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BANK AND THRIFT FAILURES

RTC Needs to Improve Planning for Professional Liability Staff Changes

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BANK AND THRIFT FAILURES: RTC NEEDS TO IMPROVE PLANNING FOR PROFESSIONAL LIABILITY STAFF CHANGES

SUMMARY OF STATEMENT BY RICHARD L. FOGEL
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The Chairman of the Senate Committee on Banking, Housing, and Urban Affairs requested GAO to discuss RTC attorney staffing of the professional liability program. On June 2, 1992, GAO testified that both RTC and FDIC needed to improve their professional liability programs. GAO noted that staff shortages, inadequate asset tracing procedures, and weak oversight had limited these agencies' ability to pursue potential civil professional liability claims arising from insured bank and thrift failures.

Staffing shortages and changes and organizational instability have hampered RTC's professional liability program. Approximately 70 RTC attorneys are currently working in the Professional Liability Section, about half of what RTC officials estimated in the past that they need. Moreover, reorganizations and reassignments of professional liability staff have plagued the program. Over the last five months, about forty percent of all RTC professional liability attorneys have left the program or been subject to reassignment orders. This includes five of seven senior professional liability headquarters and field officials. During the same period, there have been two reorganizations of professional liability staff, RTC reassigned key professional liability attorneys, and then, after congressional concerns surfaced, many of these reassignments were rescinded. As a result, RTC's professional liability program has been disrupted and its staff has become demoralized. For example, several current and former senior professional liability managers and private law firm attorneys that handle professional liability cases told GAO that the RTC professional liability program has been in a period of turmoil.

These changes are coming at a time when the bulk of RTC's professional work is yet to come. RTC professional liability attorneys must still decide whether to file claims in thrifts before the statute of limitations expires and they need to monitor and support the rapidly increasing amount of litigation.

Reorganizations and reassignments at RTC are inevitable as the agency is dissolved and work transferred to FDIC. But RTC needs to better plan for such changes to avoid disruption of the professional liability program and to allow for the orderly transfer of employees to FDIC.

Mr. Chairman and Members of the Committee:

We are pleased to be here to discuss the Resolution Trust Corporation's (RTC) attorney staffing of its professional liability program. On June 2, 1992, we testified before this committee on RTC's and the Federal Deposit Insurance Corporation's (FDIC) efforts to pursue civil professional liability claims arising from bank and thrift failures.[1] We said that FDIC's and RTC's performance in investigating and litigating civil professional liability claims could be better. In particular we noted that staffing shortages, lack of standardized and systematic asset tracing procedures, and weak oversight have limited the agencies' ability to pursue potential claims. Today, we will focus on RTC's professional liability staffing, particularly in light of recent reorganization and assignment changes affecting attorneys responsible for the program.

In summary, staffing shortages and changes have disrupted RTC's professional liability program. Since March 1, 1992, five of seven senior professional liability program managers have left RTC or been reassigned and about forty percent of all professional liability attorneys on board at the end of February 1992 have left the RTC Professional Liability Section (PLS) or been subject to reassignment notices. Both current and former professional liability officials said the program has been in a period of turmoil. These changes are coming at a time when the PLS program workload is expanding and statutes of limitations deadlines loom. Although changes to professional liability staff are inevitable as RTC is dissolved and work is transferred to FDIC, we think that RTC needs to do a much better job of planning for these changes to assure a minimum disruption of the professional liability program and the orderly transfer of staff to FDIC.

BACKGROUND

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) created RTC and gave it the responsibility for resolving thrifts failing between January 1, 1989, through September 30, 1993.[2] RTC, by law, is to cease operating by December 31, 1996. FDIC will generally become responsible for (1) resolving those thrifts that fail after September 30, 1993, and (2) completing the resolution of thrifts remaining in RTC's workload when it is abolished.

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[1] Bank and Thrift Failures: FDIC and RTC Could Do More to Pursue Professional Liability Claims (GAO/T-GGD-92-42 Jun. 2, 1992).

[2] The Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991 extended RTC's responsibility to thrifts failing before October 1, 1993.

