

GAO

Report to the President and Chief  
Executive Officer, Resolution Trust  
Corporation

November 1993

# RESOLUTION TRUST CORPORATION

## Oversight of SAMDA Property Management Contractors Needs Improvement



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

General Government Division

B-254817

November 30, 1993

The Honorable Roger C. Altman  
President and Chief Executive Officer  
Resolution Trust Corporation

Dear Mr. Altman:

As you know, the Resolution Trust Corporation (RTC) hires contractors under its Standard Asset Management and Disposition Agreement (SAMDA) program to manage and dispose of assets from failed thrifts. SAMDA contractors are required to subcontract with property management companies (PMCs) to help with this process. Since the PMCs are responsible for managing day-to-day property operations as well as collecting any revenues, it is important that their performance be monitored. We initiated this review to determine what steps had been taken to monitor the performance of selected PMCs.

## Results in Brief

RTC has given SAMDA contractors responsibility for ensuring that their subcontractors adequately perform their contractual duties and properly account for all expenditures of RTC's funds. Although the SAMDA contractors are required to diligently monitor and supervise the performance of their subcontractors, we found that five of the six SAMDA contractors reviewed had not audited their PMCs' accounting records to ensure that expenses paid were reasonable and correct and that all revenues were properly reported. Further, none of the six SAMDA contractors had completed on-site reviews of their PMCs to ensure that they were satisfactorily performing their contractual duties. As a result, the SAMDA contractors could not ensure that RTC's assets were adequately maintained or that its funds were not wasted, mismanaged, or abused.

During our visits to 21 properties, we found 8 properties in need of repairs and 5 that were not adequately protected against theft or vandalism. We also found that 10 of the 16 PMCs were unclear about their responsibilities for managing RTC properties and/or for remitting all funds due to RTC. The SAMDA contractors were not taking adequate steps to oversee their PMCs because their contracts did not specifically require that they make on-site reviews or periodically audit the accounts. Further, at the time of our review, RTC's guidance on a SAMDA contractor's responsibility for monitoring its PMCs was vague.

RTC has taken several steps to improve the oversight of its contractors and subcontractors. One improvement was the distribution of memos and a performance checklist that helped clarify the guidance. The performance checklist identified specific areas related to subcontractor oversight that RTC would check and hold the SAMDA contractor accountable for during annual performance reviews. Further, RTC stated that its Asset Management and Disposition Manual would be revised to include a PMC oversight program.

Although RTC has better explained to the SAMDA contractors what steps they should take to adequately oversee their PMCs, RTC does not have a process to ensure that the contractors will take these actions on a regular basis. As a result, we are recommending that RTC better ensure its SAMDA contractors are taking regular steps to oversee their PMCs by either completing more frequent performance reviews or requiring recurring reports from SAMDA contractors. Such periodic monitoring and oversight is important if RTC is to minimize its vulnerability to fraud, waste, and mismanagement associated with the PMCs' day-to-day operations at these revenue-producing assets.

RTC officials agreed that additional steps are needed to better ensure adequate oversight of the PMCs and stated that they would consider strengthening the SAMDA performance reviews to address our concerns.

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## Background

RTC uses private contractors to manage and dispose of billions of dollars in assets from failed thrifts. SAMDA is one of RTC's principal asset management and disposition programs. As of June 1993, RTC reported that 237 SAMDA contracts had been awarded with \$40.0 billion<sup>1</sup> in real estate and nonperforming loan assets. These contractors are expected to receive a total of about \$658 million in asset-related fees.

RTC requires that SAMDA contractors hire subcontractors to assist them in performing certain services, including appraisals, brokerage, environmental consulting, property management, and property maintenance. (See app. II for a complete list of all mandatory SAMDA subcontractor services.) PMCs have been awarded subcontractors for the day-to-day management and operation of revenue-producing properties, such as hotels, commercial office buildings, and shopping centers. As of June 1993, RTC reported that more than 2,600 PMC subcontracts had been awarded with estimated fees totaling \$39.0 million.

