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Report to the Chairman, Task Force on the Resolution Trust Corporation, Committee on Banking, Finance and Urban Affairs, House of Representatives

September 1991

RESOLUTION TRUST CORPORATION

Evolving Oversight on Interim Servicing Arrangements

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The Honorable Bruce F. Vento
Chairman, Task Force on the Resolution Trust Corporation
Committee on Banking, Finance
and Urban Affairs
House of Representatives

Dear Mr. Chairman:

This report responds to your request that we assess the Resolution Trust Corporation's (RTC) efforts to manage assets during the interim period between the sale of the thrift institution and the award of a contract for asset management services for those assets remaining with RTC. You asked us to review a sample of cases to, among other things, determine (1) whether the agreements covering the interim period contained appropriate provisions to protect the interests of the government, (2) whether RTC had sufficient procedures in place to verify bills, and (3) the extent to which RTC monitored contractor performance under the interim agreements.

Results in Brief

RTC's approach to interim asset servicing has evolved. For most of its early thrift resolutions, RTC entered into interim servicing agreements (ISA) with the thrift acquirer. The thrift sales agreement stipulated that the acquirer enter into an ISA to service those assets not bought at resolution. RTC used the ISAs because it was not organized to handle these remaining assets when it began operations. The ISA was a standard document that provided for the continued servicing of some, if not all, of the assets not bought by the thrift acquirer. RTC reimbursed the acquirer for all expenses relating to asset servicing.

During February 1990, RTC revised the interim servicing approach by discontinuing use of a separate ISA at resolution. Instead, RTC incorporated sections of the ISA into the thrift sales agreement. The revised approach requires that the acquirer provide only accounting and payroll functions to service the receivership assets. At the time of our review, RTC was using two other variations in interim asset servicing. In the Southwest Region, RTC was contracting with private firms to manage the receivership and service the RTC assets remaining after resolution. These contracts were called Resolution Assistance Agreements (RAA), and the contractors were usually accounting firms. In a second effort, RTC was attempting to put assets under management contracts while the assets were still in conservatorship. This effort should reduce the number of assets needing to be serviced under interim asset servicing arrangements. Consequently, RTC should get assets under management and disposition contracts sooner, which should reduce holding costs through faster asset marketing and sale.

While RTC's methods to service assets have evolved, there have been certain problems common to all the methods RTC has used to date. These problems have been (1) insufficient guidance to those employees responsible for contract administration, (2) insufficient contractor oversight, and (3) insufficient training for staff implementing the interim asset servicing arrangements.

The March 23, 1991, RTC Funding Act outlined specific initiatives designed to improve RTC's contracting program. These initiatives included development of a comprehensive contracting manual and implementation of a contracting training module. RTC had begun to develop the contracting manual before enactment of the legislation.

Objectives, Scope, and Methodology

Your July 3, 1990, letter asked us to assess the main requirements of asset management agreements RTC had entered into with acquirers of failed thrifts as part of the resolution process. Our objectives included determining (1) whether bidders for the failed thrifts knew of the interim servicing requirement; (2) whether RTC gave acquirers the right to purchase assets they were servicing; (3) whether agreements contained appropriate provisions to protect the interests of the government; (4) whether RTC built incentives into the agreements to encourage prompt and profitable sale of the assets and to reduce operating costs under the agreements; (5) whether RTC used a fee structure for each agreement; (6) the amount that RTC paid, either as compensation or reimbursement, for the ISAS; (7) whether RTC verified bills; and (8) whether RTC monitored contractor activities.

As agreed with the task force, our review included a cross section of agreements with at least one from each of the four RTC regional offices. We selected 10 agreements—6 ISAS and 4 revised—with a total value of \$6.9 billion in RTC-held assets.[1] As requested, we reviewed University Savings and San Antonio Savings agreements. We selected Skokie Federal and Pacific Savings agreements because these thrifts were the

[1] We were only able to quantify the amount reimbursed under 1 of the 10 agreements due to a commingling of accounts for RTC and the acquirer. For Skokie Federal, RTC reimbursed the acquirer about \$334,000 per month for servicing RTC-held assets.

largest institutions with an ISA in the North Central and Western Regions, respectively. We reviewed the Freedom Savings & Loan agreement because of our previous work at that institution.[2] We selected five additional agreements to ensure that our review covered a mix of the assets being serviced. Appendix I lists all of the agreements.

