

Office of Inspector General



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Audit Report No. 02-032

Receivership Termination Activity




CONTENTS

| | |
|--|-----------|
| BACKGROUND | 1 |
| Receivership and the Termination Process | 1 |
| The Receivership Termination System | 4 |
| The Government Performance and Results Act | 4 |
| RESULTS OF AUDIT | 5 |
| PERFORMANCE PLANNING FOR TERMINATION ACTIVITY SHOULD INCLUDE PRE-2000 RECEIVERSHIPS | 6 |
| Table 1: Receivership Termination Goals | 7 |
| RECOMMENDATIONS | 8 |
| CORPORATION COMMENTS AND OIG EVALUATION | 8 |
| APPENDIX I: Objectives, Scope, and Methodology | 10 |
| APPENDIX II: Summary of Prior Coverage | 14 |
| APPENDIX III: Pertinent Laws, Regulations, and FDIC Policies and Procedures | 15 |
| APPENDIX IV: Corporation Comments | 17 |



DATE: September 20, 2002

TO: Mitchell L. Glassman, Director
Division of Resolutions and Receiverships



FROM: Russell A. Rau
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SUBJECT: Report Entitled *Receivership Termination Activity*
(Audit Report Number 02-032)

The Office of Inspector General (OIG) has completed an audit of the Division of Resolutions and Receiverships' (DRR) actions to terminate receiverships.¹ DRR terminated 209 receiverships from January 2000 through December 2001.² On January 1, 2002 there were 168 active receiverships.³ The audit objectives were to (1) determine whether DRR terminated receiverships in accordance with corporate policies and procedures, (2) evaluate the integrity and reliability of data entered into DRR's Receivership Terminations System, and (3) determine whether DRR's annual performance planning indicators and targets covered significant receivership termination activities. Appendix I of this report discusses our objectives, scope, and methodology in more detail.

BACKGROUND

Receivership and the Termination Process

The establishment of a receivership enables the FDIC to dispose of a failed insured depository institution's⁴ (institution) assets in an orderly manner and to distribute available funds

¹ A receivership is a temporary entity that is established when the primary federal or state regulatory authority closes an insured depository institution and appoints the FDIC as a receiver to manage the business affairs of the failed institution. After August 9, 1989, under the terms of the Financial Institutions Reform, Recovery, and Enforcement Act, the FDIC must be appointed receiver for all failed institutions whose accounts are insured by the Bank Insurance Fund or Savings Association Insurance Fund.

² DRR includes 11 receiverships as terminated in 2001 for performance results purposes, though the certificates of termination for these 11 were issued on January 1, 2002.

³ The 168 exclude the 11 receiverships for which the certificates of termination were issued on January 1, 2002. Efforts to liquidate assets, resolve impediments, and clear liabilities are ongoing for all 168.

⁴ Financial institutions whose deposit accounts are insured by the Bank Insurance Fund or Savings Association Insurance Fund.

equitably to creditors.⁵ The duration of a receivership is dependent on many factors, including the progress made in reconciling accounting information, liquidating assets, and resolving litigation. The 168 receiverships active as of January 1, 2002 had an average age of 8.7 years.

When the business affairs of a receivership are substantially complete, the FDIC considers a number of factors in deciding whether termination⁶ is indicated. The DRR *Failed Institution Receivership Termination Manual* (Termination Manual)⁷ lists the following factors that have a bearing on the decision to terminate:

- Status and book value of remaining receivership assets is \$15 million or less,
- Receivership cash flow,
- Likelihood of repaying all receivership creditors,
- Extent of litigation,
- Unresolved environmental issues,
- Status of tax issues and employee benefit plans,⁸
- Termination legal requirements, and
- Potential liability to the Corporation.

To be eligible for termination, a receivership must be free of impediments that represent material financial or legal risks to the FDIC. These impediments may include: outstanding contractual liabilities, outstanding offensive or defensive litigation, potential representation and warranty asset sale claims,⁹ open employee benefit plans, open subsidiary corporations where articles of dissolution have been approved,¹⁰ and known or potential environmental contamination liabilities.¹¹

When the factors above no longer pose material impediments, DRR usually selects a Termination Coordinator (TC) who is responsible for ensuring that all necessary pre-

⁵ Prior to August 10, 1993 the law in effect at the time the institution failed determined the priority in which the proven claimants received dividends. All receiverships established after August 10, 1993, must distribute dividends according to the Federal Deposit Insurance Act, 12 U.S.C. § 1821(d)(11)(A), which mandates the following priorities: a) administrative expenses of the receiver, b) any deposit liability of the institution, c) any other general or senior liability of the institution, d) any subordinated obligations, and e) any obligations to the shareholders or members (including holding companies and their creditors).

⁶ A process by which the operations of a receivership are concluded and the entity ceases to exist.

