

GAO

Report to the Chairman, Committee on
Banking, Housing and Urban Affairs
U.S. Senate

June 1993

THRIFT FAILURES

Actions Needed to Stabilize RTC's Professional Liability Program



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General Government Division

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June 28, 1993

The Honorable Donald W. Riegle, Jr.
Chairman, Committee on Banking, Housing
and Urban Affairs
United States Senate

Dear Mr. Chairman:

Over the past year the Resolution Trust Corporation's (RTC) professional liability program has been embroiled in controversy concerning how aggressive its efforts have been in pursuing civil claims against professionals for losses they may have caused in connection with failed thrifts. The objective of this program is to pursue professional liability claims against former officers and directors, as well as other professionals such as attorneys and accountants who caused losses to failed thrifts that RTC is responsible for resolving. The attorneys responsible for this work are located in RTC's Division of Legal Services' Professional Liability Section (PLS).

On August 11, 1992, in testimony before your committee,¹ we said that staffing shortages and reorganizations had disrupted RTC's professional liability program. Three attorneys who formerly served as PLS managers also testified at the hearing and criticized the management of PLS. They said that RTC had seriously damaged the professional liability program through, among other things, its staffing and restructuring decisions and that these decisions may have been motivated by a desire to undercut the program. In a hearing before your Committee on October 1, 1992, Mr. Albert V. Casey, then RTC's President and Chief Executive Officer (CEO), rejected these allegations and maintained that "due to the reorganization, the [PLS] program is stronger today than it has ever been."

Your letter of October 8, 1992, requests our response to Mr. Casey's October 1 testimony. In addition, at the August 11 hearing and in subsequent discussions with the Committee, you asked that we assess the impact of various management changes on the PLS program and continue to monitor PLS staffing and the filing and disposition of PLS cases. You also asked that we identify steps that need to be taken to maintain the PLS program as RTC is dissolved and various functions transferred to the Federal Deposit Insurance Corporation (FDIC). This report responds to these requests.

¹Bank and Thrift Failures: RTC Needs to Improve Planning for Professional Liability Staff Changes (GAO/T-GGD-92-69, Aug. 11, 1992).

Results in Brief

We found no evidence that the staffing actions and reorganizations RTC took affecting PLS were designed to impede the professional liability work. In addition, we found that RTC litigation policy still supports negligence claims and claims against outside directors. Nevertheless, some of the management actions taken by RTC, as they affected PLS, were ill-conceived and poorly implemented. As a result, RTC's decisions to consolidate and reassign PLS attorneys demoralized PLS staff and disrupted the program.

One half of the PLS attorneys have left the program since March 31, 1992. While other attorneys have been hired, the high turnover rate has resulted in a high proportion of PLS attorneys with less experience than needed. RTC officials told us that attorneys without prior professional liability experience generally need 12 to 18 months of experience in PLS to get through the learning curve. Yet as of the end of March 1993, 45 percent of the PLS attorneys had less than 12 months' experience.

Much of RTC's professional liability work still remains to be done. As of March 1, 1993, the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA)² 3-year statute of limitations (SOL) period had not yet expired for filing claims associated with almost half of the thrifts placed under RTC control. RTC also had more than 200 PLS claims open as of the end of February 1993 that the PLS attorneys needed to monitor and manage.

The Secretary of the Treasury has recognized the need for management attention to the RTC PLS program. In March 1993, he required the RTC CEO and President to review the staffing and organization of RTC's PLS program.

With the pending dissolution of the agency and much of the professional liability work remaining, RTC needs to better plan for the future of the program. Uncertainties regarding the future of the agency and the closing of offices will undoubtedly result in additional turnover. RTC needs to take these factors into account when carrying out the Secretary of the Treasury's request to study the PLS program. In addition, RTC, in consultation with FDIC, needs to focus on actions that will increase the stability of the program.

Background

RTC pursues professional liability claims against those whose alleged professional misconduct caused losses to failed thrifts. This misconduct could involve misappropriation of funds, negligence, breach of fiduciary

²Public Law 101-73, 103 Stat. #103.

duty, breach of contract, or fraud. The claims are brought against directors, officers, accountants, attorneys, commodities and securities brokers, appraisers, and insurance carriers, among others.

PLS attorneys are to work with investigators from RTC's Office of Investigations to identify viable claims. The goal of these attorneys and investigators is to pursue claims when a sufficient factual and legal basis exists to demonstrate liability and when the expected recovery exceeds the cost of litigating the claim.³ Among other things, the investigators are to determine the losses to an institution, identify potential claims and sources of recovery, and select and supervise contract investigators. The attorneys' responsibilities include making legal analyses and determinations; recommending whether to close out, sue, or settle claims; and selecting and overseeing the outside counsel who litigate the claims. Through the end of February 1993, RTC had filed about 250 claims for approximately \$8 billion.

RTC is responsible for resolving thrifts failing between January 1, 1989, and September 30, 1993. The agency is to cease operating by December 31, 1996. FDIC will generally become responsible for (1) resolving those thrifts that fail after September 30, 1993, and (2) completing the resolution of thrifts remaining in RTC's inventory when it is abolished. Professional liability claims are assets of the failed associations; therefore, collecting them is part of the resolution process.

Objectives, Scope, and Methodology

Our objectives in this review were to (1) assess the impact of the reorganization and downsizing on the PLS program, (2) determine whether RTC changed litigation policies regarding negligence claims and claims against outside directors, (3) provide updated information on staffing and the filing and disposition of PLS cases, and (4) outline steps RTC needs to take to maintain a viable PLS. As a part of this review we looked into allegations made by the former PLS managers at the August 11, 1993, hearing and the former RTC CEO's response to those allegations at your October 1, 1993, hearing. Specifically, RTC's former CEO responded to the former managers' allegations that

- RTC implemented policies and practices that impeded the pursuit of thrift directors who harmed their thrifts,
- Division of Legal Services management engaged in a "turf war" that weakened the PLS program, and

³According to RTC, exceptions may be made for deterrent or precedential purposes.

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- the individuals now responsible for the PLS program are inexperienced and unqualified.

To meet these objectives, we interviewed the 3 former managers who made the allegations, 21 other former and current PLS managers and staff attorneys, and 6 Division of Legal Services managers with responsibility over the PLS program. We also interviewed RTC officials in Investigations and other officials outside the Division of Legal Services who were associated with the PLS program or RTC's downsizing effort. We interviewed counsel from three firms that RTC hired to handle some of the cases associated with the former managers' allegations.

We reviewed, among other things, Mr. Casey's testimony along with the extensive materials he submitted at the October 1, 1992, hearing before your Committee and the testimony of the three former managers given at the August 11, 1992, hearings. We reviewed PLS files on specific professional liability cases that the former managers cited to us to illustrate their allegations. We gathered information from headquarters staff on PLS staffing levels and operations and analyzed PLS case data maintained in an RTC PLS database. We did not independently verify the database and staffing data.

Our work was done in Dallas, Denver, Atlanta, Kansas City, and Washington, D.C., between July 1992 and March 1993 in accordance with generally accepted government auditing standards.