You also asked us to look into contracting and asset sales activities in the conservatorship program. We addressed these topics in our February 20, 1991, testimony[3] before the House Committee on Banking, Finance and Urban Affairs and our June 17, 1991, testimony[4] before the RTC Task Force, House Subcommittee on Financial Institutions Supervision, Regulation and Insurance, House Committee on Banking, Finance and Urban Affairs. (See app. II.)

We interviewed RTC headquarters, regional, and field office officials to determine what steps RTC took to ensure proper contractor oversight. We also interviewed staff at the receiverships to determine what their roles and responsibilities were in implementing the asset servicing agreements.

We reviewed the ISAs, thrift sales agreements, monthly accounting statements, and budgets at the receiverships. Appendix III lists the locations we visited during our work.

Our review was done between July 1990 and January 1991 in accordance with generally accepted government auditing standards.

RTC Used ISAs to Help Handle Its Work Load

As of September 30, 1989, almost 2 months following its inception, RTC was responsible for managing and disposing of over $112 billion in assets at the same time it was staffing and structuring the organization. Because RTC was not yet organized to handle assets not bought by the thrift acquirers, it entered into ISAs with thrift acquirers to service those assets left with RTC.

The ISA was generally used in conjunction with the early thrift sales transactions, and it provided for continued servicing of some, if not all,

[2] Resolution Trust Corporation: Excessive Loan Servicing Costs Due to Inadequate Contractor Oversight (GAO/GGD-91-19, Jan. 17, 1991).

[3] Resolution Trust Corporation: Performance Assessment to Date (GAO/T-GGD-91-7).

[4] Resolution Trust Corporation: Update on Funding and Performance (GAO/T-GGD-91-47).

of the assets not acquired by the purchaser—such as loans. As part of the package given to potential thrift acquirers, RTC included a sample ISA for review. RTC intended these agreements to be in effect for a short time—usually 6 to 10 months. The thrift sales agreement stipulated that the acquirer could buy certain assets not purchased at the time of resolution for up to 121 days after resolution. It also stipulated that these assets were to be purchased at book value unless otherwise indicated in the thrift sales agreement. As of the end of October 1990, RTC had $25 billion in assets being serviced under interim procedures.

The acquiring institution was responsible for, among other things, servicing RTC loans by collecting and recording payments, ensuring that property management contracts for the maintenance of RTC-held real estate were carried out, and providing accounting and payroll services. RTC reimbursed the acquirer for expenses incurred as a result of RTC-related activities.

RTC assets serviced under these agreements included installment, commercial, and real estate loans; securities; real estate; and other assets. Under an ISA, the acquiring institution usually retained from the failed thrift those employees needed to service both the assets it bought and those retained by RTC. These employees included accounting officers, real estate specialists, credit specialists, asset managers, and computer operators. RTC was to reimburse the acquiring institution for employee expenses related to RTC's assets.

Although the ISAs Contained No Specific Fee Provision, Acquirers Were Reimbursed for Services Provided

The ISA did not contain a fee structure outlining specific payments to the acquirer. Instead, the ISA required RTC to reimburse the acquirer for expenses incurred as a result of asset servicing. Categories of reimbursable expenses included (1) legal expenses that RTC preapproved; (2) direct out-of-pocket expenses for servicing the loans and real estate held by RTC; (3) employee expenses, including salaries, benefits, overhead, and other costs for employees administering the ISA; and (4) expenses for managing real estate held by RTC, including fees paid to providers of real estate management services and expenses incurred to maintain the physical condition and security of the properties. In practice, each month the acquiring institution was to deduct its expenses from the funds collected on RTC assets. Then, either the aquirer was to remit the balance to RTC if collections were greater than expenses or, if collections were less than expenses, RTC was to pay the difference.

RTC reimbursed the acquirer only for expenses incurred and did not give the acquiring institution a management fee for the services provided. Instead, the ISA allowed the acquirer to have use of RTC funds before remitting the funds to RTC. Asset servicing included collecting loan payments and rents for RTC loans or properties. The acquirer did not remit the funds collected under the ISA to RTC until the month following their receipt. This practice gave the acquirer use of RTC funds for an average of 40 days. During this time, the acquirer could generate and keep interest from RTC collections. At one of the receiverships, the acquirer earned a conservative estimate of over $23,000 per month on the interest from RTC-collected funds.

