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General Accounting Office
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Accounting and Financial
Management Division

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August 14, 1992

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Mr. William H. Roelle
Chief Financial Officer
Resolution Trust Corporation

Dear Mr. Roelle:

We have issued our opinion on the financial statements of the Resolution Trust Corporation (RTC) for the year ended December 31, 1991, and have reported on RTC's internal control structure and on its compliance with applicable laws and regulations for the year ended December 31, 1991 (GAO/AFMD-92-74, June 30, 1992). We gave RTC an unqualified opinion on its 1991 statement of financial position and its statement of cash flows. However, because we could not obtain reasonable assurance that the expenses related to changes in the allowance for losses on subrogated claims and unresolved cases were not materially misstated, we were unable to express an opinion on the statement of revenues, expenses, and accumulated deficit as of December 31, 1991.

Through our review and tests of control procedures and our subsequent tests of year-end account balances, we identified several problems and opportunities for improvement in the consolidated offices' handling of receivership activity and in headquarters' operations. Although the deficiencies reported here did not affect our opinion on RTC's financial statements, we believe they merit corrective action.

CONSOLIDATED OFFICE INTERNAL CONTROL PROBLEMS

From October 5, 1991, through March 6, 1992, we reviewed and tested internal controls over cash receipts, cash disbursements, and beginning balances at 40 randomly selected and 22 judgmentally selected receiverships. Our sample of 62 was selected from the 396 receiverships established as of May 31, 1991. Because the accounting and asset management functions for receiverships are handled by personnel in RTC consolidated offices, our sample required us to visit 12 of the 15 consolidated offices. At those offices, we tested 1,474 cash receipt and disbursement

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transactions and 388 settlement jacket files, which contain the official support for receiverships' beginning account balances.

While RTC acted to correct internal control weaknesses identified in conjunction with our 1990 financial statement audit, we found that some consolidated offices still did not have adequate internal control policies and procedures in the areas we tested or did not comply with existing policies and procedures during 1991. We found both previously identified and new problems at the various consolidated offices we visited.

Asset Reconciliation Reports

Our detailed review of the asset reconciliation process at two consolidated offices showed that they were not reporting the variances between the book values of loans maintained by asset servicers[1] and those recorded in the receiverships' general ledgers as RTC required. Instead, consolidated office staff compared information in the receiverships' general ledgers to the receiverships' own subsidiary loan balances which provide a breakdown of the general ledger balances by asset servicer totals. Consolidated offices maintain these subsidiary balances as intermediate records for reconciling the individual asset servicers' reports to the total in the general ledger.

During our review, staff at one consolidated office stated that servicer asset balances are to be considered correct unless proven otherwise. However, the office acknowledged that it had reported the receivership subsidiary record balances rather than the servicer asset balances on the Asset Reconciliation Report (ARR) even though the office's own analysis showed that the servicer loan balances were correct. The other consolidated office could not determine why a servicer's balance did not match receivership subsidiary records; therefore, the office elected to use the subsidiary record balance rather than the servicer's balance on the ARR. As a result, these offices were not satisfying

[1]Asset servicers are contractually responsible for maintaining the official records and processing the transactions for individual loans or other assets belonging to RTC receiverships.

the intent of this report--to reconcile servicers' records to the receiverships' general ledgers and report any differences.

RTC requires that asset and/or accounting operations personnel prepare an ARR to document any dollar variance between the book value of assets reported by the asset servicers or other asset systems of record and the receiverships' general ledger. Consolidated office staff were to identify, investigate, and resolve the documented differences. Any unreported differences between servicer loan records and the general ledger increase the possibility that variances would go unresolved and that RTC would base asset management and sales decisions on inaccurate data.

According to RTC management, the conversion to a new asset reporting system, the Control Totals Module (CTM), will resolve this problem. CTM has features to identify out of balance conditions and to require consolidated offices to reconcile receivership intermediate subsidiary records to the general ledger daily. The ARR will then be used to identify differences between the asset systems of record and the receiverships' general ledgers. However, we suggest that RTC emphasize to all consolidated offices that servicer-reported asset balances are the system of record for loans on CTM and that consolidated offices need to maintain the servicer reports of asset balances to support the accuracy of CTM data. We also suggest that RTC ensure that personnel in RTC consolidated offices have identified and resolved all of the outstanding variances that existed between servicer records and receivership subsidiary records when data were converted to CTM.

