Office of Inspector General

Office of Audits and Evaluations
Report No. AUD-13-001

DRR's Controls for Managing, Marketing, and Disposing of Owned Real Estate Assets

October 2012

Office of Inspector General

Executive Summary

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Why We Did The Audit

Within the FDIC, the Division of Resolutions and Receiverships (DRR) has primary responsibility for resolving failed FDIC-insured depository institutions, including the liquidation of assets in receivership. As of December 1, 2011, the FDIC owned 1,398 Owned Real Estate (ORE) assets with a book value of approximately $1.2 billion (5 percent of total receivership assets). From January 1, 2011 to November 30, 2011, the FDIC sold 2,259 ORE assets, with a book value over $1.5 billion and a sales price of approximately $620 million.

Our performance audit objective was to assess control activities associated with DRR's processes for managing, marketing, and disposing of ORE assets. To address our objective, we (1) reviewed policies, procedures, and control processes for managing, marketing, and disposing of ORE assets; (2) interviewed DRR officials; and (3) determined whether key control activities were implemented for 55 judgmentally selected ORE assets.

Background

When a bank fails, the FDIC establishes a receivership to liquidate the assets of the failed financial institution. In most cases, these assets include ORE, such as single-family homes, condominiums, office buildings, hotels, and undeveloped land, among other types of property. The FDIC acquires ORE initially because it is on the books of the failed bank and therefore becomes an asset of the receivership. Once the receivership is established, the FDIC acquires ORE through the foreclosure process on non-performing loans. ORE may also be discovered during the term of the receivership because, for example, the ORE asset was not appropriately included on the books of the failed bank or as the result of a settlement during litigation related to the bank's failure.

To facilitate the process of liquidating ORE assets, DRR uses the services of two nationwide ORE contractors to assist in the acquisition, management, marketing, and final disposition of all types of ORE assets. DRR also assigns one of its Resolution and Receivership Specialists (Account Officers) to monitor contractor management, marketing, and disposition efforts. The contractor maintains all original asset files and updates management and marketing information on each property. This information is available to DRR Account Officers through the contractor's Web site.

Policies and procedures regarding ORE marketing, management, and disposition are contained in DRR's *Asset Resolution Manual* (ARM), effective May 2011 (previously, the *Asset Disposition Manual*). In addition to the ARM, DRR has issued *Guidance Memorandums* to temporarily amend or add procedures to be followed by DRR Account Officers. Also, DRR has established *Job Aids*, which provide guidance for performing and documenting a variety of functions related to the management, marketing, and disposition of ORE.

Audit Results

DRR has established a number of important control activities for managing, marketing, and disposing of ORE assets, and DRR has provided Account Officers adequate guidance to facilitate DRR's monitoring of contractors. Specifically, we reviewed contractor Web sites and discussed the status of the 25 active ORE assets in our sample with DRR officials and determined that:

- Environmental Assessments had been conducted and documented in reports in accordance with DRR's ARM.
- Current appraisals had been conducted and the results documented in Appraisal Reports.
- Property tax information was obtained and documented on the contractor's Web site. Tax payments had been made or were being reviewed in accordance with the ARM.
- Property and liability insurance coverage was properly obtained.
- Congressional inquiries and consumer complaints were being tracked and addressed.

With respect to our sample of 30 inactive assets (sold, written off, or otherwise disposed of), we reviewed sales documentation and accounting entries and determined the following:

- Sales Cases were based on current appraisals.
- Approved Sales Cases were documented in the FDIC Automated Corporate Tracking System.
- Sales data and settlement information were properly recorded in DRR's Communication, Capability, Challenge, and Control (4C) System.
- Sales proceeds were properly recorded in the appropriate receivership accounting records.
- Postings to the 4C System and to the receivership accounting records were made in a timely manner, generally within 15 days of settlement.

DRR could, however, strengthen ORE control activities related to monitoring budgets and costs, maintaining property inspection reports, and transferring responsibility for assets. Enhanced procedures in these areas could promote efficiencies and consistency in DRR's management, marketing, and disposition of ORE assets. Our report also includes an observation regarding weaknesses in ORE Budget Case documentation that DRR is working to address.

Recommendations and Corporation Comments

The report contains three recommendations to:

- Develop a process for comparing actual costs incurred on ORE assets to approved budgets.
- Establish a standard location for filing property inspection reports to be readily available to all DRR personnel that may become involved with managing the property.
- Enhance procedures for the transfer of ORE assets between Account Officers in a manner that facilitates communication and document sharing.

The Director, DRR, provided a written response, dated September 21, 2012, to a draft of this report. In the response, the Director concurred with all three of the report's recommendations and described completed and planned corrective actions, which are responsive to the recommendations.

Contents

FDIC
Federal Deposit Insurance Corporation
3501 Fairfax Drive, Arlington, Virginia 22226

Office of Audits and Evaluations
Office of Inspector General

DATE: October 5, 2012

MEMORANDUM TO: Bret D. Edwards, Director
Division of Resolutions and Receiverships

[Signed]

FROM: Stephen M. Beard
Deputy Inspector General for Audits and Evaluations

SUBJECT: *DRR's Controls for Managing, Marketing, and Disposing of Owned Real Estate Assets* (Report No. AUD-13-001)

This report presents the results of our audit of the Division of Resolutions and Receiverships (DRR) controls for managing, marketing, and disposing of owned real estate (ORE) assets. As described more fully below, ORE is a property that has been acquired through foreclosure after a borrower has defaulted on a loan. As of December 1, 2011, the FDIC owned 1,398 ORE assets with a book value of approximately $1.2 billion (5 percent of total receivership assets). From January 1, 2011 to November 30, 2011, the FDIC sold 2,259 ORE assets, with a book value over $1.5 billion and a sales price of approximately $620 million.