Real Estate Property Management Contracts Were Poorly Monitored

Real estate property management contracts were to be monitored by asset managers at the receiverships. These asset managers were former employees of the failed thrift and were retained by the acquirer after resolution. Among other things, asset managers were responsible for ensuring that the property management contracts were properly administered. The property management contractors were responsible for daily operations such as collecting rents, filling vacancies, and ensuring repairs were made. Typically, the property management contracts in place during the conservatorship were continued under the ISA.

During our review, asset managers told us they rarely performed site inspections of RTC-held real estate to ensure that contracts were properly administered. In one instance, the acquirer's internal audit division discovered that asset managers had performed only one documented site inspection of the receivership's properties.

RTC Revised the Interim Servicing Approach

In February 1990, RTC revised its approach to interim asset servicing by discontinuing use of a separate ISA. Instead, RTC revised the thrift sales agreement to include a section requiring the acquirer to provide limited asset servicing functions for assets not purchased at resolution. The scope of the services provided under the revised approach was reduced—essentially requiring that the acquirer provide only accounting and payroll services. Table 1 shows a summary of differences between the ISA and the revised interim servicing approach.

Table 1: Differences in the Asset Servicing Approaches

Original ISA	Revised approach
The acquirer provides all asset servicing functions.	The acquirer provides accounting and payroll services. RTC is responsible for all other asset servicing.
Thrift personnel work on servicing both the acquirers' and RTC's assets and report to both groups.	Thrift personnel needed to service RTC assets are dedicated to RTC-related matters and report directly to RTC management.
The acquirer has exclusive use of RTC funds and keeps the interest generated on RTC collections.	The acquirer must remit to RTC at a predetermined rate interest from RTC collections.[a] The acquirer can keep the interest generated over and above the amount remitted to RTC.

[a]The interest rate is equal to the rate quoted in the Wall Street Journal for federal funds on the day of thrift resolution and the 2 days immediately preceding resolution.

After RTC revised the interim servicing approach, the ability of the acquirer to keep interest generated from RTC collections was reduced. The revised approach required that the acquirer remit some interest to RTC along with the collections each month. The acquirer was allowed to keep any interest generated over and above the amount remitted to RTC. This setup allowed both RTC and the acquirer to obtain revenue from collections.

Variations in Interim Servicing

The use of an RAA is a variation in interim servicing that was developed in June 1990 by the Metroplex Consolidated Field Office to handle staffing constraints resulting from the large number of resolved thrifts in the Southwest Region. RTC used RAAs to provide contracted services to run a receivership in lieu of having an RTC manager on site. The contractor managed the receivership and dealt with various duties, including administrative matters, accounting, data processing, and claims. At a minimum, the contractor provided a site manager, a financial officer, and an asset manager. The contractors were usually accounting firms.

RAA oversight procedures and responsibilities differed in each of the four field offices we visited. Each field office was responsible for monitoring and overseeing the RAAs. Oversight was based on formal site visits, regular monthly and quarterly receivership reports, and annual receivership operating plans. Given the differing approaches applied by the field offices and the lack of consistent information for measuring results, RTC management did not have adequate assurance that oversight activities were effective.

Another variation affecting the interim servicing period was to put assets that experience showed would not be bought by an acquirer under a Standard Asset Management and Disposition Agreement (SAMDA) while the thrift was still in conservatorship. According to RTC, this approach would reduce the number of assets needing interim servicing after resolution. For example, as of January 11, 1991, only one-half of one percent of RTC's real estate had been bought by the acquirer at resolution and the remaining 99.5 percent would need to be serviced by RTC following resolution. Under this plan, instead of waiting until after resolution, RTC would put these assets in the hands of SAMDA contractors during the conservatorship period. As of June 1991, RTC had begun to include a small percentage of conservatorship assets under the larger SAMDA contracts.

Recent RTC Actions Could Alleviate Some Weaknesses in the Asset Servicing Arrangements

During this review, we noted several weaknesses in RTC's interim asset servicing implementation and, during several testimonies[5] over the last year, we expressed similar concerns about RTC's contracting practices. These concerns included (1) insufficient guidance given to those employees responsible for contract administration and (2) insufficient contractor oversight. In addition to these problems, RTC staff administering the asset servicing agreements were not offered training on contract administration.

More specifically, we found a lack of written guidance for employees administering the asset servicing agreements. For example, neither the original ISA nor the revised interim servicing approach provided any procedures for invoice verification or the disbursement of RTC funds. Invoice verification is an important internal control designed to help ensure that bills for goods bought and services rendered are authentic, necessary, and reimbursable.

