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FEDERAL DEPOSIT INSURANCE CORPORATION (FDIC)

MISSION STATEMENT AND POLICY GUIDANCE FOR ADMINISTRATION OF ASSISTANCE AGREEMENTS UNDER THE FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION (FSLIC) RESOLUTION FUND

MISSION STATEMENT

With respect to assistance agreements under the FSLIC Resolution Fund, the FDIC prudently administers and manages financial assistance agreement cases to minimize the costs associated with the liquidation of the acquired institutions' covered asset portfolios. The FDIC manages its duties and obligations under these agreements as a total portfolio to minimize any adverse effects that asset disposition and inter-institution legal actions may have upon (1) maintaining asset values, (2) ensuring Acquiring Association accountability (3) supporting the regional and local economies, and (4) maintaining public confidence in Federally insured institutions

GOALS AND OPERATING PRINCIPLES

The FDIC has identified the following major goals:

1. To dispose of assets within the term of the assistance agreements to ensure orderly liquidation at minimum cost while maximizing asset value.

2. To assess effects of FIRREA on assisted institutions' ability to carry out duties and responsibilities under Assistance Agreements.

3. To establish and implement an improved process to monitor the Associations' asset management performance and ensure compliance with the terms, conditions and standards of the Assistance Agreements.

4. To develop and implement an enhanced management information system that is an effective resource in the management decision making process.

5. To periodically assess the delegations of authority to ensure that the organization prudently and efficiently exercises its authority.

6. To evaluate performance of the Contractors and develop a plan to reduce reliance on the Contractors in the future.

7. To establish operational relationships with outside regulatory agencies which affect the responsibilities of the FDIC.

In developing FDIC's policies for administering the assistance agreements, there are several principles that will serve as operational guidelines that should be apparent in every aspect of operations. They are designed to demonstrate the FDIC's commitment to carrying out prudently the significant responsibilities entrusted to it. These principles include:

- <u>Accountability</u>: In carrying out its responsibilities, the FDIC is aware of its fiduciary responsibilities to the taxpayers. This concept translates into how the FDIC applies proven management practices, attention to details and employment of sound business judgement with a view toward the impact its activities may have upon the financial and real estate communities. In the achievement of its mission, the FDIC will remain fully accountable to those relying upon its management decisions.

- <u>Cost Minimization</u>: Every FDIC activity should be sensitive to the federal cost-conscious environment. This translates practically into diligence in ensuring it carries out its responsibilities in the manner that provides the least cost and liability ~~to the taxpayer within the constraints of the~~ assistance ~~agreements~~.

- <u>Internal Controls</u>: The FDIC will be diligent to ensure that proper controls are in place to avoid any improprieties and to prevent any waste, fraud or abuse. Given the visibility of the assisted segment of the savings and loan industry, it is imperative this theme be actively employed throughout every aspect of the FDIC's endeavors. It translates to compliance with the Federal Managers' Financial Integrity Act (FMFIA), as well as any other applicable OMB or GAO circulars, guidelines or requirements;

- <u>Management Integrity and Conflict of Interest</u>: Given the broad scope and complex nature of FDIC's responsibilities, it is important that there be standards of conduct. This concept of standardization and integrity will include the ethics of employees and contractors, the uniformity of decisions regarding the cases and the attention to conflict of interest provisions in asset management and other important areas, FDIC will take steps to ensure that there is no element of a conflict of interest in carrying out its responsibilities; and

- Information Technology: As the FDIC's responsibilities mature, it will need to enhance the role of information technology in all aspects of its operations. Given the vital role that this component of the FDIC's operations will play, it is necessary that it be stated as an overall operational guideline.

POLICY GUIDANCE

1. BACKGROUND

The FDIC is responsible for administering all assistance agreements and related contracts under the FSLIC Resolution Fund arising from assisted mergers and acquisitions of failed thrifts. Typically, the terms of these assistance agreements range from five to ten years and vary considerably in complexity and degree of standardization. As of January 1990, the FDIC is responsible for administering approximately 200 assistance agreements that provide for oversight and disposition of the failed institutions' covered assets. Included in the FDIC's covered asset oversight responsibilities are approximately $36 billion of covered assets, primarily troubled real estate, real estate loans and investments in subsidiaries.

In addition to the oversight responsibilities for assistance agreements, five of the Southwest Plan institutions were not acquired by private investors. Consequently, these institutions (Stabilized Institutions) are managed by individuals and firms approved by the FDIC. For these institutions, the FDIC is responsible for administering the assistance agreements, overseeing the operations and for affecting a permanent resolution of the institution.