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<sup>1</sup>All assets are presented at book value.

SAMDA contractors pay the fees for all mandatory subcontracts from their operating accounts and are then reimbursed by RTC. In addition, operating expenses, such as maintenance, repairs, and utilities, incurred by the property management subcontractors are "passed through" to RTC by SAMDA contractors. However, contract management expenses such as the cost of monitoring subcontractors are not passed through to RTC for reimbursement. All property-related revenues collected by the PMCs are to accrue to RTC. Under the terms of the SAMDA, RTC has delegated to the SAMDA contractors responsibility for ensuring the satisfactory performance of their PMCS.

Several reports have been issued discussing problems and difficulties associated with monitoring SAMDA contractors' operations. In a previous report we found that RTC designed SAMDA portfolios that were inefficient and difficult to manage.<sup>2</sup> RTC structured SAMDA portfolios consisting of real estate and loans with collateral in widely dispersed geographic locations. This practice created management problems for SAMDA contractors with distant assets in their portfolios and made it more difficult for them to monitor the performance of subcontractors. Taken together, these conditions increased RTC's vulnerability to fraud, waste, and mismanagement.

Another of our reports, issued in October 1992, noted that inadequate monitoring of the PMCS' cash management practices had resulted in RTC funds being vulnerable to loss from unauthorized use.<sup>3</sup> In addition to our reports, RTC's Office of the Inspector General and RTC's Office of Contractor Oversight and Surveillance (OCOS) issued reports that stated that SAMDA contractors were not following RTC procedures in soliciting, awarding, and administering subcontracts.<sup>4</sup> Further, several of these reports specifically cite inadequacies in SAMDA contractors' monitoring of PMCS. These reports found that the SAMDA contractors were not adequately

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<sup>2</sup>Resolution Trust Corporation: Asset Pooling and Marketing Practices Add Millions to Contract Costs (GAO/GGD-93-2, Oct. 7, 1992).

<sup>3</sup>Resolution Trust Corporation: Subcontracting Cash Management Practices Violate Policy and Reduce Income (GAO/GGD-93-7, Oct. 20, 1992).

<sup>4</sup>Asset Management Contractor, Pillar Investment Co., RTC Inspector General (Report A93-008, Jan., 14, 1993); Asset Management Contractor, R&B Realty Group RTC Inspector General, (Audit Report A93-016, Mar. 16, 1993); Study and Evaluation of the Internal Accounting and Management Control Structure of BEL/Ritz, a Joint Venture and BEI Management, Inc., RTC Office of Contractor Oversight and Surveillance (RTC/OCOS-92-7-SA, Nov., 1992); Study and Evaluation of the Internal Accounting and Management Control Structure of Real Estate Recovery, Inc. RTC Office of Contractor Oversight and Surveillance (RTC/OCOS-92-16-SA, Dec., 1992); Study and Evaluation of the Internal Accounting and Management Control Structure of Wiley Brooks Co., Inc., RTC Office of Contractor Oversight and Surveillance (RTC/OCOS-92-9-SA, Dec., 1992).

monitoring the PMC's cash management practices, reviewing revenue and expense reports in a timely manner, and ensuring that properties were visited as required.

## Objectives, Scope, and Methodology

We initiated this review to assess SAMDA contractors' oversight of subcontractors' performance. To accomplish this objective, we reviewed RTC's policy and procedures governing contracting and contractor oversight, including those found in RTC's Contract Policy and Procedures Manual (CPPM), Asset Management and Disposition Manual, and the SAMDA contract. We also reviewed various documents that identified the procedures used by selected RTC field offices. We discussed the policies and procedures with officials at RTC headquarters: four field offices located in Atlanta, Dallas, Newport Beach, and San Antonio; and six SAMDA contractors. The SAMDA contractors were judgmentally selected on the basis of the following criteria: (1) at least 40 percent of their assets were real estate assets and (2) they had awarded 10 or more property management subcontracts.