A second concern with the interim servicing approach was the lack of adequate contractor oversight. For example, monitoring of property management contracts did not include formal site inspections. Site inspections are important to help ensure that goods bought and services paid for are actually received. There was no guidance requiring site inspections, and these inspections were rarely done. Receivership management cited location of the property and a lack of staff as reasons for

[5]Resolution Trust Corporation: Status of Selected Management Issues (GAO/T-GGD-91-04, Dec. 6, 1990); Resolution Trust Corporation: Update on Funding and Performance (GAO/T-GGD-91-43, June 11, 1991); and Resolution Trust Corporation: Asset Management Contracting Controls Need to Be Strengthened (GAO/T-GGD-90-53, Sept. 24, 1990).

not conducting site inspections. In one case, almost all the receivership's real estate was located out of state, and the distance and time involved in visiting the properties would have been substantial. However, even when the properties were close to the receivership, site inspections were rarely done.

Another example of insufficient oversight involves RAAS. Under the RAAS, RTC lacked information systems and personnel needed to verify data from the receiverships. As a result, RTC had been unable to get timely receivership information or to determine the day-to-day status of RTC assets.

A final concern we have with the interim asset servicing arrangement is the lack of training on contract implementation and oversight for individuals responsible for administering the contracts.

RTC has recently taken actions that could alleviate the concerns listed above. The RTC Funding Act of 1991 (P.L. 102-18) called for specific RTC management reforms that included contracting initiatives to enhance the effectiveness of the contracting process. Some of the contracting initiatives require that RTC develop and distribute (1) a contracting manual with comprehensive policies and procedures, (2) a revised directive that clearly describes the roles and responsibilities of individuals involved in contracting, and (3) a series of standardized contracting training modules for RTC contracting personnel and private contractors. RTC is required to submit a report on the progress of its initiatives by September 30, 1991.

Before enactment of the legislation, RTC had taken steps toward fulfilling the initiatives by drafting a contracting manual. The manual contains policies and procedures that address concerns raised in this report. Specifically, the manual contains a chapter on contract administration that includes guidance on performing site inspections and verifying contractor invoices. RTC anticipated distributing the manual to all offices by the end of August 1991. Also, as part of the manual, RTC issued the revised directive describing the roles of all staff involved in the contracting process. Finally, RTC is developing training modules for personnel involved in contracting; RTC expects to complete the manuals in September 1991.

Conclusions

As of October 1990, RTC had $25 billion in assets being managed under interim servicing arrangements. We noted weaknesses in RTC's monitoring of contractors, its guidance for contract administration, and its training for personnel involved in contracting. RTC is currently taking actions that, if properly implemented, should improve its contracting program.

Agency Comments

In commenting on a draft of this report, RTC officials generally agreed with our findings. Their comments are included in appendix IV.

Major contributors to this report are listed in appendix V. Please contact me on (202) 736-0479 if you or your staff have any questions concerning the report.

Sincerely yours,

Gaston L. Gianni

Gaston L. Gianni, Jr.
Associate Director,
Federal Management Issues

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Abbreviations

RTC	Resolution Trust Corporation
ISA	Interim Servicing Agreement
RAA	Resolution Assistance Agreement
SAMDA	Standard Asset Management and Disposition Agreement

List of Agreements

Failed thrift	Acquiring institution	Asset passed/ retained[a] (in millions)	RTC region	RTC consolidated field office
		ISAs		
University Savings, TX	North Carolina National Bank -TX	$723/ 2,702	Southwest	Gulf Coast, TX
San Antonio Savings, TX	1st Gibraltar Bank	1,136/ 1,179	Southwest	Southern, TX
Skokie Federal, IL	Affiliated Bank/ N. Shore National	447/ 348	North Central	Lake Central, IL
Pacific Savings, CA	Pacific First Bank	473/ 609	Western	Coastal, CA
Freedom S&L, FL	North Carolina National Bank -FL	266/ 751	Eastern	Southeast, FL
Colorado Savings, CO	Colorado Savings Bank	12/ 38	Western	InterMountain, CO
		Revised Interim Servicing Arrangements		
Sun Savings, KS	Brotherhood Bank & Trust	$126/ 32	North Central	Mid-Central, MO
American Savings, UT	Pacific 1st Federal Bank	1,135/ 530	Western	Central Western, AZ
Great Southern, GA	1st Atlanta Bank	205/ 382	Eastern	Mid-Atlantic, GA
Murray Hill Savings, TX	United Savings	809/ 316	Southwest	Metroplex, TX

[a]This information is based on RTC cost-test data; total assets passed ($5,332 million) represents the amount of assets and liabilities the acquirer purchased at resolution and the assets retained ($6,887 million) represents the amount of assets and liabilities that remained with RTC following the resolution.