The audit objective was to assess control activities associated with DRR's processes for managing, marketing, and disposing of ORE assets. To address our objective, we (1) reviewed policies, procedures, and control processes for managing, marketing, and disposing of ORE assets; (2) interviewed DRR ORE officials; and (3) determined whether key control activities were implemented for 55 judgmentally selected ORE assets with a total appraised value of approximately $202 million.[1] We conducted this performance audit in accordance with generally accepted government auditing standards. Appendix 1 of this report includes additional details on our objective, scope, and methodology. Appendix 2 contains a glossary of key terms,[2] and Appendix 3 contains a list of acronyms.

Background

When a bank fails, the FDIC establishes a receivership to liquidate the assets of the failed financial institution. In most cases, these assets include ORE, such as single-family homes, condominiums, office buildings, hotels, and undeveloped land, among other types of property. The FDIC acquires ORE initially because it is on the books of the failed

[1] See Tables 1 and 2 in Appendix 1 for a detailed description of our sample.
[2] Certain terms that are underlined when first used in this report are defined in Appendix 2, *Glossary of Terms*.

bank and therefore becomes an asset of the receivership. Once the receivership is established, the FDIC acquires ORE through the foreclosure process on non-performing loans. ORE may also be discovered during the term of the receivership because the ORE asset was not appropriately included on the books of the failed bank or as the result of a settlement during litigation related to the bank's failure.

To facilitate the process of liquidating ORE assets, DRR uses the services of two nationwide ORE contractors (contractor) to assist in the acquisition, management, marketing, and final disposition of all types of ORE assets.[3] DRR also assigns one of its Resolution and Receivership Specialists (Account Officers) to monitor contractor management, marketing, and disposition efforts. The contractor maintains all original asset files and updates management and marketing information on each property. This information is available to DRR Account Officers through the contractor's Web site.

Policies and procedures regarding ORE marketing, management, and disposition are contained in DRR's *Asset Resolution Manual* (ARM), effective May 2011 (previously, the *Asset Disposition Manual*). In addition to the ARM, DRR Directors and Assistant Directors have issued *Guidance Memorandums* to temporarily amend or add procedures for DRR Account Officers. Also, DRR has established *Job Aids*, which provide guidance for performing and documenting a variety of functions related to the management, marketing, and disposition of ORE.

Information Systems

DRR relies on the contractor's Web site for the following documentation and information regarding the day-to-day management of the ORE assets: appraisals; property tax invoices and payments; environmental assessments; property inspections; maintenance invoices; and broker names, contacts, and assignments.

DRR's inventory of ORE assets is maintained in its Communication, Capability, Challenge, and Control (4C) System. ORE assets are initially entered in the 4C System at acquisition and assigned unique identification numbers. Basic information on each asset is maintained in the 4C System, such as the property address, book value, DRR Account Officer, contractor, and receivership. When the ORE asset is sold or otherwise disposed of, the asset is coded as inactive,[4] and sales and settlement information are recorded in the 4C System. On a monthly basis, the FDIC's ORE inventory in the 4C System is reconciled with ORE inventory information provided by each of the contractors.

DRR's Business Information Systems Unit initially enters the book value of each ORE asset into DRR's Metavante Servicing System using the 4C identification number as a

[3] DRR used five contractors until November 2011 when the contracts ended with three of those contractors. ORE assets that were serviced by the three contractors were reassigned to the remaining two contractors during the fourth quarter of 2011.
[4] ORE assets coded in 4C as inactive have been sold, written off, or otherwise disposed.

unique identifier. Metavante next transmits this information to the ORE Subsidiary Ledger (Control Totals Module (CTM)). CTM then posts journal entries to the FDIC's General Ledger, which includes receivership financial statements. Subsequent journal entries as a result of the disposition of ORE assets are initially entered into the Metavante Servicing System and then follow this same path to the FDIC's General Ledger. CTM is the primary source of receivership and subsidiary journal entries posted to the FDIC's General Ledger.

As it relates to ORE, DRR utilizes the FDIC Automated Corporate Tracking System (FACTS), a Web-based tracking tool, to manage and approve cases. For example, ORE Budget and Sales Cases submitted by ORE contractors are entered into FACTS for approval by the appropriate Delegated Authority within DRR.

Management and Marketing

One of DRR's primary objectives related to ORE is to maintain or enhance property value and to ensure that the presence of the FDIC in a particular neighborhood is perceived as a contributory factor to market stability. Aside from ensuring that the property does not suffer depreciation in value from neglect or other causes, the contractor is to take the necessary steps to preserve or enhance the marketability of the property, improve the property's cash flow, and be responsive to the needs and concerns of neighbors and customers.

