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Description of document: Three Federal Deposit Insurance Corporation (FDIC) Inspector General (OIG) reports regarding legal fees paid by the Resolution Trust Corporation (RTC) during 1999

Requested date: 2016

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Report titles:

1. Legal Fees Paid by RTC to Salem, Saxon & Nielson, Report 99-012, 2/11/1999
2. Legal Fees Paid by RTC to Brobeck, Phleger & Harrison, Report 99-014, 3/12/1999
3. Legal Fees Paid by RTC to Brobeck, Phleger & Harrison, Report 99-015, 3/12/1999

Source of document: Federal Deposit Insurance Corporation
FOIA/Privacy Act Group, Legal Division
550 17th Street, NW
Washington, DC 20429-9990
[Submit Electronic FOIA Request](#)

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August 5, 2016

RE: FDIC FOIA Log Number 16-0291

This will respond to your Freedom of Information Act (FOIA) request, in which you requested a digital/electronic copy of the following FDIC Office of Inspector General publications:

1. Legal Fees Paid by RTC to Salem, Saxon & Nielson, Report 99-012, 2/11/1999
2. Legal Fees Paid by RTC to Brobeck, Phleger & Harrison, Report 99-014, 3/12/1999
3. Legal Fees Paid by RTC to Brobeck, Phleger & Harrison, Report 99-015, 3/12/1999

Enclosed please find copies of the records located by the FDIC (consisting of a total of 212 pages) which are responsive to your request. However, certain information in these records has been redacted pursuant to FOIA Exemptions 4 and 6, 5 U.S.C. §552 (b)(4) and (b)(6).

Exemption 4 permits the withholding of trade secrets, and confidential or privileged commercial or financial information obtained from a person. Exemption 6 permits the withholding of personal information the disclosure of which would constitute a clearly unwarranted invasion of personal privacy.

You may contact me at 703-562-2067, or our FOIA Public Liaison, Acting FDIC Ombudsman Gordon Talbot, by email at GTalbot@fdic.gov or telephone at 703-562-6040, for any further assistance and to discuss any aspect of your request. Additionally, you may contact the Office of Government Information Services (OGIS) at the National Archives and Records Administration to inquire about the FOIA mediation services they offer. The contact information for OGIS is as follows: Office of Government Information Services, National Archives and Records Administration, 8601 Adelphi Road-OGIS, College Park, Maryland 20740-6001, email at ogis@nara.gov; telephone at 202-741-5770; toll free at 1-877-684-6448; or facsimile at 202-741-5769.

If you are not satisfied with the response to this request, you may administratively appeal by writing to the FDIC's General Counsel. Your appeal must be postmarked or electronically transmitted within 90 days of the date of the response to your request. Your appeal should be addressed to the FOIA/PA Group, Legal Division, FDIC, 550 17th Street, NW, Washington, D.C. 20429. Please refer to the log number and include any additional information that you would like the General Counsel to consider.

This completes the processing of your FOIA request.

Sincerely,

Natasha Smith
Government Information Specialist
FOIA/Privacy Act Group

Enclosures

LEGAL FEES PAID BY FDIC TO BROBECK, PHLEGER & HARRISON

Audit Report No. 99-015
March 12, 1999



Material has been redacted from this document to protect personal privacy, confidential or privileged information.

OFFICE OF AUDITS

OFFICE OF INSPECTOR GENERAL



Federal Deposit Insurance Corporation
Washington, D.C. 20434

Office of Audits
Office of Inspector General

March 12, 1999

MEMORANDUM TO: James T. Lantelme
Assistant General Counsel
Legal Operations Section
Legal Division

(b)(6)

FROM: David H. Loewenstein
Assistant Inspector General

SUBJECT: *Legal Fees Paid by FDIC to Brobeck, Phleger & Harrison*
(Audit Report No. 99-015)

This report presents the results of an audit of Brobeck, Phleger & Harrison, a law firm hired to provide legal services to the Federal Deposit Insurance Corporation (FDIC). The Office of Inspector General (OIG) has an ongoing program for auditing law firm billings to ensure that such billings are adequately supported and comply with cost limitations set forth by the FDIC and the former Resolution Trust Corporation (RTC). This report was prepared by the independent public accounting firm (IPA) of Mitchell & Titus for the FDIC OIG.

The objectives of the audit were to ensure that fee bills were adequately supported and in compliance with the cost limitations set by FDIC and RTC and that charges for legal services provided were reasonable. The audit covered billings paid by RTC during the period January 1, 1990, through December 31, 1993. The total fees paid to the law firm during the audit period were \$4,190,922. The audit sample covered \$2,892,293, or 69 percent of the total.

The IPA identified net questioned costs of \$2,165,277. However, subsequent to the preparation of the IPA's draft report and based on additional documentation provided by the law firm, the OIG modified questioned costs to \$2,110,119. A summary of the OIG revised draft report questioned costs appears on pages 5 and 6.

The OIG made 12 recommendations to the Assistant General Counsel (AGC), Legal Operations Section, Legal Division, to disallow the questioned costs. The General Counsel (GC) provided a written response dated March 4, 1999, to a draft of this report. The response from the GC is included as an appendix to this report.

The Inspector General Act of 1978, as amended, requires the OIG to report on the status of management decisions on its recommendations in its semiannual reports to the Congress. To consider FDIC responses as management decisions in accordance with the act and related

guidance, several conditions are necessary. First, the response must describe for each recommendation

- the specific corrective actions already taken, if applicable;
- corrective actions to be taken together with the expected completion dates for their implementation; and
- documentation that will confirm completion of corrective actions.

If any recommendation identifies specific monetary benefits, management must state the amount agreed or disagreed with and the reasons for any disagreement. In the case of questioned costs, the amount FDIC plans to disallow must be included in management's response.

If management does not agree that a recommendation should be implemented, it must describe why the recommendation is not considered valid.

Second, the OIG must determine that management's descriptions of (1) the course of action already taken or proposed and (2) the documentation confirming completion of corrective actions are responsive to its recommendations.

Subsequent to the issuance of the draft audit report, the OIG re-evaluated its decision to question \$1,907,856 related to unsupported time charges. Specifically, the draft audit report, as revised, questioned \$1,907,856 for computer-generated time sheets that were not supported by original time sheets. However, based on further examination of the IPA's audit working papers and the law firm's response to the audit exit conference, the OIG concluded that the IPA's audit procedures did not fully address the reliability of the law firm's computerized time-keeping system. Therefore, because the OIG does not believe sufficient auditing procedures were applied, we do not consider the scope of work sufficient to enable us to express an opinion on the reasonableness of the \$1,907,856 in fees. Accordingly, we reduced questioned costs related to unsupported time charges to \$0.

The GC's response to a draft of this report provided the requisites for a management decision on each of the recommendations. Therefore, no further response to these recommendations is required. Management disallowed a total of \$40,340. Although management's corrective actions sometimes differed from the recommended corrective actions, we consider management's response as providing the requisites for a management decision. A summary of the GC's response to recommendations 4 through 7, 9, and 11 and our analysis follows.

Disallow \$8,592 for photocopying charges billed in excess of actual costs (questioned cost, all of which is unsupported) (recommendation 4). The GC's response allowed \$4,329 and disallowed \$4,263. The Legal Division allowed photocopying charges up to various maximum allowable rates in effect throughout the period in question. The Legal Division disallowed amounts exceeding the maximum allowable rates. Because the law firm did not provide support for its actual photocopying charges as required by FDIC guidelines, the IPA could not determine

the reasonableness of the rate used. The Legal Division subsequently revised its guidelines to allow firms to charge up to \$.08 per page for photocopying. In view of the subsequent revision to guidelines, management's position does not appear unreasonable. Moreover, the law firm provided a cost study after the completion of audit work to support its photocopying charges. Accordingly, the OIG reduced questioned costs to \$4,263.