Organizational and Staffing Changes Affected the PLS Program

Organizational and staffing changes made in 1992 have affected the PLS program by contributing to staff turnover and low morale and increasing the potential for inconsistent application of PLS practices. However, we found no evidence that the changes RTC made were designed to impede the professional liability work.

We testified in June 1992⁴ that since its formation in 1989, the PLS program has been subject to numerous changes. When RTC was created, the PLS attorneys handling RTC professional liability claims were part of FDIC's professional liability staff. In August 1990 a separate RTC legal branch was formed at FDIC to which the RTC PLS attorneys were assigned in January 1991. In September 1991 a separate RTC Legal Division was established.

⁴Bank and Thrift Failures: FDIC and RTC Could Do More to Pursue Professional Liability Claims (GAO/T-GGD-92-42, June 2, 1992).

Within the RTC legal branch at FDIC and then the RTC Division of Legal Services, PLS retained a centralized structure that generally followed the PLS model used by FDIC for its own professional liability work and was distinct from the reporting structure for other RTC legal staff. Typically, the RTC legal staff in the consolidated field offices (CFOs) reported to the managing attorney in the CFO who, in turn, reported to the regional counsel.⁵ Similarly, the legal staff in each regional office reported to their regional counsel.

The PLS staff, however, bypassed the legal division field structure. They had a direct reporting line to the Assistant General Counsel-PLS (AGC-PLS) through the Section Chief-PLS in the consolidated field offices and the Counsel-PLS in the regional office. The AGC-PLS reported directly to the RTC General Counsel.

The principal organizational changes that occurred in 1992 consisted of two separate and distinct actions. The first, which restructured reporting lines within PLS, was confined to the Division of Legal Services. The second, a "downsizing and consolidation" of staff in field locations, affected RTC as a whole.

Restructured Reporting Lines

The first action involved the restructuring of PLS, which brought its reporting structure more in line with that of the rest of the Legal Division. Among other things, the PLS attorneys in the field began reporting to their regional counsels instead of the AGC-PLS in Washington. In addition, rather than reporting directly to the General Counsel, the AGC-PLS reported to the Associate General Counsel (Litigation). This restructuring was announced in January 1992 and was to be effective April 15, 1992.

Prior to the restructuring, there was considerable debate within the Division of Legal Services and between that Division and the Chief Financial Officer over how best to organize the PLS program. The then-incumbent PLS managers in Washington and the field generally preferred a highly centralized PLS structure along the lines of the FDIC model. They viewed this structure as facilitating program direction and making the best use of program expertise. On the other hand, non-PLS managers in the Division of Legal Services in headquarters and the field saw a need to better coordinate the PLS work with RTC's other work and to

⁵RTC began the process of restructuring its field operations in 1992 from 4 regions and 15 CFOs to 6 field sites.

provide the regional counsels with greater control over the attorneys operating in their regions.

There was a great deal of support for the PLS restructuring from the business side of RTC outside the Division of Legal Services, which is a client of the Division of Legal Services. The report accompanying Mr. Casey's October 1 testimony discusses the RTC Chief Financial Officer's reasoning and efforts to change PLS' reporting structure. The Chief Financial Officer told us that he had been pressing for the restructuring for a year before it occurred. He said that he wanted to get more business input into the PLS case process earlier than was occurring and to increase interaction between the field legal staff and the PLS staff.

The former PLS managers who testified at the August 11 hearing attributed the restructuring of PLS largely to a "turf war" within the Legal Division. Many of the current and former PLS attorneys we interviewed likewise believed that the restructuring was the product of a turf war between PLS and the rest of the Legal Division. They provided accounts of personality conflicts and tension between PLS managers and non-PLS attorney managers in certain locations, particularly the Atlanta, Dallas, and Denver regions.⁶

We found no evidence, though, that the restructuring was designed to impede the PLS program. According to RTC officials, the reason for postponing its implementation from January to April was to avoid disrupting the large number of professional liability cases for which the 3-year SOL was to expire during that period.⁷ Further, this restructuring did not affect the cases handled by the Washington-based PLS staff, which are generally the most significant professional liability cases. In fact, the AGC-PLS was expressly granted authority "to designate any individual PLS matter as a significant matter" and to assume control of it.

While elements of a turf war may well have been present, we have no basis to discount the management reasons that were cited in support of the restructuring described above. It is particularly significant that a major impetus for the restructuring came from the Chief Financial Officer of RTC, an official outside of the Legal Division with no apparent stake in the allocation of turf within the Legal Division.

⁶These problems did not exist in all field locations. For example, by all accounts the PLS and non-PLS attorneys in Kansas City enjoyed excellent working relationships.

⁷Generally, RTC brings professional liability claims that are subject to a 3-year SOL period. Other SOLs may be applicable, as is explained in footnote 15.

Although we do not question the decision to restructure PLS as a means of better integrating the PLS work with other RTC work, the restructuring lessened the direct supervisory and programmatic control over the PLS attorneys in the field formerly exercised by the PLS managers in Washington. The restructuring also introduced many new regional attorneys into the PLS decision-making process, some of whom lacked prior experience with the professional liability work. As a result, the decentralized PLS structure introduced the potential for fragmented program direction, inconsistent practices and decisions among the regions, and inadequate case development. We found differing views among field attorneys and between the field and headquarters about what attributes are needed for negligence claims and claims against outside directors and about headquarters' receptivity to borderline claims, as discussed in the next two sections. RTC PLS recently has implemented some procedures that should help to promote the consistent application of PLS policies and procedures.

Downsizing and Consolidation

The second major organizational action affecting PLS, which was announced in March 1992, was the agencywide "downsizing" and the consolidation of its 15 field locations into 6 "supersites." This downsizing is to be completed by September 1993. In May 1992, as part of the downsizing process, the Division of Legal Services, with no clearly delineated selection criteria, notified in writing 16 of the 73 PLS attorneys on board that they would be reassigned to FDIC.⁸ This reassignment of employees to FDIC is commonly referred to as employees being "put back" to FDIC. Among those designated for putback were 7 of the 21 PLS managers, including the 3 who testified before your Committee.

Again, we found no evidence that the staffing decisions made in conjunction with the downsizing were designed to undercut the PLS program. As noted above, this aspect of the reorganization affected all of RTC's field operations, not just PLS. Further, while several experienced PLS attorneys lost their management positions in the field, most of those individuals placed in management positions as a result of the reorganization also were already PLS field managers.

Although we found no evidence that RTC took these changes to undermine the PLS program, we believe the actions were poorly conceived and poorly implemented and call into question the priority that RTC attached to the

⁸RTC-assigned career employees have the right to return to FDIC as career employees. Of the attorneys on board as of May 21, 1992, 58 were career and 16 were temporary.

program. Managers in the Legal Division made the putback decisions using no clear criteria. In making the decisions they gave little regard to the specific institutions and claims for which the attorneys were responsible. The 16 PLS attorneys the Legal Division designated for transfer to FDIC collectively were responsible for 140 thrifts with assets totalling nearly \$37 billion. Additionally, as we said in our August 11, 1992, testimony, it is hard to understand why RTC would attempt to put back PLS attorneys to FDIC at a time when RTC's PLS workload was increasing. Nothing in the extensive materials submitted by RTC at the October 1 hearing explains these actions. Indeed, RTC eventually rescinded the putbacks and authorized an increase in the PLS staffing level.