⁷ The FDIC Board of Directors has delegated primary authority for terminating receiverships to DRR.

⁸ A pension, profit-sharing, or stock bonus plan established by the institution or employee organization (prior to receivership) for the benefit of employees, including plans qualifying under Sections 401(a) or 401(k) of the IRS Code of 1954.

⁹ The FDIC in its Corporate capacity will assume the post-termination obligation to indemnify purchasers through representations and warranties of assets if those loans and loan related assets were sold with a Corporate Guarantee.

¹⁰ A method of disposition that allows a corporation to terminate the subsidiary's existence and pay a liquidating dividend to its shareholders for any assets in excess of corporate liabilities.

¹¹ An identified or possible environmental issue regarding contamination of real property that may reduce the property's value and subject FDIC to environmental corrective action, regulatory compliance, toxic tort liability for environmental personal injury, or civil/criminal penalties for noncompliance.

termination and post-termination steps are completed. The TC also notifies all FDIC program areas of significant events and creates and maintains files.

The successful completion of the receivership termination process requires continuous cooperation and coordination among DRR, the Division of Finance, the Legal Division, and the Division of Administration. DRR provides a list of assets subject to environmental review, environmental liability assessments, confirmation of legal notices, a list of outstanding claims, confirmation of the termination of employee benefit plans, confirmation that the settlement process¹² has been completed, confirmation that all subsidiaries have been identified, identification of repurchases¹³ that may impact the termination, and identification of industrial revenue bonds¹⁴ with outstanding letters of credit.¹⁵ DRR's Receivership Management Branch staff in Dallas has primary responsibility for receivership termination activity.

The Division of Finance is responsible for reconciling liability accounts, paying outstanding receivership expenses, preparing receivership financial statements, posting journal entries, and writing off remaining liabilities of the receivership. The Legal Division handles defensive litigation matters, professional liability issues, and legal matters related to environmental concerns. The Division of Administration is responsible for identifying any contracting issues that may impact receivership termination activity.¹⁶

According to the DRR Termination Manual, receivership termination normally encompasses the following steps:

- Providing notice of the termination to all interested parties,
- Converting the remaining assets to cash,
- Declaring and paying a final dividend¹⁷ (if funds are available),
- Establishing appropriate reserves for any liabilities assumed by the FDIC, and
- Issuing a Certificate of Termination.

When a receivership is terminated, some assets and liabilities may remain. In these instances, receivership assets and certain liabilities are transferred to FDIC Corporate through a corporate purchase and assumption agreement. In the event that a receivership asset is discovered after termination, the agreement provides a mechanism for transferring the asset to

¹² Settlement is the final disposition of accounts between a receiver and a failed bank acquirer. It is a process that normally takes place after closing a sales transaction with an acquirer.

¹³ A previously sold asset required by indemnification covenants to be bought back from the original buyer because of violations to the original sales contract.

¹⁴ Municipal bonds whose proceeds are loaned to private persons or to businesses to finance capital investment projects.

¹⁵ Document issued by a financial institution guaranteeing the payment of a customer's drafts up to a stated amount for a specified period.

¹⁶ A receivership executes contracts for loan servicing, asset management, and other goods and services, which are administered by the Division of Administration. Contracting issues include whether the FDIC should assume the contracts in its Corporate capacity or terminate them. Factors to be identified and reviewed in this decision include contract-related claims, disputes, and litigation from active and expired contracts for possible financial risk to the FDIC.

¹⁷ The final distribution of all remaining receivership funds (cash & non-cash).

Corporate on behalf of the receivership. The agreement specifically states that Corporate will assume no other liabilities of the receivership.

The Receivership Termination System

Information on termination activity is reflected in DRR's Receivership Termination System (RTS). RTS tracks receiverships through the termination process and assists DRR in meeting annual termination goals. The system tracks active and terminated receiverships, along with the impediments to termination and termination milestone dates. RTS is an Oracle database application. The Division of Information Resources Management has classified the RTS as a non-major application for purposes of Office of Management and Budget Circular A-130, Appendix III.¹⁸

The Government Performance and Results Act

The Government Performance and Results Act of 1993 (Public Law 103-62) (GPRA) requires the head of each agency to prepare and submit: (1) a strategic plan covering not less than 5 years to the Director of the Office of Management and Budget (OMB) and to the Congress, (2) annual performance plans to OMB, and (3) annual program performance reports to the President and the Congress.¹⁹ The Legal Division concluded that the FDIC is subject to GPRA, to the extent that the FDIC is required to prepare and submit the three reports. Appendix III of this report discusses GPRA's applicability to the FDIC in more detail.