In addition to the administration of assistance agreements, the FDIC is responsible for administration of FSLIC's obligations under the Guaranteed Advance Program and for the administration of Capital Instruments purchased or acquired during the acquisition of thrifts (Capital Instruments include preferred stock, capital and net worth certificates, warrants and subordinated debt). The Guaranteed Advance Program provided needed liquidity at reduced risk compared to market alternatives in the form of advances or loans made to insured members who lack sufficient collateral to secure loans.

2. ASSIGNMENT OF RESPONSIBILITY

The FDIC assigns management authority for the assistance agreements to its Division of FSLIC Operations (DFO). The FDIC is a decentralized organization and, as such, must take steps to ensure its procedures and operations reflect sound and ethical management practices that are adapted to decentralized management. From a policy perspective, this assignment includes the following operational responsibilities:

o Adherence and attention to the Federal Managers' Financial Integrity Act (FMFIA), applicable OMB circulars, as well as GAO and other applicable requirements and regulations;

o Utilization of an independent case assessment approach, where appropriate, to ensure objective, professional review of practices and a strict adherence to sound and ethical actions in the case management and related areas; and

o Assurance that there will be sufficient review of the managerial decisions to ensure integrity. Given the visibility and importance of this program, it is essential that strict attention be given to the vital areas of internal controls and management integrity.

3. ASSIGNED FUNCTIONS

The major functions assigned to DFO are:

a. Management of assistance agreements and oversight and disposition of Stabilized Institutions.

b. Oversight of the management, marketing and disposition of covered assets.

c. Review and coordination of litigation matters, including review and approval of all indemnifications and reimbursements requested by the Acquiring Associations.

d. Periodic projections of future assistance payments and cash flows related to the assistance agreements.

e. Interpretation of Assistance Agreements.

f. Administration of capital instruments purchased or acquired by the old FSLIC to facilitate the acquisition or rehabilitation of troubled institutions.

g. Administration of unique assistance plans to financially troubled institutions, to include such programs as Guaranteed Advances and open institution assistance.

h. Development of responses to Congressional and public inquiries.

4. ROLE OF ACQUIRING ASSOCIATIONS

The assistance agreements provide a framework for the management and liquidation of covered assets, settlement of legal matters and the consolidation of business operations. The guidelines of the agreements help ensure that both DFO and the Acquiring Associations meet their respective responsibilities. While DFO is responsible for ensuring compliance with the contractual terms stipulated within each of these agreements, the Acquiring Associations are responsible for the implementation and management of the individual assistance transactions.

The Acquiring Associations have assumed the responsibility to use their appropriate expertise to manage the resulting business and acquired assets and liabilities in order to:

- o Operate a thrift in accordance with applicable laws and regulations;
- o Consolidate and reduce operating costs, thereby increasing net profitability; and
- o Liquidate or convert to earning assets the non-core business and assets of the acquired or consolidated thrift(s).

Each of the Acquiring Associations is responsible for administering and dealing with all covered assets and liabilities assumed pursuant to the terms of the Acquisition Agreements. Each Acquiring Association is required to employ the higher of the standard of prudent business practice in administering the acquired assets and liabilities or the standard employed in the savings and loan industry in administering similar assets and liabilities. Furthermore, the Acquiring Association is expected to use its best efforts to minimize losses and maximize gains and recoveries for the FDIC and the Acquiring Association.

The Acquiring Association is expected to provide at its own expense the executive and managerial resources, along with adequate supporting staff, to manage and implement the terms of the assistance agreement.

5. COVERED ASSET MANAGEMENT

The DFO oversees the management and disposition of assets related to financial assistance agreements. The following policies relate to covered asset management:

- <u>Asset Disposition Strategy</u>: The Acquiring Associations are required to maximize asset value and thus minimize resolution costs for the covered assets. To ensure attainment of this objective, DFO will utilize a comprehensive asset disposition strategy. This strategy will address issues such as the timing of asset disposition, loans to facilitate financing, market absorption, hold versus sell decisions and the disposition of marketable and non-marketable assets. The strategy will be communicated to all Acquiring Associations and used as a management tool to gauge their success;