To assess the adequacy of SAMDA contractor oversight of subcontracts, we judgmentally selected 16 property management subcontractors and 21 RTC-owned properties that they were responsible for managing and operating. Each of the subcontracts had been in effect at least 6 months at the time of our review. In selecting subcontractors and related assets, we sought to include as many types of commercial properties as possible; therefore, we selected property management subcontractors that were responsible for apartments, condominiums, hotels, retail centers, mobile home parks, and office buildings. When information was readily available, we reviewed property management subcontracts that were expected to receive at least \$50,000 in management fees.

We discussed the adequacy of monitoring and oversight of these properties with both SAMDA asset managers and selected property managers, and we reviewed the asset management files. Additionally, we visited 21 RTC-owned properties and met with all 16 PMCs to observe the condition of the properties and to directly assess the property managers' performance. During our meetings with the PMCs, we selected and audited a sample of their records to determine if expenses paid were reasonable and correct and all revenues were properly accounted for.

While the specific findings from this review apply only to SAMDA contractors included in our review, similar weaknesses at other

contractors have been previously reported by the RTC Inspector General and OCOS.

We received written and oral comments from RTC on a draft of this report and incorporated changes where appropriate. The written comments are included in appendix I. We conducted our audit work from December 1991 through July 1993 in accordance with generally accepted government auditing standards.

## Guidance Needed to Ensure That SAMDA Contractors Regularly Monitor PMCs

Under SAMDA, RTC required the contractors to diligently monitor and supervise the performance of their subcontractors. In addition, the contract requires SAMDA contractors to act in the best interest of RTC and as a fiduciary in managing and protecting RTC property. RTC officials defined this standard as those actions the contractors would take in safeguarding their own property. According to RTC officials, the SAMDA contractors were familiar with the specific oversight steps that should be taken since the steps are based on standard industry practices.

However, we found that the six SAMDA contractors reviewed had not taken adequate steps to diligently monitor and ensure acceptable performances from their PMCs. Generally, we found that the SAMDA contractors' efforts to fulfill their responsibility to diligently monitor and supervise the performance of their PMCs entailed reviewing monthly activity reports, processing bills for services, and in most instances visiting the properties. We found that SAMDA contractors had visited and inspected 14 of the 21 properties included in our review.

The SAMDA contractors did not complete on-site reviews of their PMCs' performance or audit the PMCs' records. On-site reviews could have determined whether the subcontractors had established adequate internal controls, followed RTC's policies and procedures, and performed all assigned duties. However, none of the six SAMDA contractors had completed on-site reviews of their PMCs.

Further, only one of the six SAMDA contractors had audited its PMCs to ensure that asset-related funds were properly accounted for and expenses paid were reasonable and correct. This contractor, a subsidiary of a financial institution, completed audits at some PMCs at the request of its parent company. It was not clear that such audits would become a regular part of the SAMDA contractor's oversight efforts.

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One of the four RTC field offices we visited had taken steps to establish a program requiring its SAMDA contractors to periodically audit subcontracted property managers. The program was being established because accountants at this office thought that RTC's vulnerability to loss of revenue was great enough to warrant periodic audits. However, according to the RTC officials, they encountered reluctance from the SAMDA contractors to audit the subcontractors since the SAMDA contract does not require such audits. At the time of our work, the RTC officials stated that only one SAMDA contractor had agreed to complete the audits.

One SAMDA contractor told us that he did not believe he was responsible for auditing or reviewing subcontractors engaged to manage and operate RTC-owned properties unless there were "obvious problems." Other SAMDA contractors told us that the wide geographical dispersion of property management subcontractors made it difficult and costly to visit and evaluate all PMCs. On the other hand, RTC oversight managers told us that in their opinion, SAMDA contractors must make on-site reviews of subcontractors' operations in order to adequately monitor their performance.