GPRA was enacted to:

- improve the confidence of the American people in the capability of the federal government by systematically holding federal agencies accountable for achieving program results;
- initiate program performance reform with a series of pilot projects in setting program goals, measuring program performance against those goals, and reporting publicly on their progress;
- improve federal program effectiveness and public accountability by promoting a new focus on results, service quality, and customer satisfaction;
- help federal managers improve service delivery, by requiring that they plan for meeting program objectives and by providing them with information about program results and service quality;
- improve congressional decision-making by providing more objective information on achieving statutory objectives, and on the relative effectiveness and efficiency of federal programs and spending; and
- improve internal management of the federal government.

¹⁸ Circular A-130, entitled Management of Federal Information Resources, Appendix III, requires that a "major application" receive special attention to security due to the risk and magnitude of the harm resulting from the application's loss or misuse.

¹⁹ Sections 3 and 4 of GPRA outline the strategic and annual reporting requirements and are codified to 5 U.S.C. §306 and 31 U.S.C. §§1115-17, respectively.

Receivership Management is one of three major programs identified in the FDIC 2001-2006 Strategic Plan. The second strategic objective supporting the Receivership Management Program states, "Receiverships are managed to maximize net return toward an orderly and timely termination." DRR has primary responsibility for establishing annual performance planning goals, indicators, and targets²⁰ over receivership termination activities in support of the strategic objective. In establishing the termination performance indicators and targets for 2000 and 2001, DRR reviewed the status of each active receivership, including an analysis of outstanding claims, liabilities, and other impediments.

RESULTS OF AUDIT

Based on our sample,²¹ DRR complied with FDIC policies and procedures for terminating receiverships. DRR terminated, or was in the process of terminating, the receiverships in accordance with FDIC policies and procedures as prescribed in the *Failed Institution Receivership Termination Manual*. For the 6 terminated receiverships in the sample, we verified that DRR followed its stated process in terminating the receiverships and the files contained the required supporting documentation. For the 5 active receiverships in the sample, we verified that DRR was following its stated process in attempting to terminate these receiverships, but that there were open issues or impediments (such as litigation or environmental concerns) that were preventing termination. Additional details on scope and methodology are contained in Appendix I.

Additionally, tests of data contained in the Receivership Termination System for the sampled receiverships showed that the data were accurate and complete. For the 11 sampled receiverships, we concluded that selected information and dates in the original receivership file documentation matched the data in the RTS. Also, access to RTS by FDIC employees was appropriately limited.

We identified one area of concern related to DRR performance planning for receivership termination activity. Specifically, DRR's 2002 annual performance planning indicators and targets do not cover all significant receivership termination activities. The FDIC 2002 Annual Performance Plan contains one performance indicator and target related to terminating only those receiverships established since January 1, 2000. DRR officials stated that uncertainties for resolving various impediments associated with the pre-2000 receiverships complicated estimating a meaningful performance target. As a result, only 11 of the 168 active receiverships are associated with a performance indicator and target. To help maintain the focus on terminating the older receiverships, DRR needs to include the pre-2000 receiverships in performance planning for 2002 and future years.

²⁰ As used by the FDIC, the annual performance goal generally restates the long-term strategic objective. The annual performance indicator describes the action to be achieved. The annual performance target describes a numerical value to be achieved in relation to the indicator.

²¹ We judgmentally selected 6 terminated receiverships and 5 active receiverships as of September 2001.

PERFORMANCE PLANNING FOR TERMINATION ACTIVITY SHOULD INCLUDE PRE-2000 RECEIVERSHIPS

The FDIC 2002 Annual Performance Plan does not include a performance indicator and target for termination activity attributable to 157, or 93 percent, of the 168 receiverships active on January 1, 2002. DRR officials stated that uncertainties for resolving various legal, environmental, and accounting issues associated with the pre-2000 receiverships made it complicated for them to estimate a meaningful performance target. As a result, only 11 of the 168 active receiverships are associated with a termination performance indicator and target, and DRR risks losing focus on terminating the older receiverships.

The FDIC's identification of receivership terminations within the second strategic objective of the Receivership Management Program and within annual performance goals signifies the activity as a central component to achieving the strategic goal of recovering funds for creditors of failed insured depository institutions. While GPRA does not require performance planning to cover the entirety of a given activity or program, including a performance indicator and target covering the majority of receiverships in inventory would help the FDIC maintain focus on achieving its strategic objective and annual performance goal for termination activity.

DRR made significant progress terminating receiverships in 2000 and 2001 by closing 156 and 53,²² respectively. On January 1, 2002, 168 active receiverships remained in inventory dating back to those established in 1987. Unlike in 2000 and 2001, DRR's annual performance planning for 2002 does not include a significant level of receivership termination activity. The 2002 Annual Performance Plan contains one performance indicator and target related to termination activities that covers receiverships established on or after January 1, 2000. As of January 1, 2002, only 11 of the 168 active receiverships had been established on or after January 1, 2000. Further, the average age of the 157 active pre-2000 receiverships as of January 1, 2002 was 9.3 years.