The way in which the PLS staffing changes were carried out also engendered morale problems and a lack of confidence in RTC management. Many of the current PLS managers and line attorneys we interviewed said that the staffing decisions were made without any regard for their impact on the workload or on the individuals affected. They indicated that the personal preferences of attorneys were not considered and that attorneys were told with little notice that they would be relocated. Additionally, it was not always clear to the attorneys what decisions were being made. One current manager criticized the high degree of ineptitude RTC exercised in downsizing PLS. Several attorneys expressed concern that organizational and staffing matters affecting PLS have been in a constant state of flux. Many were concerned about the possibility of being subject to relocation again. One manager told us that it is hard for attorneys to concentrate on their work when further organizational and staffing changes might occur at any time.

The closing of offices, the uncertainty surrounding RTC's future, and the temporary job status afforded new RTC hires, among other factors, have made it difficult for PLS to keep and attract attorneys, according to PLS managers in the field and headquarters. For example, about 40 percent of the attorneys who were on board when the putback letters went out had left PLS by March 31, 1993. Specifically, 11 of 21 managers and 19 of 52 line attorneys left. Some of the attorneys went to other parts of RTC and others left RTC.⁹ We discuss RTC PLS attorney staffing in more detail later in this report.

⁹PLS lost one other staff attorney during this time period due to death.

No Change in PLS Litigation Policies

The materials accompanying Mr. Casey's October 1 testimony also respond to allegations by the three former PLS managers that specific professional liability cases were mishandled and that the new PLS regime that took control after the reorganization was not pursuing the cases aggressively enough. In particular, the RTC response addresses the former managers' contentions that the new regime was not giving adequate attention to negligence claims and that it is unwilling to pursue claims against outside directors of failed thrifts.

As part of our review, we examined the PLS litigation files for the seven cases that were the subject of specific allegations made by the three former managers. We also interviewed current PLS managers and line attorneys as well as three outside counsel hired for three of these cases to discuss the cases and, more generally, their understanding of PLS policies and practices. Our analysis of PLS policies and practices, discussed below, is based on these case reviews and interviews.¹⁰ In general, while the cases the attorneys cited presented some close judgment calls, we believe that the decisions PLS made reflect good faith and plausible litigation judgments.

The former managers expressed concern that the new PLS regime could be concentrating on fraud claims to the detriment of negligence claims, which are the mainstay of the professional liability work. We did not find any indication of this. Each of the seven cases we reviewed included negligence claims. The current PLS managers and line attorneys we interviewed said that negligence continues to be the primary, although not the exclusive, focus of their work. At the same time, we did encounter some differences of opinion among attorneys in different field locations over what constitutes a viable negligence claim. Several attorneys expressed uncertainty about how much supporting evidence Washington PLS reviewers need in order to approve an "authority to sue" (ATS) memorandum in a negligence case. Additionally, some attorneys believed Washington might not approve "borderline" cases. The Washington-based PLS managers expressed surprise at this, and they assured us that they expect borderline claims to be submitted to Washington for a decision on whether they should be pursued.

¹⁰Since much of the information about the individual cases we reviewed is litigation-sensitive, we cannot specifically identify them or discuss their details in this report. However, we have briefed your staff on our findings with respect to each of the cases.

Another major allegation was that PLS is unwilling to pursue claims against outside directors.¹¹ The former managers cited two cases in which PLS reviewers decided to drop outside directors as defendants in proposed professional liability suits. On the basis of our review of the case files and interviews with responsible attorneys, we believe these decisions were based on doubts about whether the directors were liable and on other plausible litigation risk and cost-benefit considerations. None of the PLS managers and line attorneys we interviewed indicated that they felt constrained from pursuing outside directors. However, as with negligence claims in general, we found some differences of opinion over what constitutes a viable claim against outside directors.¹²

The former managers also expressed more generalized concerns that the staff losses deprived PLS of the expertise necessary to vigorously develop and pursue professional liability claims. They believed that as a result of the loss of expertise and disruption from the staff changes and case reassignments, claims with expiring SOL deadlines might not receive adequate consideration. Clearly, PLS has lost a number of experienced managers and line attorneys. On the other hand, most of the new PLS managers in Washington and in the field were PLS managers before the staffing changes.

While we did not conduct a comprehensive review, we found no evidence in the cases that we reviewed that those with expiring SOLs were not adequately considered. In the one specific case cited to us by the former managers on this point, PLS did close out the case shortly before the SOL expired. The file indicates, however, that the case was fully considered. Both an ATS memorandum and a close-out memorandum (a memorandum to authorize the decision to not file a claim) were drafted and debated. The disposition of the case was a judgment call; in the final analysis, the PLS managers decided that it should not be pursued. More generally, managers and line attorneys we interviewed stated that they were sensitive to the need to ensure that all cases are thoroughly explored before the SOL expires.

¹¹An outside director's functions generally are limited to serving on the board in contrast to inside directors, who typically hold additional positions as officers or committee members or function as part of a control group. Outside directors usually are not involved in the day-to-day affairs of the institution.

¹²The Office of Thrift Supervision (OTS) led an interagency effort to prescribe more detailed guidance concerning standards of care and potential liability applicable to directors and officers of financial institutions. OTS issued its own guidance in November 1992. FDIC issued separate guidance in December 1992. At one time RTC was a participant in the effort, but it subsequently opted out.

In summary, we found no indication that RTC has adopted policies or practices designed to weaken its professional liability work. However, we did find differences of opinion among regional attorneys concerning headquarters' receptivity to certain claims. Because of these differences, we suggested to RTC that it utilize various mechanisms to promote consistency in the regions and ensure adequate case development. These mechanisms include the use of ongoing and case close-out reviews and the dissemination of policy guidance to regional staff through training and written materials.

RTC Has Taken Actions to Improve Oversight of PLS Cases

RTC has taken a number of steps to improve oversight of PLS cases. First, the AGC-PLS has reinstated an ongoing case review process used by the former AGC-PLS. This process involved quarterly meetings between the Counsels-PLS in the region and their section chiefs and attorneys to review the status of cases. The current AGC-PLS told us that between January 1992 and the first quarter of 1993, the reviews were not done as vigorously as they had been in the past because Washington did not have the staff available to participate. The AGC-PLS told us that the staff are doing the reviews in a more formal manner and they have been scheduled for the rest of the year. The AGC-PLS sees the quarterly review process as being the primary tool for ensuring case consistency.