SAMDA contractors were not periodically making on-site reviews and auditing their PMCs' accounts because these actions are not specifically required. Further, RTC had not developed clear guidelines to fully implement its requirement that SAMDA contractors diligently monitor their subcontractors' performance. Although RTC established guidelines for visiting the properties, it did not have specific guidelines to explain what actions should be taken in order to fulfill the requirement to diligently monitor and supervise. The SAMDA contracts included in our review stated that in the first 90 days following contract award, the SAMDA contractor is to "inspect every Real Estate Asset to which RTC has title."<sup>5</sup> Further, RTC's Asset Management and Disposition Manual required the SAMDA contractors to physically inspect the properties once every 3 months when such visits are "cost effective." Also, RTC has established requirements for various reports that provide a variety of data on the assets' expenses and revenues. However, specific guidance on other monitoring and supervising duties was not available. Without specific requirements for periodic audits and on-site reviews of PMCs, fraud, waste, or abuse of RTC funds could go undetected.

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<sup>5</sup>A version of the SAMDA contract issued after those included in our review modified the requirements. The revised SAMDA requires the contractor to perform an on-site inspection only if it is necessary "to secure" such assets or "to preserve their value pending approval of the asset management and disposition plan."



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Because the SAMDA contractors had not completed on-site reviews of their PMCs and most had not audited the subcontractors' accounting records, we do not believe that the SAMDA contractors could assure that their subcontractors were effectively performing their responsibilities. In addition, we could not ensure that the assets were adequately maintained or its funds not wasted, mismanaged, or abused. During our visits to 21 properties we observed that 8 needed repairs and 5 were not adequately protected against theft or vandalism. During our on-site evaluations of the 16 PMCs we determined that 10 were unclear about their responsibilities for managing the RTC properties and/or for remitting all funds. The following are examples of problems we identified while visiting selected PMCs and related assets.

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Hotel

The property manager of a hotel valued at \$1.3 million did not know the name or address of the SAMDA contractor responsible for the property even though the contract had been in place for over 6 months. The property manager told us that no one from the SAMDA contractor had met with him to discuss the management and accounting activities of the property or to evaluate his performance. Our review of asset-related revenues disclosed that the property manager had retained more than \$144,000 in rental receipts because he did not know where to forward the money. The RTC field office officials with whom we met were also unaware that all revenue had not been properly reported to and accounted for by the SAMDA contractor. These officials assured us that appropriate steps would be taken to collect all revenue due from this asset.

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Parking Lot

While visiting an RTC property, we found that a local hospital was using a rear parking lot that was part of the property. However, at the time of our visit in August 1992, the SAMDA subcontractor official responsible for overseeing the asset was unaware that the parking lot had been rented to the hospital, and we found no evidence that \$1,600 in rental income had been collected by the SAMDA contractor. In December 1992, we discussed this situation with RTC field office officials who stated that the records did not reflect any rental income from this property. They informed us that the asset had been sold, and all revenues due from the property would be collected at closing.

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Animal Clinic

We observed a broken window in the rear of an unoccupied RTC-owned animal clinic that exposed medical equipment and assorted books, office

furniture, a television, a VCR, and a microwave oven to inclement weather and possible theft. When we questioned the on-site property manager and the SAMDA contractor about the situation, we learned that it was unclear who was responsible for maintaining the clinic. Specifically, the property manager told us that he was only responsible for managing and operating an adjacent apartment complex. However, the SAMDA contractor believed that the property manager was managing and overseeing both the animal clinic and the apartment complex.

Following our visit, we discussed these issues with RTC officials who said that repairs had been made to the building and the property manager's duties had been clearly explained.

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## Contractor Oversight Improvements Initiated

RTC has taken steps to improve its oversight at the contractor and subcontractor levels. In September 1992, RTC's Office of Contractor Oversight and Surveillance initiated a program to evaluate the performance of PMCs. As of May 4, 1993, OCOS had reviewed over 360 contracts and issued 10 reports. According to an OCOS official, this program will enable RTC to review about 20 percent of the PMCs each year. Other OCOS responsibilities limited its ability to review more of the PMCs.