GPRA provides for strategic planning and performance measurement in the federal government by requiring agencies to develop a strategic plan of not less than 5 years for program activities, annual performance plans, and annual program performance reports. GPRA requires that agency annual performance plans establish performance indicators to be used in measuring or assessing the relevant outputs, service levels, or outcomes of major programs or activities.

The FDIC's 2001-2006 Strategic Plan identifies the Receivership Management Program as one of three major FDIC programs. Orderly and timely termination of receiverships is one of three objectives supporting the Receivership Management Program's strategic goal of recovering funds for creditors. In accordance with GPRA, annual performance plans have been developed since 1999 to implement strategic goals and objectives. The annual performance plan contains annual performance goals and associated indicators and targets.

²² DRR includes as "terminated" one receivership transferred to the state of New York in 2001.

The FDIC’s strategic goals, annual performance goals, indicators and targets, and outcomes related to receivership termination activity from 2000 forward are illustrated in Table 1.

Table 1: Receivership Termination Goals

| Year | Strategic Goal | Annual Performance Goal | Indicators and Targets | Target Met? |
|------|---|--|---|---------------------------------------|
| 2000 | Receivership claims are resolved in a fair and cost-effective manner. | Achieve a 35 percent reduction in the number of active receiverships in 2000. | <u>Indicator</u> : Number of receiverships terminated. <u>Target</u> : 35 percent reduction in the number of active receiverships. | Yes ^a |
| 2001 | Receivership claims are resolved in a fair and cost-effective manner. | The FDIC, as receiver, manages the receivership estate and its subsidiaries toward an orderly termination. | <u>Indicator</u> : Reduction in the number of active receiverships. <u>Target</u> : Inactivate 76 of the 106 active receiverships not impacted by goodwill ^b claims in inventory at January 1, 2001. | No ^c |
| 2002 | Recovery to creditors is achieved. | The FDIC, as receiver, manages the receivership estate and its subsidiaries toward an orderly termination. | <u>Indicator</u> : Timely termination of new receiverships. <u>Target</u> : Inactivate 75 percent of receiverships managed through the Receivership Oversight Program within 3 years of the failure date (starting with receiverships established in the Year 2000). | Goal requires no terminations in 2002 |

Source: *OIG Analysis of FDIC 2000, 2001, and 2002 Annual Performance Plans and information provided by DRR.*

^a DRR planned for and terminated precisely 156 receiverships in 2000.

^b In the 1980s, The Federal Home Loan Bank Board permitted healthy savings and loans that were acquiring failing savings and loans to classify the failing institutions’ excess debt (or negative net worth) as supervisory goodwill for regulatory capital purposes. In 1989, Congress passed the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA). FIRREA reformed capital standards including the elimination of goodwill for regulatory capital purposes. A number of these acquiring savings and loans themselves subsequently failed. Creditors of the failed institutions filed lawsuits against the U.S. Government for breach of contract and alleged that FIRREA’s elimination of goodwill contributed to the institutions’ failures. For DRR performance planning purposes, receiverships with FIRREA breach of contract claims are considered “goodwill receiverships.”

^c DRR terminated 53 receiverships in 2001. Thirty-five of the 53 were nongoodwill-related and counted towards completion of the target.

As indicated in Table 1, the 2002 performance indicator and target for terminating receiverships covers only those receiverships that were established on or after January 1, 2000. DRR officials stated that uncertainties for resolving various legal, environmental, and accounting issues associated with the pre-2000 receiverships made it complicated for them to estimate a meaningful performance target.

Performance planning in 2000 and 2001 included terminations for pre-2000 receiverships. Background information that supported 2000 and 2001 plans contained a discussion that the performance targets were established after an exhaustive review of claims, liabilities, and other impediments to termination.

While DRR established annual performance goal indicators and targets applicable to all active receiverships in 2000 and all nongoodwill receiverships in 2001, DRR did not include 157, or 93 percent, of the 168 active receiverships in performance planning in 2002. Planning, executing, and reporting on performance indicators and targets for all significant receivership termination activities helps to ensure that emphasis is placed on achieving the Corporation's Receivership Management Program strategic goal and the related strategic objective. By not setting a performance-planning indicator and target for the pre-2000 receivership termination activity, DRR has no specific standard for measuring its performance and risks losing focus on terminating the older receiverships. Further, because the 2002 performance indicator and target cover receiverships dating back to January 2000 and allows 3 years to terminate, there is no expectation for terminating any receiverships in 2002 for performance planning purposes.

On February 1, 2002, the OIG was asked to comment on the Corporation's draft 2002 Annual Performance Plan. The OIG commented that it would be appropriate to include a second indicator and target for terminating the pre-2000 active receiverships. In the final version of the Plan, narrative information was added acknowledging the pre-2000 active receiverships but DRR did not add a second performance measure. A second indicator and target is still needed for the reasons cited above.