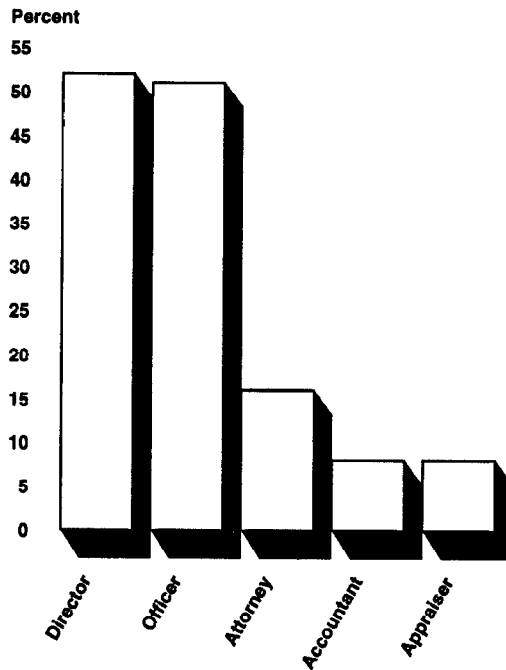
Another tool RTC has adopted is a requirement that the AGC-PLS formally approve all case close-out decisions. When it is determined that a claim should not be pursued, the responsible PLS attorney is to document this decision in a close-out memo. Until recently, the AGC-PLS had less authority over case close-out decisions than over approving lawsuits because the AGC-PLS was given 10 days only to object to close-out decisions. In March 1993, RTC adopted a requirement that the AGC-PLS approve all close-out memos.

Additionally, the AGC-PLS has taken steps to coordinate training for regional attorneys. Since the reorganization the PLS training has tended to be decentralized, with the source and substance of training varying by field location. The AGC-PLS has appointed a training coordinator, and a 3-day training conference will be held for all PLS attorneys and paralegals, Senior Counsels (Litigation), and some members of Investigations in June 1993. While particular training may still be held at individual regions, the AGC-PLS plans to have this training coordinated through headquarters.

RTC Continues to Pursue Professional Liability Claims

As of February 28, 1993, RTC had filed about 250 professional liability claims for about \$8 billion. It had executed 55 settlement agreements with parties named in these claims. Eleven of the claims had gone to trial and reached final judgment.¹³ RTC also reached settlement prior to filing a claim with potential defendants associated with approximately 60 thrifts. The judgments and the amounts agreed to in the settlement agreements total approximately \$368 million, of which RTC had collected about \$336 million. As is shown in figure 1, the most common defendants in the claims filed have been the former thrifts' directors and officers.

Figure 1: Types of Defendants in PLS Claims



Note 1: RTC data categorize the types of defendants in a claim but not the number of defendants in each type. These percentages represent the percent of claims that had at least one defendant of the listed type.

Note 2: A defendant may be categorized in more than one category if he/she held more than one type of position.

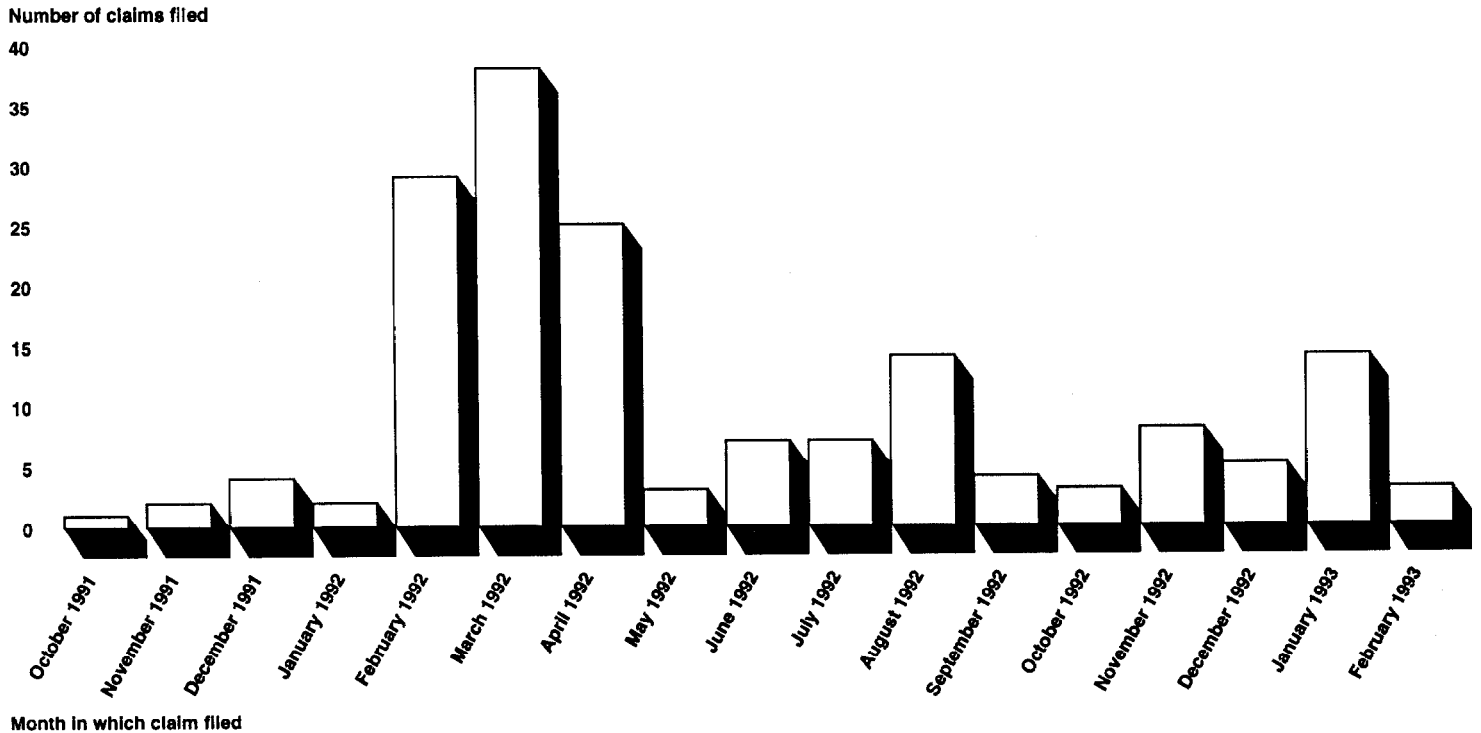
Note 3: There may be more than one type of defendant per claim.

Source: GAO analysis of RTC data.

¹³RTC won five of these lawsuits, one of which is on appeal. RTC is appealing two of the six that it lost.

Figure 2 shows the number of claims RTC has filed since October 1991, by month filed. About 200 of these claims were open as of February 28, 1993.