Disallow \$41,699 for unallowable professional fees (questioned cost) (recommendation 5). The GC's response allowed \$33,023 and disallowed \$8,676. The Legal Division allowed \$27,490 questioned for excessive review of documents because the Legal Division concluded that the questioned time was commensurate with the tasks performed. The Legal Division also allowed \$1,237 of the \$2,013 questioned for inadequate task descriptions because the Legal Division concluded the descriptions were adequate or otherwise allowable. Finally, the Legal Division allowed \$4,296 of the \$12,196 questioned for miscellaneous other categories. The OIG accepts the GC's explanations and, accordingly, reduced questioned costs to \$8,676.

Disallow \$44,540 for attorneys and paralegals who performed secretarial and clerical tasks (questioned cost) (recommendation 6). The GC's response allowed all the questioned charges. Specifically, the Legal Division allowed \$36,165 paid to an expert witness consulting firm that provided litigation support services that could not have been performed by secretaries. The Legal Division also allowed \$8,375 for services that the Legal Division concluded were not secretarial functions. The OIG accepts the GC's explanation and, accordingly, reduced questioned costs to \$0.

Disallow \$32,135 for unsupported expenses (questioned cost, all of which is unsupported) (recommendation 7). The GC's response allowed \$31,514 and disallowed \$621. The Legal Division allowed questioned charges based on expense receipts provided by the firm that correlated with the descriptions of the expenses on the invoices. The Legal Division disallowed \$621 that the firm could not substantiate. The OIG accepts the GC's explanation and, accordingly, reduced questioned costs to \$621.

Disallow \$4,637 for attorneys who performed paralegal tasks (questioned cost) (recommendation 9). The GC's response allowed all the questioned charges. Based on a review of the questioned charges, the Legal Division concluded that the questioned tasks were appropriately performed by an attorney rather than a paralegal. The OIG accepts the GC's explanation and, accordingly, reduced questioned costs to \$0.

Review Legal Division exception letters not addressed in recommendation 10, determine the amount of funds inappropriately paid to the firm, and request a refund of those funds (recommendation 11). This recommendation resulted from the accelerated payment program from the early 1990s. The RTC and FDIC Legal Divisions issued exception letters to firms that delineated disallowances of professional fees and expenses that were either unallowable or required additional information be submitted by the firms to the Legal Divisions. In recommendation 10, the OIG recommended that FDIC disallow \$1,068 related to 3 of 15 unresolved exception letters issued to Brobeck, Phleger & Harrison. Brobeck agreed with the recommendation and the Legal Division disallowed the charges.

Nonetheless, the GC's response did not agree with the recommendation to review all other exception letters to determine whether other inappropriate payments were made to the firm. The Legal Division concluded that such a review would not be cost-effective and any likely benefit would be speculative. Because the scope of the audit covered payments made more than 6 years ago and because of the relatively small amount of recoveries identified from the exception letters addressed in recommendation 10, the OIG accepts the GC's explanation.

As a result of the IPA's audit work, \$2,110,119 was questioned in the draft report transmitted to management. In addition to the recommendations previously discussed, in recommendation 2, the OIG recommended that FDIC disallow or ratify \$51,357 for work performed by unauthorized personnel. The Legal Division ratified \$43,880 and disallowed \$7,477. The OIG accepts the action taken by management and, accordingly, reduced questioned costs to \$7,477.

After considering \$40,340 in disallowances taken by management and management's comments on the IPA's findings, we will report questioned costs of \$40,340 (including \$4,884 in unsupported costs) in our *Semiannual Report to the Congress*.

**LEGAL FEES PAID TO
BROBECK, PHLEGER & HARRISON**

**BY THE FEDERAL DEPOSIT INSURANCE
CORPORATION**

**FOR THE PERIOD
JANUARY 1, 1990 TO DECEMBER 31, 1993**

FINAL REPORT - January 29 1996

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

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Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

I. INTRODUCTION

The Resolution Trust Corporation - Office of Inspector General (RTC-OIG) engaged Mitchell & Titus, LLP (Mitchell & Titus) to audit legal bills paid by the Resolution Trust Corporation (RTC) and the Federal Deposit Insurance Corporation (FDIC) to certain law firms providing legal services to the RTC and the FDIC.

Congressional interest in legal services provided to FDIC is very high because of the significant amount of money paid by FDIC for such services to support the workload of FDIC.

The purpose of our audit was to determine whether the fees paid to Brobeck, Phleger & Harrison (Brobeck) were reasonable and allowable under the terms of the Legal Services Agreements (LSAs) between Brobeck and FDIC and other applicable policies, regulations and guidelines.

Legalgard, Inc. (Legalgard), a subcontractor to Mitchell & Titus, performed detailed judgmental assessments of the reasonableness of fees charged for professional services by Brobeck on five of the matters reviewed during the audit.

The period of the audit was from January 1, 1990, to December 31, 1993. During the audit period, Brobeck was paid \$4,190,922, for various legal services provided to FDIC.

Our audit was performed primarily at the offices of Brobeck in San Francisco and Newport Beach, California from May 1993 to July 1994.

This report covers only fees paid for legal services provided to FDIC. RTC payments are covered in a separate report.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

II. SUMMARY OF FINDINGS AND QUESTIONED COSTS

	Questioned Costs				Page Ref.
	Professional Fees	Expenses	Total	Unsupported Costs	
Computerized Time Sheets	\$1,796,856		\$1,796,856	\$1,796,856	6
Brobeck Billed FDIC for Professional Fees for Individuals Without Prior Written Approval from FDIC	112,019		112,019		8
Professional Fees Billed in Excess of LSA and Approval Letters approved rates	\$74,458		\$74,458		10
Photocopying Charged in Excess of Actual Costs		55,645	55,645		11
Attorneys and Paralegals Billed for Secretarial Functions Performed	43,480		43,480		15
Other Unallowable Professional Fees	35,297		35,297		12
Supporting Documentation Missing for Paid Expenses		32,135	32,135	32,135	17
Research Billed Above the Actual Cost		6,281	6,281		19
Attorneys Billed for Paralegal Functions	4,637		4,637		20
Brobeck Billed and Received Full Payment for Professional Fees and Expenses That Were Partially Disallowed by FDIC	3,970	120	4,090		21
Other Unallowable Expenses					23
• Postage		153	153		
• Travel		80	80		
• Overhead		146	146		
Total:	\$2,070,717	\$94,560	\$2,165,277	\$1,828,991	

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

III. OBJECTIVES, SCOPE OF AUDIT AND METHODOLOGY

OBJECTIVES

The primary objectives of the audit were to determine whether:

1. the law firm's supporting documentation for the charges was proper and adequate,
2. the fees charged by the law firm are allowable under the terms of the agreement with FDIC and applicable policies, regulations and guidelines,
3. the law firm's usual hourly rates are reasonable, and
4. the hours charged to FDIC by the law firm for professional services were reasonably expended.

SCOPE OF AUDIT

The audit was performed on a test basis. During the audit, we reviewed transactions and billings from January 1, 1990, through December 31, 1993. To ensure adequate coverage for significant payments, we selected 45 FDIC invoices greater than or equal to \$25,000 totalling \$2,617,801. We also selected 32 FDIC invoices less than \$25,000 totalling \$274,492. In total, we tested 77 FDIC invoices totalling \$2,892,293 resulting in a value coverage of approximately 69 percent of the total population of \$4,190,922.

