during our 1992 audits in its time and attendance reporting processes. This action included issuing improved time and attendance reporting procedures and related additional written guidance. However, our 1993 audits found that these required procedures and guidance were not always followed, resulting in deficiencies similar to some of those we identified during our 1992 audits. These deficiencies included continued lack of adherence to required procedures in preparing time and attendance reports, lack of separation of duties between timekeeping and data entry functions, and failure to reconcile payroll reports to timecards to verify that the data on the timecards were properly entered into the payroll system. While FDIC's issuance of revised time and attendance reporting procedures and guidance was a positive step, these revised procedures do not in themselves ensure that time and attendance reporting requirements are being followed. Effective implementation of the revised procedures and guidance should correct the weaknesses that continued to exist in 1993.

2. FDIC uses its computer systems extensively, both in its daily operations and in processing and reporting financial information. Therefore, general controls over the systems are critical to producing accurate and reliable financial statements. During our 1992 audits, we found that general controls[11] over FDIC's computerized information systems did not adequately ensure that data files, computer programs, and computer hardware were protected from unauthorized access and modification. Our 1993 audits showed that this weakness continued through 1993. However, prior to completion of our fieldwork in May 1994, FDIC revised procedures to address the weakness in its computerized information systems security controls. Specifically, FDIC revised procedures to restrict access to sensitive financial and operating system programs and files. As a result, FDIC's general controls, as revised, should adequately preclude unauthorized access to or modification of data files and programs.

[11]General controls are the policies and procedures that apply to an entity's overall effectiveness and security of operations, and that 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.

Because these changes were recently implemented, this condition will require future monitoring to ensure that general controls remain adequate.

3. In our report on our 1992 audits, we reported that internal controls over contracted asset servicers were not being consistently implemented or were too limited to effectively assist FDIC in overseeing its contracted asset servicers. Although FDIC is addressing these weaknesses and has made significant progress, we found that some of these weaknesses continued during 1993. Specifically, we found that reconciling items related to the reconciliation of servicer pool balances were not cleared promptly for 22 percent of the serviced asset pools. We also found that reconciliations were not performed consistently for an additional 10 percent of the pool balances and, when performed, the reconciliations did not sufficiently document and account for all reconciling items. In addition, we found that FDIC performed only limited review procedures on the balances and activity reported by asset servicing entities, which are the source for recording transactions to FDIC's financial information system.

FDIC attributes the lack of consistent and timely reconciliations to insufficient staff. In addition, we believe the lack of sufficient verification of servicer balances and activity is attributable to inadequate coordination of oversight responsibilities between FDIC's Division of Finance and the Contractor Oversight and Monitoring Branch of its Division of Depositor and Asset Services. These weaknesses in reconciliation and verification procedures may adversely affect the reliability of the recorded asset balances and servicer accountability.

4. Because FDIC does not maintain subsidiary records for assets in serviced asset pools, it must rely on contracted servicers to establish adequate safeguarding and reporting controls over these serviced assets. In our reports on our 1992 audits, we noted that FDIC had not prepared a detailed reconciliation between asset balances in its financial information system and one of its contracted asset servicer's reported asset pool balance since the pool's inception in August 1991. While FDIC has acted to address this weakness, our work in 1993 found that weak internal controls at this servicing entity persisted. This prevented FDIC from having assurance that assets serviced by this entity were adequately safeguarded and that transactions associated with this serviced asset pool were properly reported to FDIC.

- We found that the asset pool balance reported on FDIC's financial information system could not be verified to the servicer's general ledger or to its subsidiary records. This is because the servicer did not maintain a general ledger consistent with receivership accounting and because reconciling differences between the subsidiary records and amounts reported to FDIC had not been resolved.[12]

- Because of the limitations in the servicer's accounting systems, the servicer manually prepares monthly reports to present activity associated with these serviced assets on a basis consistent with FDIC. These reports are the primary source documents FDIC uses to record transactions to its financial information system and to reconcile the asset balances. However, neither FDIC nor the servicer's internal audit department verify activity reflected in these reports.
- We also found that controls over accountability and timely processing of this servicer's collections need improvement. Control totals should be established for receipts and the total of each day's processed receipts should be reconciled to these control totals. Also, receipts received before an entity's depository deadline should be deposited the same day. However, the servicer does not reconcile checks received each day to checks processed and deposited, nor does the servicer promptly process all checks received on assets assigned for bulk sale.

Although the servicer was required to maintain a subsidiary record reflecting the legal balances of the serviced assets, its servicing agreement did not specifically require the servicer to maintain its general ledger system on a basis consistent with receivership accounting. Consequently, because the servicer's accounting systems were not maintained so as to reflect the legal balances of the serviced assets, the manually prepared activity reports became necessary in order for FDIC to appropriately apply collections between principal, interest, and other income. However, the accuracy of these reports was not verified by FDIC. We believe this is due to inadequate guidance and coordination of oversight responsibilities between FDIC's Division of Finance and its Contractor Oversight Monitoring Branch.

Because of these limitations in the servicer's accounting systems and the inadequate review of the manually prepared activity reports, significant adjustments were needed to both the activity reports and to FDIC's financial information system to appropriately apply collections each month from August 1991 through August 1993. In addition, large balances of unapplied collections as reported by the servicer have accumulated in FDIC's suspense account. Overall, these conditions have resulted in

[12]Under receivership accounting, collections on assets are applied among principal, interest, and other income so that the legal balance of the asset can be maintained.

inaccurate balances on FDIC's financial information system and have prevented FDIC from ensuring that all account balances and activity reflected in its accounting system are complete and accurate. Also, the servicer's failure to reconcile checks received to checks deposited and the holding of checks increases the risk that checks may be lost, misplaced, or stolen, and that cash transactions may be unrecorded or incomplete.

In addition to the weaknesses we have discussed, we noted other less significant matters involving FDIC's system of internal accounting control and its operations which we will be reporting separately to FDIC management.

FDIC's Compliance With the Chief Financial Officers Act

The Chief Financial Officers (CFO) Act requires that government corporations submit an annual statement on internal accounting and administrative controls, including management's assessment on the effectiveness of these controls, consistent with the requirements of the Federal Managers' Financial Integrity Act. The CFO Act also requires that government corporations have their financial statements audited annually and that corporations submit an annual management report to the Congress.

Our annual audits of FDIC's financial statements satisfy the act's auditing requirement. Also, FDIC's 1992 report on internal accounting and administrative controls, issued in July 1993, contained the results of management's assessment of internal controls in place during 1992. FDIC's assessment identified several deficiencies in internal controls that it considered material.[13] The 1992 report contained specific plans to correct these weaknesses.

FDIC is finalizing its 1993 management report. Based on our review of a draft of this report, we anticipate that FDIC will fulfill the act's reporting requirement by submitting a management report to the Congress that contains the financial statements of the three funds administered by FDIC, the annual audit report, and a statement on internal accounting and administrative controls by the Acting Chairman of FDIC consistent with the requirements of the Federal Managers' Financial Integrity Act.

[13]FDIC considers a deficiency material if (1) it violates a statutory requirement, (2) it results in a conflict of interest, (3) it significantly impairs the fulfillment of FDIC's mission, (4) it significantly weakens safeguards against waste, loss, or unauthorized use or misappropriation of funds, property, or other assets, (5) it merits the attention of the Congress, or (6) omitting it from the statements of internal accounting and administrative controls could adversely reflect on the management integrity of FDIC.

Recommendations

FDIC has not fully implemented all of the recommendations we made following our 1992 audits. Specifically, FDIC has not promptly and routinely reconciled asset balances reported by servicing entities with its general ledger control accounts, and has not ensured timely and adequate audit coverage of all critical areas of asset servicing operations through the use of asset servicing entities' internal audit departments and FDIC's personnel site visitations. Also, FDIC has not ensured that estimates of recoveries from the management and disposition of failed institution assets are determined utilizing consistent and sound methodologies. FDIC needs to continue pursuing corrective actions to fully satisfy these recommendations.

In addition, to address the weaknesses identified during 1993 regarding inconsistent and unsupported asset recovery estimation methodologies, we recommend that the Acting Chairman of the Federal Deposit Insurance Corporation direct the heads of the Division of Depositor and Asset Services and the Division of Finance to:

- Revise the Credit Manual to provide more detailed guidance on recovery estimation methods to be used, and ensure that this expanded guidance is strictly adhered to by both consolidated offices and contracted asset servicers' personnel. Specifically, the revised Credit Manual should require that (1) recoveries be estimated based on the type of asset and the liquidation strategy being pursued, (2) cash flows projected to be received beyond 1 year be discounted to their net present value, and (3) account officers adequately document the underlying assumptions they use to calculate the recovery estimates.
- Analyze and document the basis for the formulas used to calculate recoveries for assets with book values less than $250,000. In analyzing these formulas, FDIC should consider the use of appraised values to calculate recovery estimates for collateralized assets even if the asset's book value is under $250,000.

To address the weaknesses identified during 1993 in the oversight of asset servicing entities, we recommend that the Acting Chairman of the Federal Deposit Insurance Corporation direct the heads of the Division of Depositor and Assets Services and Division of Finance to verify and document the accuracy and completeness of the balances and activity reported to FDIC by contracted asset servicers back to the servicers' detail records.

To address the weaknesses identified during 1993 in the internal controls of one contracted servicer, we recommend that the Acting Chairman of the Federal Deposit Insurance Corporation direct the heads of the Division of Depositor and Asset Services and the Division of Finance to

- promptly reconcile servicer asset balances each month and resolve and document reconciling items within 30 days of the reconciliation date;
- require the servicer to maintain a general ledger and subsidiary records consistent with receivership accounting, and require FDIC's oversight personnel to verify the accuracy of the activity and balances on these systems; and
- require the servicer to reconcile checks received to checks deposited each day, and reconcile the final month-end balances in FDIC's unapplied collections account to the servicer's subsidiary records and clear these amounts within 30 days after month-end.

To address weaknesses identified in FDIC's time and attendance reporting process, we recommend that the Acting Chairman of the Federal Deposit Insurance Corporation direct FDIC's division and office heads to enforce the revised policies and procedures in FDIC's Time and Attendance Reporting Directive and related guidance to ensure that employee time charges are valid, payroll expenses are charged to the correct fund, and timekeeping and data input functions are separated.

Corporation Comments and Our Evaluation

In commenting on a draft of our report, FDIC agreed that improvements were needed in its process for estimating recoveries to be received on assets acquired from failed institutions. FDIC outlined major initiatives currently underway which are designed to correct the weaknesses identified in our 1993 audits. FDIC also outlined actions it is currently taking or plans to take to address the other reportable conditions identified in our 1993 audits. These actions, if implemented as intended, should adequately address the weaknesses discussed in our report. During the course of our audits of the 1994 financial statements of the three funds administered by FDIC, we will review the implementation of these corrective actions.

FDIC disagreed that the $410 million reduction in BIF's estimated liability for unresolved cases, which FDIC recognized in the first quarter of 1994, should have been recognized as of December 31, 1993. FDIC noted that financial information it received from financial institutions as of year-end 1993 was just one of a number of factors considered in its quarterly analysis of BIF's exposure to troubled institutions. FDIC noted that other factors used to determine that BIF's estimated liability for unresolved cases should be reduced incorporated information subsequent to December 31, 1993, and therefore, it was appropriate to include the adjustment in BIF's March 1994 financial statements.

We agree that other factors beyond the financial condition of insured institutions as reported in their unaudited statements of condition and income should be considered in evaluating BIF's exposure to future institution failures. However, the primary accountable event which triggers the reduction of an estimated loss for a troubled institution is the point at which improvements in the institution's financial condition render the loss no longer probable, as defined under generally accepted accounting principles and embodied in FDIC policy.[14] Our review of these institutions' unaudited statements of condition and income as of December 31, 1993, showed from this information alone that an improvement in financial condition sufficient to necessitate a reduction in the estimated loss for these institutions had occurred prior to year-end 1993. The additional information considered in evaluating the likelihood of an institution's failure, such as input from field examiners, only reinforced this conclusion. In fact, in several cases, the examiners referred to specific events, such as capital infusions, which had occurred prior to year-end 1993, as the basis for their opinion that an estimated loss was no longer necessary. Therefore, we believe this $410 million reduction in BIF's estimated liability for unresolved cases should have been recognized on BIF's financial statements as of December 31, 1993.

The complete text of FDIC's response to our report is included in appendix II.

Charles A. Bowsher

Charles A. Bowsher
Comptroller General
of the United States

May 6, 1994

[14] Statement of Accounting Policy (CORP-17, April 6, 1994). Retroactive to December 31, 1993.

Bank Insurance Fund's Financial Statements

Statements of Financial Position

Federal Deposit Insurance Corporation

Bank Insurance Fund

Statements of Financial Position

Dollars in Thousands	December 31 1993	1992
Assets		
Cash and cash equivalents (Note 3)	$ 483,239	$ 3,592,629
Investment in U.S. Treasury obligations, net (Note 4)	5,308,476	1,692,222
Accrued interest receivable on investments and other assets	80,776	105,690
Net receivables from bank resolutions (Note 5)	13,624,302	27,823,964
Investment in corporate-owned assets, net (Note 6)	726,584	1,461,263
Property and buildings (Note 8)	158,418	161,757
Total Assets	**20,381,795**	**34,837,525**
Liabilities and the Fund Balance (Deficit)		
Accounts payable, accrued and other liabilities (Note 15)	191,831	408,394
Federal Financing Bank borrowings (Note 9)	0	10,232,977
Liabilities incurred from bank resolutions (Note 10)	4,075,793	13,495,571
Estimated Liabilities for: (Note 11)		
Unresolved cases	2,972,000	10,782,390
Litigation losses	20,511	18,768
Total Liabilities	**7,260,135**	**34,938,100**
Commitments and contingencies (Notes 16 and 17)		
Fund Balance (Deficit)	**13,121,660**	**(100,575)**
Total Liabilities and the Fund Balance (Deficit)	**$ 20,381,795**	**$ 34,837,525**

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

Statements of Income and the Fund Balance (Deficit)

Federal Deposit Insurance Corporation

Bank Insurance Fund

Statements of Income and the Fund Balance (Deficit)

Dollars in Thousands	For the Year Ended December 31 1993	1992
Revenue		
Assessments earned (Note 12)	$ 5,784,277	$ 5,587,806
Interest on U.S. Treasury obligations	165,130	299,410
Revenue from corporate-owned assets	258,858	255,745
Other revenue	222,536	158,584
Total Revenue	**6,430,801**	**6,301,545**
Expenses and Losses		
Operating expenses	388,464	360,793
Provision for insurance losses (Note 7)	(7,677,400)	(2,259,690)
Corporate-owned asset expenses	190,641	226,433
Interest and other insurance expenses (Note 13)	306,861	836,669
Total Expenses and Losses	**(6,791,434)**	**(835,795)**
Net Income Before Cumulative Effect of a Change in Accounting Principle	**13,222,235**	**7,137,340**
Cumulative effect of accounting change for certain postretirement benefits (Note 15)	-0-	(209,973)
Net Income	**13,222,235**	**6,927,367**
Fund (Deficit) - Beginning	**(100,575)**	**(7,027,942)**
Fund Balance (Deficit) - Ending	**$ 13,121,660**	**$ (100,575)**

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

Statements of Cash Flows

Federal Deposit Insurance Corporation

Bank Insurance Fund

Statements of Cash Flows

Dollars in Thousands	For the Year Ended December 31 1993	1992
Cash Flows from Operating Activities		
Cash provided from:		
Assessments	$ 5,789,779	$ 5,586,547
Interest on U.S. Treasury obligations	160,697	346,600
Recoveries from bank resolutions	8,739,202	9,545,685
Recoveries from corporate-owned assets	1,241,305	1,486,523
Miscellaneous receipts	32,927	161,785
Cash used for:		
Operating expenses	(538,616)	(301,163)
Interest paid on liabilities incurred from bank resolutions	(169,872)	(520,669)
Disbursements for bank resolutions	(4,197,535)	(14,905,758)
Disbursements for corporate-owned assets	(368,529)	(666,702)
Miscellaneous disbursements	(15,779)	(47,608)
Net Cash Provided by Operating Activities (Note 20)	**10,673,579**	**685,240**
Cash Flows from Investing Activities		
Cash provided from:		
Maturity and sale of U.S. Treasury obligations	1,700,000	1,600,000
Cash used for:		
Purchase of U.S. Treasury obligations	(5,322,969)	0
Property and buildings	0	(1,652)
Net Cash Provided by (Used by) Investing Activities	**(3,622,969)**	**1,598,348**
Cash Flows from Financing Activities		
Cash provided from:		
Federal Financing Bank borrowings	0	4,540,000
Cash used for:		
Payments of indebtedness incurred from bank resolutions	0	(1,021)
Repayments of Federal Financing Bank borrowings	(10,160,000)	(4,999,954)
Net Cash Used by Financing Activities	**(10,160,000)**	**(460,975)**
Net (Decrease) Increase in Cash and Cash Equivalents	**(3,109,390)**	**1,822,613**
Cash and Cash Equivalents - Beginning	**3,592,629**	**1,770,016**
Cash and Cash Equivalents - Ending	**$ 483,239**	**$ 3,592,629**

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

Notes to the Financial Statements

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. The FIRREA created the Bank Insurance Fund (BIF), the Savings Association Insurance Fund (SAIF) and the FSLIC Resolution Fund (FRF). It also designated the Federal Deposit Insurance Corporation (FDIC) as the administrator of these three funds. The BIF insures the deposits of all BIF-member institutions (normally commercial or savings banks) and the SAIF insures the deposits of all SAIF-member institutions (normally thrifts). The FRF is responsible for winding up the affairs of the former Federal Savings and Loan Insurance Corporation (FSLIC). All three funds are maintained separately to carry out their respective mandates.