Figure 2: Number of Claims Filed by Filing Date



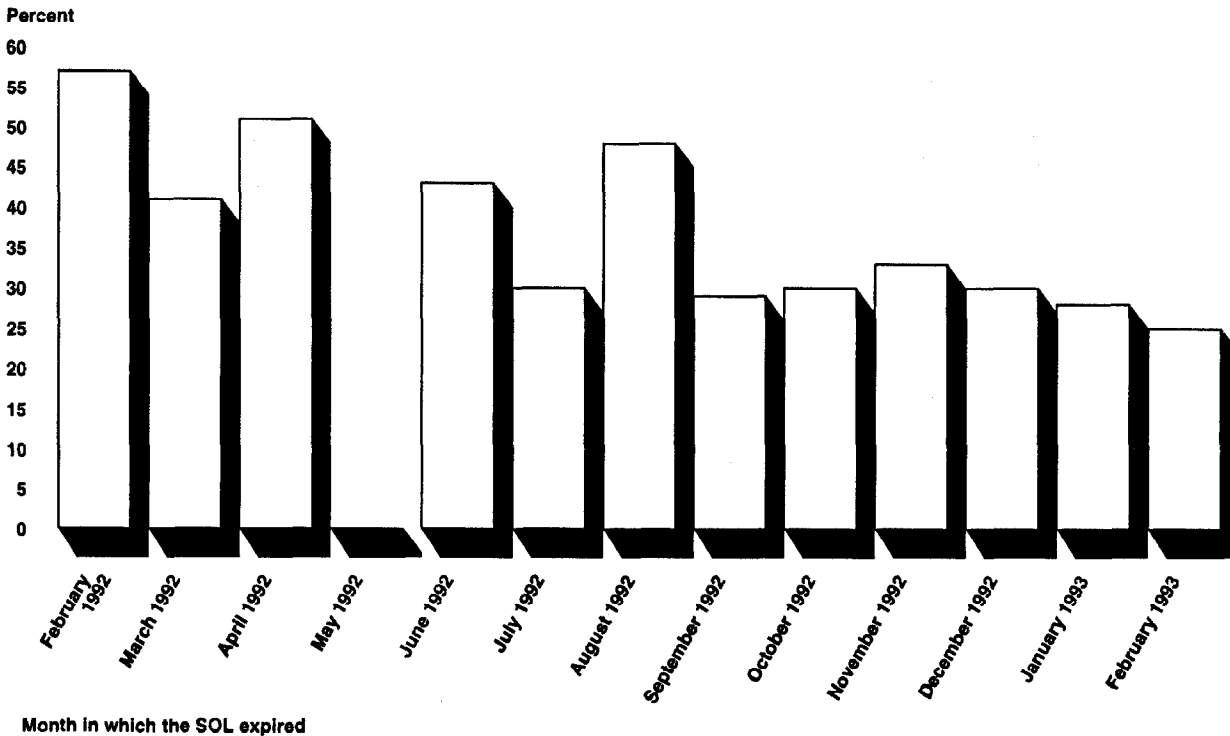
Source: GAO analysis of RTC data.

Figure 3 provides information on the percent of RTC institutions for which RTC filed at least one claim.¹⁴ The data are organized by the month that the

¹⁴These percentages could increase somewhat over time if RTC filed additional claims concerning these thrifts. This could occur for claims that are not subject to the 3-year SOL or against prospective defendants that entered into tolling agreements, which temporarily suspend the running of the statute of limitations.

SOL expired.¹⁵ For example, in February 1992, the SOL expired for filing suits associated with 37 thrifts. As of February 28, 1993, RTC had filed at least one suit in association with 21 of these thrifts. Hence, RTC filed at least one suit associated with 57 percent of the thrifts for which the SOL expired in February 1992.

Figure 3: Percent of Thrifts With at Least One Claim Filed as of February 28, 1993



Note 1: These percentages are calculated by dividing the number of thrifts for which the SOL expired during the month by the number of these thrifts for which RTC filed at least one claim.

Note 2: There were no institutions for which a claim would be subject to the SOL expiring in May 1992.

Source: GAO analysis of RTC data.

¹⁵Most professional liability claims brought by RTC are subject to the 3-year FIRREA statute of limitations for tort claims. Unless otherwise stated, our references to an SOL period refer to this 3-year period. Generally, the limitation period begins to run on the date of appointment of RTC as conservator or receiver, or the date on which the cause of action accrues, whichever is later. Actions that may be brought beyond the 3-year limitation period include contract claims (6-year limitation period) and claims with longer applicable state limitation periods. Additionally, RTC and potential defendants may enter into tolling agreements, which temporarily suspend the running of the statute of limitations.

Appendices I and II provide detailed data depicted in these figures.

RTC Needs to Maintain a Strong Professional Liability Program

Much of the PLS work remains to be done. In order to effectively deal with its current and future workload, RTC needs to be able to attract and retain experienced PLS attorneys. Uncertainties regarding the future of the agency and the closing of offices have contributed to a high turnover of PLS attorneys. RTC and FDIC need to work together to stabilize the PLS program and ensure its viability.

Most PLS Work Has Yet to Be Completed

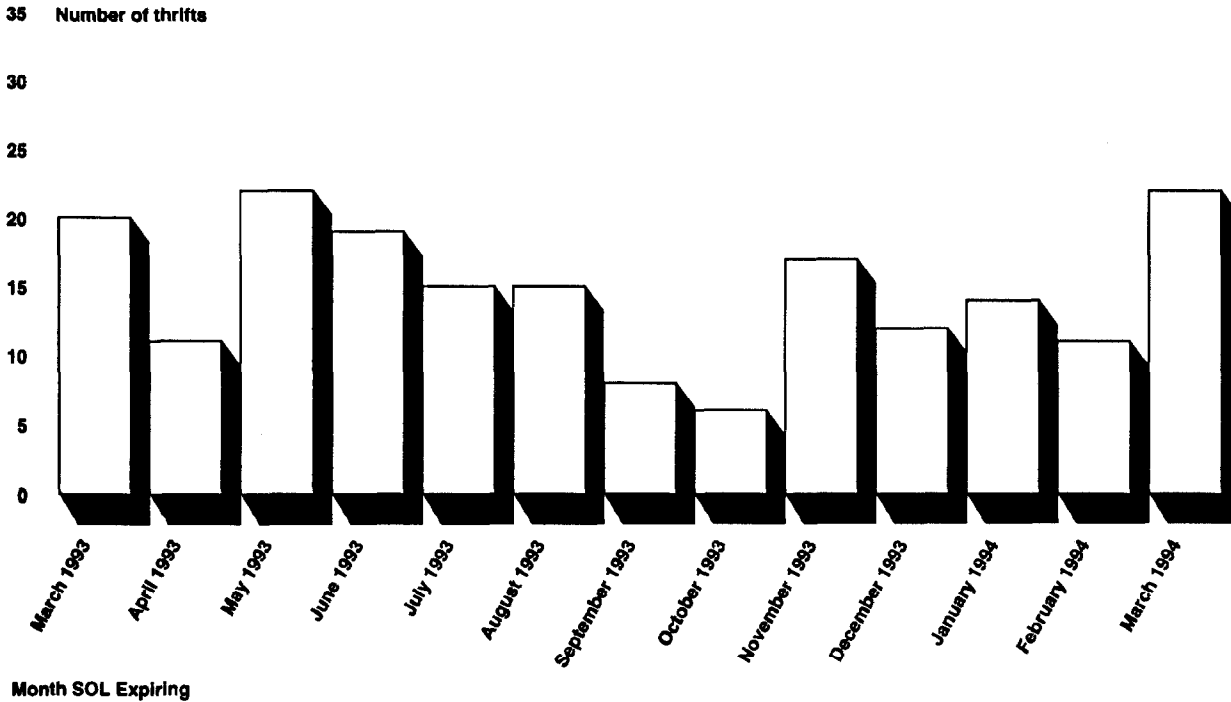
RTC's future workload for PLS includes the need to (1) determine whether to recommend that RTC pursue claims and/or settlements in connection with almost half of the thrifts RTC has taken over; and (2) monitor, support, and bring to conclusion open and future claims. As of March 1, 1993, the 3-year FIRREA SOL had yet to expire on claims associated with almost 50 percent of the 737 thrifts that had come under RTC control as of that date.¹⁶