METHODOLOGY

Based on the sample selected, we performed the following procedures to verify compliance with the LSAs:

- Reviewed and evaluated the internal control system over billings.
- Reviewed and evaluated the billing procedures.
- Reviewed the LSAs and all other agreements between FDIC and the law firm, as well as all applicable guidelines, policies and regulations.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

- Conducted compliance and substantive tests of fees billed to FDIC by the law firm to determine whether:
 - the law firm's documentation adequately supports the bills, and
 - the fees charged by the law firm were allowable and reasonable under the agreed terms.
- Reviewed compliance with conflict of interest rules.
- Reviewed professional biographical information of those professionals who billed time to FDIC and assessed whether the usual rates charged were consistent with each professional's background and experience and within the range of rates charged for a comparable skill level within the relevant geographical area.
- Reviewed supporting billing detail to assess whether hours charged to FDIC were reasonably expended.
- Verified that all professionals listed on the invoice had been approved to perform work on FDIC matters.
- Reviewed background information and experience of all professionals listed to ensure that their classification and titles were consistent with their background and work performed.
- Verified that the billing rates had been approved by FDIC.
- Ascertained that hours billed were supported by original time sheets.
- Verified the mathematical accuracy of the invoices.
- Obtained explanations for professionals billing more than 12 hours a day.
- Determined whether the FDIC was billed excessive hours by new professionals assigned to FDIC matters for time spent familiarizing themselves with the matter.
- Determined and reviewed the systems in place to identify and correct conflict of interest situations.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

- Verified that the firm has complied with conditions imposed by any "conditional waivers of conflicts of interest."
- Verified that the law firm did not bill FDIC for time spent researching its own conflicts of interest.
- Ascertained that professionals performing work on FDIC matters were not performing services for other clients of the law firm that may present a conflict of interest situation.
- Determined and reviewed the systems in place to ensure that research projects were approved by FDIC prior to their commencement.
- Determined that research projects were approved by the FDIC prior to their commencement.
- Determined that the charges were adequately supported and relate to applicable FDIC matter.
- Determined and reviewed the system for proper control and accounting of reimbursable expenses.
- Determined that expenses charged were allowable under the LSAs.
- Ascertained that charges/reimbursements represented the lower of actual cost incurred or the contracted rates.
- Verified that expenses were adequately supported by original documentation, invoices, etc.
- Determined that travel time complied with LSAs and outside Legal Services Guidelines.
- Performed an exit conference at Brobeck's offices in San Francisco. The participants were Brobeck, RTC-OIG, Mitchell & Titus, RTC Legal Division - Newport Beach and RTC Legal - Washington, D.C. representatives (via phone). At the exit conference Mitchell & Titus presented the findings and reviewed with Brobeck the appropriate ways to respond to each finding and the timetable for the response.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

IV. FINDINGS AND RECOMMENDATIONS

Computerized Time Sheets

As part of the review of legal fees, we reviewed computer generated time sheets used from the automated time records systems maintained by the law firm. The purpose of this procedure was to enable us to verify that the computer-generated time records were supported by original time sheets or other input documents. The original time entry documents could be used to verify the accuracy and validity of the automated time records.

Brobeck informed us that the system was one in which the original, uniform and verifiable entry is an electronic entry. For any invoices where original time sheets were required, Brobeck would have had to produce printouts of those original entries since they did not exist.

With the use of advanced data processing systems, potential risk is enhanced by two factors: manually prepared records being replaced by computer output and audit trails being eliminated or made more difficult to follow. The lack of source input documentation prohibited us from performing transaction testing to verify the following:

- Input data were correctly recorded.
- All authorized transactions were processed without additions or omissions.
- Appropriate audit trails exist.

The absence of source documents to support time entries in the system and the elimination of the input audit trail is considered a deficiency in the internal control structure.

Accordingly, our test of professional hours billed from January 1, 1990, to December 31, 1993, in the amount of \$2,031,450 was done using the computer-generated records. Brobeck extracted records from the main time and billing database and created a new dataset that included time entries for FDIC matters and redacted time entries for all non-FDIC matters. These time entries are considered an output data and not original input data that can be confirmed as accurate and reliable.

The FDIC Guide for Outside Counsel states that "Outside Counsel is required to retain copies of all bills and underlying supporting material, including original time sheets and time and expense adjustment records for at least four years after final payment".

We questioned all professional time billed for the period noted above because the absence of source documents to support time entries is considered a deficiency in the internal control structure.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

This amount includes costs questioned under other criteria within this report as follows:

Total paid to professionals without original time sheets	\$2,031,450
Less: Amount questioned under other criteria	
Employees without prior written approval (See Page #8)	(160,136)
Employees using rates in excess of LSA (See Page #10)	<u>(74,458)</u>
Net amount questioned	<u>\$1,796,856</u>

Recommendation:

1. We recommend that FDIC disallow the \$1,796,856 in billing not supported by original timesheets. (Questioned cost, all of which is unsupported).

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. However, the documentation provided did not address the issue of the absence of input documentation, or system internal controls to preclude changes to input data without a record of such changes.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Professional Fees Billed for Individuals Without Prior Written Approval

During our test of professional fees paid from January 1, 1990, through December 31, 1993, we found that Brobeck billed FDIC for a number of professionals who worked on FDIC matters without prior written approval from FDIC.

The LSAs incorporate Legal Division policies and procedures with which outside counsel must comply. In addition, the LSAs identify the firm's staff who are authorized to work on FDIC's legal matters and the rates authorized for those employees.

Section 3 of the LSA (Rate Structure) states the following: "...personnel may be added to the list, but only by written mutual agreement of the firm and FDIC."

Formal written approval of attorneys and paralegals authorized to work on FDIC matters is not only required but is critical in facilitating FDIC's supervising attorneys' oversight role.

The total amount of fees paid for such professionals was \$160,136.

This amount includes costs questioned under other criteria within this report as follows:

Total paid to professionals without written prior approval	\$ 160,136
Less: Amount questioned under other criteria	
Attorneys and paralegals performing secretarial functions (See Page #15)	(43,480)
Attorneys performing paralegal functions (See Page #20)	(4,637)
Net amount questioned for professionals billed without prior written approval	<u><u>\$ 112,019</u></u>

Recommendation:

- We recommend that FDIC request a refund of \$112,019 from Brobeck for fees billed for employees not included on the firm's LSA.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Professional Fees Billed in Excess of the LSA Approved Rates and Approval Letters

During our testing of professional fees paid from January 1, 1990, through December 31, 1993, we found that Brobeck billed FDIC using professional hourly rates up to \$60 per hour higher than prevailing contract rates for 10 professionals with total of 1,652 hours.

Law firms must charge for legal services in accordance with the fee or hourly rate structure set forth on the schedules attached to the Legal Services Agreements (LSAs) and any subsequent approval letters.

Additionally, section 3 of the LSA states that "The hourly rates for each attorney and para-professional in the Firm who is to work on FDIC matters is set forth on the Rate Structure, attached hereto as Exhibit C and incorporated herein by this reference."

As a result of the condition noted, Brobeck was not in compliance with the LSAs and the incorporated guidance and overbilled FDIC \$74,458.

Recommendation:

3. We recommend that FDIC disallow 74,458 billed in excess of the LSA's approved rates (questioned cost).

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Photocopying Charged in Excess of Actual Costs

We noted that Brobeck billed FDIC for photocopying using an higher rate per page than the maximum allowed by FDIC guidance (e.g., \$0.20 to \$0.22 instead of \$0.15, \$0.15 instead of \$0.08).