The Omnibus Budget Reconciliation Act of 1990 (1990 Act) 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 (FDICIA) was enacted to further strengthen the insurance funds administered by the FDIC. The FDIC's authority to borrow from the U.S. Treasury, on behalf of the BIF and the SAIF, to cover insurance losses was increased from $5 billion to $30 billion. However, the FDIC cannot incur any additional obligation for the BIF or the SAIF if incurring the obligation would result in the amount of total obligations in the respective Fund exceeding 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) the total amount authorized to be borrowed from the U.S. Treasury, excluding FFB borrowings. This restriction against incurring additional obligations is known as the Maximum Obligation Limitation (see Note 2). At December 31, 1993, the BIF had approximately $44 billion in remaining obligation authority.

The FDICIA requires that the FDIC repay U.S. Treasury borrowings under the $30 billion authorization from assessment revenues. The FDIC must provide the U.S. Treasury with a repayment schedule demonstrating that assessment revenues are adequate to make payment when due. In addition, the FDIC has the 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 FDICIA required the FDIC to: 1) implement capital standards and regulatory controls designed to strengthen the banking industry; 2) implement a risk-based assessment system; and 3) limit insurance coverage for uninsured liabilities. The FDICIA also requires the FDIC to 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.

Operations of the BIF

The primary purpose of the BIF is to: 1) insure the deposits and protect the depositors of insured banks and 2) finance the resolution of failed banks including managing and liquidating their assets. In addition, the FDIC, acting on behalf of the BIF, examines state chartered banks that are not members of the Federal Reserve System and provides and monitors assistance to failing banks.

The BIF is funded from the following sources: 1) BIF-member assessment premiums; 2) interest earned on investments in U.S. Treasury obligations; 3) income earned on and funds received from the management and disposition of assets acquired from failed banks; and 4) U.S. Treasury and FFB borrowings.

2. Summary of Significant Accounting Policies

General

These financial statements pertain to the financial position, results of operations and cash flows of the BIF, and are presented in accordance with generally accepted accounting principles. 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 book value, which is the face value of securities plus the unamortized premium or less the unamortized discount. However, in 1992, book value was the purchase price of securities less the amortized premium or plus the unamortized discount. Such amortizations 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 effective interest method.

Allowance for Losses on Receivables from Bank Resolutions and Investment in Corporate-Owned Assets
The BIF records as a receivable the amounts advanced for assisting and closing banks. The BIF also records as an asset the amounts advanced for investment in corporate-owned assets. Any related 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 putback 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 probable losses from litigation against the BIF in both its corporate and receivership capacities. The FDIC's Legal Division recommends these estimates on a case-by-case basis. The litigation loss estimates related to receiverships are included in the Allowance for Losses for Receivables from Bank Resolutions.

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. Also, the income and expenses attributable to receiverships are accounted for as transactions of those receiverships. Indirect liquidation expenses incurred by the BIF on behalf of the receiverships are recovered from those receiverships through a cost recovery process.

Cost Allocations Among Funds
Certain 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 operating expenses were incurred by the Funds. The cost of furniture, fixtures and equipment purchased by the FDIC on behalf of the three Funds under its administration is allocated among these Funds on a pro rata basis. The BIF expenses its share of furniture, fixtures and equipment at the time of acquisition because of their immaterial amounts.

Postretirement Benefits Other Than Pensions
Effective January 1, 1992, the FDIC implemented the requirements of the Statement of Financial Accounting Standards (SFAS) No. 106, "Employer's Accounting for Postretirement Benefits Other Than Pensions." This standard mandates the accrual method of accounting for postretirement benefits other than pensions based on actuarially determined costs to be recognized during employees' years of active service. This was a significant change from the FDIC's previous policy of recognizing these costs in the year the benefits were provided (i.e., the cash basis). In 1992, the BIF provided the accounting and administration of these postretirement benefits on behalf of the SAIF, the FRF and the Resolution Trust Corporation (RTC). In 1993, the FDIC established a plan administrator to provide the accounting and administration of these benefits on behalf of the BIF, the SAIF, the FRF and the RTC.

Depreciation
The FDIC has designated the BIF administrator of facilities owned and used in its operations. Consequently, the BIF includes the cost

of these facilities in its financial statements and provides the necessary funding for them. The BIF charges other Funds sharing the facilities a rental fee representing an allocated share of its annual depreciation expense.

The Washington office buildings and the L. William Seidman Center in Arlington, VA, 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.

Maximum Obligation Limitation (MOL)
In 1993 and 1992, for purposes of calculating the maximum obligation limitation, the FDIC allocated the total authorized borrowings of $30 billion to the BIF. In subsequent periods no portion of the $30 billion U.S. Treasury borrowing authority will be allocated to the SAIF unless the SAIF has primary resolution authority for thrift institutions as of the date of the MOL calculation for SAIF or projected borrowing needs for SAIF-insured institutions. Any future allocation of U.S. Treasury borrowing authority will be based upon projected borrowing needs of the FDIC. "Borrowing needs" is defined as the projected borrowing needed over the next twelve months based on FDIC's financial projection models. Any remaining amount to be allocated will be based on insured deposits as published in the latest FDIC Annual Report.

In calculating the maximum obligation limitation, "other assets" consisting of receivables from bank resolutions and investments in corporate owned assets are valued at 90 percent of their net realizable value. In addition, the BIF's estimated liability for future financial institution failures or assistance transactions is excluded in determining the BIF's total obligations where there is no contractual agreement between FDIC and the troubled institution comprising the estimated liability.

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

Reclassifications
Reclassifications have been made in the 1992 Financial Statements to conform to the presentation used in 1993.

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 1993, cash restrictions included $13.8 million for health insurance payable and $3.2 million for funds held in trust. In 1992, cash restrictions included $12.4 million for health insurance payable and $842 thousand for funds held in trust.

Cash and Cash Equivalents

Dollars in Thousands	December 31	
	1993	1992
Cash	$ 52,999	$ 71,859
One-day special Treasury certificates	430,240	3,520,770
	$ 483,239	**$3,592,629**

4. U.S. Treasury Obligations

All cash received by the BIF is invested in U.S. Treasury obligations unless the cash is: 1) used to defray operating expenses; 2) used for outlays related to assistance to banks and liquidation activities; or 3) invested in one-day special Treasury certificates.

U.S. Treasury Obligations

December 31, 1993

Dollars in Thousands

Maturity	Description	Yield at Purchase	Book Value	Market Value	Face Value
Less than one year	U.S. Treasury Notes & Bonds	3.38%	$ 906,328	$906,573	$900,000
1-3 years	U.S. Treasury Notes & Bonds	4.02%	2,292,267	2,286,586	2,200,000
3-5 years	U.S. Treasury Notes & Bonds	4.59%	2,109,881	2,091,443	2,000,000
			$5,308,476	**$5,284,602**	**$5,100,000**

December 31, 1992

Dollars in Thousands

Maturity	Description	Yield at Purchase	Book Value	Market Value	Face Value
Less than one year	U.S. Treasury Bills, Notes & Bonds	7.99%	$1,692,222	$1,729,233	$1,700,000

In 1993, the unamortized premium, net of unamortized discount, was $208.5 million. In 1992, the unamortized discount, net of unamortized premium, was $7.8 million.

5. Net Receivables from Bank Resolutions

The FDIC resolution process results in different types of transactions depending on the unique facts and circumstances surrounding each failing or failed institution. Payments to prevent a failure are made to operating institutions when cost and other criteria are met. Such payments may facilitate a merger or allow a failing institution to continue operations. Payments for institutions that fail are made to cover insured depositors' claims and represent a claim against the receivership's assets.

In an effort to maximize the return from the sale or disposition of assets and to minimize realized losses from bank resolutions, the FDIC, as receiver for failed banks, engages in a variety of strategies to dispose of assets held by the banks at time of failure.

A failed bank acquirer can purchase selected assets at the time of resolution and assume full ownership, benefit and risk related to such assets. In certain cases, the receiver offers a period of time during which an acquirer can sell assets back to the receivership at a specified value (i.e., an asset "putback" option). Alternately, the receiver can enter into a loss-sharing arrangement with an acquirer whereby, for specified assets and in accordance with individual contract terms, the two parties share in credit losses and certain qualifying expenses. These arrangements typically direct that the receiver pay to the acquirer a specified percentage of the losses triggered by the charge-off of assets covered by the loss-sharing agreement terms. The receiver absorbs the majority of the losses incurred and shares in the acquirer's future recoveries of previously charged-off assets. Failed bank assets can also be retained by the receiver to either be managed and disposed of by in-house FDIC liquidation staff or managed and liquidated by private-sector servicers with oversight from the FDIC through asset servicing contracts.

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

As of December 31, 1993 and 1992, the BIF, in its receivership capacity, held assets with a book value of $30.1 billion and $51.3 billion, respectively. The estimated cash recoveries from the sale of these assets (excluding cash and miscellaneous receivables of $7.4 billion in 1993 and $16.3 billion in 1992) are regularly evaluated, but remain subject to uncertainties because of changing economic conditions. These factors could reduce the claimants' actual recoveries upon the sale of these assets from the level of recoveries currently estimated.

Net Receivables from Bank Resolutions

Dollars in Thousands	December 31 1993	December 31 1992
Assets from Open Bank Assistance:		
Redeemable preferred stock	$ 51,045	$ 1,243,156
Subordinated debt instruments	124,000	164,500
Notes receivable	62,037	334,479
Other open bank assistance	33,593	1,125,670
Accrued interest receivable	1,865	3,167
Allowance for loss (Note 7)	(215,446)	(2,203,158)
	57,094	**667,814**
Receivables from Closed Banks:		
Loans and related assets	1,376,597	1,628,857
Resolution transactions	35,742,150	49,277,763
Capital instruments	25,000	25,000
Depositors' claims unpaid	18,758	24,983
Deferred settlements (a)	(403,901)	(403,901)
Allowance for losses (Note 7)	(23,191,396)	(23,396,552)
	13,567,208	**27,156,150**
	$ 13,624,302	**$ 27,823,964**

(a) Proceeds from the sale of equity investments related to the Continental Bank, Chicago, IL, in an agreement dated September 26, 1984, have been deferred pending final termination.

6. Investment in Corporate-Owned Assets, Net

The BIF acquires assets in certain failing and failed bank cases by either purchasing an institution's assets outright or purchasing the assets under the terms specified in each resolution agreement. In addition, the BIF can purchase assets remaining in a receivership to facilitate termination. The vast majority of corporate-owned assets are real estate and mortgage loans.

The BIF recognizes income and expenses on these assets. Income consists primarily of the portion of collections on performing mortgages related to interest earned. Expenses are recognized for administering the management and liquidation of these assets.

Investment in Corporate-Owned Assets, Net

Dollars in Thousands	December 31	
	1993	1992
Investment in corporate-owned assets	$1,468,399	$1,886,720
Allowance for losses (Note 7)	(741,815)	(425,457)
	$726,584	**$1,461,263**

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

Provision for insurance losses includes the estimated losses for bank resolutions that occurred during the year for which an estimated loss was not established. It also includes loss adjustments for bank resolutions that occurred in prior years.

In the following charts, transfers include reclassifications from the line item "Estimated Liabilities for Unresolved Cases" to the line item "Total Allowance/Estimated Liabilities Failed Banks." Terminations represent final adjustments to the estimated cost figures for those bank resolutions that were completed and for which the operations of the receivership ended.

Analysis of Changes in Allowance for Losses and Estimated Liabilities

1993

Dollars in Millions

	Beginning Balance 01/01/93	Provision for Insurance Losses			Net Cash Payments	Transfers/ Terminations	Ending Balance 12/31/93
		Current Year	Prior Years	Total			
Allowance for Losses:							
Open bank assistance	$ 2,203	$ 40	$ (890)	$ (850)	$ 19	$ (1,157)	$ 215
Corporate-owned assets	425	0	317	317	0	0	742
Closed banks	23,397	(224)	99	(125)	0	(81)	23,191
Total	**26,025**	**(184)**	**(474)**	**(658)**	**19**	**(1,238)**	**24,148**
Estimated Liabilities for:							
Assistance agreements	208	0	34	34	(97)	1	146
Litigation losses	19	0	2	2	0	0	21
Total	**227**	**0**	**36**	**36**	**(97)**	**1**	**167**
Total Allowance/Estimated Liabilities Failed Banks	**26,252**	**(184)**	**(438)**	**(622)**	**(78)**	**(1,237)**	**24,315**
Estimated Liabilities for:							
Unresolved cases	**10,782**	**818**	**(7,873)**	**(7,055)**	**0**	**(755)**	**2,972**
Total		**$ 634**	**$ (8,311)**	**$ (7,677)**			

1992							
Dollars in Millions							
	Beginning Balance 01/01/92	Provision for Insurance Losses Current Year	Prior Years	Total	Net Cash Payments	Transfers/ Terminations	Ending Balance 12/31/92
Allowance for Losses:							
Open bank assistance	$ 1,199	$ (100)	$ (31)	$ (131)	$ 24	$ 1,111	$ 2,203
Corporate-owned assets	659	-0-	(223)	(223)	-0-	(11)	425
Closed banks	21,749	(2,711)	(1,504)	(4,215)	-0-	5,863	23,397
Total	23,607	(2,811)	(1,758)	(4,569)	24	6,963	26,025
Estimated Liabilities for:							
Assistance agreements	298	1	494	495	(587)	2	208
Litigation losses	161	-0-	(142)	(142)	-0-	-0-	19
Total	459	1	352	353	(587)	2	227
Total Allowance/Estimated Liabilities Failed Banks	24,066	(2,810)	(1,406)	(4,216)	(563)	6,965	26,252
Estimated Liabilities for:							
Unresolved cases	16,346	5,634	(3,678)	1,956	-0-	(7,520)	10,782
Total		$2,824	$(5,084)	$(2,260)			

8. Property and Buildings

Property and Buildings

Dollars in Thousands	December 31 1993	1992
Land	$ 29,631	$ 29,631
Office buildings	151,442	151,442
Accumulated depreciation	(22,655)	(19,316)
	$158,418	**$161,757**

9. Federal Financing Bank (FFB) Borrowings

The FDIC is authorized to borrow from the FFB under the 1990 Act. On January 8, 1991, the FDIC and the FFB entered into a Note Purchase Agreement that is renewable annually and permits the FDIC to borrow funds to meet its financing requirements. Funds borrowed will be repaid to the FFB through the liquidation of assets from failed institutions.

The Note Purchase Agreement provides for the rollover of amounts advanced, plus interest where necessary, on a quarterly basis. It also requires the submission of estimates for subsequent quarter financing needs. Interest is payable quarterly based on the U.S. Treasury bill auction rate in effect during the quarter plus 12.5 basis points. The agreement also provides the FDIC with the option to repay, at any time, any or all of the principal and interest outstanding.

FFB borrowings were $10.2 billion as of December 31, 1992. This obligation was fully satisfied on August 6, 1993. The interest expense on the outstanding borrowings for 1993 and 1992 was $97 million and $468 million, respectively. The effective annualized rate of interest paid on the outstanding borrowings in 1993 was 3.3% and in 1992 was 3.8%.

10. Liabilities Incurred from Bank Resolutions

The FDIC resolution process can provide different types of transactions depending on the unique facts and circumstances surrounding each failing or failed institution. The BIF can assume certain liabilities that require future payments over a specified period of time.

The estimated liabilities for assistance agreements resulted from several large transactions where problem assets were 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 asset administration plus an incentive fee.