Many decisions are facing SOL deadlines. Figure 4 shows that the SOL will expire for nearly 200 thrifts over the 12-month period beginning March 1993.¹⁷

¹⁶FDIC PLS is handling the professional liability work for four of these thrifts.

¹⁷In May 1993 we supported the extension of the SOL for professional liability cases concerning RTC thrifts in order to provide adequate time to consider potential claims before the decision must be made whether to file suit.

Figure 4: Expiring Statute of Limitations

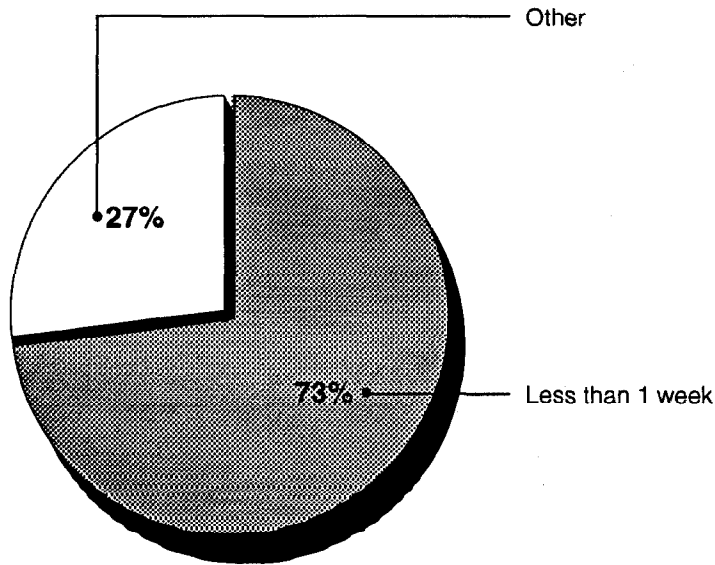


Source: GAO analysis of RTC data.

According to the AGC-PLS, RTC needs to decide whether to pursue claims in almost all the thrifts for which the statute of limitations has not run out.

RTC has continued to file many of the professional liability claims less than a week before the expiration of the statute of limitations. Figure 5 shows the percentage breakout of claims filed between January 1, 1992, and February 28, 1993, by the amount of time left before the SOL would have expired when the claim was filed. Appendix III has, based on filing date, a monthly breakout of claims filed with the number filed less than a week before the expiration of the SOL.

Figure 5: Percent of Claims Filed Less Than a Week Before the SOL Expired for Claims Filed Between January 1, 1992, and February 28, 1993

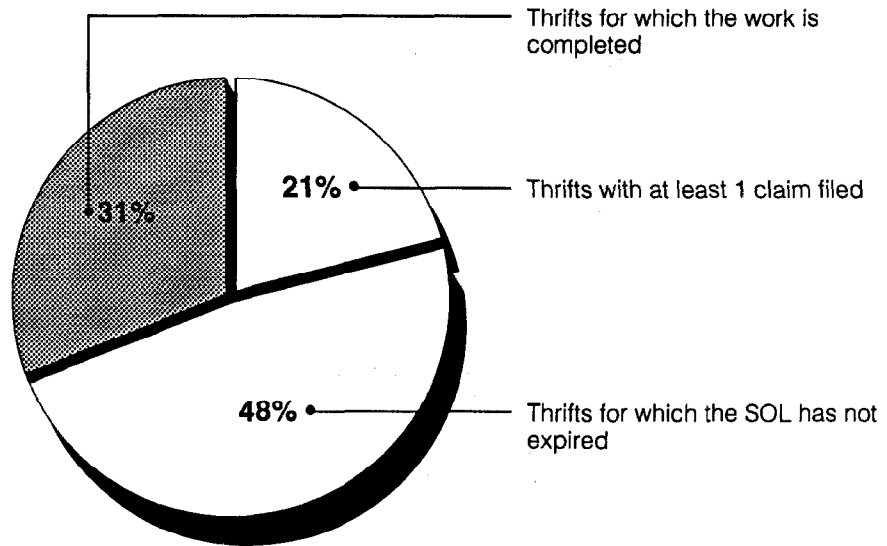


Source: GAO analysis of RTC data.

In addition to the work that needs to be done to determine whether claims should be filed, the PLS attorneys also need to remain involved in the decisions on the numerous claims that have already been filed but not yet resolved. About 210 of the 249 PLS claims filed were still pending as of February 28, 1993. It often takes 2 to 3 years to resolve a claim after its filing date. According to the AGC-PLS, after claims are filed they require substantial amounts of PLS attorney time to ensure, among other things, that they are handled in a cost-effective manner.

Figure 6 shows the percent of thrifts for which PLS still has work remaining. For those thrifts that failed as of the end of February 1993, the figure shows the percent (1) with professional liability work completed, (2) with at least one claim filed, and (3) for which the SOL had not expired as of February 28, 1993.

Figure 6: Percent of Thrifts for Which Work Remains to Be Done



Source: GAO analysis of RTC data.

RTC Has Had Difficulty Retaining PLS Attorneys

Even though RTC needs to complete a substantial amount of professional liability work, PLS continues to experience attorney shortages and has undergone a high level of staff turnover. The section recently hired a number of new attorneys but was still operating below authorized attorney levels as of March 31, 1993. The turnover has resulted in a substantial percentage of PLS attorneys who are still in the learning curve for professional liability work.

As we discussed in our June 2, 1992, testimony, RTC's PLS has historically had staffing shortages. As late as October 1990, when the RTC professional liability claims were still being worked under the FDIC PLS, there were 18 attorneys assigned to the RTC teams. These attorneys oversaw the work on almost 500 thrifts. In October 1990 RTC PLS was authorized a total of 73 attorney positions. Attorneys were hired to fill the new positions by May 1991, according to the former AGC-PLS.

In an August 1991 memo outlining Legal Division staffing needs, RTC's General Counsel told the Executive Director that PLS "is still not adequately staffed to meet the work required by the financial institutions

in, and to come into, RTC conservatorships and receiverships. As statutes of limitations deadlines are fast approaching, PLS needs are barely being met by hiring of outside counsel to help perform this sensitive and important work." He requested PLS be authorized 144 attorney positions. At that time there were 73 PLS attorneys. PLS did not get the staffing increase. According to the former General Counsel, he later reevaluated PLS's staffing needs, and determined that 70 attorneys were enough to handle the section's workload.