In addition, Brobeck provided us with a Facsimile and Copy Cost Summary (cost study) to support the rate charged for photocopying. This cost study was prepared by Brobeck and included apparently unallowable overhead items such as secretarial salaries and space rental costs. We were unable to verify the cost study data because we did not received it until November 1994, three months after the completion of audit field work. We requested Brobeck to explain certain items in the study and were provided with a revised cost study that still included similar, unallowable overhead items. The cost studies prepared by Brobeck do not support actual, unburdened photocopying rates that are required for FDIC billings.

Section 5D., Billing of the LSA, effective September 28, 1990, states that " FDIC will pay for photocopying at actual cost, which will generally not exceed \$.15 per page."

The LSA, effective February 1, 1992, states that "Our relationship also will be governed by and subject to the policies, requirements, practices and procedures set forth in the FDIC's "Guide for outside Counsel" previously provided to you and incorporated herein by reference...."

The FDIC Guide for Outside Counsel states that "Charges for photocopying shall not exceed eight cents per page unless supported by a cost study."

As a result of the condition noted, Brobeck was not in compliance with the FDIC guidance and overbilled FDIC \$8,592 for photocopying.

Additionally, since Brobeck could not support its actual cost for photocopying, we were unable to determine the reasonableness of the rate used for photocopying charges in the amount of \$55,645.

Recommendation:

4. We recommend that FDIC disallow \$55,645 for photocopying charges billed (questioned cost, all of which is unsupported).

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional information supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information (a revised cost study) to support its position. The revised cost study did not support actual, unburdened photocopying rates that are required for FDIC billing. Therefore, the questioned costs were not modified and the findings remains as stated.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Other Unallowable Professional Fees

We noted that Brobeck billed professional's time to FDIC for the following tasks:

- excessive time expended in review and revision of documents
- research Brobeck's own conflict of interest
- preparation of bills
- preparation of case budgets
- preparation of status reports

In addition, Brobeck billed professional's time for excessive review and preparation of documents. The review was done by an attorney with one year experience and was billed at the composite rate of \$200 per hour.

The FDIC Guide for Outside Counsel states that "We [FDIC] do not otherwise pay for outside counsel's overhead. 'Overhead' that we do not pay includes, without limitation, ...time devoted to the preparation of bills."

The General Case Management section of the above mentioned Guide states that "We [FDIC] also expect you to control time carefully and to avoid both unnecessary review of documents and files and extensive polishing of documents."

As a result of the condition noted, Brobeck was not in compliance with the FDIC guidance and overbilled the FDIC \$35,297 based on the following computation:

• Inadequate task description	\$ 906
• Excessive review of documents	27,490
• Research of conflict/preparation of bills, budget and status reports	6,901
	<hr/>
Total Disallowance:	<u>\$ 35,297</u>

Recommendation:

5. We recommend that FDIC disallow \$35,297 for unallowable professional fees (questioned cost).

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Attorneys and Paralegals Billed for Common Secretarial Functions

We noted that Brobeck billed attorneys and paralegal time to FDIC for the performance of secretarial functions such as:

- photocopying documents
- organizing documents
- organize for storage
- supervising file organization
- file and refile
- collate documents
- process vendor bills

These are administrative and clerical tasks that are considered overhead to the Firm and, accordingly, should not be billed to FDIC.

The FDIC Guide for Legal Representation states that "We [FDIC] do not pay any overhead expenses." Additionally, it concluded that "We [FDIC] will not typically reimburse for general overhead expenses."

As a result of the condition noted, Brobeck was not in compliance with the FDIC Guidelines (referenced in the FDIC-LSA) and overbilled the FDIC \$43,480 for time incurred on overhead activities based on the following computation:

Actual overhead/administrative charged by Brobeck	\$	7,315
Actual overhead/administrative charged by subcontractor		36,165
TOTAL	\$	<u><u>43,480</u></u>

Recommendation:

6. We recommend that FDIC disallow \$43,480 for unallowable billing for attorneys and paralegals performing secretarial and clerical tasks (questioned cost).

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Supporting Documentation Missing for Paid Expenses

We selected a sample of 77 invoices paid by FDIC for testing and asked Brobeck to provide us with the source documentation, including original time sheets for professional fees; invoices from third parties and internal reports and expenses supporting all the items selected for testing. However, we were unable to verify certain invoices for expenses because either Brobeck could not locate the appropriate supporting documentation or the supporting documentation presented to us was not appropriate (e.g., photocopying amount with no number of copies made). The total amount of unsupported expenses is \$32,135.

Section 5 of the LSA states that "The Firm shall keep all of its billing records for at least three years from billing date. The Firm shall permit FDIC to conduct an audit or review of the Firm's billing procedures. Firm further agrees to provide additional information concerning its billing procedures and practices and other reports which the FDIC may request without charge."

The FDIC Guide for Outside Counsel states that "Outside counsel is required to retain copies of all bills and underlying supporting material, including original time sheets and time and expense adjustment records for at least four years after final payment. The submission of erroneous bills or requests for reimbursement of inappropriate charges may result in serious sanctions."

All items billed should be supported by adequate documentation, such as original invoices. The documentation should be retained and available for review to establish the validity and reasonableness of amounts billed.

As a result of the conditions noted, Brobeck was not in compliance with the LSAs and FDIC Guidance.

Recommendation:

7. We recommend that unsupported expenses of \$32,135 that were billed to FDIC be disallowed. (questioned cost of \$32,135, all of which is unsupported).

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Legal Research (Westlaw, Lexis) Billed Above the Actual Cost

We noted that Brobeck billed FDIC for research (computer time) at a rate that reflected a 50 percent markup above the actual cost to the firm during the period covered under our review (1990 through 1993).

The FDIC Guide for Outside Counsel states that: "Outside counsel must include in its fees and rates for legal services all "overhead" and "profit." We do not otherwise pay for outside counsel's overhead. "Overhead" that we do not pay includes, without limitation...charges for word processing or computer time (except actual charges for Westlaw or Lexis)...."

As a result of the condition noted, Brobeck was not in compliance with the FDIC guidance and overbilled FDIC \$6,281 for research charges mark-up.

Recommendation:

8. We recommend that FDIC disallow \$6,281 for research charges mark-up (questioned cost).

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Attorneys Billed Paralegal Functions

We noted that Brobeck billed attorney time to FDIC for common paralegal tasks such as:

- preparation of exhibit list
- preparation of witness list
- preparation of interrogatories (Form)
- summarization of depositions
- preparation of records request(s)

These tasks are classified as common paralegal functions by our legal expert (Legalgard) and, accordingly, are billable to FDIC at the paralegal's rate structure and not at the attorney's rate structure.

The FDIC Guides for Legal Representation states that "In connection with bank liquidation matters, the FDIC's Legal Division seeks to provide its client, the Division of Liquidation (DOL), with high quality legal representation a timely, efficient and cost-effective manner."

Additionally, Section 2 of the above mentioned Guide states that "Our [FDIC] overall objective is to seek the best possible resolution of legal matters at the lowest practicable cost."

As a result of the condition noted, Brobeck was not in compliance with FDIC guidance and overbilled FDIC \$4,637 (the difference between attorney and paralegal rates) for time incurred by attorneys performing paralegal functions.

Recommendation:

9. We recommend that FDIC disallow \$4,637 for unallowable billing for attorneys performing paralegal tasks (questioned cost).