Liabilities Incurred from Bank Resolutions

Dollars in Thousands	December 31 1993	1992
Escrowed funds from resolution transactions	$3,897,677	$12,870,125
Funds due to bridge banks	0	376,156
Funds held in trust	3,195	842
Depositors' claims unpaid	18,758	24,983
Notes indebtedness	1,266	1,106
Estimated liabilities for assistance agreements (Note 7)	146,383	208,252
Accrued interest/other liabilities	8,514	14,107
	$4,075,793	**$13,495,571**

Maturities of Liabilities

Dollars in Thousands

1994	1995	1996
$3,937,915	$1,845	$136,033

11. Estimated Liabilities for:

Unresolved Cases

The BIF records an estimated loss for banks that have not yet failed but have been identified by the regulatory process as likely to fail within the foreseeable future as a result of regulatory insolvency (equity less than 2% of assets). This includes banks that were 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 fail in the future. The FDIC relies on this finding regarding regulatory insolvency as the determining factor in defining the existence of the "accountable event" that triggers loss recognition under generally accepted accounting principles.

As with any of its estimated losses, the FDIC cannot predict the timing of events with reasonable accuracy. These liabilities and a corresponding reduction in the Fund Balance are recognized 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.

The estimated liabilities for unresolved cases as of December 31, 1993 and 1992, were $3 billion and $10.8 billion, respectively. 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 banks with combined assets of approximately $13 billion will probably fail in 1994 and 1995. The BIF has recognized a loss of $3 billion for these potential failures. The greatest concentration of weak bank assets at year-end was in the Northeast region and in California; these two areas have been affected by poor regional economies and weak real estate markets. The further into the future projections of bank solvency are made, the greater the uncertainty of banks failing and the magnitude of the loss associated with those failures. The accuracy of these estimates will largely depend on future economic conditions, particularly in the real estate markets and the level of future interest rates.

Litigation Losses

The FDIC records as an estimated loss on the BIF's financial statements an estimated cost for unresolved legal cases to the extent those losses are considered to be both probable in occurrence and estimable in amount. In addition to these losses, the FDIC's Legal Division has determined that losses from unresolved legal cases totaling $765 million are reasonably possible. This includes $61 million in losses for the BIF in its corporate capacity and $704 million in losses for the BIF in its receivership capacity (see Note 2).

12. Assessments

The 1990 Act authorized 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 all banks for calendar year 1992 was 0.230 percent (23 cents per $100 of domestic deposits). The FDICIA authorized the FDIC to increase assessment rates for BIF-member institutions as needed to ensure that funds are available to satisfy the BIF's obligations.

On September 15, 1992, the FDIC's Board of Directors agreed on a transitional risk-based assessment system that charges higher rates to those banks that pose greater risks to the BIF. Under the new rule, beginning in 1993, each bank paid an assessment rate of between 23 cents and 31 cents per $100 of domestic deposits, depending on its risk classification. To arrive at a risk-based assessment for a particular bank, the FDIC placed each bank in one of nine risk categories using a two-step process based first on capital ratios and then on other relevant information. On June 17, 1993, the Board issued a final rule on the risk-based assessments system effective on October 1, 1993. The final rule made limited changes to the transitional risk-based assessment system effective during 1993. The Board expects to review premium rates at least once every six months. For calendar year 1994, the FDIC estimates that banks will pay an average rate of about 24.3 cents per $100 of domestic deposits.

The FDICIA 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. The schedule has been published in the *Federal Register.*

13. Interest and Other Insurance Expenses

The BIF incurs interest expense on funds borrowed to finance its resolution activity. Other insurance expenses are incurred by the BIF as a result of payments to insured depositors in closed bank payoff activity and the administration of assistance transactions (including funding "bridge bank" operations).

Interest and Other Insurance Expenses

Dollars in Thousands	December 31 1993	December 31 1992
Interest Expense for:		
Escrowed funds from resolution transactions	$ 204,969	$ 338,153
FFB borrowings	96,895	467,604
	301,864	**805,757**
Insurance Expense for:		
Resolution transactions	1,570	2,569
Assistance transactions	3,427	28,343
	4,997	**30,912**
	$306,861	**$836,669**

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 offset 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 also can 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 FDIC employees may also participate in an FDIC-sponsored tax-deferred savings plan with matching contributions. The BIF pays its share of the employer's portion of all related costs.

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.

The liability to employees for accrued annual leave is approximately $37.7 million and $29.8 million at December 31, 1993 and 1992, respectively.

Pension Benefits and Savings Plans Expenses

Dollars in Thousands	December 31 1993	1992
Civil Service Retirement System	$ 8,890	$ 7,804
Federal Employee Retirement System (Basic Benefit)	29,254	23,484
FDIC Savings Plan	16,267	10,250
Federal Thrift Savings Plan	8,742	6,483
	$63,153	**$48,021**

15. Postretirement Benefits Other than Pensions

The FDIC provides certain health, dental and life insurance coverage for its eligible retirees, the retiree's beneficiaries and covered dependents. Eligible retirees are those who have elected the FDIC's health and/or life insurance program and are entitled to an immediate annuity. However, dental coverage is provided to all retirees regardless of the plan selected.

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 wraparound. Dental care is underwritten by Connecticut General Life Insurance Company. The life insurance program is underwritten by Metropolitan Life Insurance Company.

The FDIC contributes toward health insurance premiums at the same rate for both active and retired employees. The FDIC uses a "minimum premium funding arrangement" in which premiums are held in a restricted account. Medical claims and fixed costs are paid to Blue Cross/Blue Shield from this account on a weekly basis. Under this arrangement, the FDIC's liability exposure is limited in any one contract year. The life insurance program provides basic coverage at no cost to retirees and allows converting optional coverages to direct-pay plans with Metropolitan Life Insurance Company. The dental insurance program provides coverage at no cost to retirees.

Beginning March 1994, the FDIC health insurance coverage will be self-insured for hospital/medical, prescription drug, mental health and chemical dependency, and the FDIC has purchased additional risk protection through stop-loss and fiduciary liability insurance from Aetna Life Insurance Company. All claims will be administered on an Administrative Services Only basis with the hospital/medical claims administered by Aetna Life Insurance Company, the mental health and chemical dependency claims administered by OHS Foundation Health Psychcare Inc., and the prescription drug claims administered by Caremark.

As part of adopting SFAS No. 106 (see Note 2), the FDIC elected to immediately recognize the accumulated postretirement benefit liability, measured as of January 1, 1992. The accumulated liability (transition obligation) represents that portion of future retiree benefit costs related to service already rendered by both active and retired employees up to the date of adoption. The BIF recorded an expense of $210 million for this liability in 1992, which was reflected in the Statements of Income and the Fund Balance (Deficit) as the cumulative effect of a change in accounting principle for periods prior to 1992.

The BIF expensed $49 million and $29 million for such benefits for the years ended December 31, 1993 and 1992, respectively. In

1993 the BIF funded the majority of its postretirement liability of $271 million.

For measurement purposes, the FDIC assumed the following: 1) a discount rate of 6 percent; 2) an increase in health costs in 1993 of 14 percent, decreasing down to an ultimate rate in 1998 of 8 percent; and 3) an increase in dental costs for 1993 and thereafter of 8 percent. Both the assumed discount rate and health care cost rate have a significant effect on the amount of the obligation and periodic cost reported.

If the health care cost rate were increased one percent, the accumulated postretirement benefit obligation as of December 31, 1993, would have increased by 7.5 percent. The effect of this change on the aggregate of service and interest cost for 1993 would be an increase of 28.8 percent.

Net Periodic Postretirement Benefit Cost

Dollars in Thousands	December 31 1993	December 31 1992
Service cost (benefits attributed to employee service during the year)	$ 30,274	$ 27,204
Interest cost on accumulated postretirement benefit obligation	15,549	16,627
Amortization of prior service cost	39	0
Amortization of unrecognized transition obligation	(1,222)	0
Return on plan assets	4,339	0
	$ 48,979	**$ 43,831**

As stated in Note 2, beginning in December, 1993 the FDIC established a plan administrator to provide accounting and administration on behalf of the BIF, the SAIF, the FRF and the RTC. The BIF has transferred the majority of its share of this long-term liability to the plan administrator. In 1992 the BIF provided the accounting and administration of this obligation. The BIF has funded the majority of its obligation and these funds are being managed by the administrator as "plan assets".

Accumulated Postretirement Benefit Obligation by Participant

Dollars in Thousands	December 31 1993	1992
Retirees	$ 65,956	$ 67,637
Fully eligible active plan participants	12,383	12,159
Other active participants	209,638	202,586
Total Obligation	287,977	282,382
Plan assets at fair value (1)	270,532	0
Postretirement benefit liability included on the Statements of Financial Position	**$ 17,445**	**$ 282,382**

(1) Consists of one-day special Treasury Certificates

For 1992, the accumulated liability is presented in the Statements of Financial Position - "Accounts payable, accrued and other liabilities." In the absence of the accounting change, this line item would have been $169 million, for the year ended December 31, 1992. As stated in Note 2 the BIF funded its 1993 liability to the plan administrator.

16. Commitments

Leases

The BIF currently is sharing in the FDIC's leased space. The BIF's allocated share of lease commitments totals $170.9 million for future years. The agreements contain escalation clauses resulting in adjustments, usually on an annual basis. The BIF recognized leased space expense of $46.8 million and $40.7 million for the years ended December 31, 1993 and 1992, respectively.

Leased Space Fees

Dollars in Thousands

1994	1995	1996	1997	1998
$53,415	$41,861	$28,972	$26,632	$20,027

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 "putback," or resold, to the receivership. The value at which the assets are putback and the time limit to putback assets are defined within each agreement. It is possible that the BIF could be called upon to fund the purchase of any or all of the "unexpired putbacks" at any time prior to expiration. The FDIC's estimate of the volume of assets subject to repurchase under existing agreements is $11.4 billion (see Note 17). The actual amount subject to repurchase should be significantly lower because the estimate does not reflect subsequent collections on or sales of assets kept by the acquirer. It also does not reflect any decrease due to acts by the acquirers which might disqualify assets from repurchase eligibility. Repurchase eligibility is determined by the FDIC when the acquirer initiates the asset putback procedures. The FDIC projects that a total of $596 million in book value of assets will be putback.

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:

Concentration of Credit Risk

Dollars in Millions — **December 31, 1993**

	South-east	South-west	North-east	Mid-west	Central	West	Total
Net receivables from bank resolutions	$ 243(a)	$2,596	$ 9,292	$ 477	$ 56	$ 957(b)	$ 13,621
Corporate-owned assets, net	9	562	45	0	32	79	727
Asset putback agreements (off-balance sheet)	0	0	11,375	0	0	0	11,375(c)
Total	**$ 252**	**$ 3,158**	**$ 20,712**	**$ 477**	**$ 88**	**$1,036**	**$ 25,723**

(a) The net receivable excludes $491 thousand of the SAIF's allocated share of maximum credit loss exposure from the resolution of Southeast Bank, N.A., Miami, FL. There is no risk that the SAIF will not meet this obligation.

(b) The net receivable excludes $3.3 million of the SAIF's allocated share of maximum credit loss exposure from the resolution of Olympic National Bank, Los Angeles, CA. There is no risk that the SAIF will not meet this obligation.

(c) See Note 16 Commitments - *Asset Putbacks*.

Insured Deposits
As of December 31, 1993, the total deposits insured by the BIF is approximately $1.9 trillion. This would be the accounting loss if all depository institutions fail and if any assets acquired as a result of the resolution process provide no recovery.

18. Disclosures about the Fair Value of Financial Instruments

Cash and cash equivalents are short-term, highly liquid investments and are shown at actual or approximate fair value. The fair value of the investment in U.S. Treasury obligations is disclosed in Note 4 and is based on current market prices. The carrying amount of accrued interest receivable on investments, accounts payable, FFB borrowings and liabilities incurred from bank resolutions approximates their fair value due to their short maturities or comparisons with current interest rates.

It was not practical to estimate the fair value of net receivables from bank resolutions. These assets are unique, not intended for sale to the private sector and have no established market. The FDIC believes that a sale to the private sector would require indeterminate, but substantial discounts, for an interested party to profit from these assets because of credit and other risks. Additionally, a discount of this proportion would significantly increase the cost of bank resolutions to the FDIC. Further, comparisons with other financial instruments do not provide a reliable measure of their fair value. Due to these and other factors, the FDIC cannot determine an appropriate market discount rate and, thus, is unable to estimate fair value on a discounted cash flow basis. As shown in Note 5, the carrying amount is the original amount advanced net of the estimated allowance for loss, which is estimated cash recovery value.

The majority of the investment in corporate-owned assets, net (except real estate), is comprised of various types of financial instruments (investments, loans, accounts receivable, etc.) and to a lesser degree, other assets acquired from failed banks. As with Net Receivables from Bank Resolutions, it was not practicable to estimate fair values. Cash recoveries are primarily from the sale of poor quality assets. They are dependent upon market conditions which vary over time and can occur unpredictably over many years following resolution. Since the FDIC cannot reasonably predict the timing of these cash recoveries, it is unable to estimate the fair value on a discounted cash flow basis. As shown in Note 6, the carrying amount is the original amount advanced net of the estimated allowance for loss, which is the estimated cash recovery value.

As stated in Note 11, the carrying amount of the estimated liability for unresolved cases is the total of estimated losses for banks that have not yet failed, but which the regulatory process has identified as probably requiring resolution in the near future. It does not consider discounted future cash flows because the FDIC cannot predict the timing of events with reasonable accuracy. For this reason, the FDIC considers the total estimate of these losses to be the best measure of their fair value.

19. Disclosure about Recent Financial Accounting Standards Board Pronouncements

The Financial Accounting Standards Board has issued Statement of Financial Accounting Standards No. 112 (Employer's Accounting for Postemployment Benefits) which the FDIC is required to adopt by 1994. This new statement establishes accounting standards for employers who provide benefits to former or inactive employees after employment but before retirement. This statement requires employers to recognize the obligation to provide postemployment benefits. However, the BIF's obligation for these benefits is not recognized because the amount cannot be reasonably estimated.

In May, 1993, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 114, "Accounting by Creditors for Impairment of a Loan." Based upon an initial study and analysis, this statement is not expected to have a material impact on the BIF when it is adopted on January 1, 1995.

In May, 1993, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities." This statement is not expected to have a material impact on the BIF when it is adopted on January 1, 1994.

20. Supplementary Information Relating to the Statements of Cash Flows

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 the Statements of Cash Flows presentation, cash outflows for bank resolutions excludes $3.7 billion in 1993 and $12.5 billion in 1992 for assets purchased.