Asset Suspense Accounts

Consolidated office personnel are not clearing items from suspense accounts promptly. We found that 44 transactions in 19 receiverships were in suspense accounts for over 30 days and that 39 of these transactions were in suspense for more than 60 days. RTC established suspense accounts to hold items that could not be identified for same day posting or that required additional approval prior to processing. For example, general ledger account 1981--Cash Collections in Process--holds monetary items, such as principal, interest, late fees, and escrow, until documentation detailing the allocation of the funds is received from asset servicers.

In May 1991, RTC issued its Asset Operations Manual which required suspense items to be researched, identified, and posted within 5 working days from receipt of cash. Many consolidated offices told us that this time frame for clearing the asset suspense accounts was not reasonable. Three consolidated offices stated that they did not receive, from the servicer, the supporting documentation necessary to clear the accounts within the required 5-days. In addition, one stated that the analysis of complex transactions involving more than one receivership often takes several days. The accuracy of account balances depends on the prompt clearing of suspense accounts. Until suspense accounts are cleared, balances in related asset, liability, income, and expense accounts are inaccurate and staff cannot determine whether RTC has received all monies due.

As of March 1992, RTC reported that consolidated offices had reduced suspense account balances due to increased resource allocation, early identification of problem items, and close monitoring of aging account balances. In addition, the offices have planned or are acting to (1) establish suspense item management as a performance goal to be measured and (2) implement a system to identify and reconcile cash suspense items earlier.

Efforts to monitor and clear suspense accounts can only be successful if asset servicers promptly provide consolidated office staff with adequate documentation to support cash collected and remitted. We believe that RTC's current criteria, requiring suspense items to be posted within 5 working days from receipt of cash, is not practical given their delays in receiving necessary documentation. We suggest that RTC require asset servicers to provide the necessary information within 30 days of cash remittance. Because cash collections are sometimes net of other fees, servicers should clearly account for gross collections, not just those remitted to the office. In addition, we suggest that RTC's criteria specify that cash remitted by servicers be cleared from suspense accounts within 5 working days of receipt of supporting documentation.

<u>Interest Expense</u>

RTC's corporate funding group advances funds to receiverships when their cash is not sufficient to meet their needs. As cash later becomes available, receiverships must repay RTC the amount advanced plus interest. According to RTC management, the repayment process incorporates periodic reconciliations of receivership and RTC records and requires regional/consolidated office personnel to notify the RTC corporate funding group of any discrepancies in principal or interest owed. RTC management told us that this requirement implies a recalculation of interest by consolidated office personnel. Furthermore, RTC management stated that the purpose of this requirement is to (1) provide verification for the RTC funds tracking system, which is used to calculate advance interest accruals and the allocation of advance repayments, and (2) facilitate periodic reconciliations of RTC corporate funding and regional office records. Substantiating the amount of interest owed also ensures that receiverships are not over or underpaying interest to RTC.

Seven of the 12 consolidated offices we visited were not recalculating interest due on RTC cash advances. Five of these offices stated that they relied on figures reported by headquarters; one reported that the information necessary to perform the recalculation was not provided by headquarters; and one provided no explanation but later implemented a policy requiring that the recalculation of interest be performed prior to repayment. One consolidated office, which stated it did perform interest recalculations, was unable to provide us with any evidence of recalculation for 12 of the 20 advances tested.

We suggest that RTC establish a written policy that specifically requires consolidated office personnel to recalculate interest due on advances prior to repayment and to report any discrepancies to the RTC corporate funding group. We also suggest that the policy include a requirement that the consolidated offices develop and maintain documentation to support the interest recalculation for each receivership.