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Brobeck Billed and Received Full Payment for Professional Fees and Expenses that Were Partially Disallowed by FDIC

We reviewed 15 exception letters issued by FDIC, as a result of a review of certain invoices by the Legal Divisions. These exception letters delineated disallowances of professional fees and expenses that were either unallowable by the LSA and the incorporated guidance or required additional information to be submitted by Brobeck to the Legal Divisions. All but three exception letters were resolved by Brobeck and FDIC. However, three exception letters that were unresolved (representing four invoices with questioned costs of \$4,090) were paid in full by FDIC.

The FDIC Guide for Outside Counsel states that "In the event the FDIC disputes any bill that has been paid, we [Law Firm] waive all rights to retain the disputed amount promptly on request of the FDIC pending resolution of the dispute."

Section Billing of the FDIC Guide for Outside Counsel states that "Outside Counsel is required to retain copies of all FDIC and RTC-related bills and underlying supporting material, including original time sheets and other time and expense adjustment records, for at least four years after final payments. Please note that invoices already approved by the Legal Division may be included in the audit. Also, the submission of erroneous bills or requests for reimbursement of inappropriate charges may result in sanctions."

Brobeck received all payments in full when they submitted the original bills. Therefore, it is within FDIC's interest to pursue and follow the disallowance letters immediately and either deduct the disallowed amount from the next payment or reach a settlement with Brobeck as to the final disallowed amount.

As a result of the condition noted, Brobeck was paid in full by FDIC \$4,090 that was originally questioned and disallowed.

Recommendations:

10. We recommend that FDIC request Brobeck to refund the FDIC \$4,090 (questioned cost).
11. We also recommend that FDIC review all other exception letters and determine the amount of funds inappropriately paid to the firm and request a refund of those funds.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Other Unallowable Expenses

We noted that Brobeck billed FDIC for various types of expenses that are specifically prohibited in the FDIC guidance, such as:

- postage;
- expenses that are customarily included in the normal overhead or administrative expense of running a law firm, such as office supplies (e.g., binders, stationary);
- travel expenses such as meals and entertainments while on travel.

Section 5., Billing of the FDIC LSA, effective September 28, 1990, and expired on September 27, 1992, states that "FDIC will not pay for ordinary postage charges."

Section 1.B.5 of the FDIC Guide for Legal Representation states that "We [FDIC] do not pay any overhead expenses." Additionally, Section 1.B.5 conclude this section as follows: "We [FDIC] will not typically reimburse for general overhead expenses."

The FDIC Guide for Outside Counsel states that "Hotel accommodations must be moderately priced, and expenses for luxury hotels or special services are not to be charged to the FDIC and are not reimbursable."

As a result of the condition noted, Brobeck was not in compliance with the FDIC guidance and overbilled the FDIC \$379 based on the following computation:

Postage charges	\$ 153
Overhead charges	146
Travel charges	<u>80</u>
Total	<u>\$ 379</u>

Recommendation:

12. We recommend that FDIC disallow \$379 for other unallowable expenses (questioned cost).

Legal Fees Paid to Brobeck, Phleger & Harrison
by FDIC
From January 1, 1990 - December 31, 1993

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

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LEGAL DIVISION COMMENTS¹



FDIC
Federal Deposit Insurance Corporation
550 17th Street, NW, H-10070, Washington, DC 20429

Legal Division
Legal Operations Section/Outside Counsel Unit

March 4, 1999

MEMORANDUM TO: David H. Loewenstein
Assistant Inspector General

THROUGH: William F. Kroener, III [redacted] (b)(6)
General Counsel

(b)(6) William S. Jones
Supervisory Counsel

(b)(6) FROM: Andre M. Douek [redacted]
Counsel

SUBJECT: Audit of Legal Fees Paid by the FDIC to
The Law Firm of Brobeck Phleger & Harrison
(San Francisco, California)

RECEIVED
 INSPECTOR GENERAL
 MARCH 11 1999
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This memorandum constitutes the Legal Division's response to both the Office of Inspector General's ("OIG") draft audit report dated July 30, 1998 (Exhibit A) and the law firm's response dated November 2, 1998 (Exhibit B). The audit report pertains to invoices paid for work performed on behalf of the Federal Deposit Insurance Corporation (FDIC) by the law firm of Brobeck, Phleger & Harrison ("BP&H").¹ Owing to their voluminous nature, the supporting schedules to the audit report are not included in the Exhibits.

The Inspector General's audit report included an examination of 77 FDIC invoices totaling \$2,892,293 which corresponds to approximately 70% of the \$4,190,922 paid to the firm from January 1, 1990 through December 31, 1993. Of the 77 invoices, the auditors selected 45 FDIC invoices greater than or equal to \$25,000 totaling \$2,617,801 and 32 invoices less than \$25,000 totaling \$274,492. After adjustment by the OIG, the draft audit report identified 11 general areas of questioned costs totaling \$2,110,029 and broken down as follows: \$2,062,522 in professional fees and \$47,507 in expenses.

¹ It should be noted that the audit of Brobeck Phleger & Harrison was done by Mitchell & Titus, LLP ("MT"), a public accounting firm contracted by the RTC OIG. MT, in turn, subcontracted the assessments of the reasonableness of the fees charged for professional services to Legalgard, Inc.

¹The attachments referred to in the Legal Division's response are not included in this appendix.

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In response to the audit report, the law firm submitted a comprehensive and detailed letter with supporting documentation addressing each questioned cost and the OIG's recommendations and conclusions. The firm also criticized the timing of the audit report, noting the exit conference with Mitchell & Titus occurred in July, 1995, but the draft audit report was not received until three years later.

In conducting the audit, the auditors performed certain procedures to verify compliance with the firm's LSA. They also examined original documentation and invoices for accuracy and to determine whether they were properly reimbursable. In addition, the auditors undertook an examination of, among other things, a review of the internal control system over billings, a review and an evaluation of the billing procedures, a review of the LSA, and compliance and substantive testing to determine whether the law firm's documentation adequately supported the bills, and whether the fees charged by the firm were allowable and reasonable under the agreed terms. After weighing the merits of the arguments presented by both sides, the Legal Division determined that it will seek reimbursement from the law firm for the disallowed amounts indicated below totaling \$40,340 and will pursue collection activities as appropriate.

With this background in mind, our conclusions regarding each finding and recommendation and the law firm's response are set forth below.

Condition 1: Computerized Time Sheets

The OIG questioned \$1,907,856 in billings because the firm did not have original time sheets to back its computer-generated time records. The auditors indicated that the firm had informed them that the record-keeping system was one "in which the original, uniform and verifiable entry is an electronic entry" rather than a hard-copy entry on an original time sheet.

The auditors indicated that the risk of relying on computer-generated time records was increased by two factors: "manually prepared records being replaced by computer output and audit trails being eliminated or made more difficult to follow." The auditors cautioned that the "lack of source input documentation" prevented them from ascertaining whether the data was transmitted correctly, whether all authorized transactions were processed without additions or omissions, and whether "appropriate audit trails" existed. The auditors concluded that the absence of original source material to support the time entries and the elimination of an "appropriate audit trail" created a deficiency in the internal control structure of the firm. Accordingly, they questioned all professional time billed during the audit period and recommended that

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the Legal Division disallow \$1,796,856 net of amounts questioned under other criteria. (That figure was later revised by the OIG to reflect a net amount of questioned costs under this Condition totaling \$1,907,856.)

For its part, the firm explained that the original time sheets as "required by the contracts have been retained by the firm—they are in electronic form—and appropriate time adjustment records have also been maintained. The firm operates on a computerized billing system with all necessary and appropriate safeguards to insure integrity and reliability. There is not even a hint or suggestion in the MT draft report that the Corporations were billed inappropriately or erroneously as a consequence of the Firm's use of its computerized billing system."