RECOMMENDATIONS

We recommend that the Director, DRR:

- (1) Establish a 2002 interim performance indicator and target for the termination of pre-2000 active receiverships.
- (2) Develop performance indicators and targets that include all active receiverships when formulating future annual performance plans.

CORPORATION COMMENTS AND OIG EVALUATION

The Director, DRR, provided a written response, dated September 11, 2002, to the draft report. The response is presented in Appendix IV to this report.

DRR concurred with the two recommendations. In response to Recommendation 1, DRR established that 20 pre-2000 receiverships would be targeted for termination before the end of 2002, in addition to 52 receiverships terminated year-to-date through September 1. Recommendation 1 is resolved, dispositioned, and closed.

In response to Recommendation 2, DRR indicated that it would set appropriate annual goals for the termination of all active receiverships during DRR's normal goal-setting activities and complete the process by November 30, 2002. Therefore, recommendation 2 is resolved but will remain undispositioned and open for reporting purposes until we have determined that agreed-to corrective action has been completed and is effective. DRR further indicated that the normal goal-setting process would include setting internal goals for receiverships not terminated within 3 years of the institution's failure.

DRR's response indicated that terminating 52 receiverships year-to-date and planning to terminate 20 additional pre-2000 receiverships demonstrates that DRR is very familiar with impediments to termination. In the last paragraph of this report's Background section, we acknowledge DRR's familiarity with the status of each active receivership as part of its goal-setting activities for 2000 and 2001. By establishing and articulating formal performance indicators and targets, DRR can maintain a steady focus on program performance and outcomes.

OBJECTIVES, SCOPE, AND METHODOLOGY

The audit objectives were to (1) determine whether DRR is terminating receiverships in accordance with corporate policies and procedures, (2) evaluate the integrity and reliability of data entered into DRR's Receivership Terminations System, and (3) determine whether DRR's annual performance planning indicators cover significant receivership termination activities. We performed our work from September 2001 through April 2002 in accordance with generally accepted government auditing standards.

Scope and Methodology

The scope of our first objective, to determine whether DRR is terminating receiverships in accordance with corporate policies and procedures, included active and terminated receiverships as of September 1, 2001. We developed an audit universe of 203 active receiverships, of which 96 did not involve goodwill-related litigation.¹ From January 1, 2000 through September 1, 2001, the universe of terminated receiverships numbered 162. We selected a judgmental sample (based on early bank failure dates) of 6 terminated receiverships and 5 active receiverships for detailed review. The bank failure dates for the 6 terminated receiverships ranged from April 4, 1986 to July 6, 1990. The bank failure dates for the 5 active receiverships ranged from June 1, 1990 to April 30, 1993. By January 2002, 3 of the 5 active receiverships in our sample were terminated. The dates of termination for the 9 terminated receiverships in our sample ranged from January 1, 2000 to January 1, 2002. The average elapsed time from institution failure to termination was 10 years and 11 months, or almost 11 years.

In developing the audit steps to review the receivership and termination files, we used the information contained in the DRR *Failed Institution Receivership Termination Manual*, dated April 1998, and in the Division of Finance's (DOF) *Field Finance Operations Accounting Manual – Terminations*, dated December 2000. For the 6 initial terminated receiverships, we verified that DRR followed its stated process and that the files contained evidence of:

- Controls over employee benefit plans to deter fraud and abuse.
- Approved termination case signed by properly delegated DRR and DOF officials.
- Correspondence and opinions from the FDIC Legal Division on receivership litigation.
- Sales contract between the FDIC as "Receiver" and the FDIC, the "Corporation."
- Published notice of intention to terminate the receivership.
- Clearance memoranda obtained from DRR, DOF, DOA, and the Legal Division.
- DRR termination instructions to DOF.
- Corporate Purchase and Assumption Agreement.
- Corporate Purchase Asset and Liability Listing.
- Calculation of the final dividend, if any.
- DOF General Ledger² entries.
- Certificate of Termination.

¹ See explanatory note "b" to Table 1 for a discussion of goodwill litigation.

² A collection of all asset, liability, owners' equity, revenue and expense accounts.

For the 5 active receiverships in the sample, we verified that DRR was attempting to terminate the receivership in accordance with the stated process. We also verified that the files contained evidence of the following:

- Open issues or impediments (e.g., litigation or environmental issues) that are preventing termination.
- Proper notice to creditors, subordinated debt holders,³ stockholders, and other interested parties of the FDIC's intention to terminate a receivership.
- Elapsed time since the receivership's inception.
- Value of remaining assets.
- Actions taken by DRR to resolve any impediments.