Key tasks related to the management and marketing of ORE assets include:

- **Environmental Assessments.** According to the ARM, all ORE properties, with the exception of those under sales contract or under a Purchase and Assumption Agreement at the time of bank closing, and all pre-foreclosure loans with real estate collateral must have an environmental assessment in accordance with DRR's *Environmental Guidelines Manual*. The primary objective of the environmental assessment is an effective and timely evaluation to assess and manage environmental risks associated with an asset. The policies and procedures help to ensure that assets with environmental issues are handled consistently and reduce the possibility of diminished recovery or exposure to lawsuits. DRR's environmental procedures address not only assets with environmental issues but also properties that are protected for future conservation purposes or considered historically significant.

- **Budget Cases.** DRR must authorize all transactions regarding each asset under its delegation or authority. The ORE Budget Case documents authorization of expenditures for managing and marketing ORE and for determining the amount of any Task Order to be issued and approved under appropriate delegations of authority. To provide approval for expenditures for ORE assets, the initial budget is prepared for an 18-month period, and annual budgets are prepared for every succeeding 12-month period thereafter. All cases and approvals are documented in DRR's FACTS database.

- **Appraisal Reports.** DRR's ARM provides that appraisals on ORE with an appraised value greater than $250,000 should generally be obtained annually to be considered current. Appraisals on ORE with an appraised value of $250,000 or less are required only every 24 months.

- **Contractor Property Inspection Reports**. DRR's ARM states that physical inspection of ORE should be considered on all properties and generally should be performed on all properties with improvements, crops, livestock, or mineral/oil/gas/timber rights. An initial inspection should be completed within 30 days but no later than 60 days, after assumption of ownership, and periodic inspections should be performed no less frequently than every 30 days thereafter.

- **Property Tax Payment Information.** The FDIC is subject to state and local real property taxes for ORE only if those taxes are assessed according to the property's value. For each ORE property, the Account Officer, or designee, is responsible for ensuring that each tax bill has been received and reviewed.

Contractors are paid a monthly management fee based on the property type, value, and length of time the property has been on the market. The FDIC is billed monthly by the contractor for the management fee as well as for any pass-through costs that may be incurred for subcontracted services such as property inspections, appraisals, property maintenance, and other property management costs. Contractor invoices are submitted to DRR's Accounting Department for processing and to DRR's Contract Oversight Department for review and approval.

DRR Account Officers provide guidance to the contractor and monitor the management and marketing effort. According to the ARM, Account Officers are responsible for:

- Reviewing the contractor's Web site for accuracy regarding: appraisals, title reports, property inspection reports, environmental assessments, property taxes, and other pertinent documents maintained on the asset.
- Ensuring clear and marketable title on the property.
- Verifying adequate insurance coverage.
- Reviewing the accuracy of all property budgets and monitoring approved expenditures.
- Conducting property inspections and meeting with brokers.

As of December 1, 2011, ORE assets were assigned to 40 DRR Account Officers located in the Dallas Regional Office (DRO), Dallas, Texas; East Coast Temporary Satellite Office (ECTSO), Jacksonville, Florida; and Midwest Temporary Satellite Office (MWTSO), Schaumburg, Illinois. At the time of our fieldwork, many of these ORE assets had been recently reassigned from the West Coast Temporary Satellite Office (WCTSO), Irvine, California, which was closed at the end of 2011.

Disposition

Most ORE assets are disposed of by selling the property through a real estate broker, bulk sale, or auction. DRR's general goals for the sale of ORE are:

- Timely sales that maximize financial recovery to the FDIC on a net present value basis.
- On a very limited basis, use of seller financing when necessary to facilitate the sale of ORE.
- Adequate exposure of all properties to targeted markets.
- Fair and consistent treatment of the public in the marketing and disposition of ORE assets.
- Continued education of the brokerage community and general public on the disposition and acquisition of FDIC properties.
- Complete, accurate, and current information on all available receivership properties.
- Compliance with legislative and DRR requirements regarding the disposition of affordable housing.

The contractor is responsible for preparing a Sales Case that provides the marketing strategy for selling an ORE asset. Sales Cases are required to be prepared in accordance with FDIC Circular 7000.6, as amended August 2010, which establishes case preparation guidelines. The Sales Case is submitted to the ORE Core Desk in the DRO. The Core Desk enters the Sales Case into FACTS, and a Case Number is immediately created to track the review and approval of the sales methodology. The Sales Case is then assigned to the appropriate delegated authority for review and approval based on the dollar value of the asset. Authority for approving ORE Sales Cases ranges from a DRR Section Chief for assets less than $2.5 million to the DRR Senior Management Oversight Committee (SMOC) for assets over $25 million.

After the Sales Case is approved, the ORE contractor executes the sale and provides settlement documentation, including the Settlement Statement, cash wire documentation, and Sales Case to the ORE Core Cash Desk. Sales proceeds are wired to the appropriate receivership/subsidiary account, and the cash receipt is documented in DRR's Accounting Department. Based on the settlement documentation, the ORE Core Cash Desk prepares a 4C Service Request, which indicates the sales amount, sales receipts and expenses, and sales proceeds, and submits it electronically to DRR Accounting. DRR Accounting verifies the 4C Service Request information with the sales proceeds wired to the receivership account and prepares the appropriate journal entries in the Metavante Servicing System that updates the receivership/subsidiary accounting records in CTM. Once the sale is recorded in the receivership/subsidiary accounting records, the ORE Core Desk is notified, and the asset is coded as inactive and sold in the 4C System. All original hardcopy documentation is maintained in the asset file and stored with Iron Mountain.[5]

[5] Iron Mountain is a private company providing document and imaging storage management services.