- <u>Management Oversight</u>: DFO personnel assure that proposed transactions comply with applicable assistance agreement provisions and represent the most likely alternative available to minimize costs and maximize gains and recoveries. Certain decision making authority is delegated to the Acquiring Associations through specific provisions contained in the assistance agreements. Further authority is delegated through approved business plans, asset plans and collection plans. To assist in this process, DFO has developed expanded asset plan and budget formats and standards to ensure that Acquiring Associations submit documentation suitable for DFO decision making. DFO regularly monitors the Associations' compliance with assistance agreement terms, management processes and standards, and periodically tests specific asset and special reserve account transactions;

- <u>Acquiring Associations' Asset Management Processes</u>: Due to the magnitude of the transactions (both dollar value and number of assets), DFO is dependent on the Acquiring Associations' compliance with prudent asset management processes. Therefore, each Acquiring Association is required to develop and submit written asset management policies and procedures. DFO reviews these policies and procedures and tests for compliance on a regular basis;

- <u>Compliance</u>: DFO utilizes a number of programs to monitor the Acquiring Associations' compliance with the terms, management standards and intent of the assistance agreements. Compliance monitoring activities will include:

- Case Compliance Reviews: This activity involves the periodic review of a case by an independent group of DFO personnel from another case management section. The case compliance scope will include reviewing the Association's compliance with asset management processes, as well as DFO Contractor and Case Manager compliance with DFO's internal operating policies and procedures;

- Structured Evaluations of the Association: Periodically the Case Manager and DFO Contractor review individual Association Asset Managers to assess the quality of the Association's asset management, monitor compliance with Association policies and procedures and evaluate the Asset Manager's general and specific management of the assets;

- Examination Liaison: In connection with examinations by the Office of Thrift Supervision and the FDIC's Division of Supervision, DFO will coordinate additions to the development of the examinations' scope to include special concerns regarding compliance with Assistance Agreements;

- Special Investigations: Based on findings and conclusions, complaints, and/or general concerns, special investigations (often performed without the knowledge of the Acquiring Associations) will continue to be performed to ensure that the Acquiring Associations are disposing of assets in compliance with the terms and conditions of the assistance agreement for the highest and best price available;

o Assistance Agreement Interpretation: DFO, with the assistance of the Legal Division, is responsible for interpreting the provisions of the assistance agreements. Due to the unique nature of the agreements, resolution of an interpretation issue may result in the development of specific policies or assistance agreement modifications. DFO is developing an assistance agreement issues resolution process for tracking, disseminating and referencing interpretations. Examples of issues include disposition financing, marketing, appraisals, loan participations and management standards.

6. LITIGATION

DFO will monitor all legal proceedings to ensure the Acquiring Associations are using their best efforts to preserve the interests of the FDIC and to minimize costs and expenses in all litigation matters. The Acquiring Associations will also strive to maximize any potential recoveries through pursuit of related claims. DFO will coordinate the approval of all litigation matters with the FDIC's Legal Division. Since indemnification for major settlements requires the Legal Division's concurrence, DFO's role is to analyze and consider the effect of any proposed actions upon the ultimate costs to the FSLIC Resolution Fund.

To facilitate DFO's ability to monitor the status of legal activity, the Acquiring Associations, as directed by the assistance agreements, must submit litigation schedules, plans and budgets on a regular basis. Any expenditure of Acquiring Associations' funds for legal matters that are reimbursable by the FDIC must ultimately be approved by the FDIC, either by written consent of DFO, through the approval of plans/budgets, or the approval of transactions through the Special Reserve Accounts.

DFO has the authority to intervene in the conduct of any litigation matter to protect the FDIC's best interests. More specifically, DFO has the right to:

- o Monitor and direct the defense or prosecution of the matter;
- o Defend or prosecute the matter with FDIC attorneys; and
- o Require the Acquiring Association to assign its right, title or interest in the matter, any defense related to the matter, or proceeds from the matter to the FDIC.

Additionally, the Acquiring Associations must cooperate with DFO in defense or prosecution of legal matters. The Acquiring Associations may also be required to provide DFO with all applicable books, records or other relevant information in its control.

The Acquiring Associations may take immediate action concerning a litigation matter if that action is required to protect the interests of the FDIC and the Acquiring Associations. The Acquiring Associations may take such emergency steps only if it is unable, due to time or other constraints, to obtain verbal or written approval of DFO.