Source: RTC.

Contracting and Assets Sales Activities in Conservatorships

RTC had assumed control of 578 thrifts as of March 31, 1991; 374 of these thrifts were resolved, and 204 of these thrifts were in the conservatorship program.[1] Sales from these thrifts during conservatorship amounted to almost $53 billion, and collections during conservatorship amounted to over $42 billion. About 94 percent of these sales and collections were from financial assets.

RTC recently began to expedite the contracting process by starting to put assets under Standard Asset Management and Disposition Agreements (SAMDA) while the thrift is in conservatorship.[2] As of June 1991, RTC had begun to put a small percentage of conservatorship assets under the larger SAMDA contracts.

[1] Resolution Trust Corporation: Update on Funding and Performance (GAO/T-GGD-91-47, June 17, 1991).

[2] Resolution Trust Corporation: Performance Assessment to Date (GAO/T-GGD-91-7, Feb. 20, 1991).

Offices Visited

RTC Headquarters	Asset & Real Estate Management Division, Washington, D.C.
RTC Regional Offices	North Central, Kansas City, MO Eastern, Atlanta, GA Southwestern, Dallas, TX Western, Denver, CO
RTC Consolidated Field Offices	Coastal, Costa Mesa, CA Gulf Coast, Houston, TX Lake Central, Elk Grove Village, IL Metroplex, Dallas, TX Mid-Atlantic, Atlanta, GA Mid-Central, Kansas City, MO North Central, Burnsville, MN Northern, Tulsa, OK Southeast, Tampa, Fl Southern, San Antonio, TX
RTC Receiverships	American Savings & Loan Association, Salt Lake City, UT Colorado Savings & Loan Association, Englewood, CO Great Southern Federal Savings & Loan Association, Savannah, GA Murray Savings & Loan Association, Dallas, TX Pacific Savings Bank, Costa Mesa, CA San Antonio Saving & Loan Association, San Antonio, TX Skokie Federal Savings & Loan Association, Skokie, IL Sun Savings & Loan Association, Kansas City, KS University Savings & Loan Association, Houston, TX

Comments From the Resolution Trust Corporation

RTC
Resolution Trust Corporation

August 6, 1991

Mr. J. William Gadsby
Director, Federal Management Issues
General Accounting Office
441 G Street, N.W
Washington, D.C. 20548

Dear Mr. ~~Gadsby~~ Bill:

Thank you for the opportunity to review and provide you with comments on the draft report entitled Resolution Trust Corporation: Evolving Oversight on Interim Servicing Arrangements. As the draft report did not contain any recommendations, our review only focused on factual accuracy. I am pleased to inform you that we do not disagree with the general accuracy of the report as drafted. However, I would like to provide you with the following comments to further clarify our contracting initiatives as they pertain to the RTC Funding Act of 1991, which you reference.

Work on the development of a comprehensive contracting manual containing policies and procedures had been initiated by the RTC several months prior to, and not as a result of, the enactment of the Funding legislation. The manual is currently being finalized for delivery to the printer. Distribution to all RTC Offices is projected for the end of August.

A revised Directive, "RTC Contracting Roles and Responsibilities," was issued on May 6, 1991. This Directive superseded a previously issued memorandum dated May 8, 1990, which originally defined the contracting process and the roles, authorities and responsibilities associated with the contracting process.

We have recently completed an initial draft of a training module in the fundamentals of the RTC contracting process. The comprehensive course will be held over a five-day period, and we currently anticipate finalization and distribution by the end of September. Work is also ongoing in developing an Executive Overview, Program Personnel, Managing Agent, and SAMDA Contractor modules. The Executive Overview module is scheduled to be completed in September, with the other modules shortly thereafter.

Mr. Gadsby
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As we have indicated on numerous occasions, the RTC since inception has been and will continue to be committed to developing adequate controls over its contracting process. We believe that these aforementioned initiatives, as well as numerous completed RTC contacting initiatives previously described in testimony and in response to other reports, will further improve the contracting process.

We would be delighted to discuss these and other initiatives with you at your earliest convenience.

Sincerely,

David C. Cooke
Executive Director

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