Audit Results

DRR has established a number of important control activities for managing, marketing, and disposing of ORE assets, and DRR has provided Account Officers adequate guidance to facilitate DRR’s monitoring of contractors. Specifically, we reviewed contractor Web sites and discussed the status of the 25 active ORE assets in our sample with DRR officials and determined that:

- Environmental Assessments had been conducted and documented in reports in accordance with DRR’s ARM.
- Current appraisals had been conducted and the results documented in Appraisal Reports.
- Property tax information was obtained and documented on the contractor’s Web site. Tax payments had been made or were being reviewed in accordance with the ARM.
- Property and liability insurance coverage was properly obtained.
- Congressional inquiries and consumer complaints were being tracked and addressed.

With respect to our sample of 30 inactive assets, we reviewed sales documentation and accounting entries and determined the following:

- Sales Cases were based on current appraisals.
- Approved Sales Cases were documented in FACTS.
- Sales data and settlement information were properly recorded in the 4C System.
- Sales proceeds were properly recorded in the appropriate receivership accounting records.
- Postings to the 4C System and to the receivership accounting records were conducted in a timely manner, generally within 15 days of settlement.

DRR could, however, strengthen ORE control activities related to monitoring budgets and costs, maintaining property inspection reports, and transferring responsibility for assets. Enhanced procedures in these areas could promote efficiencies and consistency in DRR’s management, marketing, and disposition of ORE assets. Our report also includes an observation regarding weaknesses in ORE Budget Case documentation that the ORE Department is working to address.

ORE Budget and Cost Monitoring

DRR established procedures for Account Officers to conduct ongoing monitoring of budgeted expenses for each of the ORE assets assigned to ORE contractors. However, for the active ORE assets we reviewed, we found that Account Officers were not consistently monitoring the ORE contractors’ actual expenses as required. For 17 of the 25 ORE assets we sampled, the Account Officers informed us that they did not monitor actual expenses because they do not receive monthly contractor billing reports or review contractor invoices.

DRR's ARM provides that DRR Account Officers should monitor actual expenses and compare these amounts to the property budget expenditures for each of the assets in their portfolios. When actual expenditures to date for the budget period exceed 75 percent of the total expenses budgeted for the period, a revised budget should be prepared immediately for a new 12-month period.

Monthly billing reports are submitted by the contractors to DRR's ORE Contract Oversight Department and Accounting Department. However, Contract Oversight Department and Accounting Department officials informed us that these reports are not utilized by either department to compare actual ORE asset expenses to budgeted costs. Also, monthly ORE contractor invoices are submitted to the DRR Contract Oversight Department for review prior to payment approval. However, Contract Oversight Department personnel are not involved in the management or marketing of the ORE properties and, therefore, cannot evaluate the reasonableness of the charges. Also, none of the Account Officers we interviewed who were responsible for the 25 sampled active ORE assets had been informed by DRR management that the contractor billing reports were available on the DRR Accounting SharePoint Site.

DRR officials explained that because the 4C System was not developed to manage ORE, they lost the ability to electronically track budgeted and actual expenses at the asset level when the 4C System replaced the prior ORE information system. In addition, during 2009, the FDIC maintained an average inventory of 2,850 ORE assets as a result of the recent financial crises. Therefore, DRR considered having Account Officers reviewing expenses billed for each ORE asset inefficient and impractical because doing so would require a large volume of individual asset spreadsheets to track every ORE asset. As an alternative, DRR only monitored and tracked ORE contractor expenses at the Task Order level (i.e., by receivership).

We contacted the ORE contractors to obtain current cost information regarding the ORE assets we reviewed. Both contractors were able to provide us a spreadsheet detailing pass-through costs and management fees charged to date for each of the sampled 25 active ORE assets. Furthermore, they advised us that the information included all subcontractor costs passed through to the FDIC that are included in their monthly reporting packages to DRR. We reviewed the monthly reports and found the costs incurred by FDIC for these properties to be within budgeted amounts. Also, although they are not formatted in a manner that facilitates a comparison with the property budget, the reports nevertheless provide details of the management and marketing costs for ORE assets.

Because ORE asset management and marketing costs are not actively monitored on an asset-level basis, Account Officers:

- cannot fully comply with the ARM requirement to ensure costs incurred are authorized, prudent, reasonable, and within budget, and

- lack useful information for developing management, marketing, and disposition strategies.

Recommendation

(1) We recommend that the Director, DRR, develop a process or system to provide actual ORE contractor cost information, including management fees and pass-through costs, to the responsible DRR Account Officers for a comparison of actual costs incurred on the ORE assets to approved budgets as prescribed by the ARM.

ORE Property Inspections

In addition to the property inspections conducted by the contractors, DRO, ECTSO, and MWTSO established inspection programs to review the contractor's maintenance and marketing of ORE properties. Further, DRR Account Officers are required to become familiar with their assigned ORE assets by personally inspecting the property and filing a standard property inspection report. However, Account Officers assigned to 7 of the 25 ORE assets we sampled did not know whether the property had been inspected by prior Account Officers or whether a property inspection report had been completed.

DRR issued a *Guidance Memorandum on Property Inspections*, on January 21, 2011, that requires Account Officers to conduct a property inspection within 90 days of the asset being assigned. The primary purpose is to gain knowledge of the real estate market in the area where the property is located and assess the property condition. The guidance states that a property inspection report is to be completed and sent to the National Field Office Branch (NFOB) Property Inspection Desk. Additional guidance provided to Account Officers in the form of an ORE Management and Marketing Job Aid states that the property inspection report should include an assessment of the condition of the property, including the need for maintenance items or repairs, and recommendations as appropriate.