Reconciliation of Net Income to Net Cash Provided by Operating Activities

Dollars in Thousands	For the Year Ended December 31 1993	1992
Net Income	$ 13,222,235	$6,927,367
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Income Statement Items:		
Provision for insurance losses	(7,677,400)	(2,259,690)
Amortization of U.S. Treasury securities	6,715	10,638
Interest on Federal Financing Bank borrowings	(72,977)	(53,033)
Depreciation on buildings	3,339	3,361
Change in Assets and Liabilities:		
Decrease in accrued interest receivable on investments and other assets	24,915	58,296
Decrease (increase) in receivables from bank resolutions	14,384,772	(12,816,626)
Decrease (increase) in corporate-owned assets, net	418,322	1,101,121
(Decrease) increase in accounts payable, accrued and other liabilities	(216,563)	324,559
(Decrease) increase in liabilities from bank resolutions	(9,419,779)	7,389,247
Net Cash Provided by Operating Activities	$ 10,673,579	$ 685,240

Savings Association Insurance Fund's Financial Statements

Statements of Financial Position

Federal Deposit Insurance Corporation

Savings Association Insurance Fund

Statements of Financial Position

Dollars in Thousands	December 31 1993	December 31 1992
Assets		
Cash and cash equivalents, including restricted amounts of $3,285 for 1993 and $93,267 for 1992 (Note 3)	$ 15,735	$ 341,151
Investment in U.S. Treasury obligations, net (Note 4)	1,263,608	0
Entrance and exit fees receivable, net (Note 5)	60,655	84,896
Accrued interest receivable on investments and other assets (Note 6)	28,038	45,181
Net receivables from thrift resolutions (Note 7)	174,948	0
Total Assets	**1,542,984**	**471,228**
Liabilities and the Fund Balance		
Accounts payable, accrued and other liabilities (Note 8)	3,875	10,328
Due to the FSLIC Resolution Fund (Note 7)	175,507	112
Liability incurred from thrift resolutions (Note 7)	932	0
Estimated liability for unresolved cases (Note 9)	18,000	3,700
Total Liabilities	**198,314**	**14,140**
Commitments and contingencies (Notes 14 and 15)		
SAIF-Member Exit Fees and Investment Proceeds Held in Reserve (Note 5)	**188,941**	**178,061**
Fund Balance	**1,155,729**	**279,027**
Total Liabilities and the Fund Balance	**$1,542,984**	**$ 471,228**

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

Statements of Income and the Fund Balance

Federal Deposit Insurance Corporation

Savings Association Insurance Fund
Statements of Income and the Fund Balance

Dollars in Thousands	For the Year Ended December 31	
	1993	**1992**
Revenue		
Assessments earned (Note 10)	$ 897,692	$ 172,079
Interest earned	25,305	6,544
Entrance fee revenue (Note 5)	48	9
Other revenue	471	11
Total Revenue	**923,516**	**178,643**
Expenses and Losses		
Operating expenses	30,283	39,374
Provision for insurance losses (Note 11)	16,531	(14,945)
Interest expense	0	(5)
Total Expenses and Losses	**46,814**	**24,424**
Net Income Before Funding Transfer and Cumulative Effect of a Change in Accounting Principle	**876,702**	**154,219**
Cumulative effect of accounting change for certain postretirement benefits (Note 13)	0	(4,558)
Net Income Before Funding Transfer	**876,702**	**149,661**
Funding Transfer from the FSLIC Resolution Fund	0	35,446
Net Income	**876,702**	**185,107**
Fund Balance - Beginning	**279,027**	**93,920**
Fund Balance - Ending	**$1,155,729**	**$ 279,027**

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

Statements of Cash Flows

Federal Deposit Insurance Corporation

Savings Association Insurance Fund

Statements of Cash Flows

Dollars in Thousands	For the Year Ended December 31 1993	1992
Cash Flows from Operating Activities		
Cash provided from:		
Assessments	$ 911,071	$ 265,365
Interest on U.S. Treasury obligations	16,415	9,451
Interest on exit fees	4,406	2,698
Entrance and exit fee collections (Note 5)	31,605	34,798
Operating expenses funded by the FSLIC Resolution Fund	7,182	29,561
Recoveries from "Oakar" bank resolutions	18,645	0
Recoveries from thrift resolutions	2,012	0
Miscellaneous receipts	620	0
Cash used for:		
Operating expenses	(43,047)	(36,685)
Disbursements for thrift resolutions	(3,182)	0
Disbursements for "Oakar" bank resolutions	(3,700)	(20,114)
Interest paid on liabilities incurred from "Oakar" bank resolutions	0	(604)
Miscellaneous disbursements	(11)	0
Net Cash Provided by Operating Activities (Note 18)	**942,016**	**284,470**
Cash Flows from Investing Activities		
Cash provided from:		
Maturity and sale of U.S. Treasury obligations	51,305	0
Cash used for:		
Purchase of U.S. Treasury obligations	(1,318,737)	0
Net Cash Used by Investing Activities	**(1,267,432)**	**0**
Net (Decrease) Increase in Cash and Cash Equivalents	**(325,416)**	**284,470**
Cash and Cash Equivalents - Beginning	**341,151**	**56,681**
Cash and Cash Equivalents - Ending	**$ 15,735**	**$ 341,151**

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

Notes to the Financial Statements

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. The FIRREA created the Bank Insurance Fund (BIF), the Savings Association Insurance Fund (SAIF) and the FSLIC Resolution Fund (FRF). It also designated the Federal Deposit Insurance Corporation (FDIC) as the administrator of these three funds. The BIF insures the deposits of all BIF-member institutions (normally commercial or savings banks) and the SAIF insures the deposits of all SAIF-member institutions (normally thrifts). The FRF is responsible for winding up the affairs of the former Federal Savings and Loan Insurance Corporation (FSLIC). All three funds are maintained separately to carry out their respective mandates.

The FIRREA created the Resolution Trust Corporation (RTC), which manages and resolves all thrifts previously insured by the FSLIC for which a conservator or receiver was appointed during the period January 1, 1989, through August 8, 1992. The Resolution Trust Corporation Refinancing, Restructuring and Improvement Act of 1991 (1991 RTC Act) extended the RTC's general resolution responsibility through September 30, 1993, and beyond that date for those institutions previously placed under RTC control.

The Resolution Trust Corporation Completion Act of 1993 (1993 RTC Act) enacted December 17, 1993, extended the RTC's general resolution responsibility through a date between January 1, 1995 and July 1, 1995. The Chairperson of the Thrift Depositor Protection Oversight Board will select the date.

The Resolution Funding Corporation (REFCORP) was established by the FIRREA to provide funds to the RTC for use in thrift resolutions. The Financing Corporation (FICO), established under the Competitive Equality Banking Act of 1987, is a mixed-ownership government corporation whose sole purpose was to function as a financing vehicle for the FSLIC. Effective December 12, 1991, as provided by the Resolution Trust Corporation Thrift Depositor Protection Reform Act of 1991 (RTC Reform Act), the FICO's ability to serve as a financing vehicle was terminated.

The Omnibus Budget Reconciliation Act of 1990 (1990 Act) 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) on terms and conditions determined by the FFB.

The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) was enacted to further strengthen the insurance funds administered by the FDIC. The FDIC's authority to borrow from the U.S. Treasury, on behalf of the BIF and the SAIF, to cover insurance losses was increased from $5 billion to $30 billion. However, the FDIC cannot incur any additional obligation for the BIF or the SAIF if incurring the obligation would result in the amount of total obligations in the respective Fund exceeding 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) the total amount authorized to be borrowed from the U.S. Treasury excluding FFB borrowings. This restriction against incurring additional obligations is known as the Maximum Obligation Limitation (see Note 2). At December 31, 1993, the SAIF had approximately $1.2 billion in remaining obligation authority.

The FDICIA requires that the FDIC repay U.S. Treasury borrowings under the $30 billion authorization from assessment revenues. The FDIC must provide the U.S. Treasury with a repayment schedule demonstrating that future assessment revenues are adequate to repay principal borrowed and pay interest due.

Operations of the SAIF

The primary purpose of the SAIF is to insure the deposits and to protect the depositors of insured thrifts. In this capacity, the SAIF currently has financial responsibility for: 1) all federally insured depository institutions that became members of the SAIF after August 8, 1989, for which the RTC does not have resolution authority and 2) all deposits insured by the SAIF that are held by BIF-member banks, so-called "Oakar" banks, created pursuant to the "Oakar amendment" provisions found in Section 5(d)(3) of the Federal Deposit Insurance Act. On a date between January 1, 1995 and July 1, 1995, the SAIF will assume resolution responsibility for all SAIF-member depository institutions that had not been previously placed under the RTC control. Any administrative facilities or supplies remaining upon the dissolution of the FRF will be transferred to the SAIF.

The "Oakar amendment" provisions referred to above allow, with approval of the appropriate federal regulatory authority, any insured depository institution to merge, consolidate or transfer the assets and liabilities of an acquired institution without changing insurance coverage for the acquired deposits. Such acquired deposits continue to be either SAIF-insured deposits and assessed at the SAIF assessment rate or BIF-insured deposits and assessed at the BIF assessment rate. In addition, any losses resulting from the failure of these institutions are to be allocated between the BIF and the SAIF based on the respective dollar amounts of the institution's BIF-insured and SAIF-insured deposits.

The SAIF is funded from the following sources: 1) reimbursement by the FRF of administrative and supervisory expenses incurred between August 9, 1989, and September 30, 1992 (these expenses had priority over other obligations of the FRF); 2) SAIF-member assessments from "Oakar" banks; 3) other SAIF assessments that are not required for the FICO or the FRF (through December 31, 1992); 4) U.S. Treasury payments not to exceed $8 billion for losses for fiscal years 1994 through 1998 contingent upon appropriations from the U.S. Treasury for that purpose; 5) U.S. Treasury payments from unused appropriations to the RTC for losses for two years after the date the RTC is terminated; 6) Federal Home Loan Bank borrowings; and 7) U.S. Treasury and FFB borrowings.

The 1993 RTC Act places significant restrictions on funding from sources 4) and 5) above. Among other restrictions, the FDIC must certify to Congress before appropriated funds from either source are used that: 1) SAIF-insured institutions are unable to pay premiums sufficient to cover insurance losses without adversely affecting their ability to raise and maintain capital or to maintain the assessment base and 2) an increase in premiums could reasonably be expected to result in greater losses to the government.

2. Summary of Significant Accounting Policies

General

These financial statements pertain to the financial position, results of operations and cash flows of the SAIF, and are presented in accordance with generally accepted accounting principles. These statements do not include reporting for assets and liabilities of closed thrifts for which the SAIF acts as receiver or liquidating agent. Periodic and final accountability reports of the SAIF'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 book value, which is the face value of securities plus the unamortized premium or less the unamortized discount. Such amortizations 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 effective interest method.

Escrowed Funds from Resolution Transactions

A thrift operating under a FSLIC assistance agreement was placed into SAIF receivership in 1993 and sold. Since these transactions were executed in order to terminate the assistance agreement, the FRF funded SAIF's payment to the acquirers (the difference between failed thrift liabilities assumed and assets purchased, plus or minus any premium or discount). The SAIF 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 (see Note 7).

Assessment Revenue Recognition

The FICO has priority and, through December 31, 1992, the FRF had priority over the SAIF for receiving and utilizing SAIF-member assessments to ensure availability of funds for specific operational activities. Accordingly, the SAIF recognized as assessment revenue only that portion of SAIF-member assessments not required by: 1) the FICO in 1993 or 1992 and 2) the FRF in 1992. Assessments on

SAIF-insured deposits held by "Oakar" banks are retained in the SAIF and, thus, are not subject to draws by the FICO or the FRF (see Note 10).

Receivership Administration
The SAIF is responsible for controlling and disposing of the assets of failed thrift institutions placed in SAIF receivership 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.

Litigation Losses
The SAIF accrues, as a charge to current period operations, an estimate of probable losses from litigation against the SAIF in its corporate capacity. The FDIC's Legal Division recommends these estimates on a case-by-case basis.

Cost Allocations Among Funds
Certain 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 operating expenses were incurred by the Funds. The FDIC includes the cost of facilities used in operations in the BIF's financial statements. The BIF charges the SAIF a rental fee representing an allocated share of its annual depreciation. The cost of furniture, fixtures and equipment purchased by the FDIC on behalf of the three Funds under its administration is allocated among these Funds on a pro rata basis. The SAIF expenses its share of these allocated costs at the time of acquisition because of their immaterial amounts.

Postretirement Benefits Other Than Pensions
Effective January 1, 1992, the FDIC implemented the requirements of the Statement of Financial Accounting Standards (SFAS) No. 106, "Employer's Accounting for Postretirement Benefits Other Than Pensions." This standard mandates the accrual method of accounting for postretirement benefits other than pensions based on actuarially determined costs to be recognized during employees' years of active service. This was a significant change from the FDIC's previous policy of recognizing these costs in the year the benefits were provided (i.e., the cash basis). In 1992, the SAIF funded its yearly

charge for these expenses and the BIF provided the accounting and administration of these postretirement benefits on behalf of the SAIF.

In 1993, the FDIC established a plan administrator to provide the accounting and administration of these benefits on behalf of the BIF, the SAIF, the FRF and the RTC. The SAIF funded its 1993 expense directly to the plan administrator.

Maximum Obligation Limitation (MOL)
In 1993 and 1992, for purposes of calculating the maximum obligation limitation, the FDIC, through its allocation policy, allocated the total authorized borrowings of $30 billion to the BIF. In subsequent periods no portion of the $30 billion U.S. Treasury borrowing authority will be allocated to the SAIF unless the SAIF has primary resolution authority for thrift institutions as of the date of the MOL calculation for the SAIF or projected borrowing needs for SAIF-insured institutions. Any future allocation of U.S. Treasury borrowing authority will be based upon projected borrowing needs of the FDIC. "Borrowing needs" is defined as the projected borrowing needed over the next 12 months based on FDIC's financial projection models. Any remaining amount to be allocated will be based on insured deposits as published in the latest FDIC Annual Report.

In calculating the maximum obligation limitation, "other assets" consisting of receivables from thrift resolutions are valued at 90 percent of their net realizable value. In addition, the SAIF's estimated liability for future financial institution failures or assistance transactions is excluded in determining the SAIF's total obligations where there is no contractual agreement between FDIC and the troubled institution comprising the estimated liability.

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

Reclassifications
Reclassifications have been made in the 1992 Financial Statements to conform to the presentation used in 1993.

3. Cash and Cash Equivalents

The SAIF considers cash equivalents to be short-term, highly liquid investments with original maturities of three months or less. Substantially all the restricted cash is comprised of the SAIF exit fees collected plus interest earned on exit fees. These funds may only be used to meet the SAIF's potential obligation to the FICO (see Note 5).

In 1993, cash restrictions included $317 thousand for health insurance payable, $375 thousand for cash not invested and $2.593 million for exit fee and related interest collections invested in one-day special Treasury certificates. In 1992, cash restrictions included $406 thousand for health insurance payable and $92.86 million for exit fee and related interest collections.

Cash and Cash Equivalents

Dollars in Thousands	December 31	
	1993	1992
Cash	$ 13,142	$ 198
One-day special Treasury certificates	2,593	340,953
	$ 15,735	**$341,151**

4. U.S. Treasury Obligations

All cash received by the SAIF is invested in U.S. Treasury obligations unless the cash is: 1) to defray operating expenses; 2) used for outlays related to liquidation activities; or 3) invested in one-day special Treasury certificates.

In 1993, cash restrictions included $121.8 million for exit fee and related interest collections invested in long-term U.S. Treasury notes.

U.S. Treasury Obligations

December 31, 1993

Dollars in Millions

Maturity	Description	Yield at Purchase	Book Value	Market Value	Face Value
Less than one year	U.S. Treasury Notes & Bonds	3.2%	$ 52.2	$ 52.2	$ 51.8
1-3 years	U.S. Treasury Notes & Bonds	4.0%	1,211.4	1,213.0	1,210.0
			$ 1,263.6	**$ 1,265.2**	**$ 1,261.8**

In 1993, the unamortized premium, net of unamortized discount, was $1.8 million.

5. Entrance and Exit Fees Receivable, Net

The SAIF receives entrance and exit fees for conversion transactions in which an insured depository institution converts from the BIF to the SAIF (resulting in an entrance fee) or from the SAIF to the BIF (resulting in an exit fee). Regulations approved by the FDIC's Board of Directors and published in the *Federal Register* on March 21, 1990, directed that exit fees paid to the SAIF be held in a reserve account until the FDIC and the Secretary of the Treasury determine that it is no longer necessary to reserve such funds for the payment of interest on obligations previously issued by the FICO. The exit fee collections are invested in Treasury securities and are held in reserve pending determination of ownership. Interest received on these investments was $3 million and $2.7 million for 1993 and 1992, respectively.

The SAIF records entrance fees as revenue after the BIF-to-SAIF conversion transaction is consummated. However, due to the requirement that the SAIF exit fees be held in a reserve account, thereby restricting the SAIF's use of such proceeds, the SAIF does not recognize exit fees, nor any interest earned, as revenue. Instead, the SAIF recognizes the consummation of a SAIF-to-BIF conversion transaction by establishing a receivable from the institution and an identical reserve account to recognize the potential payment to the FICO. As exit fee proceeds are received, the receivable is reduced while the reserve remains pending the determination of funding requirements for interest payments on the FICO's obligations.

Within specified parameters, the regulations allow an acquiring institution to pay its entrance/exit fees interest free, in equal annual installments over a period of not more than five years. When an institution elects such a payment plan, the SAIF records the entrance or exit fee receivable at its present value. The discount rates (current value of funds) for 1993 and 1992 were 4 percent and 6 percent, respectively.

Entrance and Exit Fees Receivable, Net (1993)

Dollars in Thousands

	Beginning Balance 01/01/93	New Receivables	Collections	Net Change in Unamortized Discount	Ending Balance 12/31/93
Entrance fees	$ 0	$ 48	$ (45)	$ 0	$ 3
Exit fees	84,896	1,946	(31,560)	5,370	60,652
	$ 84,896	**$ 1,994**	**$(31,605)**	**$ 5,370**	**$60,655**

Entrance and Exit Fees Receivable, Net (1992)

Dollars in Thousands

	Beginning Balance 01/01/92	New Receivables	Collections	Net Change in Unamortized Discount	Ending Balance 12/31/92
Entrance fees	$ 0	$ 9	$ (9)	$ 0	$ 0
Exit fees	91,015	26,163	(34,789)	2,507	84,896
	$91,015	**$26,172**	**$(34,798)**	**$2,507**	**$84,896**

6. Accrued Interest Receivable on Investments and Other Assets

Approximately half of the accounts receivable balance is comprised of unpaid assessments due from RTC receiverships.