When RTC takes over a federally insured thrift through receivership or conservatorship, it receives the right to pursue civil professional liability claims. In pursuing these claims, RTC seeks recovery (1) from former directors or officers of the failed institution based primarily on their obligations as directors or officers; (2) from accountants, attorneys, commodities or securities brokers, and appraisers based primarily on their obligations to the institution as professionals; or (3) under a fidelity bond or from insurers of these individuals.

In pursuing civil actions, RTC is attempting to recover funds for losses brought about by culpable individuals. Recoveries can come directly from the assets of the individuals or from insurance policies covering professional misconduct. Ultimately, the recoveries are to help cover the cost of resolving the failed institutions.

RTC investigators and attorneys assess the viability of professional liability claims. The goal of these investigators and attorneys is to pursue claims where a sufficient factual and legal basis exists to demonstrate liability and when the expected recovery exceeds the cost of the suit. Among other things, investigators review prior examination reports, loan files, and other records to identify wrongdoing and look for insurance coverage or assets that could be recovered through a civil claim.[3] Attorneys in the RTC Professional Liability Section advise the investigators on information needed to develop and support claims.

For the most part, RTC professional liability attorneys do not actually litigate the claims in court. Instead, they hire private law firms to litigate the claims. However, a key responsibility of these attorneys is to oversee and manage these claims. Frequently, the claims are extremely complex, and the RTC attorneys must help to ensure that the agency is taking consistent positions throughout the country. The RTC attorneys must approve all major strategic decisions by the private law firms.

RTC PROFESSIONAL LIABILITY PROGRAM CONTINUES TO EXPERIENCE STAFF SHORTAGES AND CHANGES

RTC attorney staffing not only continues to remain below RTC's estimated needs, but reorganizations and staff reassignments also plague the program. Approximately 70 RTC attorneys are currently working in PLS, about half the number that RTC officials estimated in August 1991 that they needed. Since March 1992, the professional liability program has experienced significant changes including:

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[3]RTC expects to contract out about 60 percent of its investigative work in 1992.

-- a reorganization that decentralized the PLS program by requiring PLS attorneys to report through regional counsels,

-- the planned elimination of the consolidated field offices as a part of RTC's overall streamlining effort,

-- the forced reassignment of several PLS attorneys to FDIC, and

-- the rescinding of some of these reassignments.

In January 1992, RTC's Legal Division decided to require PLS regional attorneys to report through regional counsels rather than directly to PLS headquarters. RTC officials said that a key reason for this changed reporting requirement was to better coordinate all Legal Division work. This change, however, was not favored by former PLS management and created friction in some locations between the PLS program and the rest of the Legal Division.

In March 1992, RTC announced plans to reduce staff and consolidate operations. This restructuring is part of RTC's phase-down as the number of conservatorships projected to come under RTC's control decreases. By September 1993, RTC will merge 15 consolidated field offices and 4 regional offices into 6 field offices and will reduce its field staff by about 50 percent. Even though professional liability staff were not targeted for reductions, the planned closing of various offices heightened staff anxiety.

Then in May 1992, RTC, with no clearly delineated criteria, told 16 experienced field PLS attorneys that they were being sent to FDIC. According to RTC officials, these reassignments were part of RTC's streamlining efforts, which affected staff members throughout the Legal Division. According to RTC officials, the decisions on which attorneys should be retained, including those in PLS, were made in a series of meetings held in April and early May that were attended by senior headquarters and field division legal officials. No professional liability managers attended these meetings. RTC officials said no minutes or other written documentation were available concerning these meetings. In addition, RTC officials could provide little specific criteria for the decisions. In fact, there is conflicting information on what criteria were considered. Officials said the decisions were based on such factors as the need to conform to a new field structure, the need to replace permanent staff with temporary staff, and effective overall management. Several senior RTC officials told us that performance was also considered in the decisions. However, in RTC memoranda to employees who have grieved reassignment decisions, RTC said performance was not a factor in the decisions. RTC officials also told us no performance appraisals were reviewed in the decision meetings. In addition, in making their decisions, RTC officials did not consider each attorney's institution workload.