We contacted the DRR Account Officer responsible for each of the active ORE assets in our sample to determine whether the property had been inspected by DRR personnel. For 18 of the 25 ORE assets we reviewed, property inspection reports completed by the current or a prior Account Officer were provided. However, for six of the ORE assets, the Account Officers informed us that the ORE asset had been recently transferred to their portfolios from another Account Officer and that they could not locate a property inspection report and could not determine whether the property had been inspected. These Account Officers were also not familiar with the NFOB Property Inspection Desk. We followed up with DRR ORE management and verified that a DRR property inspection had been conducted for these six assets. However, the benefit of the property inspection reports was reduced because they were not available to the DRR personnel primarily responsible for the property.

We discussed this matter with ORE officials, and they agreed there is a need to coordinate, in a more fluid fashion, the various inspection programs and associated results. ORE officials told us that there has been a revitalization of the programs and new staff assigned for the specific goal of streamlining the report posting processes and "opening" the files to anyone needing access to the information. To further simplify the process, the Account Officer's property inspection reports will reside in the ORE SharePoint Site. A single location has been identified in the ORE SharePoint Site to house all new property inspection reports. The property inspection reports will be organized by receivership to facilitate access by personnel outside of the ORE organization. Additionally, DRR is in the process of writing a Job Aid to further simplify access to the reports for those not familiar with ORE processes, procedures, and nomenclatures.

Recommendation

(2) We recommend that the Director, DRR, issue guidance to DRR Account Officers establishing and communicating a standard location for filing property inspection reports to be readily available to other DRR personnel that may become involved with the property.

Transferring Responsibility for ORE Assets

Due to changes in the ORE asset inventory, office closings, and staffing changes, DRR management found it necessary to reassign oversight responsibility for some ORE assets among Account Officers within the same office or between DRR offices. During our review, many of the current Account Officers assigned to an asset had difficulty providing us with management information and marketing history on the ORE assets because, according to our interviews, they had recently been assigned the assets and were unaware of the work the prior Account Officers had conducted. The lack of availability of such information may hamper the Account Officers' work to efficiently and effectively monitor ORE assets.

Based on ORE asset information obtained from the 4C System, we contacted the Account Officer assigned to each of the 25 active ORE assets in our sample to obtain information regarding budget cases, property inspections, and marketing history. Generally, the Account Officer was able to provide us with the information we requested. However, for 11 of the ORE assets, the Account Officers told us that the asset had been recently assigned to them and that they could not provide some of the documentation and information we requested. Specifically, regarding the 25 active ORE assets we reviewed, the current Account Officers could not provide:

- budget cases for 10 ORE assets,
- the name of the prior Account Officer for 9 ORE assets, and
- property inspection reports for 6 ORE assets.

The inability to provide this information was largely a result of the closing of the WCTSO at the end of 2011 when responsibility for ORE assets previously monitored by WCTSO personnel was transferred to Account Officers located in the DRO. DRR ORE management advised us that DRR's goal for the transitioning of ORE assets between

Account Officers was that the process be conducted in a manner that facilitates the ability of the new Account Officers to effectively manage, market, and dispose of the ORE asset. In anticipation of closing the WCTSO, a "shadow" DRO Account Officer was also assigned to monitor assets with the existing WCTSO Account Officer. The goal for this action was to provide the DRO Account Officers an opportunity to become familiar with the ORE assets that would ultimately become their responsibility for monitoring.

Based on our discussions with DRR ORE managers and Account Officers, we concluded that reassignment of assets prior to the WCTSO closing was not consistently conducted in a manner that ensured the new Account Officer would be familiar with the reassigned asset prior to the closing of the WCTSO. For example, Account Officers did not maintain notes on ORE properties in a shared file available for other Account Officers. In some cases, ORE assets had been reassigned within the WCTSO because the original WCTSO Account Officer had left the FDIC before the ORE asset was reassigned to a new DRO Account Officer. Therefore, neither the most recent WCTSO Account Officer nor the DRO Account Officer responsible for the asset could provide the information we requested.

We discussed the results of our review with DRR ORE managers who advised us that they were aware of these transition shortcomings associated with the WCTSO closing. They explained that the situation was exacerbated by a high volume of Account Officer reassignments during the transition of the WCTSO workload into the DRO. They informed us that DRR's strategy was to have the WCTSO retain as many assets as possible through the closing date, which resulted in continuous reassignment of assets during the transition period as some Account Officers departed for jobs in the private sector.

DRR further explained that improved procedures will be implemented during future office closings, including reassigning the portfolio of departing Account Officers from the closing offices to the DRO shadow Account Officer to ensure continuity. Specifically, this approach is in the transition plan for the MWTSO. DRR officials also explained that the lack of face-to-face debriefing sessions between the receiving Account Officer and the departing Account Officer saved travel costs but limited communication that would have mitigated some of the transition issues that occurred. In this regard, the MWTSO transition plan calls for the receiving Account Officer to coordinate a pre-debriefing session and a final face-to-face debriefing session should an Account Officer leave ahead of schedule.

Recommendation

(3) We recommend that the Director, DRR, establish procedures for the reassignment of ORE assets between Account Officers in a manner that facilitates communication and document sharing between the Account Officers involved in the transfer.