Duplicate Payments

Three consolidated offices told us that they did not have controls in place to detect duplicate payments. All three offices stated that the Field Accounts Payable System, which processes expenses chargeable to a specific receivership, does not have edit checks to detect duplicate payments. According to RTC management, program changes were not made to remedy this control weakness. However, as of November 1990, RTC required Field Accounts Payable personnel to verify that all invoices paid were (1) paid from original invoices and that (2) balances carried forward were valid.

A fourth office reported that controls were in place to detect duplicate payments, but original invoices were not being voided after payment was made. According to that office's personnel, voiding original invoices was not necessary because all payments require an original invoice which is attached to the check request and retained under the control of the accounts payable unit.

To avoid possible duplicate payments, RTC requires that consolidated office staff only pay on original invoices and that they investigate old[2] invoices or invoices submitted for payment more than once. If a duplicate copy is submitted for payment, it must have a notation from the originating department stating that the original invoice was never submitted. RTC does not specifically require that original invoices be voided after payment. However, without adequate controls to prevent and detect duplicate payments, receiverships could overpay creditors thereby reducing the funds available for payment to RTC.

RTC is developing a new accounts payable/purchase order system, which will replace the Fields Accounts Payable System. According to RTC management, this system will be implemented in November 1992 and will contain all the necessary edit checks to prevent and detect duplicate payments. However, to minimize the possibility of processing the same invoice twice, we suggest that all consolidated offices be required to void original invoices after payment.

Journal Entries

Some consolidated offices were not following proper procedures for processing journal entries. We identified 17 transactions for which consolidated office staff did not review journal entries prior to input into the receivership's general ledger. We also noted that four consolidated offices had delegated the journal entry review function to contractors. Finally, we found that transactions were recorded to the wrong accounts at 7 of the 12 consolidated offices we visited. Most of these errors were made to miscellaneous accounts.

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[2]In April 1992, RTC issued its Field Accounting Manual which defines "old" as invoices over 60 days.

RTC requires that all journal entries be reviewed by appropriate personnel[3] prior to posting to the general ledger. The reviewer of the journal entry is responsible for ensuring that the associated documentation supports the dollar value and general ledger account numbers assigned. The reviewer must sign and date the journal entry voucher to certify its accuracy. The review function provides assurance that general ledger accounts are being posted accurately and in accordance with management's policies. Without proper review of journal entries prior to input, account balances could be misstated.

We suggest that RTC enforce its requirement that consolidated office personnel review all journal entries to ensure they are accurate and supported. We also suggest that the review function be performed by office employees familiar with the chart of accounts and that journal entry review not be delegated to contractor employees. In addition, we suggest that RTC identify infrequent/unusual transactions, document the appropriate journal entries for recording these transactions, and require all consolidated offices to follow the new guidance.

Wire Disbursements

Some consolidated offices are not posting disbursement transactions in a timely manner. Of the 393 wire disbursement transactions tested, we found that 37 had not been posted to the general ledger until 6 to 10 days after the date of disbursement. An additional 24 transactions were not posted until more than 10 days after the date of the disbursement.

RTC requires that consolidated office staff process disbursements on a timely basis. However, "timely" is not defined. Delayed reporting of disbursements results in overstated receivership cash balances. Because RTC and consolidated office staff use receivership cash balances to determine the amount available for repayment of RTC advances and for dividends, inaccurate balances could result in

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[3]RTC's Field Accounting Manual requires that all journal entries be reviewed and approved in the originating department by a person who is at least the preparer's immediate supervisor or designee and by personnel in the General Ledger Function.

payments to RTC that leave the receivership without sufficient cash to meet its other obligations.

We suggest that RTC establish a time limit for posting disbursement transactions to the general ledger and establish a written policy for recording transactions within that period.

Segregation of Cashiering Tasks

As of December 31, 1991, one consolidated office reported that cashiering tasks were still not segregated. In that office, for example, the cashier who prepared the deposit slip also checked the deposit for accuracy. This included comparing the total on the deposit slip with the total receipts. Office staff attributed the lack of segregation to the insufficient number of employees within the cashier's unit available to perform such tasks.