In July 1992, citing congressional concerns, RTC reversed its decision and suspended the transfer of all legal staff to FDIC including the 16 PLS attorneys mentioned earlier. RTC officials asked field assistant general counsels to reconsider their staffing needs and make recommendations to headquarters by August 17, 1992. PLS officials told us earlier this month that although no decisions have been made, most of the PLS attorneys will remain with RTC, but some will be asked to move to a new location. Again, RTC officials provided little verbal and no written guidance on the criteria for these decisions.

STAFFING CHANGES HAVE IMPACTED THE PROFESSIONAL LIABILITY PROGRAM

These reorganizations and personnel decisions have been disruptive to RTC's PLS program. Although it is difficult to quantify the effects of these personnel decisions, the program has clearly not been aided by RTC's recent management.

This change to the PLS program is coming at a time when the bulk of RTC's PLS work is yet to come. RTC attorneys not only must decide whether to file claims in thrifts before expiration of the FIRREA 3-year statute of limitations,[4] but also must monitor and support the rapidly increasing litigation. According to agency officials, it takes an average of 2 to 3 years from the date that an institution fails for RTC to determine whether or not to file a claim. If RTC files a claim, resolution often takes another 2 to 3 years. As of August 1992, RTC had made decisions on whether to file claims concerning over 200 thrifts. There are about 420 additional thrifts for which RTC must make these decisions between August 1992 and the end of 1994. Figure 1 shows the number of institutions in which there are claims that will be time-barred in the 12 months beginning August 1992.

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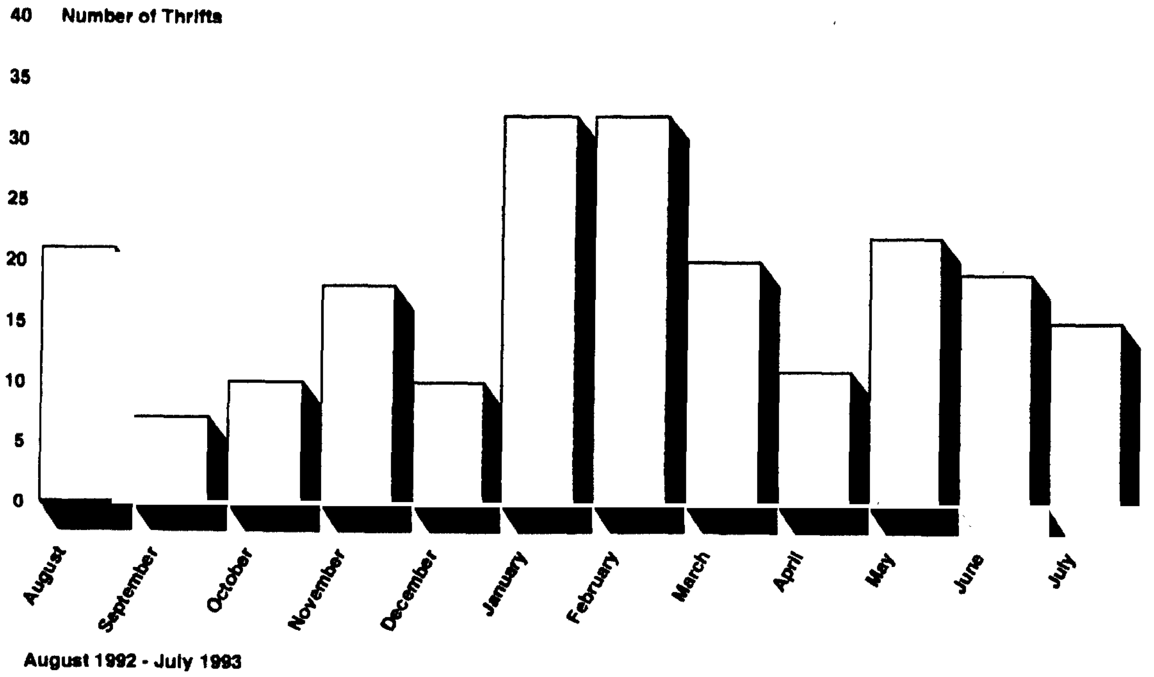
[4]The 3 year FIRREA statute of limitations for tort claims begins to run on the date of appointment of RTC as conservator or receiver, or the date on which the cause of action accrues, whichever is later. Actions may also be brought, in certain circumstances, beyond this 3-year period. First, actions may be brought under the limitations period applicable under state law. FDIC noted in recent testimony that 14 states have a longer limitations period than FIRREA. Second, RTC may enter into tolling agreements that temporarily extend the statute of limitations.