In March 1993 the Chairman of the Thrift Depositor Protection Oversight Board presented a 10-point program of reforms for the President and CEO of RTC to implement immediately. One of these reforms addresses RTC contracting and specifically addresses strengthening its contractor oversight.

In July and August 1993 RTC issued memos to its field offices and SAMDA contractors that emphasized the importance of monitoring and overseeing PMCs and stated that the Asset Management and Disposition manual would be revised to include a more definitive PMC oversight program. Along with these memos, RTC issued a list of priorities for contractors to use in overseeing PMCs and a performance checklist for oversight managers to use during annual performance reviews to assess whether the SAMDA contractors have taken adequate steps to oversee their PMCs. The priority listing and the performance checklist help clarify the guidance to SAMDA contractors. However, although these measures explain to the SAMDA contractors what steps they should take to adequately oversee their PMCs, they do not ensure that the contractors will take these actions on a regular basis. At best, these measures will ensure that the SAMDA contractors' records of oversight actions will be reviewed annually.

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## Conclusions

RTC needs to better ensure that SAMDA contractors are adequately overseeing and monitoring their property management subcontractors. Although the SAMDA contractors had visited most of the properties included in our review, none of them were periodically performing on-site reviews of their PMCs to ensure that RTC's interests were adequately protected. Further, only one of these six SAMDA contractors had audited its PMCs to ensure that expenses paid were reasonable and correct and that all revenues were properly reported. We found that because the SAMDA contractors had not audited the PMCs or performed on-site reviews, revenues were not properly reported, PMCs were unclear about their responsibilities, and properties were not adequately protected against theft or vandalism.

RTC has taken several steps to improve oversight of PMCs. A program to evaluate the performance of PMCs was initiated in September 1992, and in March 1993 RTC developed a plan to strengthen its contractor oversight and improve the management of the SAMDA subcontracting process. Further, RTC distributed memos and documents that stressed the importance of overseeing subcontractors and stated that its asset management manual will be revised to include a section on PMC oversight. The changes in procedures help clarify what RTC expects SAMDA contractors to do to monitor and supervise its PMCs.

However, these changes do not ensure that the SAMDA contractors will take adequate steps to oversee the PMCs on a regular basis. The checklist used during the annual performance reviews will be the primary method for determining whether the SAMDA contractors have taken adequate steps to oversee their PMCs. Since PMCs are responsible for the day-to-day management and operation of RTC's revenue-producing properties, RTC needs to better ensure that its SAMDA contractors conduct thorough and regular reviews of their PMCs' operations.

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## Recommendation

We recommend that when revising the Asset Management and Disposition Manual, the President and CEO of RTC should either (1) change RTC's SAMDA performance reviews by completing them more than once a year and during those reviews include specific steps focused on the SAMDA contractors' efforts to oversee their PMCs, or (2) require the SAMDAs to regularly report on steps taken to oversee their PMCs.

## RTC Comments

We obtained both oral and written comments from RTC officials on a draft of this report. RTC officials agreed with our findings, conclusions, and the thrust of our recommendation. They asked that we incorporate the additional guidance provided to SAMDA contractors regarding their oversight responsibilities. RTC officials commented that in addition to the requirement to diligently monitor and supervise their subcontractors, the SAMDA contract provides that contractors are to give their "best efforts" and use "sound business judgement" in acting as a "fiduciary" for RTC. According to RTC officials, this standard means that the contractors should provide RTC property with the same level of care that they provide to their own properties. Furthermore, the officials stated that the specific actions needed for adequate oversight were based on accepted industry practices, and the SAMDA contractors were familiar with these standards.

We acknowledge that the above standards are required of the SAMDA contractors in the SAMDA contract and we added this information to the report. Nonetheless, the SAMDA contractors had not taken adequate steps to ensure that RTC's assets were adequately maintained or its funds were not wasted, mismanaged, or abused. As described in the report, none of the six SAMDA contractors completed on-site reviews of their PMCs to ensure that they were satisfactorily performing their contractual duties.