The scope of our second objective, to evaluate the integrity and reliability of data entered into DRR's Receivership Termination System (RTS), included verification of data for the 11 receiverships in our sample. Specifically, we tested the data contained in the 27 fields (92 possible data elements) of the RTS Receivership and Milestone Dates screens.

We also obtained from DRR a list of staff with access to the RTS. The list contained 15 staff with access at two levels: (1) read/write, and (2) read/write/delete. We tested one employee from each of the two levels and verified that access was limited to the level specified. Furthermore, two of the OIG audit staff, along with the termination coordinator, were tested and verified to have "read only" access.

In addition to verifying the accuracy and consistency of the RTS information with that contained in the receivership files, we also obtained and reviewed the following:

- The RTS Security Manual, Version 1.4 dated August 2000.
- The RTS User Manual, Version 1.4 dated August 2000.
- FDIC Corporate Security Controls Program *Sensitivity Assessment Questionnaire*.
- Office of Management and Budget Circular A-130 on Management of Federal Information Resources.

We arranged for direct access to the RTS database for purposes of verifying the RTS data to the original file documentation. We obtained from DRR the receivership files for the active and terminated receiverships in our sample. We also obtained from DOF the termination files for the terminated receiverships in the sample. We cross-checked the information contained in the DRR and DOF files and in the RTS for accuracy and consistency.

The scope of our third objective, to determine whether DRR's annual performance planning indicators covered significant receivership termination activities, included a review of the FDIC 2001-2006 Strategic Plan and FDIC Annual Performance Plans for 2000, 2001, and 2002. We reviewed the strategic goals, annual goals, and performance measure indicators and targets for each year. We interviewed DRR officials located in both Washington, D.C., and Dallas, Texas, to determine how the goals and performance measures were established. For 2000 and 2001, we compared the receivership termination results that DRR achieved to the planned goals and performance measures. We also reviewed the requirements of the

³ An obligation or liability to pay or render something to another, subject to the control or authority of another.

Government Performance and Results Act (GPRA) for developing strategic and performance plans.

Use of Computer-Processed Data

Our second objective specifically addressed the integrity and reliability of the RTS. As described above, we tested the RTS for accuracy and integrity of access. Because our tests did not disclose any discrepancies, we were able to rely upon the information contained in the database. The RTS is used as an information source and monitoring device by DRR terminations staff. The RTS is not a mainframe database and, other than receiving termination financial information from DOF, is not interconnected with other FDIC databases. The RTS is a local system in Dallas and its use is restricted to DRR personnel who have receivership termination responsibilities.

Management Controls Reviewed

We reviewed the following management controls related to the process for terminating receiverships:

- The FDIC and DRR strategic and performance plans for 2000, 2001, and 2002 with regard to the establishment of performance planning indicators and targets for receivership termination activity. We also referred to the requirements of GPRA.
- Delegations of Authority as set forth in the Redelegations of Authority matrix that charts employee names and titles against the redelegated authority for several types of transactions, such as selling property, releasing collateral, paying court-ordered judgments, selling loans and securities, paying dividends, and terminating receiverships.
- RTS data entry and accuracy. We compared and verified the accuracy of RTS information with the receivership file documentation. We also tested RTS access controls at three different levels.

For the controls identified in the DRR and DOF manuals that follow, we confirmed that the work was completed for the 6 terminated receiverships, where applicable, but we did not review all of these processes and procedures.

- The DRR *Failed Institution Receivership Termination Manual* that prescribes the procedures to be used in the receivership termination process, as follows:
 1. Identifying receiverships as candidates for termination.
 2. Identifying assets and due diligence.
 3. Collecting and reviewing case documentation. This task sets forth the information to be included in clearance memoranda on impediments to termination by the following DRR, DOF, DOA, and Legal Division program areas: Accounting, Asset Claims, Claims, Contracts, Employee Benefit Plans, Environmental, Investigations/PLS, Legal Division, Mortgage Servicing, Risk Management, Non-Asset Defensive Litigation, Securities/Capital Markets, Settlement, and Subsidiaries.
 4. Preparing and processing the termination case.
 5. Requesting for receivership to be placed in termination status (T-status).
 6. Coordinating the corporate purchase.

7. Signing corporate purchase and assumption agreement.
 8. Assigning corporate-purchased assets.
 9. Coordinating the final dividend distribution.
 10. Notifying stockholders, claimants, etc.
 11. Inactivating the receivership.
 12. Obtaining all necessary court approvals required for judicial terminations.
 13. Signing certificate of termination.
 14. Listing of termination file contents.
- The DOF *Field Finance Operations Accounting Manual – Terminations* that sets forth procedures for the following:
 1. Requirements for judicial review.
 2. DOF process for pre-case approval.
 3. DOF process for receipt of an approved case.
 4. Corporate purchase procedures.
 5. Affordable housing review.
 6. Final dividends.
 7. Post-insolvency interest claims.
 8. Termination statements.
 9. Inactivation.
 10. Termination file contents.