In September 1992, the AGC-PLS requested that PLS' authorized attorney staffing level be increased to 91. He based the increase on PLS' workload at that time and on expected closings and litigation. The Acting General Counsel and the RTC President and CEO approved the increase that month.

In November 1992 RTC opened vacancy announcements to fill all but one of the PLS vacancies. Applications were due by early December 1992. The announcement for a senior counsel position in headquarters was opened in early December and closed near the end of the month. A total of 29 positions were advertised. RTC career attorneys applying for positions were to be considered for permanent appointments. Non-RTC applicants, including those from FDIC, were to be considered for 1-year temporary appointments or term appointments not-to-exceed 2 or 4 years. According to the AGC-PLS, the attorneys hired under these announcements for term appointments were hired into positions not-to-exceed 2 years.

According to the AGC-PLS and some of the managers we spoke to in the field, the temporary nature of the agency and the temporary job status afforded new RTC hires has made it difficult to attract experienced attorneys. At the end of March 1993, PLS had 79 attorneys either on board or having accepted a position. PLS was in the process of filling the remaining 12 vacancies. Appendix IV contains a breakout of the distribution of PLS attorneys authorized and on board by location as of March 31, 1993.

Even though RTC has hired several attorneys, many experienced attorneys have left the program. Between January 1992 and March 1993, 39 attorneys joined PLS and 40 attorneys left PLS. The attorney turnover has resulted in a large number of PLS attorneys having less experience than needed "to hit the ground running," according to the AGC-PLS. RTC officials said that the learning curve for PLS attorneys is 12 to 18 months for attorneys with no prior professional liability experience. Although RTC hires outside counsel

to help develop and litigate the cases, all strategic case decisions and any settlement negotiation decisions must be made by the PLS attorney.

As of the end of March 1993, 45 percent of the PLS attorneys on board had less than 12 months' experience in RTC PLS. Appendix V has a monthly breakout of the staffing changes since October 1991. RTC PLS managers said they expected to continue to see attorneys leave RTC unless something is done to stabilize the tenuous job situation and the PLS attorneys are provided with specific information about the future of their positions.

The tenure of FDIC's PLS program is much more certain. Not only is it expected that this program will be responsible for those thrifts that fail after September 30, 1993, but FDIC is also expected to take over RTC's PLS workload when RTC is dissolved. Despite the continuing need for experienced PLS attorneys, many RTC PLS attorneys do not have rehire rights with FDIC. New RTC employees hired under the recently issued vacancy announcements for the PLS attorney positions have no FDIC employment rights. Employees now being hired by FDIC and RTC (with the general exception of RTC employees moving to FDIC as they are released by RTC) are being hired under temporary appointments. Furthermore, under an agreement reached between the heads of FDIC and RTC, career permanent FDIC employees cannot accept a position at RTC without giving up their rehire rights with FDIC. FDIC officials said that transferring employees to RTC could disrupt FDIC programs.

With RTC's impending dissolution and transfer of work to FDIC, PLS will be facing additional periods of change. To help counter the difficulties of maintaining an adequate staffing level, RTC needs to focus on planning PLS' future (both internally and with FDIC) and to communicate these plans to the staff. RTC, with FDIC input, needs to ensure that it plans for these changes. Making these transitions run smoothly is crucial both for RTC and FDIC because the bulk of the PLS work is yet to come.

The Secretary of the Treasury recognized the need for management attention to the RTC PLS program. In March 1993, he required RTC's President and CEO to review staffing and organization of RTC's PLS program. This request was 1 of 10 initiatives concerning critical areas in RTC that the Secretary, as Chairman of the Thrift Depositor Protection Oversight Board, requested the RTC CEO to study.

Conclusions

On the basis of our review, we found no indication that RTC or PLS management sought to undermine the professional liability work. However, we believe there is some risk that the development of future claims may suffer from inadequate staffing and staff's lack of experience.

We believe it is essential that top RTC management restore some sense of stability to the PLS staff for the duration of RTC's PLS existence and continue its efforts to increase the PLS staff to its authorized strength. Because RTC is a temporary agency, hiring and retaining PLS attorneys will be difficult. However, under current law FDIC will assume responsibility for the RTC PLS program when RTC is dissolved. Therefore, it is important for RTC and FDIC management to work together to explore ways to ensure that RTC maintains a viable PLS program and that the transfer to FDIC is smooth.

Recommendations

To ensure a strong PLS program and to help smooth the transition of PLS work to FDIC, we recommend the RTC President and CEO work with the Chairman of FDIC to analyze and address the agencies' current and future operational and staffing needs of the PLS program. This analysis should consider various staffing options and organizational structures, taking into account both agencies' current and future professional liability requirements. A key goal of this analysis should be the stabilization of RTC's professional liability program both currently and in the future as it is merged with FDIC's PLS program. RTC's CEO should take these factors into consideration when reviewing and recommending improvements to PLS's organization and staffing, as he was requested to by the Secretary of the Treasury. And finally, regardless of what actions are taken, the RTC CEO and President should keep the PLS attorneys informed of the agencies' plans and decisions concerning PLS to help decrease the level of uncertainty surrounding the program.

Agency Comments

We discussed our findings, conclusions, and recommendations with, among others, RTC's former President and CEO, Acting General Counsel, and Assistant General Counsel-PLS. We also discussed this report with the Thrift Depositor Protection Oversight Board General Counsel and FDIC officials. These officials agreed with our findings and conclusions and were generally receptive to our recommendations.

As agreed with the Committee, we plan no further distribution of this report until 30 days from the date of this letter, unless you publicly

announce its contents earlier. At that time, we will provide copies of this report to officials at RTC and other interested parties and make copies available to others upon request.

Major contributors to this report are listed in appendix VI. If you have any questions about the report, please call me on (202) 512-5156.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Henry R. Wray". The signature is fluid and cursive, with a long horizontal stroke at the end.