Figure 1: Expiring Statute of Limitations



Source: RTC.

RTC's attorneys are also being challenged by the rapidly expanding number of claims they are filing. During the first 6 months of 1992, RTC filed 105 claims, significantly more than any previous period. As noted earlier, even though these claims will be litigated by private counsel, RTC attorneys will need to support and oversee this litigation.

Our analysis shows that those attorneys identified in May 1992 for FDIC assignment were responsible for a significant number of thrifts and claims. Of the 16 PLS attorneys slated for return to FDIC, four were section chiefs and three were regional managers. These regional managers oversaw about 400 of RTC's 700 thrifts.

The 16 attorneys designated for transfer to FDIC were directly responsible for about 140 thrifts. These thrifts had assets totaling nearly $37 billion. The attorneys were also responsible for overseeing the litigation of about 20 claims in 13 of these thrifts. The amount of these claims totalled about $260 million. The attorneys suspected wrongdoing on the part of directors, officers, and other professionals in more than 90 of the institutions for which they were responsible. Furthermore, five of the attorneys slated for transfer to FDIC were working on thrifts whose statutes of limitations expired in June or July of 1992.

In addition, our interviews with current and former PLS officials and private law firm attorneys working on PLS cases suggest that the program has operated far from smoothly. One high-ranking RTC official told us that he could cite no documentation outlining downsizing procedures and plans. According to this same official, even after RTC rescinded its decision to return its employees to FDIC, there remained questions concerning staffing levels because RTC had not yet finished analyzing the expected and actual workload for each office. A current PLS manager described the reorganization as "neolithic". He noted that work slowed on many cases as early as March of this year as attorneys began wondering whether they still had jobs. Private law firm attorneys told us that cases they were working on were left unattended for 4 to 6 weeks, therefore there was no one to answer their questions.

BETTER PLANNING NEEDED TO MINIMIZE PROBLEMS AS RTC DOWNSIZES AND IS DISSOLVED

Reorganizations and reassignments at RTC are inevitable as the agency is dissolved and work is transferred to FDIC. But RTC needs to better plan for such changes to minimize disruption of professional liability work and to allow for the orderly transfer of employees back to FDIC.

RTC did not effectively manage the changes to the professional liability program over the past several months. Key PLS attorneys with critical workloads were selected for reassignment with little regard for the institutions and claims they were working on. Specific assignments were not considered as a part of the staffing decisions. In addition, communication with FDIC officials on the transfer of RTC Legal Division staff to FDIC was poor. FDIC officials said that RTC did not provide critical biographical and location preference information about the employees on the transfer list that would have aided them in determining specific FDIC positions for transferred RTC employees.

In our June testimony, we said that FDIC and RTC need to plan for the orderly transition of RTC work and need to address a number of issues. The primary issue is how to integrate the work of the two agencies. The agencies have developed their own methods of doing professional liability work and have different management styles and approval processes. As is evident by the failure of previous attempts by these agencies to work together and the problems associated with the most recent staffing decisions, integrating the work of the two agencies will not be an easy task.

In our June testimony, we recommended that FDIC and RTC work together to plan for the future of the professional liability program. Such planning needs to include staffing strategies to ensure the continuity of critical professional liability cases.

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In summary, Mr. Chairman, RTC's ability to pursue civil professional liability cases depends on the timely completion of its casework. If RTC is unable to meet statute of limitations deadlines, then the cases are simply lost and the assets from the directors, officers, and other professionals who caused the losses to the institutions remain unrecovered. In such a climate, RTC must be especially careful to design strategies to ensure that transitions (such as the one just attempted) are smooth ones. In this most recent instance, downsizing policies were ill-defined and the transition proved to be anything but smooth: pivotal attorneys were removed from assignments at a time when the work demanded regular and systematic attention. Although RTC has rescinded its transfer decisions, there remain underlying problems with RTC's philosophy for merging with FDIC that are likely to resurface in the future if they are not explicitly addressed now.

That concludes my statement, Mr. Chairman, we would be happy to respond to any questions.

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