The FRF owes the SAIF $2.7 million in interest on escrowed funds as of December 31, 1993 (as explained in Note 7). In 1993, the FRF paid $7.2 million to the SAIF for operating expenses and postretirement benefits.

As of December 31, 1993, the BIF owes the SAIF: 1) $6.2 million for an allocation adjustment and 2) $1.9 million for a refund resulting from the change in the loss estimate for the failure of Southeast Bank, N.A., Miami, FL, and its affiliate Southeast Bank of West Florida, Pensacola, FL, which held deposits insured by the BIF and the SAIF pursuant to the "Oakar Amendment" provisions (as explained in Note 2). In 1993, the BIF transferred to the SAIF:

1) $18.6 million resulting from the 1992 revision of the estimated loss for SAIF's allocated share of the failure of Southeast Bank, N.A., Miami, FL, and its affiliate Southeast Bank of West Florida, Pensacola, FL, and 2) $18.4 million for assessment revenues resulting from the erroneous allocation of assessments from "Oakar" banks for the years 1990 through 1992 (see Note 2).

Accrued Interest Receivable on Investments and Other Assets

Dollars in Thousands	December 31 1993	December 31 1992
Accrued interest receivable on investments	$ 11,928	$ 0
Accounts receivable	5,298	802
Due from the FSLIC Resolution Fund	2,670	7,295
Due from the Bank Insurance Fund	8,142	37,084
	$ 28,038	**$ 45,181**

7. Net Receivables from Thrift Resolutions

The Heartland Federal Savings and Loan Association (Heartland), Ponca City, Oklahoma, was a SAIF-insured institution that became party to a 10-year assistance agreement with the FSLIC upon the failure of its predecessor, Frontier Federal Savings and Loan Association, in 1988. FSLIC obligations were assumed by the FRF upon the enactment of the FIRREA in 1989. Section 32 of the assistance agreement effectively gave the FRF sole equity interest in Heartland. Section 2.13 of the agreement entitled "Additional Operating Terms and Conditions" gave the FDIC, as manager of the FRF, authority to take such action as might be necessary to effect the acquisition of Heartland. The FDIC determined that the value of the FRF's equity interest in Heartland would be maximized and total assistance cost would be minimized by a termination of the assistance agreement and sale of Heartland, thereby returning it to the private sector. To effect the sale, a receiver was appointed for Heartland for the purpose of transferring assets and liabilities to the acquirers.

Technically, Heartland was not a "failing institution" because of its well-capitalized condition, which resulted from the government assistance provided. Heartland's Board of Directors consented to the Office of Thrift Supervision's appointment of the FDIC (SAIF) as receiver on October 8, 1993. The FDIC was appointed receiver because, at that time, RTC's authority to resolve FSLIC-insured thrifts had not yet been extended by the RTC Completion Act.

Because Heartland was not failing, all uninsured depositors and general trade creditors were paid in full, leaving only the FRF as sole creditor. Payment to the acquirers of Heartland to cover insured depositors' claims was funded by the FRF and represents a claim against the receivership's assets. The receiver will reimburse the FRF as claims are satisfied through the liquidation process. As of December 31, 1993, the receiver owes the FRF $175 million. The SAIF accounts currently reflect $932 thousand held in escrow on behalf of the receivership.

As of December 31, 1993, the SAIF, in its receivership capacity, held assets with a book value of $72 million. Estimated cash recoveries from the management and disposition of assets (excluding cash and miscellaneous receivables of $1.6 million) are regularly evaluated, but ultimate recoveries remain uncertain because of changing economic conditions. Any loss as a result of reduced recoveries will be borne by the FRF as provided in the agreement terminating the assistance agreement and as described in the FDIC board case.

8. Accounts Payable, Accrued and Other Liabilities

Accounts Payable, Accrued and Other Liabilities

Dollars in Thousands	December 31 1993	December 31 1992
Miscellaneous payable	$ 3,350	$ 4,174
Due to the Bank Insurance Fund	525	6,154
	$3,875	**$10,328**

9. Estimated Liabilities for:

Unresolved Cases

The SAIF records an estimated loss for thrifts or "Oakar" banks that have not yet failed, but have been identified by the regulatory process as likely to fail within the foreseeable future as a result of regulatory insolvency (equity less than 2% of assets). The FDIC relies on this finding regarding regulatory insolvency as the determining factor in defining the existence of the "accountable event" that triggers loss recognition under generally accepted accounting principles.

As with any of its estimated losses, the FDIC cannot predict the timing of events with reasonable accuracy. These liabilities and a corresponding reduction in the Fund Balance are recognized 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 SAIF to recover some or all of these losses and that these amounts have not been reflected as a reduction in the losses.

The estimated liability for unresolved cases is derived in part from estimates of recoveries from the sale of the assets of these probable thrift or "Oakar" bank failures. The estimated cash recoveries from the sale of assets are subject to uncertainties because of changing economic conditions. This could understate the ultimate costs to the SAIF from probable "Oakar" bank or thrift failures.

For the years ending December 31, 1993, and December 31, 1992, the SAIF was responsible for establishing an estimated loss for those thrifts chartered after August 8, 1989, and for Oakar banks. The RTC was responsible for other thrift institutions (see Note 1).

Litigation Losses
The FDIC records as an estimated loss on the SAIF's financial statements an estimated cost for unresolved legal cases to the extent those losses are considered to be both probable in occurrence and estimable in amount. In addition to these losses, the FDIC's Legal Division has determined that losses from a receivership's unresolved legal case totaling $10 million are reasonably possible.

10. Assessments

The 1990 Act authorized the FDIC to set assessment rates for the SAIF members semiannually, to be applied against a member's average assessment base. The assessment rate for all thrifts for calendar year 1992 was 0.230 percent (23 cents per $100 of domestic deposits). The FDICIA authorized the FDIC to increase assessment rates for SAIF-member institutions as needed to ensure that funds are available to satisfy the SAIF's obligations.

On September 15, 1992, the FDIC's Board of Directors agreed on a transitional risk-based assessment system that charges higher rates to those thrifts that pose greater risks to the SAIF. Under the new rule, beginning in January 1993, each thrift paid an assessment rate of between 23 cents and 31 cents per $100 of domestic deposits, depending on its risk classification. To arrive at a risk-based assessment for a particular thrift, the FDIC placed each thrift in one of nine risk categories using a two-step process based first on capital ratios and then on other relevant information. On June 17, 1993, the Board issued a final rule on the risk-based assessments system effective on October 1, 1993. The final rule made limited changes to the transitional risk-based assessment system effective during 1993. The Board expects to review premium rates at least once every six months. For calendar year 1994, the FDIC estimates that thrifts will pay an average rate of about 24.8 cents per $100 of domestic deposits.

Secondary Reserve Offset
The FIRREA authorized insured thrifts to offset against any assessment premiums their pro rata share of amounts that were previously part of the FSLIC's "Secondary Reserve." The Secondary Reserve represented premium prepayments that insured thrifts were required by law to deposit with the FSLIC during the period 1961 through 1973 to quickly increase the FSLIC's insurance reserves to absorb losses if the regular assessments were insufficient. The allowable offset is limited to a maximum of 20 percent of an institution's remaining pro rata share for any calendar year beginning before 1993. After calendar year 1992, there is no limitation on the remaining offset amount.

The Secondary Reserve offset serves to reduce the gross SAIF-member assessments due (excluding assessments from "Oakar" banks), thereby reducing the assessment premiums available to the FICO and the SAIF. The remaining Secondary Reserve credit was \$2 million and \$200 million for 1993 and 1992, respectively.

SAIF Assessments

Dollars in Thousands	December 31 1993	December 31 1992
SAIF-member assessments	$1,650,394	$1,668,011
Less: Secondary Reserve offset/other adjustments/credits	(221,404)	(51,153)
Cash received for prior period assessments	(18,439)	0
FICO assessment	(779,214)	(772,300)
FRF assessment	0	(844,558)
Plus: Assessment receivables outstanding	5,269	0
SAIF-Member Assessments Earned, (Net)	**636,606**	**0**
SAIF assessments from "Oakar" banks - current period	261,086	172,079
SAIF Assessments Earned	**$ 897,692**	**$ 172,079**

11. Provision for Insurance Losses

Provision for Insurance Losses

Dollars in Thousands	December 31 1993	1992
SAIF's allocated share of loss from failure of Southeast Bank, N.A., Miami, FL	$ (1,469)	$(18,645)
Estimated loss for unresolved cases (see Note 9)	18,000	3,700
	$ 16,531	**$(14,945)**

12. Pension Benefits, Savings Plans and Accrued Annual Leave

Eligible FDIC employees (i.e., all permanent and temporary employees with an appointment 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 offset 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 also can 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 FDIC employees may also participate in an FDIC-sponsored tax-deferred savings plan with matching contributions. The SAIF pays its share of the employer's portion of all related costs.

Although the SAIF 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.

The liability to employees for accrued annual leave is approximately $756 thousand and $958 thousand at December 31, 1993 and 1992, respectively.

Pension Benefits and Savings Plans Expenses

Dollars in Thousands	December 31	
	1993	1992
Civil Service Retirement System	$ 1,628	$ 616
Federal Employee Retirement System (Basic Benefit)	1,146	1,254
FDIC Savings Plan	663	646
Federal Thrift Savings Plan	337	341
	$ 3,774	$ 2,857

13. Postretirement Benefits Other than Pensions

The FDIC provides certain health, dental and life insurance coverage for its eligible retirees, the retiree's beneficiaries and covered dependents. Eligible retirees are those who have elected the FDIC's health and/or life insurance program and are entitled to an immediate annuity. However, dental coverage is provided to all retirees regardless of the plan selected.

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 wraparound. Dental care is underwritten by Connecticut General Life Insurance Company. The life insurance program is underwritten by Metropolitan Life Insurance Company.

The FDIC contributes toward health insurance premiums at the same rate for both active and retired employees. The FDIC uses a "minimum premium funding arrangement" in which premiums are held in a restricted account. Medical claims and fixed costs are paid to Blue Cross/Blue Shield from this account on a weekly basis.

Under this arrangement, the FDIC's liability exposure is limited in any one contract year. The life insurance program provides for basic coverage at no cost to retirees and allows converting optional coverages to direct-pay plans with Metropolitan Life Insurance Company. The dental insurance program provides coverage at no cost to retirees.

Beginning March 1994, the FDIC health insurance coverage will be self-insured for hospital/medical, prescription drug, mental health and chemical dependency, and the FDIC has purchased additional risk protection through stop-loss and fiduciary liability insurance from Aetna Life Insurance Company. All claims will be administered on an Administrative Services Only basis with the hospital/medical claims administered by Aetna Life Insurance Company, the mental health and chemical dependency claims administered by OHS Foundation Health Psychcare Inc. and the prescription drug claims administered by Caremark.

As part of adopting SFAS No. 106 (see Note 2), the FDIC elected to immediately recognize the accumulated postretirement benefit liability, measured as of January 1, 1992. The accumulated liability (transition obligation) represents that portion of future retiree benefits costs related to service already rendered by both active and retired employees up to the date of adoption. In 1992, the SAIF recorded an expense of $4.6 million for this liability, which has been reflected in the Statements of Income and the Fund Balance as the cumulative effect of a change in accounting principle for periods prior to 1992.

The SAIF expensed $1.9 million and $1.6 million for such benefits for the years ended December 31, 1993 and 1992, respectively.

For measurement purposes, the FDIC assumed the following: 1) a discount rate of 6 percent; 2) an increase in health costs in 1993 of 14 percent, decreasing down to an ultimate rate in 1998 of 8 percent; and 3) an increase in dental costs in 1993 and thereafter of 8 percent. Both the assumed discount rate and health care cost rate have a significant effect on the amount of the obligation and periodic cost reported.

If the health care cost rate were increased one percent, the accumulated postretirement benefit obligation as of December 31, 1993, would have increased by 7.5 percent. The effect of this change on the aggregate of service and interest cost for 1993 would be an increase of 28.8 percent.

Net Periodic Postretirement Cost

Dollars in Thousands	December 31 1993	December 31 1992
Service cost (benefits attributed to employee service during the year)	$ 1,195	$ 991
Interest cost on accumulated postretirement benefit obligation	613	605
Amortization of prior service cost	(48)	0
Amortization of unrecognized transition obligation	171	0
Return on plan assets	2	0
Net Periodic Postretirement Cost Before Funding Transfer	**1,933**	**1,596**
Funds transferred from the FSLIC Resolution Fund	0	(1,197)
	$ 1,933	**$ 399**

As stated in Note 2, beginning in December 1993, the FDIC established a plan to be supervised by a plan administrator to provide accounting and administration of these benefits program on behalf of the BIF, the SAIF, the FRF and the RTC. The SAIF portion of this long-term liability has been transferred to the plan administrator. In 1992, the BIF provided the accounting and administration of this obligation. The SAIF has funded its obligation and these funds are being managed by the administrator as "plan assets".

Accumulated Postretirement Benefit Obligation by Participant

Dollars in Thousands	December 31 1993
Retirees	$ 1,852
Full eligible active plan participants	347
Other active participants	5,887
Total obligation	8,086
Less: Plan assets at fair value (1)	7,680
Postretirement benefit liability included in the Statements of Financial Position	$ 406

(1) Consists of one-day special Treasury certificates

14. Commitments

The SAIF currently is sharing the FDIC's leased space. The SAIF's allocated share of lease commitments totals $3.5 million for future years. The agreements contain escalation clauses resulting in adjustments, usually on an annual basis. The SAIF recognized leased space expense of $1.7 million and $1.8 million for the years ended December 31, 1993 and 1992, respectively.

Leased Space Fees

Dollars in Thousands

1994	1995	1996	1997	1998
$1,238	$965	$638	$430	$212

15. Concentration of Credit Risk

The SAIF is counterparty to financial instruments with entities located in two regions of the United States experiencing problems in both loans and real estate. The SAIF's maximum exposure to possible accounting loss for these instruments is $491 thousand for

Southeast Bank, N.A., Miami, FL, and $3.3 million for Olympic National Bank, Los Angeles, CA.

Insured Deposits
As of December 31, 1993, the total deposits insured by the SAIF is approximately $696 billion. This would be the accounting loss if all the depository institutions fail and if any assets acquired as a result of the resolution process provide no recovery, and to the extent these losses are not covered by the RTC.

16. Disclosures about the Fair Value of Financial Instruments

Cash and cash equivalents are short-term, highly liquid investments and are shown at actual or approximate fair value. The fair value of the investment in U.S. Treasury Obligations is disclosed in Note 4 and is based on current market prices. The carrying amount Due from the FSLIC Resolution Fund, short-term receivables, and accounts payable and other liabilities approximates their fair value due to their short maturities. As explained in Note 5, entrance and exit fees receivable are net of discounts calculated using an interest rate comparable to U.S. Treasury Bill or Government bond/note rates at the time the receivables are accrued. The fair value of these receivables at December 31, 1993 and 1992, respectively, is $61 and $85 million, and is net of an applicable discount based on current rates of interest.

It was not practical to estimate the fair value of net receivables from thrift resolutions. These assets are unique, not intended for sale to the private sector and have no established market. The FDIC believes that a sale to the private sector would require indeterminate, but substantial discounts for an interested party to profit from these assets because of credit and other risks. Additionally, a discount of this proportion would significantly increase the cost of bank resolutions to the FDIC. Further, comparisons with other financial instruments do not provide a reliable measure of their fair value. Due to these and other factors, the FDIC cannot determine an appropriate market discount rate and, thus, is unable to estimate fair value on a discounted cash flow basis.

As stated in Note 9, the carrying amount of the estimated liability for unresolved cases is the total of estimated losses from thrifts or "Oakar" banks that have not yet failed, but which the regulatory process has identified as probably requiring resolution in the near future. It does not consider discounted future cash flows because the FDIC cannot predict the timing of events with reasonable accuracy. For this reason, the FDIC considers the total estimate of these losses to be the best measure of their fair value.

17. Disclosure about Recent Financial Accounting Standards Board Pronouncements

The Financial Accounting Standards Board (FASB) has issued Statement of Financial Accounting Standards No. 112 (Employer's Accounting for Postemployment Benefits) which the FDIC is required to adopt for 1994. This new statement establishes accounting standards for employers who provide benefits to former or inactive employees after employment but before retirement. This statement requires employers to recognize the obligation to provide postemployment benefits. However, the SAIF's obligation for these benefits is not recognized because the amount cannot be reasonably estimated.