Observation - ORE Budget Cases

Budget Cases documenting approval for asset expenditures were not consistently prepared and approved in FACTS as prescribed by DRR guidelines. We noted 2 exceptions associated with 32 of the 55 ORE assets we reviewed: (1) ORE contractors did not prepare budgets within prescribed timeframes and (2) DRR did not return approved budgets that had been submitted for use in managing assets, and/or did not upload approved budgets to the FACTS system. Consequently, DRR was not in compliance with the policies established for Budget Case preparation and approval, and the FACTS system did not contain key documents authorizing expenditures for managing and marketing the 32 assets. DRR has already taken some mitigating steps to address these areas.

DRR's ARM establishes the requirement that FDIC staff, or designee, responsible for the ORE asset should prepare and submit the Budget Case for approval 2 months before the start of each succeeding 12-month budget period. No expenditures should be incurred without an approved budget except for (a) expenditures necessary to remedy emergency situations and (b) expenditures relating to appraisals, title work, asset search, and Environmental checklists and Phase I Environmental Site Assessments that are within guidelines for such expenditures. Budget Cases are prepared and submitted by the contractor to the ORE Core Desk in the DRO and distributed to the appropriate delegated authority within DRR for approval.

We attempted to verify that Budget Cases were approved for each of the 25 active and 30 inactive ORE assets in our audit sample by entering the 4C asset identification number in FACTS. However, for 10 of the 25 active ORE assets and 22 of the 30 inactive ORE assets, we could not locate an approved Budget Case. We submitted the list of Budget Cases we could not locate to ORE officials and were informed that the budgets could not be located by the asset identification number and needed to be researched.

ORE officials were ultimately able to find approved budgets for 9 of the 10 active ORE assets and 21 of the 22 inactive ORE budgets we could not locate. We were informed that the budgets could not be located because they were maintained by receivership, rather than by ORE asset, and to locate the individual property budgets required considerable research. ORE officials further explained that due to the large number of bank failures from 2008 to 2010 and limited ORE staffing, the budget approval process was too cumbersome and inefficient given the unprecedented and continuous influx of ORE assets. Therefore, the budget process was amended and the use of a budget spreadsheet, by receivership, was adopted. During this time, the FDIC's Contract Oversight Manager engaged the ORE contractor based on an estimate of projected expenses for the receivership, instead of approving individual property budgets. In November 2010, the ORE Department asked all ORE contractors to prepare new budgets on all ORE properties. As of April 30, 2012, there were only 28 properties in the ORE inventory of 1,051 properties without an approved budget; however, these budgets were in the process of being prepared.

We acknowledge that the banking crises resulted in a tremendous workload for DRR and the need for management to ensure resources were efficiently utilized. We also recognize that the ORE Department is working to ensure all ORE assets have approved budgets. DRR has also informed us that they are in the process of creating a more efficient and effective budget tracking system. Therefore, we are not recommending further corrective action. However, we encourage DRR to ensure that initiatives to update policies, procedures, and systems for the review, approval, and tracking of ORE property budgets receive the resources necessary to accomplish this task in a timely manner.

Corporation Comments and OIG Evaluation

The Director, DRR, provided a written response, dated September 21, 2012, to a draft of this report. The response is presented in its entirety in Appendix 4. In the response, the Director concurred with all three of the report's recommendations and described completed and planned corrective actions to address the recommendations.

A summary of the Corporation's corrective actions is presented in Appendix 5. The completed or planned actions are responsive to the recommendations, and the recommendations are resolved.

Objective, Scope, and Methodology

Objective

Our audit objective was to assess control activities associated with DRR's processes for managing, marketing, and disposing of ORE. We conducted this performance audit from November 2011 to May 2012 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Scope and Methodology

The scope of this audit included the FDIC's active ORE asset inventory as of December 1, 2011 and ORE disposed of from January 1, 2011 through November 30, 2011. The scope of our work was limited to control activities performed by DRR Account Officers and other DRR personnel as described in the report. We did not conduct procedures related to ORE contractors' oversight of subcontractors or other internal procedures of the ORE contractors.

To assess control activities, we gained an understanding of DRR's control objectives and processes related to managing, marketing, and disposing of ORE by interviewing cognizant officials and reviewing relevant policies and procedures. This included obtaining an understanding of DRR's processes for updating and utilizing DRR's 4C system, FACTS, and contractor Web sites. Specifically, to understand the control objectives and processes, we:

- Interviewed DRR officials in the FDIC's DRO, ECTSO, and MWTSO.
- Interviewed managers, Account Officers and other personnel in DRR's ORE, Contract Oversight, and Accounting Department.
- Interviewed contracting officials in the FDIC's Division of Administration.
- Interviewed the Financial Reporting Manager of Prescient Asset Management, Inc., in Coral Gables, Florida.
- Interviewed the Corporate Comptroller of Quantum Partners, in Houston, Texas.
- Reviewed DRR's ARM and other guidance related to managing, marketing, and disposing of ORE assets.

As shown in Tables 1 and 2, to test the effectiveness of control activities, we judgmentally selected 25 active ORE assets assigned to ORE contractors as of December 1, 2011 and 30 inactive ORE assets from January 1, 2011 to November 30, 2011.