The Acquiring Associations are expected to pursue all related claims and, when appropriate, file actions with respect to potential recoverable claims. These legal actions should be pursued in an effort to reduce or minimize the indemnity payments the FDIC will be required to pay. If necessary, the

FDIC may direct the Acquiring Association to pursue or prosecute potential claims. DFO will coordinate with the Legal Division with respect to the assignment of and pursuit of claims acquired through the agreements.

Any significant settlement for a litigation matter must be approved by DFO with concurrence from the Legal Division. DFO will coordinate the approval of settlements in an expedient manner to eliminate any potential economic loss that may result from delays in approval processing.

7. **TAX, AUDIT, FINANCIAL MANAGEMENT AND REPORTING**

FDIC oversees the following financial areas:

o <u>Tax</u>: Where applicable, the tax-related provisions of Assistance Agreements vary widely and many are technically detailed in nature. Within the framework of each agreement, FDIC's intent is to maximize the U.S. Government's share of net tax benefits. Acquiring Associations are responsible for providing FDIC copies of their tax returns filed with the Internal Revenue Service. Each agreement specifies the information that Acquiring Associations shall submit to FDIC in support of tax-related credits and/or payments to the agency.

o <u>Audits</u>: FDIC has a priority goal to expedite completion of remaining opening-inventory audits of assisted associations. These audits help FDIC to determine negative capital and the inventory of covered assets. FDIC will also periodically initiate compliance audits to ensure that an Acquiring Association's claim for reimbursement and related activities are consistent with the terms of the agreement. Acquiring Associations are responsible for cooperating fully with the auditors and providing on a timely basis such background work papers and schedules as the auditors may require.

o <u>Payment of Claims</u>: FDIC will generally pay all valid and properly documented claims in cash upon receipt, in lieu of accruing such obligations at interest. Where agreements allow, the agency may elect to defer such payments with interest. This option will normally be applied only during periods when the FSLIC Resolution Fund's cost of financing (i.e., cost of U.S. Treasury borrowings), is less than the interest cost to defer payments of claims.

- Reporting: FDIC will maintain a financial reporting system to track the Government's actual and projected costs under the Assistance Agreements. Costs will be separated among a number of individual expense categories. The reporting system will include a variance analysis capability to compare estimated with actual costs. The system will also include cash flow forecasting of the timing and amounts paid under Assistance Agreements. This will assist the U.S. Treasury to minimize its cost of financing funds that are transferred to the FSLIC Resolution Fund.

8. RESOURCES

DFO relies on staff members located in Washington, D.C., and field staff in Dallas and Houston, Texas, and Irvine, California to carry out its oversight responsibilities. In addition, DFO leverages itself through the judicious use of independent contractors to provide specialized expertise.

In carrying out its mission with respect to assistance agreements, DFO has adopted policy perspectives with regard to two important organizational/administrative components:

- Contractors: While currently there is a significant reliance upon contractors to assist DFO in carrying out its responsibilities, DFO envisions this reliance will decrease as its own staff members continue to expand in size and increase in capability; and

- Technology: The development of an accurate and reliable information resources management capability is an important goal for DFO. DFO will place increased emphasis upon this component of its operations to gauge programmatic needs and to assess the efficient employment of resources. While this portion of DFO's capability is still in the early developmental stages, DFO intends to place continued emphasis upon it as a vital component of its operation.

9. MANAGEMENT REPORTING

To properly evaluate and monitor the performance of the Acquiring Associations and to determine the overall performance of the consolidated DFO portfolio, a reliable, accurate management information system is critical. The development of a comprehensive covered asset management and compliance monitoring system continues to be a high priority of DFO. A number of information processes have been, or are being, developed to address those needs.

DFO collects monthly and quarterly Acquiring Association activity data, from which a series of management reports will be generated. This information includes data on covered asset status, disposition activity , submission activity, financial performance, staffing, assistance paid, litigation and consolidation activities. The reports generated provide two-levels of management information: general information to track overall asset management progress and specific information to identify potential problems at institutions that may require special action and additional monitoring.

DFO will produce periodic reports on the status of DFO's current caseload, the disposition of covered assets, the Acquiring Associations' relative assistance agreement compliance, the Acquiring Associations' financial performance (e.g. watch list), and corrective actions underway. Reports will also be provided on the status of opening inventory and compliance audits, as well as on total assistance expenditures to date and projected cash flows.

To provide the level of management information necessary for effective reporting and control purposes, DFO requires mainframe support from the FDIC. The current developmental efforts represent interim or prototype processes that are designed to provide the high level information required to manage the assistance transactions over the short-term.