In May, 1993, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 114, "Accounting by Creditors for Impairment of a Loan." Based upon an initial study and analysis, this statement is not expected to have a material impact on the SAIF when it is adopted on January 1, 1995.

In May, 1993, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities." This statement is not expected to have a material impact on the SAIF when it is adopted on January 1, 1994.

18. Supplementary Information Relating to the Statements of Cash Flows

As stated in the Summary of Significant Accounting Policies (see Note 2, *Escrowed Funds from Resolution Transactions*), the FDIC pays the acquirer the difference between failed thrift liabilities assumed and assets purchased, plus or minus any premium or discount. The SAIF considers the assets purchased portion of this transaction to be a non-cash adjustment. Accordingly, for the Statements of Cash Flows presentation, cash outflows for thrift resolutions excludes $932 thousand in 1993 for assets purchased.

Reconciliation of Net Income to Net Cash Provided by Operating Activities

Dollars in Thousands	For the Year Ended December 31 1993	1992
Net Income	$ 876,702	$ 185,107
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Income Statement Items:		
Provision for insurance losses	16,531	(14,945)
Interest expense	0	(5)
Amortization of U.S. Treasury securities (unrestricted)	37	0
Change in Assets and Liabilities:		
Decrease in amortization of U.S. Treasury Securities (restricted)	3,787	0
Decrease in amount due from the FSLIC Resolution Fund	0	102,378
Decrease in entrance and exit fees receivable	24,241	6,119
Decrease (Increase) in accrued interest receivable and other assets	18,611	(11,734)
(Increase) in receivables from thrift resolutions	(174,948)	0
(Decrease) in accounts payable, accrued and other liabilities	(6,453)	(13,930)
Increase in amount due to the FSLIC Resolution Fund	175,396	112
Increase in liability incurred from thrift resolutions	932	0
(Decrease) in estimated liabilities for unresolved cases	(3,700)	0
Increase in exit fees and investment proceeds held in reserve	10,880	31,368
Net Cash Provided by Operating Activities	**$ 942,016**	**$ 284,470**

FSLIC Resolution Fund's Financial Statements

Statements of Financial Position

Federal Deposit Insurance Corporation

FSLIC Resolution Fund

Statements of Financial Position

Dollars in Thousands	December 31	
	1993	1992
Assets		
Cash and cash equivalents (Note 3)	$ 1,603,931	$ 1,787,578
Net receivables from thrift resolutions (Note 4)	2,238,065	2,004,951
Investment in corporate-owned assets, net (Note 5)	577,161	544,746
Due from the Savings Association Insurance Fund (Note 6)	168,960	0
Other assets, net (Note 7)	38,898	45,729
Total Assets	**4,627,015**	**4,383,004**
Liabilities		
Accounts payable, accrued and other liabilities	106,391	136,752
Liabilities incurred from thrift resolutions (Note 8)	3,596,908	3,465,760
Estimated liabilities for:		
Assistance agreements (Note 9)	1,290,412	2,346,688
Litigation losses (Note 9)	70,000	73,404
Total Liabilities	**5,063,711**	**6,022,604**
Commitments and contingencies (Notes 15 and 16)		
Resolution Equity (Note 11)		
Contributed capital	43,991,000	42,028,000
Accumulated deficit	(44,427,696)	(43,667,600)
Total Resolution Equity	**(436,696)**	**(1,639,600)**
Total Liabilities and Resolution Equity	**$ 4,627,015**	**$ 4,383,004**

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

Statements of Income and Accumulated Deficit

Federal Deposit Insurance Corporation

FSLIC Resolution Fund

Statements of Income and Accumulated Deficit

Dollars in Thousands	For the Year Ended December 31 1993	1992
Revenue		
Assessments earned (Note 12)	$ (63)	$ 844,558
Interest on U.S. Treasury obligations	26,768	28,441
Revenue from corporate-owned assets	181,298	336,730
Other revenue	47,280	37,445
Total Revenue	**255,283**	**1,247,174**
Expenses and Losses		
Operating expenses	34,908	34,125
Interest expense	57,080	397,016
Corporate-owned asset expenses	53,461	128,185
Provision for losses (Note 10)	860,425	799,105
Other expenses	9,505	71,637
Total Expenses and Losses	**1,015,379**	**1,430,068**
Net Loss Before Funding Transfer and Cumulative Effect of a Change in Accounting Principle	**(760,096)**	**(182,894)**
Cumulative effect of accounting change for certain postretirement benefits (Note 14)	0	(5,892)
Net Loss Before Funding Transfer	**(760,096)**	**(188,786)**
Funding Transfer to the Savings Association Insurance Fund	0	(35,446)
Net Loss	**(760,096)**	**(224,232)**
Accumulated Deficit - Beginning	**(43,667,600)**	**(43,443,368)**
Accumulated Deficit - Ending	**$(44,427,696)**	**$(43,667,600)**

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

Statements of Cash Flows

Federal Deposit Insurance Corporation

FSLIC Resolution Fund

Statements of Cash Flows

Dollars in Thousands	For the Year Ended December 31 1993	1992
Cash Flows from Operating Activities		
Cash provided from:		
Assessments (Note 12)	$ (63)	$ 844,558
Interest on U.S. Treasury obligations	29,662	28,484
Recoveries from thrift resolutions	1,846,163	1,199,906
Recoveries from corporate-owned assets	393,804	505,492
Miscellaneous receipts	80,513	85,972
Cash used for:		
Operating expenses	(60,797)	(20,267)
Interest paid on indebtedness incurred from thrift resolutions	(50,267)	(477,306)
Disbursements for thrift resolutions	(2,477,719)	(6,376,833)
Disbursements for corporate-owned assets	(327,712)	(179,212)
Miscellaneous disbursements	(43,871)	(278,672)
Net Cash Used by Operating Activities Before Funding Transfer	**(610,287)**	**(4,667,878)**
Funding transfer to the Savings Association Insurance Fund	(7,182)	(29,561)
Net Cash Used by Operating Activities (Note 19)	**(617,469)**	**(4,697,439)**
Cash Flows from Investing Activities	**-0-**	**-0-**
Cash Flows from Financing Activities		
Cash provided from:		
U.S. Treasury payments	1,963,000	13,793,000
Cash used for:		
Payments of indebtedness incurred from thrift resolutions	(1,529,178)	(8,075,322)
Net Cash Provided by Financing Activities	**433,822**	**5,717,678**
Net Increase (Decrease) in Cash and Cash Equivalents	**(183,647)**	**1,020,239**
Cash and Cash Equivalents - Beginning	**1,787,578**	**767,339**
Cash and Cash Equivalents - Ending	**$ 1,603,931**	**$ 1,787,578**

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

Notes to the Financial Statements

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. The FIRREA created the Bank Insurance Fund (BIF), the Savings Association Insurance Fund (SAIF) and the FSLIC Resolution Fund (FRF). It also designated the Federal Deposit Insurance Corporation (FDIC) as the administrator of these three funds. The BIF insures the deposits of all BIF-member institutions (normally commercial or savings banks) and the SAIF insures the deposits of all SAIF-member institutions (normally thrifts). The FRF is responsible for winding up the affairs of the former Federal Savings and Loan Insurance Corporation (FSLIC). All three funds are maintained separately to carry out their respective mandates.

The FIRREA created the Resolution Trust Corporation (RTC), which manages and resolves all thrifts previously insured by the FSLIC for which a conservator or receiver was appointed during the period January 1, 1989, through August 8, 1992. The Resolution Trust Corporation Refinancing, Restructuring and Improvement Act of 1991 (1991 RTC Act) extended the RTC's general resolution responsibility through September 30, 1993, and beyond that date for those institutions previously placed under the RTC's control. The Resolution Trust Corporation Completion Act of 1993 (1993 RTC Act), enacted December 17, 1993, extended the RTC's general resolution responsibility through a date between January 1, 1995 and July 1, 1995. The Chairperson of the Thrift Depositor Protection Oversight Board will select the date.

The Resolution Funding Corporation (REFCORP) was established by the FIRREA to provide funds to the RTC for use in thrift resolutions. The Financing Corporation (FICO), established under the Competitive Equality Banking Act of 1987, is a mixed-ownership government corporation whose sole purpose was to function as a financing vehicle for the FSLIC. Effective December 12, 1991, as provided by the Resolution Trust Corporation Thrift Depositor Protection Reform Act of 1991, the FICO's ability to serve as a financing vehicle was terminated.

Operations of the FRF

The primary purpose of the FRF is to liquidate the assets and contractual obligations of the now defunct FSLIC. The FRF will complete the resolution of all thrifts that failed before January 1, 1989, or were assisted before August 9, 1989. The FIRREA provided that the RTC manage any receiverships resulting from thrift failures that occurred after December 31, 1988 but prior to the enactment of the FIRREA. There were seven such receiverships that are included in the FRF financial statements because the FRF remains financially responsible for the losses associated with these resolution cases.

The FRF is funded from the following sources, to the extent funds are needed, in this order: 1) income earned on and proceeds from the disposition of assets of the FRF; 2) liquidating dividends and payments made on claims received by the FRF from receiverships to the extent such funds are not required by the REFCORP or the FICO; and 3) amounts assessed against the SAIF's members by the FDIC that are not claimed by the FICO or by the REFCORP during the period from inception (August 9, 1989) through December 31, 1992 (FRF received no assessments in 1993). Excluded are assessments paid by BIF-member banks, so- called "Oakar" banks, created pursuant to the "Oakar amendment" provisions found in Section 5(d)(3) of the Federal Deposit Insurance Act (FDI Act) on SAIF-insured deposits. If these sources are insufficient to satisfy the liabilities of the FRF, payments will be made from the U.S. Treasury in amounts necessary, as are appropriated by the Congress, to carry out the purpose of the FRF.

The 1991 RTC Act amended the FIRREA by extending the FRF funding of the SAIF administrative and supervisory expenses through September 30, 1992. The 1993 RTC Act amended the termination date of the RTC from December 31, 1996 to no later than December 31, 1995. All assets and liabilities of the RTC will be transferred to the FRF, after which all future net proceeds from the sale of such assets will be transferred to the REFCORP for interest payments. The FRF will continue until all of its assets are sold or otherwise liquidated and all of its liabilities are satisfied. Upon the dissolution of the FRF, any funds remaining will be paid to the U.S. Treasury. Any administrative facilities and supplies will be transferred to the SAIF.

2. Summary of Significant Accounting Policies

General

These financial statements pertain to the financial position, results of operations and cash flows of the FRF, and are presented in accordance with generally accepted accounting principles. These statements do not include reporting for assets and liabilities of closed insured thrift institutions for which the FRF acts as receiver or liquidating agent. Periodic and final accountability reports of the FRF's activities as receiver or liquidating agent are furnished to courts, supervisory authorities and others as required.

Allowance for Losses on Receivables and Investment in Corporate-Owned Assets

The FRF records as a receivable the amounts advanced for assisting and closing thrift institutions. The FRF records as an asset the amounts advanced for investment in corporate-owned assets. Any related 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 the assisted or failed thrift institution, net of all estimated liquidation costs.

Estimated Liabilities for Assistance Agreements

The FRF establishes an estimated liability for probable future assistance payable to acquirers of troubled thrifts under its financial assistance agreements. Such estimates are presented on a discounted basis.

Litigation Losses

The FRF accrues, as a charge to current period operations, an estimate of probable losses from litigation against the FRF in both its corporate and receivership capacities. The FDIC's Legal Division recommends these estimates on a case-by-case basis. The litigation loss estimates related to its receivership capacity are included in the allowance for losses for receivables from thrift resolutions.

Receivership Administration

The FRF 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. Also, the income and expenses attributable to receiverships are accounted for as transactions of those receiverships. Indirect liquidation expenses incurred by the FRF on behalf of the receiverships are recovered from those receiverships through a cost recovery process.

Cost Allocations Among Funds

Certain 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 operating expenses were incurred by the Funds.

The FDIC includes the cost of facilities used in operations in the BIF's financial statements. The BIF charges the FRF a rental fee representing an allocated share of its annual depreciation. The cost of furniture, fixtures and equipment purchased by the FDIC on behalf of the three Funds under its administration is allocated among these Funds on a pro rata basis. The FRF expenses its share of these allocated costs at the time of acquisition because of their immaterial amounts.

Postretirement Benefits Other Than Pensions

Effective January 1, 1992, the FDIC implemented the requirements of the Statement of Financial Accounting Standards (SFAS) No. 106, "Employer's Accounting for Postretirement Benefits Other Than Pensions." This standard mandates the accrual method of accounting for postretirement benefits other than pensions based on actuarially determined costs to be recognized during employees' years of active service. This is a significant change from the FDIC's previous policy of recognizing these costs in the year the benefits were provided (i.e., the cash basis). In 1992, the FRF funded its yearly charge for these expenses and the BIF provided the accounting and administration of these postretirement benefits on behalf of the FRF. In 1993, the FDIC established a plan administrator to provide the accounting and administration of these benefits on behalf of the BIF, the SAIF, the FRF, and the Resolution Trust Corporation (RTC). The FRF funded its 1993 expenses directly to the plan administrator.

Assessment Revenue Recognition
The FICO has priority and, through December 31, 1992, the FRF had priority over the SAIF for receiving and utilizing SAIF-member assessments to ensure availability of funds for specific operational activities. Accordingly, the FRF recognized as assessment revenue in 1992 only that portion of SAIF-member assessments not required by the FICO. Assessments on SAIF-insured deposits held by "Oakar" banks are retained in the SAIF and, thus, are not subject to draws by the FICO or the FRF (see Notes 1 and 12).

Wholly Owned Subsidiary
The Federal Asset Disposition Association (FADA) is a wholly owned subsidiary of the FRF. The FADA was placed in receivership on February 5, 1990. However, due to outstanding litigation, a final liquidating dividend to the FRF will not be made until such time as the FADA's litigation liability is settled or dismissed. The investment in the FADA is accounted for using the equity method and is included in the line item "Other assets, net" (Note 7). As of December 31, 1993, the value of the investment has been adjusted for projected expenses relating to the liquidation of the FADA. The FADA's estimate of probable litigation losses is $3.3 million. Accordingly, a $3.3 million litigation loss has been recognized as a reduction in the value of the FRF's investment in the FADA. This represents a $1.7 million increase from probable litigation losses of $1.6 million at December 31, 1992. Additional litigation losses considered reasonably possible as of December 31, 1993, are estimated to be $6 thousand and remain unrecognized.

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

Reclassifications
Reclassifications have been made in the 1992 Financial Statements to conform to the presentation used in 1993.

Restatement
The 1992 financial statements were restated due to the correction of errors: 1) there were duplicate entries made during the conversion of the balance sheet balances from the former FSLIC to the FRF; and

2) a legal opinion clarified the FRF's obligation to ongoing institutions for their claims against the Secondary Reserve. These errors overstated the line items "Liabilities incurred from thrift resolutions" by $29.6 million and "Accounts Payable, accrued and other liabilities" by $20.8 million, respectively. These restatements adjust the beginning fund balance for 1992 by $50.4 million.

3. Cash and Cash Equivalents

The FRF considers cash equivalents to be short-term, highly liquid investments with original maturities of three months or less. In 1993, cash restrictions included $1 million for health insurance payable and $2.7 million for funds held in trust. In 1992, cash restrictions included $2 million for health insurance payable and $31.4 million for funds held in trust.

Cash and Cash Equivalents

Dollars in Thousands	December 31 1993	December 31 1992
Cash	$ 34,483	$83,174
One-day special Treasury certificates	1,569,448	1,704,404
	1,603,931	1,787,578

4. Net Receivables from Thrift Resolutions

As of December 31, 1993 and 1992, the FRF, in its receivership capacity, held assets with a book value of $1.8 billion and $3.8 billion, respectively. The estimated cash recoveries from the sale of these assets (excluding cash and miscellaneous receivables of $226 million in 1993 and $435 million in 1992) 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 FRF's actual recoveries upon the sale of these assets from the level of recoveries currently estimated.

Receivables from operating thrifts include amounts outstanding to qualified institutions under the Capital Instrument Program. The FSLIC purchased capital instruments such as Income Capital Certificates (ICCs) and Net Worth Certificates (NWCs) from insured institutions either in a non-cash exchange (by issuing a note payable of equal value) or by cash payments. The total amount of ICCs outstanding as of December 31, 1993 and 1992, is $62 million and $157 million, respectively. Likewise, the total amount of NWCs outstanding as of December 31, 1993 and 1992, is $3 million and $115 million, respectively.