Table 1: Active ORE Sample

ORE Property Type	Number of ORE Assets	Total Appraised Value
Multi-Family	4	$102,075,000
Single-Family Residence	4	$1,107,000
Bank Premises	4	$9,642,000
Retail	3	$2,890,000
Land	3	$10,210,000
Industrial	2	$1,015,000
Office	2	$2,680,000
Other	2	$640,000
Lodging	1	$1,213,000
Total	**25**	**$131,472,000**

Table 2: Inactive ORE Sample

ORE Property Type	Number of ORE Assets	Total Appraised Value
Multi-Family	3	$4,620,000
Single-Family Residence	6	$11,355,000
Bank Premises	3	$17,845,000
Retail	3	$8,290,000
Land	3	$3,230,000
Industrial	3	$2,780,000
Office	3	$6,995,000
Other	3	$11,145,000
Lodging	3	$3,892,000
Total	**30**	**$70,152,000**

Our samples were based on the highest dollar amount related to property type, DRR satellite office, and ORE contractor hired to manage and market ORE assets. In addition, we conducted property inspections of 10 active ORE assets that were not included in our testing sample. None of the sampling techniques that we used can be projected to the intended population by standard statistical methods. Specifically, we:

- Reviewed documentation of Budget Cases, Environmental Assessment, tax payments, property and liability insurance, cost monitoring, property inspections, appraisals, and 4C inventory information for 25 active ORE assets.
- Conducted property inspections of 12 active ORE assets to verify property maintenance and that sales information were clearly displayed.

- Reviewed information on congressional inquiries and consumer complaints related to ORE assets in our active ORE sample.
- Verified receipt of HUD-1 [6] Settlement Statements, documentation of wired sales proceeds to receivership accounts, accuracy of journal entries to the Metavante Servicing System, and sales records in the 4C System for 30 ORE sales.
- Reviewed timeframes for posting ORE sales activity to the 4C System and applicable receivership accounting records.
- Verified whether sales were based on current appraisals and that approved sales cases were properly documented.
- Verified whether ORE Budget Cases were properly approved for 30 inactive ORE assets.
- Evaluated the transition of ORE assets from the former WCTSO to the DRO.

We used non-statistical sampling techniques to support the findings, conclusions, and recommendations in this report. We performed the audit work at the FDIC's offices in Arlington, Virginia; and Dallas, Texas.

Internal Control, Reliance on Computer-processed Information, Performance Measurement, and Compliance with Laws and Regulations

Consistent with the stated objective, we focused on control activities as described above and did not assess the DRR's overall internal control or management control structure. We obtained data from the DRR's information systems; however, we did not assess the information systems controls other than verifying the accuracy and completeness of data recorded in DRR's 4C system and the Metavante Servicing System for sampled items by tracing information from supporting documentation to the systems.

The Government Performance and Results Act of 1993 (the Results Act), as amended, directs Executive Branch agencies to develop a customer-focused strategic plan, align agency programs and activities with concrete missions and goals, and prepare and report on annual performance plans. For this audit, we assessed DRR's 2012 Divisional Goal for enhancing DRR's management reporting related to the FDIC's ORE inventory maintained in the 4C System.

Regarding compliance with laws and regulations, we performed limited tests to determine compliance with certain aspects of the *FDI Act Section 11(d) Powers and Duties of Corporation as Conservator or Receiver* and did not identify any instances of noncompliance. We assessed the risk of fraud and abuse in designing our test procedures and in the course of evaluating audit evidence.

[6] U. S. Department of Housing and Urban Development Settle Statement (HUD-1).

Glossary of Terms

Term	Definition
Book Value	The value of an ORE asset established from the balance sheet of the failed financial institution.
Contractor	An individual, corporation, partnership, joint-venture, or other third-party entity that enters into a contract with the FDIC to provide goods, services, or other requirements pursuant to its terms and conditions.
General Ledger	A consolidation of all FDIC financial accounts and records from which the FDIC's financial statements are created. The General Ledger is supported by subsidiary ledgers detailing specific financial accounts.
Management Fees	Fees billed to the FDIC by ORE contractors that are established at a standard rate, generally billed monthly, and documented in a contract for specified services to be performed.
Pass-Through Costs	Generally, these costs include expenditures that satisfy unfunded commitments, such as construction advances, or that protect the FDIC's interest in an asset, such as appraisal fees, property inspection costs, landscaping, repairs, and maintenance.
Property Inspection Reports	A standard report completed during inspection of an ORE property. The report includes a description of the surrounding neighborhood, evaluates property maintenance, recommendations for repair or maintenance, and other marketing concerns to be addressed.
Purchase and Assumption Agreement	An agreement documenting the sale of assets and assumption of liabilities between the receivership and acquiring institution.
SharePoint Site	A Web site designed for managing and organizing documents that need to be stored, found, and collaborated on, updated, managed, documented, traced, or restored.
Subcontractor	An individual, corporation, partnership, joint-venture, or other third-party entity that has entered into a contract with an FDIC contractor to perform work on behalf of the FDIC.
Subsidiary Ledger	A group of similar financial accounts whose combined balances equal the balance in a specific general ledger account.
Task Order	Orders for the acquisition of goods or services, issued under a Basic Ordering Agreement with a contractor.