In support of its position, the law firm argued that case law held that computerized records are "originals." The firm pointed out that FDIC and RTC guidelines did not require fee counsel to use and retain original handwritten time sheets; and because the Corporation received value for the services rendered, it cannot now raise a technicality as justification for disallowing those fees. Moreover, the firm argued that under the legal principle of quantum meruit, it is entitled to the fair value of the benefit conferred on the RTC.

The FDIC guidelines in effect during the audit period did not require that the firm use and retain handwritten time sheet entries, nor did they describe what records must be generated and maintained or require that the firm establish a particular kind of record-keeping system. On December 31, 1997, the Legal Division published its electronic billing guidelines to address the types of concerns raised by the auditors. These guidelines became effective for legal fees incurred on or after February 15, 1998. Since the Legal Division's own policies during the audit period did not require the law firm to maintain handwritten time sheets, nor did they specify internal controls for electronic billing systems, we cannot impose on the firm requirements that were not present when the legal services were rendered. **Accordingly, the Legal Division will not disallow any questioned costs under this recommendation.**

Condition 2: Professional Fees Billed for Individuals Without Prior Written Approval

The OIG questioned \$51,357 of costs for professional fees that were billed "for a number of professionals who worked on FDIC matters without prior written approval from FDIC."² In its report, the auditors quoted from the September 28, 1990 LSA which provides the following under Section 3 (Rate Structure):

² MT assessed the questioned costs under this Condition at \$112,019 but the OIG reduced that amount to \$51,357.

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The hourly rates for each attorney and paraprofessional in the Firm who is to work on FDIC matters is set forth on the Rate structure, attached hereto as Exhibit C and incorporated herein by this reference. Personnel may be added to the list, but only by written mutual agreement of the Firm and the FDIC.

In addition, the OIG indicated that the LSA rate schedules can only be amended with the written consent of the Legal Division. The auditors pointed out that, "Formal written approval of attorneys and paralegals authorized to work on FDIC matters is not only required but is critical in facilitating FDIC's supervising attorneys' oversight role." The underlying basis for questioning these fees is the auditors' concern for quality control to ensure that all employees working for outside counsel firms are qualified and have been properly evaluated by the supervising attorney and by Legal Division management.

The December, 1991 FDIC Guide for Outside Counsel also provides the following:

Complete the matrix form to identify as to each attorney or paraprofessional in the firm who may provide services to us: state licenses; area(s) of expertise; years in practice; time with the firm; status within the firm as partner or shareholder, senior associate, associate, paraprofessional, etc.; billable rate under the firm's usual rate structure; hourly rates to the Legal Division; lowest billable rate currently in effect with public sector or non-profit clients; and minority and women attorney status or information.

Furthermore, the February 1, 1992 LSA which the firm entered into with the FDIC provides as follows concerning this issue:

You represent, warrant and covenant that...(iii) each of the attorneys and paraprofessionals in your firm who provides services to the FDIC has reviewed, understands and agrees to act strictly in compliance with all provisions, requirements and policies (including statutory and regulatory provisions) identified in the Guide.

This LSA is also clear on the issue that changes must be made only with the written consent of the Legal Division.

Your firm agrees to provide legal services in accordance with the fee or hourly rate structure (for each attorney and paraprofessional assigned to work on FDIC matters) set forth on the attached schedule(s), which may be amended only by written consent of the Legal Division.

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In its response the law firm admitted that "[S]ome work was done by the Firm with less than complete technical compliance with timekeeper 'pre-approval' requirements (such as the requirement that timekeepers be listed in an addendum to an LSA)." However, it also pointed out that this work was performed "with no objection by the clients," and added the following comment:

We worked for years under circumstances in which our people pitched in as needed to help the RTC with no complaint or objection by those at the Corporation supervising our work....A blanket position that nothing should be paid—even though valuable services were provided—is unfair, wrong, and contrary to law, including principles of quantum meruit.

The Guide for Outside Counsel was developed to ensure that the FDIC obtained "the very best legal advice possible in a professional and cost-effective manner." General Counsel Alfred J.T. Byrne explained in his introduction to the Guide that the Guide "sets forth the policies and procedures governing the Legal Division's relationship with outside counsel, including our expectations of counsel engaged to assist us." The General Counsel concluded his message to outside counsel with the following comment:

Our outside counsel is obligated to conform to the requirements set forth in this Guide. Every attorney we employ is expected to read and retain a copy of this Guide.

In addition, the Guide itself reinforces the General Counsel's position that the Guide is an integral component of the contract for legal services entered into between the firm and the FDIC by expressing the following policy:

This Guide is an integral part of the terms under which attorneys are engaged to represent the FDIC and governs all such engagements. Every attorney and paraprofessional who works on FDIC matters must read and maintain familiarity with this Guide.

Moreover, the December, 1991 Guide provides the following:

Outside counsel is required to charge the same rates for all matters it handles on behalf of the FDIC. Such matters include all work done for entities in conservatorship or receivership, and all matters the legal fees for which are reimbursed by the FDIC. The rates charged by outside counsel shall be the lowest of (a) the fee schedules attached to the LSA, (b) the rates negotiated with any FDIC office for any matter, or (c) the rates charged by outside counsel for similar work performed on behalf of clients other than the FDIC.

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The firm was under a contractual obligation to obtain written approval from the FDIC before it engaged any additional personnel to work on FDIC matters. As pointed out above, the policies of the Legal Division are clear on this issue. The Legal Division examined all of the questionable invoices where individuals billed for their services without being listed on the LSA and without prior written approval from the Division. In the absence of information required by the Guide, such as years in practice and usual hourly billing rates, the Legal Division has determined that it will ratify the rates of the affected individuals at the lowest approved rate for a professional in their category (e.g., attorneys, case assistants, legal assistants, summer associates, and paralegals). In determining the allowable rate for each category of employee, we approved the rate for that professional at the lowest agreed billing rate as it appears on the various agreements signed with the firm, the 01/24/90 FDIC letter to Brobeck, the 09/18/90 LSA, or the 02/01/92 LSA, depending on the date of the invoice where unauthorized billers appear (please see attached Exhibit C).

For example, where it appears that an unauthorized billing attorney billed at \$130 per hour during the month of January, 1991, we ratified that attorney's rate at the lowest agreed billing rate for attorneys on the 09/28/90 LSA and as specified in the 01/24/90 FDIC letter to the firm. The lowest rate in that case is \$105 per hour for attorneys as indicated in those agreements. Consequently, the Legal Division ratified this particular attorney's rate at \$105 per hour and disallowed the \$25 per hour which was not approved or agreed to by the FDIC. In addition, the fees of categories of employees such as summer associates or employees whose title was "others" who were not listed as a category of employee in the agreements during the period in question were not ratified, and their billable hours were disallowed entirely.³

Similarly, where it appeared that the employee in question billed at a rate equal to the lowest agreed billing rate for that category of employee, the employee's rate was ratified and no amount from his or her billable hours was disallowed. For example, where a case assistant billed at a rate of \$50 per hour, that rate was ratified and approved for payment since it equaled the agreed billing rate for case assistants as listed on the agreements during the period of services in question.⁴

³ Those amounts totaled \$2,548.50 and consisted of the billings of four different individuals whose category of work was not included in any agreement during the period of services under review.

⁴ The rate for paralegals also was ratified at \$85 per hour because this was the agreed upon billing rate for paralegals as listed on the fee matrix of the LSA dated 02/01/92. Since all of the unauthorized paralegals billed at the same rate as the authorized paralegals identified on the LSA, no amount from the billable fees of the unauthorized billers was disallowed.