SUMMARY OF PRIOR COVERAGE

The FDIC OIG and the former Resolution Trust Corporation (RTC) OIG conducted two audits and one evaluation related to receivership termination activities:

1. RTC OIG Audit Report A95-DA-008, *Dallas Terminated Receiverships* dated September 19, 1995. The audit involved two terminated receiverships; its objectives were to determine whether the terminations complied with RTC policies and procedures, appropriately accounted for final termination transactions, and properly accounted for the disposition of receivership assets during the termination process. The audit stated that the process had some disposition documentation problems in 1993, but a significant improvement in documentation was made in 1994. The report concluded that RTC complied with the termination policies and procedures and performed final transactions appropriately.
2. FDIC OIG Audit Report No. 97-052, *Receivership Terminations in the Midwest Service Center*, dated May 8, 1997. The audit involved five terminated receiverships. The objectives were to determine whether the final accounting was appropriate; legal, environmental, and tax matters were appropriately resolved; remaining assets were appropriately valued; and receivership accounting treatment was appropriate. The report stated that generally the five receiverships audited complied with receivership policies and procedures in effect at the time, appropriately completed termination actions, accounted for assets, and prepared appropriate journal entries. The report concluded that the OIG did not identify any conditions during the audit that would warrant a recommendation or auditee response.
3. FDIC OIG Evaluation Report No. 98-003, *Review of the Division of Resolutions and Receiverships' Reporting of Termination Activity in FDIC Quarterly Performance Reports*, dated November 23, 1998. The objective was to evaluate the integrity and reliability of Receivership Termination System (RTS) data. The OIG concluded that the RTS was reliable and the termination case file adequately supported termination activity.

PERTINENT LAWS, REGULATIONS, AND FDIC POLICIES AND PROCEDURES

1. Federal Deposit Insurance Act.

Section 9 (a)¹ states, “Upon the date of enactment of the Banking Act of 1933, the Corporation shall become a body corporate and as such shall have power...To act as receiver...To prescribe by its Board of Directors such rules and regulations as it may deem necessary to carry out the provisions of this Act or of any other law which it has the responsibility of administering or enforcing....”

2. DRR *Failed Institution Receivership Termination Manual* dated April 1998.

The termination manual describes the receivership termination process and is divided into 14 tasks that must be accomplished before termination is completed. The tasks are as follows:

- Identifying receiverships as candidates for termination,
- Identifying assets and performing due diligence,
- Collecting and reviewing case documentation from the various FDIC program areas,
- Preparing and processing the termination case,
- Placing receiverships in termination status (T-Status),
- Coordinating the purchase of receivership assets by the Corporation,
- Executing the Corporate Purchase and Assumption Agreement,
- Assigning properly the assets purchased by the Corporation,
- Determining the final dividend and coordinating its distribution,
- Providing proper notification to stockholders and claimants,
- Inactivating the receivership,
- Coordinating with the Legal Division to verify that all necessary court approvals have been obtained,
- Executing the Certificate of Termination, and
- Listing the termination file contents.

3. Division of Finance *Field Finance Operations Accounting Manual – Terminations* dated December 2000.

The Division of Finance termination manual contains chapters on the responsibilities of the DRR and Legal Division, judicial review requirements, pre-case approval, processing of approved termination cases, corporate purchase procedures, affordable housing, final dividends, interest claims, termination financial statements, and inactivation procedures.

¹ FDI Act Section 9(a) is codified to 12 United States Code 1819(a)

4. Government Performance and Results Act of 1993 (Public Law 103-62) (GPRA).

GPRA was enacted to improve the efficiency and effectiveness of federal programs by setting goals for program performance and to measure results. The FDIC is clearly covered by portions of GPRA. Section 306 (Strategic plans) states “the head of each agency shall submit to the Director of the Office of Management and Budget and to the Congress a strategic plan for program activities.” For purposes of GPRA, an “executive agency” is defined in 5 United States Code § 105, and includes government corporations, such as the FDIC.

While the FDIC is subject to the GPRA, it is not subject to regulations promulgated by the Office of Management and Budget (OMB) under budget authority of 31 U.S.C. §1105, implementing GPRA requirements. GPRA requires each agency “carrying out provisions of §1105(a)(29)... to prepare an annual performance plan covering each program activity set forth in the budget of such agency.” OMB Circular A-11 implements this provision by requiring agencies in their performance plans to “display, generally by GPRA program activity, the amount of funding being applied to achieve the performance goals and indicators for that activity.” §220.8(d). OMB does not have authority to require the FDIC to submit its budget for approval. However, OMB’s performance plan requirement linking budgetary numbers and the performance plan is authorized by GPRA. Therefore, the FDIC has elected to submit budgetary information as part of its performance plan for purposes of GPRA compliance, while disclaiming that it is providing budget information for approval and review by OMB.