The FRF pays interest on notes payable to an assisted institution in cash, while the institution only accrues interest payable on the certificates to the FRF. If an institution is profitable, it will actually pay interest owed to the FRF. Because of the uncertainty surrounding the collection of interest, the FRF only recognizes interest revenue when interest payments are received from an institution.

During 1993, the FDIC's Board of Directors delegated to the RTC, the authority to execute partnership agreements on behalf of the FDIC. Under that authority, the FDIC secured a limited partnership interest in two partnerships, Mountain AMD and Brazos Partners, in order to achieve a least cost resolution.

In the larger of these two partnerships, Brazos Asset Management, Inc. has been designated the general partner of Brazos Partners Limited Partnership and the FDIC, as manager of the FRF, is a limited partner along with Brazos Fort Associates and Brazos Worth Associates. The FDIC issued a note payable to New West Federal Savings and Loan Association (New West), which included capital loans to the Brazos partners, to purchase assets from New West. The FDIC contributed these assets to the partnership. In addition, the FDIC provided an advance to the Brazos Partners Limited Partnership for working capital.

Net Receivables from Thrift Resolutions

Dollars in Thousands	December 31 1993	December 31 1992
Assets from Open Thrift Assistance:		
Collateralized loans	$ 380,000	$ 470,000
Other loans	125,153	264,280
Capital instruments	65,000	272,496
Interest in limited partnerships	972,915	0
Preferred stock from assistance transactions	470,955	865,193
Accrued interest receivable	2,992	20,125
Allowance for losses (Note 10)	(423,296)	(971,550)
	1,593,719	**920,544**
Receivables from Closed Thrifts:		
Resolution transactions	9,677,150	10,449,964
Collateralized advances/loans	305,264	322,279
Other receivables	210,795	231,435
Allowance for losses (Note 10)	(9,548,863)	(9,919,271)
	644,346	**1,084,407**
	$2,238,065	**$2,004,951**

5. Investment in Corporate-Owned Assets, Net

The FRF's investment in corporate-owned assets is comprised of amounts that: 1) the FSLIC paid to purchase assets from troubled or failed thrifts and 2) the FRF pays to acquire receivership assets, terminate receiverships and purchase covered assets. The vast majority of these assets are real estate and mortgage loans.

The FRF recognizes income and expenses on these assets. Income consists primarily of the portion of collections on performing mortgages related to interest earned. Expenses are recognized for administering the management and liquidation of these assets.

Investment in Corporate-Owned Assets, Net

Dollars in Thousands	December 31 1993	1992
Investment in corporate-owned assets	$3,565,463	$3,515,803
Allowance for losses (Note 10)	(2,988,302)	(2,971,057)
	$ 577,161	$ 544,746

6. Due from the Savings Association Insurance Fund

The Heartland Federal Savings and Loan Association (Heartland), Ponca City, Oklahoma, was a SAIF-insured institution that became party to a 10-year Assistance Agreement with the FSLIC upon the failure of its predecessor, Frontier Federal Savings and Loan Association, in 1988. FSLIC obligations were assumed by the FRF upon the enactment of the FIRREA in 1989. Section 32 of the Assistance Agreement effectively gave the FRF sole equity interest in Heartland. Section 2.13 of the agreement entitled "Additional Operating Terms and Conditions" gave the FDIC, as manager of the FRF, authority to take such action as might be necessary to effect the acquisition of Heartland. The FDIC determined that the value of the FRF's equity interest in Heartland would be maximized and total assistance cost would be minimized by a termination of the Assistance Agreement and sale of Heartland, thereby returning it to the private sector. To effect the sale, a receiver was appointed for Heartland for the purpose of transferring assets and liabilities to the acquirers.

Technically, Heartland was not a "failing institution" because of its well-capitalized condition, which resulted from the government assistance provided. Heartland's Board of Directors consented to the Office of Thrift Supervision's appointment of the FDIC (SAIF) as receiver on October 8, 1993. The FDIC was appointed receiver because, at the time, RTC's authority to resolve FSLIC-insured thrifts had not yet been extended by the RTC Completion Act.

Because Heartland was not failing, all uninsured depositors and general trade creditors were paid in full, leaving only the FRF as sole creditor. Payment to the acquirers of Heartland to cover insured depositors' claims was funded by the FRF and represents a claim against the receivership's assets. The receiver will reimburse the FRF as claims are satisfied through the liquidation process. As of December 31, 1993, the receiver owes the FRF a net receivable of $169 million. This amount includes an allowance for loss of $6.5 million for this transaction.

7. Other Assets, Net

Other Assets, Net

Dollars in Thousands	December 31 1993	1992
Investment in FADA	$25,000	$25,000
Allowance for losses (Note 10)	(11,258)	(9,862)
	13,742	15,138
Accounts receivable	158	1,829
Allowance for losses	(0)	(93)
	158	1,736
Due from other government agencies	24,998	28,855
	$38,898	$45,729

8. Liabilities Incurred from Thrift Resolutions

The FSLIC issued promissory notes and entered into assistance agreements in order to prevent the default and subsequent liquidation of certain insured thrift institutions. These notes and agreements required the FSLIC to provide financial assistance over time. Under the FIRREA, the FRF assumed these obligations. The FRF presents its notes payable and its obligation for assistance agreement payments incurred but not yet paid as a component of the line item "Liabilities incurred from thrift resolutions." Estimated future assistance payments under its assistance agreements are presented as a component of the line item "Estimated liabilities for: Assistance agreements" (see Note 9).

Liabilities Incurred from Thrift Resolutions

Dollars in Thousands	December 31 1993	1992
Notes payable to Federal Home Loan Banks/U.S. Treasury	$380,000	$ 470,000
Capital instruments (Note 4)	725	24,350
Assistance agreement notes	683,455	913,308
Accrued assistance agreement costs	2,414,915	1,866,531
Accrued interest	7,983	14,158
Other liabilities to thrift institutions	109,830	177,413
	$3,596,908	**$3,465,760**

Maturities of Liabilities

Dollars in Thousands

1994	1995	1996	1997	1998
$2,698,318	$481,121	$96,477	$226,312	$94,680

9. Estimated Liabilities for:

Assistance Agreements

The "Estimated liabilities for: Assistance agreements" line item represents, on a discounted basis, an estimate of future assistance payments to acquirers of troubled thrift institutions. The nominal dollar amount of this line item as of December 31, 1993 and 1992, was $1.3 billion and $2.4 billion, respectively. The interest rate applied as of December 31, 1993 and 1992, was 3.5 percent, based on U.S. money rates for federal funds.

Future assistance stems from the FRF's obligation to: 1) fund losses inherent in assets covered under the assistance agreements (e.g., by subsidizing asset write-downs, capital losses and goodwill amortization); and 2) supplement the actual yield earned from covered assets as necessary for the acquirer to achieve a specified yield (the "guaranteed yield"). Estimated total assistance costs recognized for current assistance agreements with institutions involving covered assets include estimates for the loss expected on the assets based on their appraised values. The FRF is obligated to fund any losses sustained by the institutions on the sale of the assets. If asset losses are incurred in excess of those recognized, the possible cash requirements and the accounting loss could be as high as $2.5 billion, should all underlying assets prove to be of no value (see Note 16). The costs and related cash requirements associated with the maintenance of covered assets are calculated using an applicable cost of funds rate and would change proportionately with any change in market rates.

The RTC, on behalf of the FRF, had authority to modify, renegotiate or restructure the 1988 and 1989 assistance agreements with FSLIC-assisted institutions with terms more favorable to the FRF. This authority ended June 30, 1993. In accordance with a 1991 RTC Board Resolution, any FSLIC-assisted institution that has been placed in RTC conservatorship or receivership is subject to revised termination procedures.

The assistance agreements outstanding as of December 31, 1993 and 1992, were 71 and 100, respectively. The last agreement is scheduled to expire in December 1998.

The estimated liabilities for assistance agreements are affected by several factors, including adjustments to expected notes payable, the terms of the assistance agreements outstanding and, in particular, the salability of the related covered assets. The variable nature of the FRF assistance agreements will cause the cost requirements to fluctuate. This fluctuation will impact both the timing and amount of eventual cash flows. Although the "Estimated liabilities for: Assistance agreements" line item is presented on a discounted basis, the following schedule details the projected timing of the future cash flows as of December 31, 1993, on a nominal dollar basis:

Estimated Assistance Payments

Dollars in Thousands

1994	1995	1996	1997	1998/Thereafter
$882,689	$228,707	$126,429	$31,308	$61,787

Litigation Losses

The FDIC records as an estimated loss on the FRF's financial statements an estimated cost for unresolved legal cases to the extent those losses are considered to be both probable in occurrence and estimable in amount. In addition to these losses, the FDIC's Legal Division has determined that losses from unresolved legal cases totaling $732 million are reasonably possible. This includes $683 million in losses for the FRF in its corporate capacity and $49 million in losses for the FRF in its receivership capacity (see Note 2).

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

Transfers include reclassifications from the line item "Estimated liabilities for: Assistance agreements" to the line item "Liabilities incurred from thrift resolutions" for notes payable and related accrued assistance agreement costs. Terminations represent final adjustments to the estimated cost figures for those thrift resolutions that were completed and for which the operations of the receivership ended.

Analysis of Changes in Allowance for Losses and Estimated Liabilities

1993

Dollars in Millions

Allowance for Losses:	Beginning Balance 01/01/93	Provision for Losses	Net Cash Payments	Transfers/ Terminations	Ending Balance 12/31/93
Open Thrift Assistance	$ 972	$106	$ -0-	$ (655)	$ 423
Closed thrifts	9,919	(273)	-0-	(97)	9,549
Corporate-owned assets	2,971	17	-0-	-0-	2,988
Due from the Savings Association Insurance Fund	-0-	7	-0-	-0-	7
Investment in FADA	10	1	-0-	-0-	11
Total Allowances	**13,872**	**(142)**	**-0-**	**(752)**	**12,978**
Estimated Liabilities for:					
Assistance agreements	2,347	1,075	(1,496)	(636)	1,290
Litigation losses'	73	(73)	-0-	70	70
Total Estimated Liabilities	**2,420**	**1,002**	**(1,496)**	**(566)**	**1,360**
Total		**$860**			

Analysis of Changes in Allowance for Losses and Estimated Liabilities

1992

Dollars in Millions

Allowance for Losses:	Beginning Balance 01/01/92	Provision for Losses	Net Cash Payments	Transfers/ Terminations	Ending Balance 12/31/92
Open Thrift Assistance	$ 660	$ 340	$ (28)	$ -0-	$ 972
Closed thrifts	9,932	45	-0-	(58)	9,919
Corporate-owned assets	2,968	3	-0-	-0-	2,971
Investment in FADA	13	(3)	-0-	-0-	10
Total Allowances	**13,573**	**385**	**(28)**	**(58)**	**13,872**
Estimated Liabilities for:					
Assistance agreements	7,411	509	(5,444)	(129)	2,347
Litigation losses	168	(95)	-0-	-0-	73
Total Estimated Liabilities	**7,579**	**414**	**(5,444)**	**(129)**	**2,420**
Total		**$799**			

11. Resolution Equity

The Accumulated Deficit includes $7.5 billion in non-redeemable capital certificates and redeemable capital stock issued by the FSLIC. Capital instruments have been issued by the FSLIC and the FRF to the FICO as a means of obtaining capital. Effective December 12, 1991, the FICO's authority to issue obligations as a means of financing for the FRF was terminated (see Note 1). Furthermore, the implementation of the FIRREA, in effect, has removed the redemption characteristics of the capital stock issued by the FSLIC.

Resolution Equity

1993

Dollars in Thousands	**Beginning Balance 01/01/93**	**Net Loss**	**Treasury Payments**	**Ending Balance 12/31/93**
Contributed capital	$42,028,000	$ -0-	$1,963,000	$43,991,000
Accumulated deficit	(43,667,600)	(760,096)	-0-	(44,427,696)
	$ (1,639,600)	**$ (760,096)**	**$1,963,000**	**$ (436,696)**

1992

Dollars in Thousands	**Beginning Balance 01/01/92**	**Net Loss**	**Treasury Payments**	**Ending Balance 12/31/92**
Contributed capital	$ 28,235,000	$ -0-	$13,793,000	$42,028,000
Accumulated deficit	(43,443,368)	(224,232)	-0-	(43,667,600)
	$(15,208,368)	**$(224,232)**	**$13,793,000**	**$(1,639,600)**

12. Assessments

The FRF's authority to receive SAIF assessments expired December 31, 1992 (see Notes 1 and 2).

Secondary Reserve Offset
The FIRREA authorized insured thrifts to offset against any assessment premiums their pro rata share of amounts that were previously part of the FSLIC's "Secondary Reserve." The Secondary Reserve represented premium prepayments that insured thrifts were required by law to deposit with the FSLIC during the period 1961 through 1973 to quickly increase the FSLIC's insurance reserves to absorb losses if the regular assessments were insufficient. The allowable offset is limited to a maximum of 20 percent of an institution's remaining pro rata share for any calendar year beginning

before 1993. After calendar year 1992, there is no limitation on the remaining offset amount.

The FRF also is required to pay in cash (or reduce an outstanding indebtedness) the remaining portion of the thrift's full pro rata distribution when the institution loses its insured status or goes into receivership. The FRF establishes a payable to that institution or its receiver with a corresponding charge to expense. As of December 31, 1993 and 1992, the Secondary Reserve payable, included in the line item "Accounts payable, accrued and other liabilities," was $89.8 million and $110 million, respectively.

The remaining Secondary Reserve credit at December 31, 1993 and 1992, was $2 million and $200 million, respectively. This amount was reduced primarily by offsets against assessment premiums, because most thrifts fully applied their remaining secondary reserve credit against their 1993 assessment. Offsets in 1993 had no impact on the FRF as SAIF assessments were no longer available to the FRF.

13. Pension Benefits, Savings Plans and Accrued Annual Leave

Eligible FDIC employees (i.e., all permanent and temporary employees with an appointment 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 offset 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 also can 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 FDIC employees may also participate in an FDIC-sponsored tax-deferred savings plan with matching contributions. The FRF pays its share of the employer's portion of all related costs.

Although the FRF 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.

The liability to employees for accrued annual leave is approximately $2.3 million and $4.4 million at December 31, 1993 and 1992, respectively.

Pension Benefits and Savings Plans Expenses

Dollars in Thousands	December 31	
	1993	1992
Civil Service Retirement System	$ 577	$ 743
Federal Employee Retirement System (Basic Benefit)	2,383	2,827
FDIC Savings Plan	1,267	1,037
Federal Thrift Savings Plan	734	815
	$ 4,961	$5,422

14. Postretirement Benefits Other than Pensions

The FDIC provides certain health, dental and life insurance coverage for its eligible retirees, the retiree's beneficiaries and covered dependents. Eligible retirees are those who have elected the FDIC's health and/or life insurance program and are entitled to an immediate annuity. However, dental coverage is provided to all retirees regardless of the plan selected.

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 wraparound. Dental care is underwritten by Connecticut General Life

Insurance Company. The life insurance program is underwritten by Metropolitan Life Insurance Company.

The FDIC contributes toward health insurance premiums at the same rate for both active and retired employees. The FDIC uses a "minimum premium funding arrangement" in which premiums are held in a restricted account. Medical claims and fixed costs are paid to Blue Cross/Blue Shield from this account on a weekly basis. Under this arrangement, the FDIC's liability exposure is limited in any one contract year. The life insurance program provides for basic coverage at no cost to retirees and allows converting optional coverages to direct-pay plans with Metropolitan Life Insurance Company. The dental insurance program provides coverage at no cost to retirees.

Beginning March 1994, the FDIC health insurance coverage will be self-insured for hospital/medical, prescription drug, mental health and chemical dependency, and FDIC has purchased additional risk protection through stop-loss and fiduciary liability insurance from Aetna Life Insurance Company. All claims will be administered on an Administrative Services Only basis with the hospital/medical claims administered by Aetna Life Insurance Company, the mental health and chemical dependency claims administered by OHS Foundation Health Psychcare Inc., and the prescription drug claims administered by Caremark.

As part of adopting SFAS No. 106 (see Note 2), the FDIC elected to immediately recognize the accumulated postretirement benefit liability, measured as of January 1, 1992. The accumulated liability (transition obligation) represents that portion of future retiree benefit costs related to service already rendered by both active and retired employees up to the date of adoption. The FRF recorded an expense of $5.9 million for this liability, which has been reflected in the Statements of Income and Accumulated Deficit as the cumulative effect of a change in accounting principle for periods prior to 1992.

The FRF expensed $3 million and $2.3 million for such benefits for the years ended December 31, 1993 and 1992, respectively.