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Accordingly, the Legal Division will disallow the amounts in excess of the lowest LSA rate for those categories of employees listed on the attached Exhibit C. Those amounts total \$7,477.25. The remaining questioned amounts are ratified.⁵

Condition 3: Professional Fees Billed in Excess of the LSA Approved Rates and Approval Letters

The OIG questioned \$11,575 for professional fees paid from January 1, 1990, through December 31, 1993, that were billed "up to \$60 per hour higher than prevailing contract rates for 10 professionals with a total of 1,652 hours." The OIG argued that law firms must charge for legal services in accordance with the fee or hourly rate structure set forth on the schedules found in the LSA and any subsequent approval letters. The OIG cited the LSA as a basis for questioning these fees. The pertinent parts of the September 28, 1990 LSA provide as follows:

The hourly rates for each attorney and paraprofessional in the Firm who is to work on FDIC matters is set forth on the Rate Structure, attached hereto as Exhibit C and incorporated herein by this reference. Personnel may be added to the list, but only by written mutual agreement of the Firm and the FDIC.

The February 1, 1992 LSA confirms this position and allows that:

Your firm agrees to provide legal services in accordance with the fee and hourly rate structure (for each attorney and paraprofessional assigned to work on FDIC matters) set forth on the attached schedule(s), which may be amended only by written consent of the Legal Division.

In addition, the December, 1991, FDIC Guide for Outside Counsel provides that :

If rates, abilities, areas of expertise, conflicts of interest and other factors used in evaluating outside counsel on a competitive basis are acceptable, the Division will contact you to negotiate the proposed fee schedule attached to the LSA that you executed and submitted with your application materials. The Division generally enters into a two-year LSA. Absent compelling reasons, no increase in the fee or rate schedule attached to the LSA will be permitted during its term.

⁵ Since the General Counsel has complete delegated authority regarding the hiring and paying of outside counsel with respect to issues raised by the report, his signing of this memorandum should be deemed a ratification or approval of billing rates to the extent indicated herein.

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The RTC Guide for Outside Counsel, published in February, 1992, takes a similar position:

The Legal Division generally enters into a two-year LSA. Absent compelling reasons, no increase in the fee or rate schedule will be permitted during the term of the LSA.

The law firm responded to the auditors' recommendations by indicating that for a period of time from July 1991 through January 1992, "a firmwide rate adjustment was reflected in FDIC billings with no corresponding change in the LSA. But, some portion of this gross amount has already been refunded by the Firm." However, the firm did not provide any evidence that it refunded the amounts overbilled. It cited various reasons, such as the passage of time and the expense involved in researching these matters, as mitigating reasons for not submitting the necessary back-up documentation.

As indicated above, the contractual agreements entered into between the firm and the FDIC make it clear that no increase in the rate structure would be permitted, unless by written mutual agreement or because of compelling reasons. The firm did not provide any letter granting it authorization to increase its rates, nor did it provide any explanation that would justify an increase in the rates beyond what was contractually agreed to in the LSA matrix. **Accordingly, the Legal Division will disallow the entire amount under this Condition totaling \$11,575, but will reconsider its decision if the firm provides adequate documentation showing FDIC approval of an increase in the approved rates.**

Condition 4: Photocopying Charged in Excess of Actual Cost

The OIG questioned \$8,592 (reduced from \$55,645 originally questioned by the auditors) for photocopying costs charged to the FDIC at a higher rate per page than the maximum rate allowable by the FDIC. The auditors reference the FDIC LSA dated September 28, 1990 which provides that, "FDIC will pay for photocopying at actual cost, which will generally not exceed \$.15 per page."

In its response, the firm indicated the following:

Our various contracts with FDIC and RTC employed several different standards for photocopy expense....Before September 28, 1990, there was no overarching written fee agreement on FDIC or RTC work. Cases and matters were assigned to the Firm on an ad hoc basis. Our normal billing rates were applied, as modified by specific agreements between the parties. As to photocopy expense, our August 8, 1989 letter from :

explained that our photocopy rates were \$.20 and \$.22 cents

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per page, depending upon which Firm office was involved. These were the rates charged until we entered into an LSA on September 28, 1990. That LSA covered both FDIC and RTC work.

, dated August 8, 1989 did, in fact, exist in Legal Division files. That letter provided the following regarding copying:

The firm charges 20 cents per page (22 cents per page in Los Angeles) for copying, which represents our cost and does not include a profit mark-up or administrative surcharge. The firm provides copying as a necessary service to its clients but it does not view copying as a profit creating activity.

On September 28, 1990, the firm signed an LSA with the FDIC which also covered the RTC. This agreement provided the following in connection with photocopying:

FDIC will pay for photocopying at actual cost, which will generally not exceed \$.15 per page. When economically feasible, large copying projects should be sent out to a copying service. Clerical time for photocopying will not be paid.

Thereafter, the FDIC signed an LSA with the firm on February 1, 1992 which incorporated the FDIC's position vis-à-vis photocopying set forth in the December, 1991, FDIC Guide for Outside Counsel which provided that "[c]harges for photocopying shall not exceed eight cents per page unless supported by a cost study."

Accordingly, the law firm's photocopying charges for the audit period were governed by three different agreements. Prior to the first LSA, the Legal Division allowed the firm to bill for photocopying at \$.20 per page (or \$.22 per page if the Los Angeles office was used). This agreement remained in effect for a period of nine months during the audit period at which time the first LSA took effect on September 28, 1990. As indicated earlier, the first LSA reduced the photocopying charge to actual cost, generally not to exceed \$.15 per page. The Legal Division customarily allowed firms to bill at this maximum rate until publication of the Guide in December, 1991, which further reduced the photocopying charges to \$.08 per page.

In addition, the firm indicated that it provided the auditors with a cost study to support the rate charged for photocopying. In its letter, however, the firm included a spreadsheet titled "Analysis of FDIC Copying Expenses," which showed all the charges for photocopying by the firm on all invoices audited by MT. In the "Comments" section of that spreadsheet, the firm made several notations to explain its charges for photocopying and any excess charges the firm made above the authorized rate. In its analysis of these expenses the firm made the following four (4) points:

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1. "Through 9/28/90, the firm's contract with RTC/FDIC provided for 20 cents or 22 cents per page, depending on the firm office involved....Although the selected invoices before 10/31/90 generally did not state the number of pages copied, it is clear that the charges before 10/31/90 (i.e., the invoice dated 10/31/90 which covered fees billed from 10/01/90) were at those rates."

2. "As is apparent from the data displayed (in the spreadsheet), there was a brief period of time after the RTC/FDIC LSA took effect in which photocopy charges were made at the 'old' rates. It is also apparent that the rates were reduced to \$.15 per page beginning April 30, 1991. The total 'excess' above 15 cents per page from 10/31/90 through 3/31/91 is \$3,189.29. The firm billed at \$.15 per page thereafter through the 06/30/92 invoice."

3. "It appears that there was a brief period after the new RTC LSA (the LSA dated 02/01/92) became effective during which some copying was charged at the 'old' rate of \$.15 per page. The total 'excess' above 8 cents per page is \$1,001.28."

4. "Virtually all per page charges calculated from the face of the invoices were at 8 cents beginning July 31, 1992 and it is therefore apparent that the per page charge was almost certainly 8 cents in those instances where the invoice did not state the number of pages copied. The total of post-July 31, 1992 charges in 'excess' of \$.08 per page was \$72.00."