Henry R. Wray
Director, Administration of
Justice Issues

Types of Defendants in PLS Claims

| Month and year | Number of claims filed | Director | | Officer | | Attorney | | Accountant | | Appraiser | | Other | |
|----------------|------------------------|------------|-----------|------------|-----------|-----------|-----------|------------|----------|-----------|----------|-----------|-----------|
| | | # | % | # | % | # | % | # | % | # | % | # | % |
| Before 10/91 | 84 | 24 | 29 | 24 | 29 | 8 | 10 | 6 | 7 | 4 | 5 | 40 | 48 |
| 10/91 | 1 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 11/91 | 2 | 1 | 50 | 1 | 50 | 0 | 0 | 1 | 50 | 1 | 50 | 1 | 50 |
| 12/91 | 4 | 2 | 50 | 2 | 50 | 0 | 0 | 0 | 0 | 1 | 25 | 1 | 25 |
| 1/92 | 2 | 1 | 50 | 2 | 100 | 0 | 0 | 0 | 0 | 1 | 50 | 0 | 0 |
| 2/92 | 29 | 20 | 69 | 20 | 69 | 8 | 28 | 2 | 7 | 1 | 3 | 6 | 21 |
| 3/92 | 38 | 28 | 74 | 25 | 66 | 7 | 18 | 3 | 8 | 2 | 5 | 10 | 26 |
| 4/92 | 25 | 15 | 60 | 15 | 60 | 3 | 12 | 2 | 8 | 7 | 28 | 3 | 12 |
| 5/92 | 3 | 1 | 33 | 1 | 33 | 2 | 67 | 0 | 0 | 1 | 33 | 1 | 33 |
| 6/92 | 7 | 5 | 71 | 5 | 71 | 2 | 29 | 2 | 29 | 0 | 0 | 2 | 29 |
| 7/92 | 7 | 5 | 71 | 5 | 71 | 1 | 14 | 1 | 14 | 0 | 0 | 1 | 14 |
| 8/92 | 14 | 9 | 64 | 10 | 71 | 3 | 21 | 2 | 14 | 0 | 0 | 6 | 43 |
| 9/92 | 4 | 3 | 75 | 3 | 75 | 0 | 0 | 0 | 0 | 0 | 0 | 1 | 25 |
| 10/92 | 3 | 3 | 100 | 2 | 67 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 11/92 | 8 | 5 | 63 | 4 | 50 | 5 | 63 | 0 | 0 | 1 | 13 | 1 | 13 |
| 12/92 | 5 | 1 | 20 | 2 | 40 | 0 | 0 | 1 | 20 | 0 | 0 | 1 | 20 |
| 1/93 | 14 | 5 | 36 | 7 | 50 | 2 | 14 | 0 | 0 | 1 | 7 | 4 | 29 |
| 2/93 | 3 | 3 | 100 | 1 | 33 | 0 | 0 | 0 | 0 | 0 | 0 | 1 | 33 |
| Total | 253 | 131 | 52 | 129 | 51 | 41 | 16 | 20 | 8 | 20 | 8 | 80 | 32 |

Legend

= number of cases
% = percent of cases filed

Note 1: The numbers listed under the defendant categories are the number of claims filed with a defendant of that type. The percent is the percentage of claims filed during the time frame with that type of defendant. A claim may be filed against more than one defendant type. Consequently, the monthly totals for the number of types of defendants may exceed the number of claims filed that month. Additionally, (1) more than one defendant may be associated with each defendant type in a claim and (2) a defendant may be categorized in more than one type if he/she held more than one position with the thrift. Therefore, the sum of the total percentages exceeds 100 percent.

Note 2: "Other" includes borrowers, securities and commodities brokers, insurers, and what is defined in RTC's CTS as other.

Note 3: RTC filed another seven claims as of February 28, 1993, for which the suit date was not in its database at the time of our analysis.

Source: GAO analysis of RTC data.

All RTC PLS Claims Filed Based on the Month in Which the SOL Expired

| Month in which SOL expired | Number of thrifts with SOL expiring | Number of thrifts with at least one claim | Percent of thrifts with at least one claim |
|----------------------------|-------------------------------------|---|--|
| January 1992 | 0 | 0 | N/A |
| February 1992 | 37 | 21 | 57 |
| March 1992 | 138 | 56 | 41 |
| April 1992 | 43 | 22 | 51 |
| May 1992 | 0 | 0 | N/A |
| June 1992 | 14 | 6 | 43 |
| July 1992 | 20 | 6 | 30 |
| August 1992 | 21 | 10 | 48 |
| September 1992 | 7 | 2 | 29 |
| October 1992 | 10 | 3 | 30 |
| November 1992 | 18 | 6 | 33 |
| December 1992 | 10 | 3 | 30 |
| January 1993 | 32 | 9 | 28 |
| February 1993 | 32 | 8 | 25 |
| Total | 382 | 152 | 40 |

N/A = Not applicable

Source: GAO analysis of RTC data.

Claims Filed Based on the Date Filed and the Number Filed Less Than a Week Before the SOL Expired

| Month and year | Number of claims filed | Number filed up to 6 days before the SOL expired | Percent filed up to 6 days before the SOL expired |
|----------------|------------------------|--|---|
| January 1992 | 2 | 0 | 0 |
| February 1992 | 29 | 25 | 86 |
| March 1992 | 38 | 31 | 82 |
| April 1992 | 25 | 21 | 84 |
| May 1992 | 3 | 0 | 0 |
| June 1992 | 7 | 4 | 57 |
| July 1992 | 7 | 5 | 71 |
| August 1992 | 14 | 9 | 64 |
| September 1992 | 4 | 1 | 25 |
| October 1992 | 3 | 2 | 67 |
| November 1992 | 8 | 4 | 50 |
| December 1992 | 5 | 5 | 100 |
| January 1993 | 14 | 9 | 64 |
| February 1993 | 3 | 2 | 67 |
| Total | 162 | 118 | 73 |

Source: GAO analysis of RTC data.

Distribution of PLS Attorneys

| Location | Number of attorneys: | |
|---------------|----------------------|-------------------------------|
| | Authorized | On board as of March 31, 1993 |
| Atlanta | 11 | 8 |
| Dallas | 15 | 8 |
| Denver | 7 | 8 |
| Kansas City | 15 | 10 |
| Newport Beach | 9 | 9 |
| Valley Forge | 10 | 10 |
| Headquarters | 24 | 16 |
| Total | 91 | 69 |

Note: PLS had commitments from applicants for 10 other positions as of March 31, 1993.

Source: GAO analysis of RTC data.

Monthly PLS Staffing Changes

| Month | Number of attorneys: | | | On board at the end of the month |
|----------------|--|----------------------------|------------------------------|----------------------------------|
| | On board at the end of the prior month | That left during the month | That joined during the month | |
| October 1991 | 69 | 1 | 1 | 69 |
| November 1991 | 69 | 0 | 0 | 69 |
| December 1991 | 69 | 0 | 1 | 70 |
| January 1992 | 70 | 0 | 1 | 71 |
| February 1992 | 71 | 0 | 2 | 73 |
| March 1992 | 73 | 2 | 5 | 76 |
| April 1992 | 76 | 1 | 0 | 75 |
| May 1992 | 75 | 4 | 3 | 74 |
| June 1992 | 74 | 7 | 9 | 76 |
| July 1992 | 76 | 8 | 4 | 2 |
| August 1992 | 72 | 3 | 1 | 70 |
| September 1992 | 70 | 1 | 1 | 70 |
| October 1992 | 70 | 4 | 0 | 66 |
| November 1992 | 66 | 0 | 0 | 66 |
| December 1992 | 66 | 3 | 3 | 66 |
| January 1993 | 66 | 2 | 0 | 64 |
| February 1993 | 64 | 3 | 3 | 64 |
| March 1993 | 64 | 2 | 7 | 69 |

Source: GAO analysis of RTC data.

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