The cashier function is responsible for ensuring the proper segregation of duties and the safeguarding of all monetary items. RTC requires that the cashiering tasks be rotated among cashier personnel. Without proper segregation of duties, a cashier is in a position to both perpetrate and conceal errors or irregularities relating to monetary items.

We suggest that RTC require all consolidated offices to properly segregate cashier duties from tasks related to receiving, processing, or recording monetary items. In addition, we suggest that all consolidated offices develop procedures for periodically rotating cashier duties. We also suggest that consolidated offices with limited staff reassign the various cashiering tasks, as appropriate, among personnel throughout the General Ledger Function.

Settlement Jacket Files

Settlement jacket files (jackets) for some receiverships do not contain an accurate listing of the jacket documents that support the receivership beginning balances. Of the 388 jackets reviewed, 60 did not have any table of contents, 40 had items listed on the table of contents that were not in the jacket, and 97 had items in the jacket that were not listed on the table of contents.

Jackets, prepared by RTC teams that close failed institutions, become the official support for receiverships' beginning account balances. These jackets typically include letters requesting verification of account balances, responses to those letters, exception lists, and narratives of action taken. RTC relies on the documentation in the jackets to (1) provide information supporting beginning account balances, (2) aid in the production of an asset inventory, and (3) provide the initial step in testing the integrity of events subsequent to the closing of the institution. Without an accurate listing of all documents maintained in the jackets, consolidated office personnel have little control over file contents--information could be deleted or inserted without leaving any evidence of change.

We suggest that RTC establish a written policy requiring that a complete table of contents be prepared for every settlement jacket and that the table of contents be updated if any information is added to the file after closing. We also suggest that the policy state that item descriptions in the table of contents must correspond to the documents in the jacket.

HEADQUARTERS' INTERNAL CONTROL PROBLEMS

From November 16, 1991, through May 15, 1992, we reviewed and tested internal controls over RTC headquarters operations concerned with resolved institutions, unresolved institutions, Federal Financing Bank borrowings, cash receipts and disbursements, and the processing of journal entries for the general ledger and preparation of financial statements. We also performed tests of account balances throughout the year and at year-end. Our tests did not uncover any material deficiencies in the design or operation of headquarters' internal control structure. However, we did note other less significant problems that warrant management's attention.

General Ledger Account Reconciliations

Headquarters' staff did not reconcile some accounts properly or promptly. For example, we found that

-- Account 1122 (Accounts Payable-APS) had not been reconciled with accounts payable reports and subsidiary ledger balances since June 1991. Because staff were unsure of the reliability of the reports and ledger balances related to this account, they were unable to prepare the December 31, 1991, reconciliation.

-- Account 0356 was not properly reconciled as of December 31, 1991. The general ledger was reconciled to a subsidiary ledger that did not reflect current information and general ledger adjustments identified were not recorded. In addition, staff were unable to provide supporting documentation for 7 of the 15 reconciling items for that month. Several monthly reconciliations for 1991 could not be located.

-- Account 1124 (Government Agencies Payable) was not reconciled as of December 31, 1991. Therefore, we were unable to reconcile the amount RTC recorded as a payable to the Bank Insurance Fund with the amount the Bank Insurance Fund had independently recorded as a receivable from RTC.

-- Reconciliations for account 1219 (Validated Federal Tax Deposit Receipts) were not properly maintained. RTC staff were unable to provide us with several of the monthly reconciliations necessary to research a posting error noted in our testing. The error had been made early in 1991 but was not corrected until February 1992.

-- The accounting group has never reconciled the general ledger accounts which are used to record cash (0612-Recovery on Subrogated Claims Paid) and noncash (0619-Non-cash Recovery on Subrogated Claims) dividends with the subsidiary ledgers maintained by the corporate funding and claims groups. Our tests uncovered numerous differences between the general ledger balances and subsidiary records.