The RTC officials also agreed that more could be done to better ensure that SAMDA contractors are periodically taking steps to oversee their PMCs. But they also commented that if they required the SAMDA contractors to prepare another recurring report it may increase RTC's costs, since RTC would probably have to pay the contractors to prepare that report. The officials stated that to address our concerns they would consider making changes to their SAMDA performance reviews. Although the additional report could increase RTC's costs, the potential amount of lost revenues associated with inadequate monitoring of the PMCs could be far greater.

On the basis of the oral comments, we agreed that changes to the SAMDA performance reviews could address our concerns if either (1) the reviews were done more frequently than once a year and included specific steps directed to the SAMDA contractors' efforts to oversee their PMCs, or (2) the SAMDA contractors were required to regularly report on steps taken to oversee their PMCs. If properly implemented, either of these actions would better ensure that SAMDA contractors are regularly taking steps to oversee their PMCs' operations. We therefore modified our recommendation accordingly. In addition, we incorporated other RTC comments in the final report where appropriate. RTC reviewed the revised report and agreed to

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implement the revised recommendation. RTC's written comments are enclosed in appendix I.

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Since RTC was created as a mixed-ownership government corporation, it is not required by 31 U.S.C. 720 to submit a written statement on actions taken on our recommendation to the Senate Committee on Governmental Affairs, House Committee on Government Operations, and the House and Senate Committees on Appropriations. However, we would appreciate receiving such a statement within 60 days after the date of this report to facilitate our follow-up actions and to allow us to keep appropriate congressional committees informed.

We will send copies of this report to interested congressional committees and other interested parties. Copies will be made available to others upon request.

The major contributors to this report are listed in appendix III. Please contact me on (202) 736-0479 if you have any questions concerning this report.

Sincerely yours,



Gaston L. Gianni, Jr.  
Associate Director, Government  
Business Operations Issues

# Comments From the Resolution Trust Corporation



**RESOLUTION TRUST CORPORATION**  
Resolving The Crisis  
Restoring The Confidence

October 8, 1993

Mr. Gaston L. Gianni, Jr.  
Associate Director,  
Government Business Operations Issues  
U.S. General Accounting Office  
Washington, D.C. 20548

Dear Mr. Gianni:

This letter is in response to your September, 1993 draft report titled Oversight of SAMDA Property Management Contractors Needs Improvement. The Corporation finds the report's findings to be substantially accurate and fully supports the recommendation. We are especially pleased to note that the report recognizes initiatives undertaken by the Office of Contractor Oversight and Surveillance and the Office of SAMDA Program Management to address the issue of property management company oversight.

We appreciate the opportunity to have worked with your staff during this review. If you have any questions regarding our comments, please contact James R. Wigand, Acting Director, Office of SAMDA Program Management, at (202) 416-7133.

Sincerely,

A handwritten signature in cursive script that reads "Lamar".

Lamar C. Kelly, Jr.  
Senior Vice President for  
Asset Management and Sales

cc: Donna Cunnigham  
Thomas P. Horton  
James R. Wigand  
Howard W. Cox

801 17th Street, N.W. Washington, D.C. 20434

# Mandatory Subcontracting Services Required of SAMDA Contractors

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1. Property management, maintenance, and leasing
2. General construction and construction subcontracting services
3. Architectural/engineering consulting services
4. Construction consulting services
5. Environmental consulting services
6. Property tax consulting services
7. Title work
8. Financial investigation services
9. Appraisal services
10. Commission brokerage services for sales and rentals
11. Marketing signage and printing services
12. Surveying services

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# Major Contributors to This Report

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## General Government Division, Washington, D.C.

Carolyn M. Taylor, Assistant Director, Government Business  
Operations Issues  
Leon H. Green, Senior Evaluator  
Eluma P. Obibuaku, Evaluator  
Donna M. Leiss, Reports Analyst

---

## Dallas Regional Office

Jeanne M. Barger, Regional Management Representative  
James G. Cooksey, Evaluator-in-Charge  
Norman C. Poage, Site Senior



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