For measurement purposes, the FDIC assumed the following: 1) a discount rate of 6 percent; 2) an increase in health cost in 1993 of 14 percent, decreasing down to an ultimate rate in 1998 of 8 percent; and 3) an increase in dental costs in 1993 and thereafter of 8 percent. Both the assumed discount rate and health care cost rate have a significant effect on the amount of the obligation and periodic cost reported.

If the health care cost rate were increased one percent, the accumulated postretirement benefit obligation as of December 31, 1993 would have increased by 7.5 percent. The effect of this change on the aggregate of service and interest cost for 1993 would be an increase of 28.8 percent.

Net Periodic Postretirement Benefit Cost

Dollars in Thousands	December 31 1993	1992
Service cost (benefits attributed to employee service during the year)	$ 1,825	$ 1,401
Interest cost on accumulated postretirement benefit obligation	937	856
Amortization of prior service cost	(74)	0
Amortization of unrecognized transition obligation	262	0
Return on plan assets	3	0
Net Periodic Postretirement Benefit Cost Before Funding Transfer	2,953	2,257
Funds transferred to the Savings Association Insurance Fund	0	1,197
	2,953	3,454

As stated in Note 2, beginning in December, 1993 the FDIC established a plan administrator to provide the accounting and administration on behalf of the BIF, the SAIF, the FRF and the RTC. The FRF portion of this long-term liability has been transferred to the plan administrator. In 1992 the BIF provided the accounting and administration of this obligation. The FRF has funded its obligation and these funds are being managed by the administrator as "plan assets".

Accumulated Postretirement Benefit Obligation by Participant

Dollars in Thousands	December 31 1993
Retirees	$ 7,937
Full eligible active plan participants	469
Other active participants	2,497
Total Obligation	10,903
Less: Plan assets at fair value (1)	10,125
Postretirement benefit liability included in the Statements of Financial Position	$ 778

(1) Consists of one-day special Treasury certificates

15. Commitments

The FRF currently is sharing in the FDIC's leased space. The FRF's allocated share of lease commitments totals $23.5 million for future years. The agreements contain escalation clauses resulting in adjustments, usually on an annual basis. The FRF recognized leased space expense of $8.9 million and $8.3 million for the years ended December 31, 1993 and 1992, respectively.

Leased Space Fees

Dollars in Thousands

1994	1995	1996	1997	1998
$9,842	$6,411	$3,552	$2,861	$822

16. Concentration of Credit Risk

The FRF 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 FRF'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:

Concentration of Credit Risk

Dollars in Millions	December 31, 1993						
	South-east	South-west	North-east	Mid-west	Central	West	Total
Net receivables from thrift resolutions	$143	$ 296	$61	$12	$ 44	$ 1,682	$2,238
Investment in corporate-owned assets, net	2	413	2	0	11	149	577
Due from the SAIF	-0-	169	-0-	-0-	-0-	-0-	169
Assistance agreements covered assets, net of estimated capital loss (off-balance sheet)	9	2,216	-0-	-0-	209	41	2,475
Total	**$154**	**$3,094**	**$63**	**$12**	**$264**	**$1,872**	**$5,459**

17. Disclosures about the Fair Value of Financial Instruments

Cash and cash equivalents are short-term, highly liquid investments and are shown at actual or approximate fair value. The carrying amount of accounts payable, liabilities incurred from thrift resolutions and the estimated liabilities for assistance agreements approximates their fair value due to their short maturities or comparisons with current interest rates.

It was not practical to estimate fair values of net receivables from thrift resolutions. These assets are unique, not intended for sale to the private sector and have no established market. The FDIC believes that a sale to the private sector would require indeterminate, but substantial discounts for an interested party to profit from these assets because of credit and other risks. Additionally, a discount of this proportion would significantly increase the cost of bank resolutions to the FRF. Further, comparisons with other financial instruments do not provide a reliable measure of their fair value. Due to these and other factors, the FDIC cannot determine an appropriate market discount rate and, thus, is unable to estimate fair value on a discounted cash flow basis. As shown in Note 4, the carrying amount is the original amount advanced net of the estimated allowance for loss, which is the estimated cash recovery value.

The majority of the net investment in corporate-owned assets, (except real estate) is comprised of various types of financial instruments (investments, loans, accounts receivable, etc.), and to a lesser degree other assets, acquired from failed thrifts. As with net receivables from thrift resolutions, it was not practical to estimate fair values. Cash recoveries are primarily from the sale of the assets which are poor quality. They are dependent upon market conditions which vary over time, and can occur unpredictably over many years following resolution. Since the FDIC cannot reasonably predict the timing of these cash recoveries, it is unable to estimate fair value on a discounted cash flow basis. As shown in Note 5, the carrying amount is the original amount advanced net of the estimated allowance for loss, which is the estimated cash recovery value.

18. Disclosure about Recent Financial Accounting Standards Board Pronouncements

The Financial Accounting Standards Board (FASB) has issued Statement of Financial Accounting Standards No. 112 (Employer's Accounting for Postemployment Benefits) which the FDIC is required to adopt by 1994. This new statement establishes accounting standards for employers who provide benefits to former or inactive employees after employment but before retirement. This statement requires employers to recognize the obligation to provide postemployment benefits. However, the FRF's obligation for these benefits is not recognized because the amount cannot be reasonably estimated.

In May, 1993, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 114, "Accounting by Creditors for Impairment of a Loan." Based upon initial study and analysis, this statement is not expected to have a material impact on the FRF when it is adopted on January 1, 1995.

In May, 1993, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities." This statement is not expected to have a material impact on the FRF when it is adopted on January 1, 1994.

19. Supplementary Information Relating to the Statement of Cash Flows

Reconciliation of Net Loss to Net Cash Used by Operating Activities

Dollars in Thousands	December 31 1993	1992
Net Loss	$ (760,096)	$ (224,232)
Adjustments to Reconcile Net Loss to Net Cash Used by Operating Activities:		
Income Statement Items:		
Provision for losses	860,425	799,105
Change in Assets and Liabilities		
Decrease in accrued interest receivable on investments and other assets	79,592	15,801
Decrease in thrift resolution receivable	798,974	1,488,844
(Increase) decrease in corporate-owned assets	(49,660)	39,233
Decrease in accounts payable, accrued and other liabilities	(29,310)	(13,451)
Decrease in liabilities from thrift resolutions	(1,517,394)	(6,802,739)
Net Cash Used by Operating Activities	**$(617,469)**	**$ (4,697,439)**

Non-cash financing activities for the year ended December 31, 1993, include: 1) canceled notes payable (NWCs) of $6.5 million; and 2) collateralized loans guaranteed by the FRF decreased $90 million (see Note 4). Non-cash financing activities for the year ended December 31, 1992, include: 1) canceled notes payable (NWCs) of $13.4 million; and 2) collateralized loans guaranteed by the FRF decreased $90 million (see Note 4).

Scope and Methodology

In order to fulfill our responsibilities as auditor of record for the Federal Deposit Insurance Corporation, we:

- Examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements of each of the three funds.
- Assessed the accounting principles used and significant estimates made by FDIC management.
- Evaluated the overall presentation of the financial statements of each of the three funds.
- Evaluated internal controls designed to (1) safeguard assets against loss from unauthorized acquisition, use, or disposition, (2) assure the execution of transactions in accordance with management authority and with laws and regulations, and (3) properly record, process, and summarize transactions to permit the preparation of financial statements in accordance with generally accepted accounting principles. These included relevant internal controls over the following significant cycles, classes of transaction, and account balances.
    - Troubled institutions.
    - Closed assistance.
    - Assessments.
    - Open assistance.
    - Expenses.
    - Treasury.
    - Financial reporting.
- Tested compliance with significant provisions of the Federal Deposit Insurance Act, as amended; the Chief Financial Officers Act; and the Federal Home Loan Bank Act, as amended. The provisions selected for testing included, but were not limited to, those relating to
    - assessment rates,
    - investment of amounts held by the funds,
    - maximum obligation limitations,
    - disbursements for bank and thrift resolutions,
    - external financial reporting, and
    - accounting for administrative expenses.

We limited our work to accounting and other controls necessary to achieve the objective outlined in our opinion on internal controls. We conducted our audits between August 1993 and May 1994. Our audits were conducted in accordance with generally accepted government auditing standards.

Comments From the Federal Deposit Insurance Corporation

FDIC
Federal Deposit Insurance Corporation
3501 Fairfax Drive, Arlington, VA 22226 Chief Financial Officer

June 9, 1994

Mr. Gene L. Dodaro
Assistant Comptroller General
U.S. General Accounting Office
441 G Street NW, Room 6112
Washington, D.C. 20548

Re: Federal Deposit Insurance Corporation's 1993 and 1992 Financial Statements GAO/AIMD-94-135

Dear Mr. Dodaro:

The FDIC is pleased to respond to the above-referenced draft audit report regarding the FDIC's financial statements. A number of recommendations from your staff for improving procedures and controls were also included within the report. Our response is directed to the weaknesses and reportable conditions described in the report.

We appreciate the effort you and your staff have devoted to the audit of the FDIC's 1993 financials, and recognize the challenge of auditing in a multi-fund environment. The suggestions and frank discussions with your staff have been beneficial to the FDIC in improving its control procedures.

We also appreciate having been given the opportunity to review the above captioned report in draft form, prior to its issuance. We believe this is another positive step towards the FDIC and the GAO working more closely together to achieve a common goal.

The entire staff of the FDIC is dedicated to conducting the Corporation's business effectively and efficiently, and we welcome constructive suggestions.

The following responses are organized around findings in your report:

1993 MATERIAL WEAKNESS:

During their 1993 audits, GAO identified a material weakness in FDIC's internal accounting controls over its process for estimating recoveries which will be realized on the management and disposition of failed BIF and FRF institution assets. GAO

states that the FDIC's internal accounting controls are not adequate to ensure that consistent and sound methodologies are used to estimate recoveries on failed institution assets. GAO further states that FDIC's internal controls are not effective in ensuring that proper documentation is maintained to support recovery estimates. GAO recommends that the FDIC Credit Manual be revised regarding recovery estimation methods, and that formulas used for estimating recoveries on assets with book values less than $250,000 be analyzed and documented.

FDIC RESPONSE:

The FDIC agrees that improvements should be made in the process for estimating Gross Cash Recovery (GCR) estimates for assets in liquidation, whether managed directly by FDIC personnel or by servicing contractors under the oversight of the FDIC. Deficiencies in the process for estimating GCRs were identified by FDIC management and reported as a material weakness, along with a corrective action plan, in its 1993 CFOA Statement of Internal Accounting and Administrative Controls.

FDIC is currently involved with at least three major initiatives to improve the GCR process and its implementation in order to provide for the use of consistent and sound methodologies that are appropriately documented and supported.

With respect to assets under $250,000 (assets with formula-computed GCRs), FDIC is currently developing recovery percentages based upon historical results. The percentages will be by LAMIS asset type. It is anticipated that this project will be completed in late 1994.

FDIC is in the process of reviewing the entire Credit Manual for revision as appropriate. As part of this project, the section pertaining to GCRs is undergoing revision. The revisions are intended to clarify issues such as those raised by the GAO in its 1993 financial audit of FDIC. It should be noted, however, that the GCR estimates will continue to be considered a subjective process. Accordingly, variations from the guidelines of the Credit Manual can occur so long as they do not directly contradict the Credit Manual and that the rationale is properly documented. It is anticipated that the Credit Manual revisions will be released in late 1994.

In 1994 FDIC initiated a project to review the overall GCR process and methodologies. GAO's expressed concerns and input will be part of the review. The resulting report will either validate the existing approach with suggestions for improvements or recommend a different approach to estimating the loan loss reserve.

NON-MATERIAL 1993 ESTIMATED LIABILITY ISSUE:

Within their report, GAO discusses a $410 million dollar reduction in the Bank Insurance Fund's estimated liability for troubled institutions, which FDIC reported on the fund's first quarter 1994 financial statements. GAO reports that this adjustment resulted from conditions as of December 31, 1993, and therefore the $410 million dollar reduction would have been more appropriately reflected in BIF's financial statements as of December 31, 1993.

FDIC RESPONSE:

The FDIC does not agree with the General Accounting Office (GAO) that the $410 million reduction in the Bank Insurance Fund's (BIF) estimated liability for troubled institutions which was made in the first quarter of 1994 should be reflected as of 12/31/93. While it is correct that one factor considered in this adjustment is financial information from financial institutions as of 12/31/93, it is only one factor among several considered by FDIC in its quarterly methodology for establishing this liability estimate. Other factors which established this downward adjustment were fully attributable to information obtained in 1994. The FDIC believes that the amount reflected in its financial statements was appropriate to comply with generally accepted accounting principles. As with all estimates this amount is subject to revision as additional information becomes available. Since the FDIC's established methodology based upon 1993 and first quarter 1994 information required a downward adjustment of $410 million, the FDIC appropriately reflected this amount in the BIF's first quarter 1994 financial statements.

1993 REPORTABLE CONDITIONS:

GAO reported that Time and Attendance procedures and guidance were not always followed, resulting in deficiencies similar to those identified during the 1992 audit. GAO recommends that the Acting Chairman direct the heads of FDIC divisions and offices to enforce the revised policies and procedures documented in FDIC's Time and Attendance Reporting directive and related guidance, to

FDIC'S Response to GAO's Draft 1993 Audit Report Page 3 *ensure that employee time charges are valid, payroll expenses are charged to the correct fund, and timekeeping and data input functions are separated.*

FDIC RESPONSE:

The FDIC's Office of Personnel Management is currently developing and implementing a program to conduct on-site reviews/audits of the biweekly time and attendance reporting process. Once implemented, staff will conduct periodic visits to field sites to monitor compliance with time and attendance reporting requirements, including separation of functional duties and reconciliation of time and attendance reports to worksheets.

GAO had previously stated (as a reportable condition in their 1992 audits) that internal controls over contracted asset servicers were not being consistently implemented or were too limited to effectively assist FDIC in overseeing its contracted asset servicers. GAO now states that although FDIC has taken steps to address these weaknesses and has made significant progress, some of these weaknesses continued to exist during 1993, and therefore this problem is identified again as a reportable condition in their 1993 report. GAO has recommended that FDIC verify and document the accuracy and completeness of the balances and activity reported to FDIC by contracted asset servicers, back to the servicers' detail records.

FDIC RESPONSE:

In the third quarter of 1993, FDIC's Division of Finance (DOF) hired additional personnel to address the reconciliation of serviced asset pool (SAP) balances and the clearing of related reconciling items. DOF developed a plan to bring the reconciliations current and to post adjustments to FDIC's Financial Information System (FIS). We estimate a completion date of July 31, 1994, for identifying and clearing reconciling items pertaining to SAPs and for ensuring all SAPs are in balance. All reconciliations currently prepared by DOF are done on a timely and consistent basis.

The Division of Depositor and Asset Services (DAS) has on-site accountants who review the contractor's accounting and financial records for accuracy and completeness. DOF coordinates with DAS to resolve issues affecting the accuracy of the financial information. Both divisions jointly participate in annual visitations of servicers. Additional enhancements to systems and procedures will be implemented to address the concerns expressed by GAO.

Another GAO reportable condition states that weak internal controls persist at one of FDIC's contracted servicing entities. GAO recommends that FDIC perform timely reconciliations each month of servicer asset balances, require the servicer to maintain a general ledger and subsidiary records consistent with receivership accounting, and require the servicer to clear its unapplied collections account within 30 days after month-end.

FDIC RESPONSE:

A comprehensive program has been developed to cure the acknowledged internal control weaknesses at the FDIC contracted servicer referred to in the report. Specifically, DAS and DOF are working with the servicer to devise a system of reconciliations to verify the accuracy of the asset pool activity and balances, converting the servicer's accounting system and records to the receivership basis of accounting, and strengthening the cash receipts procedures to ensure greater control and timely processing of collections. It is anticipated that the weaknesses will be resolved in mid-1994.

FDIC would also like to clarify a comment made by GAO as background to the reportable condition concerning the servicer. GAO stated that FDIC does not maintain subsidiary records for assets in serviced asset pools. It is FDIC policy in contracting work to outside servicers that FDIC does not maintain separate subsidiary records for assets in serviced asset pools (SAPs). The intent is for servicers to maintain the detailed subsidiary records; to do otherwise would be inefficient.

Thank you again for giving us the opportunity to comment on your draft report. Other suggestions relating to the wording of the draft report text have been given to GAO staff.

Sincerely yours,

Steven A. Seelig
Chief Financial Officer

cc: Chairman Hove

FDIC'S Response to GAO's Draft 1993 Audit Report — Page 5

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