RTC does not have a written policy requiring prompt reconciliations and the maintenance of supporting documentation. However, according to RTC management, the account reconciliation process is considered an integral part of its normal accounting practices and procedures. As such, management expects reconciliations to be performed regularly and any adjustments to be processed promptly. Reconciliations are control procedures that provide an independent check on performance and proper valuation of recorded amounts. Without reconciliations, errors in account balances could go undetected. In particular, without accurate cash and noncash dividends records, RTC cannot be sure it has received all subrogated claims recoveries to which it is entitled.

In June 1992, RTC established the Reconciliation Working Group to review and reconcile each general ledger account. We suggest that this group establish and enforce written policies and procedures to regularly reconcile general ledger account balances to subsidiary ledgers or related accounts. In addition, we suggest that the policies and procedures require that reconciliations be supported by adequate documentation and be reviewed and approved by staff at appropriate levels.

Wire Disbursements

The cash management unit was processing some corporate wire disbursements without the required approval of the corporate funding group. We found that 2 of the 25 payment authorization vouchers we tested as part of our work on account 0611 (Subrogated Claims Paid Depositors) and account 0621 (Corporate Disbursements-Receivership) were missing authorizing signatures approving the disbursement of funds. Corporate funding indicated that the omitted signatures were probably due to the volume of payment authorization vouchers processed daily.

RTC requires that wire disbursements be supported by payment authorization vouchers. Corporate funding staff are required to approve a payment authorization voucher prior to funds being disbursed. Without proper approval, disbursements could be made for improper purposes or to the wrong entities.

We suggest that RTC enforce its policy that requires the cash management unit to ensure corporate funding has approved the payment authorization vouchers before requesting the Department of the Treasury to disburse any funds.

General Ledger Account Usage

Headquarters' staff were using certain general ledger accounts in ways that were inconsistent with account descriptions. For example, we found that account 3442 (Income From the Sales of Reports of Condition, Income and Public File Documents) was not used during 1991 to record income from the RTC Reading Room. Instead, such revenue was recorded in account 3455 (Miscellaneous RTC Generated Income) and refunds of RTC seminar fees were inappropriately posted to account 3442. Headquarters' staff were also improperly using account 1169 (Miscellaneous Payables) to record year-end accruals that should have been recorded in account 1123 (Publics Payable-Other). Inconsistent treatment of transactions could result in misstated account balances and misleading management reports.

RTC is creating the chart of accounts to be used with its new general ledger system, the Financial Management System. We suggest that RTC ensure that account descriptions match intended account usage and that general ledger transactions are recorded, reviewed, and approved by employees knowledgeable about proper account usage.

Administrative Operating Expenses

Of the 57 administrative operating expense transactions tested, we found that eight location codes and/or account numbers had been transferred incorrectly from the supporting documentation to the general ledger. RTC relies on Federal Deposit Insurance Corporation (FDIC) staff to prepare and post these operating expense transactions. An incorrect location code could result in expense recovery from the wrong institution. Other coding errors could result in incorrect individual account balances.

For another three transactions, FDIC staff were unable to provide supporting documentation for the recorded expenses because of problems with vendor identification numbers or with regional documentation. Without proper supporting documentation, neither FDIC nor RTC staff can verify the validity and accuracy of transactions entered in the general ledger.

We suggest that RTC ensure that FDIC staff verify all data entered into the general ledger for accurate input. We also suggest that RTC enforce the requirement in its Circular 1250.1, "Internal Control Systems," that staff document all financial transactions from inception through recording in the general ledger and make these documents available to managers and auditors. In addition, we suggest that RTC ensure that supporting documentation is properly maintained in files to facilitate transaction review.

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We have discussed these issues with the Assistant Vice President of the Department of Contracts, Oversight, and Evaluation; the Director of the Office of Accounting Services; and the Director of the Office of Field Accounting and Asset Operations. We would appreciate your response to our suggestions. We will follow up on planned corrective actions as part of our audit of RTC's 1992 financial statements. If you would like to discuss any of these issues, please contact Molly Boyle, Assistant Director, on (202) 275-9524.

Sincerely yours,

Robert W. Gramling

Robert W. Gramling
Director, Corporate Financial Audits

cc: The Honorable Albert V. Casey
Chief Executive Officer
Resolution Trust Corporation

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