Acronyms

4C	Communication, Capability, Challenge, and Control System
ARM	Asset Resolution Manual
CTM	Control Totals Module
DIF	Deposit Insurance Fund
DRO	Dallas Regional Office
DRR	Division of Resolutions and Receiverships
ECTSO	East Coast Temporary Satellite Office
FACTS	FDIC Automated Corporate Tracking System
MWTSO	Midwest Temporary Satellite Office
NFOB	National Field Office Branch
ORE	Owned Real Estate
SMOC	Senior Management Oversight Committee
WCTSO	West Coast Temporary Satellite Office

Corporation Comments

FDIC

550 17th Street NW, Washington, D.C. 20429-9990 Division of Resolutions and Receiverships

DATE: September 21, 2012

MEMORANDUM TO: Stephen M. Beard
Deputy Inspector General for Audits and Evaluations

FROM: Bret D. Edwards, Director /**Signed**/
Division of Resolutions and Receiverships

SUBJECT: Response to Draft Audit Report Entitled, *DRR's Controls for Managing, Marketing, and Disposing of Owned Real Estate Assets (Assignment No. 201 1-064)*

This memorandum is in response to the recommendations in the subject draft audit report dated August 22, 2012.

DRR has been working with the OIG to coordinate the audit involving Owned Real Estate (ORE) assets. DRR appreciates the many relevant observations and recommendations provided by the OIG. We look forward to working with the OIG to ensure that the oversight of ORE conforms to all applicable program area objectives.

OIG Audit Recommendation 1: Develop a process for comparing actual costs incurred on ORE assets to approved budgets.

> DRR Response: The ORE group concurs with the recommendation and together with BOS, BIS, DOA Contracting and Contract Oversight, the group is developing a mechanism to capture actual expenses from NFE and compare these to the expenses under the approved budget. The process being developed is similar to that available prior to the implementation of 4C; allowing the capture or expenses at the asset level. This will require certain contract modifications to ensure standardization in reporting and would entail modification to those contracts that provide services outside the scope of the Nationwide ORE Contractors such as, appraisals, environmental assessments, etc. With future enhancements to ORE Tracker and DIT assistance in the capturing and feeding of expenses from NFE to ORE Tracker, the ORE group should be in a position to develop a process to compare actual to budgeted expenses at the asset level.
>
> This project is expected to be completed prior to August 31, 2013.

OIG Audit Recommendation 2: Establish standard location for filing property inspections reports to be readily available to all DRR personnel that may become involved with managing the property.

> DRR Response: The ORE group agrees with the recommendation. Going forward the inspection report data will be housed in the ORE SharePoint site which can be accessed by all ORE personnel.

DFOB personnel are in the process of updating, classifying and grouping all ORE inspections performed under the Contract Oversight Inspection Program (COPS) and the inspections conducted by TSO personnel.

Completion date of this project is expected by November 30, 2012.

OIG Audit Recommendation 3: Enhance procedures for the transfer of ORE assets between Account Officers in a manner that facilitates communication and document sharing.

DRR Response: The ORE group agrees with the recommendation.

Although the internal transfer of assets within R&R Specialists in the same department is not recommended, at times it is necessary. A specific job aid has been developed to ensure proper asset transfer protocols are followed and is available for review upon request.

It is noted that simultaneous with the transition of the WCTSO ORE assets into the Dallas Office, three of the five National ORE Contractors portfolios were also being transitioned into two remaining ORE Contractors (Prescient & Quantum). CBRE, one of the two original ORE Contractors, practically the most experienced, and the contractor with the most assets was being transitioned at the same time the WCTSO was being closed. The initial OIG interview process with the DFOB R&R Specialist occurred in the early part of the first quarter of 2012, at a time when ORE assets were being absorbed by the DFOB ORE staff.

Lessons learned from the WCTSO transition have been implemented with noted differences in processes being used to transition the MWTSO ORE/OOA assets into DFOB.

Summary of the Corporation's Corrective Actions

This table presents corrective actions taken or planned by the Corporation in response to the recommendations in the report and the status of the recommendations as of the date of report issuance.

Rec. No.	Corrective Action: Taken or Planned	Expected Completion Date	Monetary Benefits	Resolved:[a] Yes or No	Open or Closed[b]
1	DRR is developing a mechanism to capture actual expenses and compare these to the expenses under the approved budget. The process being developed is similar to that available prior to the implementation of 4C; allowing the capture of expenses at the asset level.	08/31/2013	$0	Yes	Open
2	Going forward, the inspection report data will be housed in the ORE SharePoint site, which can be accessed by all ORE personnel. DRR personnel are in the process of updating, classifying and grouping all ORE inspections performed under the Contract Oversight Inspection Program and the inspections conducted by Temporary Satellite Office personnel.	11/30/2012	$0	Yes	Open

3	A specific job aid has been developed to ensure proper asset transfer protocols are followed and is available for review upon request. Lessons learned from the WCTSO transition has been implemented with noted differences in processes being used in the transition for the MWTSO.	09/21/2012	$0	Yes	Closed

[a] Resolved – (1) Management concurs with the recommendation, and the planned, ongoing, and completed corrective action is consistent with the recommendation.
(2) Management does not concur with the recommendation, but alternative action meets the Intent of the recommendation.
(3) Management agrees to the OIG monetary benefits, or a different amount, or no ($0) amount. Monetary benefits are considered resolved as long as management provides an amount.

[b] Recommendations will be closed when (a) Corporate Management Control notifies the OIG that corrective actions are complete or (b) in the case of recommendations that the OIG determines to be particularly significant, when the OIG confirms that corrective actions have been completed and are responsive.