Key elements of GPRA include:

Section 306(c)² states, “The performance plan...shall be consistent with the agency’s strategic plan.”

Section 1115(a)(1)³ states, “establish performance goals to define the level of performance to be achieved by a program activity....”

Section 1115(a)(2) states, “express such goals in an objective, quantifiable, and measurable form....”

Section 1115(a)(4) states, “establish performance indicators to be used in measuring or assessing the relevant outputs, service levels, and outcomes of each program activity....”

² GPRA Section 3(c) is codified to 5 United States Code 306

³ GPRA Section 4 is codified to 31 United States Code 1115(a)(1), (a)(2), and (a)(4).

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Division of Resolutions and Receiverships

September 11, 2002

TO: Russell A. Rau
Assistant Inspector General For Audits

FROM: Mitchell L. Glassman *Mitchell L. Glassman*
Director

SUBJECT: Draft Report Entitled *Receivership Termination Activity*
(Assignment Number 2001-723)

This will serve as the DRR response to the issues and recommendations outlined in the draft OIG Audit report dated August 12, 2002.

RECOMMENDATION

That the Director, DRR:

1. Establish a 2002 interim performance indicator and target for the termination of pre-2000 active receiverships.

DRR RESPONSE

We concur with this recommendation.

With regard to pre-2000 failures, the OIG indicated there is no Corporate goal for terminating active receiverships. The Audit Report further stated that by not setting a performance-planning indicator and target for the pre-2000 receivership termination activity, DRR has no specific standard for measuring its performance, and risks losing focus on terminating the older receiverships. It should be noted that the goal of inactivating 75% of the receiverships established in and after 2000 within three years is based on reviewing historic terminations. Historically, most, but not all, impediments to termination are eliminated in three to four years. This Corporate goal also acknowledges that not all receiverships can be terminated within three years because of various long-term impediments. The receiverships that were established prior to 2000 and remain active today, are, in effect, the other 25%, which could not be terminated in a short timeframe.

For the pre-2000 receiverships, all impediments to termination have been identified. The impediments are as follows:

| <u>IMPEDIMENT</u> | <u>NO. OF IMPEDIMENTS</u> | <u>NO. OF RECS. AFFECTED</u> |
|------------------------|---------------------------|------------------------------|
| Accounting/Tax | 11 | 9 |
| Assets | 11 | 7 |
| Claims | 3 | 3 |
| Employee Benefit Plans | 1 | 1 |
| Environmental Issues | 4 | 4 |
| Goodwill | 63 | 63 |
| Investigations/PLU | 23 | 14 |
| Litigation | 67 | 35 |
| Mort. Servicing/LSFO | 13 | 6 |
| Securities | 98 | 22 |
| Subsidiaries | 35 | 26 |

As can be seen by the above number of impediments and receiverships affected by those impediments, the Terminations Department is very familiar with the receiverships and has refined and accounted for all impediments that affect the pre-2000 receiverships. As those impediments are eliminated, the receiverships will be terminated.

Based on the above, we believe that twenty additional pre-2000 receiverships can be terminated before the end of 2002.

RECOMMENDATION

That the Director, DRR:

2. Develop performance indicators and targets that include all active receiverships when formulating future annual performance plans.

DRR RESPONSE

We concur with this recommendation.

At the present time, the FDIC Corporate goal, which was established in 2002, is to inactivate 75% of receiverships managed through the Receivership Oversight Program within three years of the failure date, starting with receiverships established in the year 2000.

Although the OIG is correct when they state that the Corporate goal omits the year 2002, it should be noted that fifty-two receiverships have been terminated year-to-date, through September 1, 2002. Furthermore, by reviewing the impediments for the remaining receiverships, as previously stated, it is anticipated that an additional twenty receiverships will be terminated by year-end 2002. It is believed that terminating a total of seventy-two

receiverships in 2002 demonstrates that FDIC is focusing on all receiverships in order to achieve timely termination results, even though a specific goal has not been established.

Finally, it should be pointed out that termination goals were first established approximately five years ago in order to focus on all receiverships. The objectives of the previous goals were to reduce the number of outstanding receiverships as well as the length of time they remained opened. Since those goals were established, receiverships have been reduced from over 800 to the present number of 149. Additionally, the average life of the newer receiverships has been reduced from over seven years to less than three years. As a result of the previous goals, we have developed processes that allow us to monitor all receiverships in a manner that will promote timely termination of all receiverships.

During DRR's normal goal setting process, DRR will set appropriate annual goals for the termination or inactivation of all active receiverships, including setting internal goals for receiverships which have not been terminated within three years of failure. DRR will complete the process of goal setting by November 30, 2002.

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