Based on the foregoing, it appears that the law firm overcharged the FDIC \$4,262.57 in photocopying expenses. The firm's cost study was made available to the auditors, but was not included in the firm's response to the draft audit report. We agree with the firm as to charges prior to 09/28/90, the date of the first LSA. Thereafter, the firm was permitted to charge \$.15 per page until December 31, 1991 (publication of the FDIC Guide) when a rate of \$.08 per page became effective.

Accordingly, the Legal Division will disallow \$4,262.57 under this Condition and will demand reimbursement from the firm for this amount.

Condition 5: Other Unallowable Professional Fees

The OIG questioned \$41,699 that the firm billed for professional time for various reasons such as excessive time expended in review and revision of documents, researching the firm's own conflict of interest, and preparing bills, case budgets and

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status reports.⁶ In addition, the auditors indicated that the firm billed excessively for professional time by reviewing and preparing documents when the attorney in question had only one year experience and billed at a composite rate of \$200 per hour.⁷

The auditors identified three (3) separate areas of questioned costs under the general rubric of "Unallowable Professional Fees." The questioned costs determined by the OIG are: inadequate task description \$2,013 (originally \$906 per MT); excessive review of documents \$27,490; and research of conflict/preparation of bills, budget and status reports \$12,196 (originally \$6,901 per MT).

The OIG bases its position on the following provision which is found in the FDIC Guide for Outside Counsel:

Outside counsel must include in its fees and rates for legal services all "overhead" and "profit." We do not otherwise pay for outside counsel's overhead. "Overhead" that we do not pay includes, without limitation, secretarial or clerical overtime (unless such overtime is requested by us or occasioned by an emergency situation created by the FDIC), charges for word processing or computer time (except actual charges for Westlaw or Lexis), and time devoted to the preparation of bills.

In addition, the OIG references the following paragraph in the Guide to support its position that the FDIC does not authorize spending excessive time reviewing and revising documents.

We also expect you to control time carefully and to avoid both unnecessary review of documents and files and extensive polishing of documents. We expect timely, cost-effective solutions.

For its part, the law firm made the following argument:

⁶ There are two figures reflected under this category of questioned costs as the amount for total recommended disallowances. The workpapers indicate that this figure is \$41,699, while the draft audit report lists the total recommended disallowance as \$35,297. But the draft audit report was corrected subsequently with a handwritten notation that read, "See revised summary of questioned costs" to reflect the figure arrived at in the auditors' workpapers of \$41,699.

⁷ The LSA dated February 1, 1992 contained the following statement which appeared on the fee matrix: "The firm has decided to offer a 'blended rate' of \$200.00 for all attorneys listed (which includes partners and associates). The \$85 paralegal hourly rate remains the same." This is consistent with provisions of the Guide which state that "[t]he Division also welcomes offers involving alternative rate structures such as blended, flat, contingent and other innovative rate proposals."

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We believe the descriptions comport with practice in the profession and with the requirements of our contracts. So far as we can tell, MT retained legal "consultants" who profess to apply judgmental standards to time descriptions. The "consultant" had no substantive understanding of the legal issues involved in the many cases involved in the audit. Neither was the consultant able, long after the bills had been sent and approved for payment, to step into the shoes of the supervising attorney who reviewed and approved those bills when they were received (i.e., when the circumstances allowed a person familiar with the facts of the case and the Firm's work to understand the descriptions of the services provided). This resulted in an exercise of judgment that was not informed by any of the facts necessary to make a good judgment.

Inadequate Task Description

Under the category "inadequate task description," the audit workpapers identified three entries totaling \$906. MT control number 1 of invoice number 1015476 for \$180 appears to be a duplicate entry generated on the same day by the same attorney and describing the same activity. On March 1, 1993, attorney hours for the following activity: "Read and analyze requests for documents received from defendant." This identical entry appears again on the same page in invoice number 1015476. This does not appear to be an "inadequate task description." **However, since this is an apparent duplicate entry, it will be disallowed.**

MT control number 21 of invoice number 741607 questions \$596 for travel time that was not discounted at 50% as required by the Guide. On November 16, 20, and 28, 1990, case assistant traveled to the FDIC offices in Irvine, California "to review documents in preparation of upcoming document production." On all three entries, the time was billed at the full rate of the case assistant rather than at the discounted rate of 50% of her hourly rate of \$50. Again, this does not appear to be an "inadequate task description." **However, since this is a violation of the Guide which provides that outside counsel will reduce its hourly rate by 50% while on travel status, the entire amount of \$596, which represents the 50% overcharge, will be disallowed.**

MT control number 23 of invoice number 754092 for \$130 was questioned by the auditors for not being specific in describing what was researched. On January 9, 1991, attorney charging an hourly rate of \$130, billed for the following activity: "Ownership of director's qualifying shares and permissibility of a pledge - research 12 USC Section 72." The description of the research is specific and requires no additional explanation. No other questioned entries for "inadequate task description" were identified in the audit workpapers. **Accordingly, only \$776 will be disallowed under this category (\$180 plus \$596).**

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Excessive Review of Documents

Under the category titled "excessive review of documents," the auditors questioned \$27,490. MT control number 42 of invoice number 943442 lists 290 separate transactions over a period of time from November 5, 1992 to November 25, 1992 for a total of 113.20 hours billed at an hourly rate of \$200 for a total of \$22,640. The number of transactions identified range from 7 per day to a high of 47 where the auditors determined that an excessive amount of time was spent reviewing documents.

The auditors noted in the workpapers that this was the first month that attorney was assigned to case." They added the following comment: "[g]etting familiarize [sic] with the case, not contribute to the case." In short, the auditors argued that since the attorney was new to the case, he should not have billed 113.20 hours for the purpose of "reviewing documents." However, an examination of some of the individual entries under this subcategory provides a different perspective.

On November 6, 1992 attorney billed 12.50 hours in 47 separate invoice entries. These entries range from .10 hours in duration each to .75 hours and describe specific work which the attorney in question performed. A representative sampling of this work reads as follows: "review documents for use deposition to select trial exhibits" for .50 hours; "review file regarding assignment restrictions in leases to select trial exhibits" for .25 hours; "review memorandum regarding exhibit list provisions to select trial exhibits" for .25 hours; "review file regarding capital restructure workpapers - file 1, to select trial exhibits" for .50 hours; "review file regarding capital restructure workpapers - file 2, to select trial exhibits" for .25 hours; "review file regarding September 1987 restructure proposal" for .25 hours; "review file modifications" for .50 hours; "review file regarding for .20 hours; and "review file regarding insurance" for .25 hours. None of the entries is duplicated. Each entry reviews a different aspect of trial exhibits, documents used in depositions, and files related to a plan of restructuring. These are legitimate entries in preparation for trial, and the amount of time expended on each entry does not appear excessive by any means. Spending fifteen or twenty minutes to review documents contained in a file is not unusual and is consistent with the amount of time other attorneys under similar circumstances would spend. **Accordingly, none of these charges will be disallowed.**

Under another subcategory of "excessive review of documents," the auditors questioned the use of a legal assistant for a task the auditors believed should have been performed by a secretary for a total of \$3,310. For example, in one entry dated 11/11/92, the auditors questioned \$212.50 billed for the preparation of documents for production because they concluded that this was a "common secretarial function." In

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another entry, the auditors questioned \$2,200 for "common secretarial function" performed by a legal assistant over 11 hours on 11/05/92.⁸ However the task description for this entry makes clear that this task could not have been performed by a secretary. The entry reads as: "document production, reading and selecting documents for preference backups. (Deadline required 11 hours)." **Accordingly, none of these charges will be disallowed.**

Another entry under this subcategory is found in MT control number 43 of invoice number 980570 for \$2,050. The explanation put forth by the auditors for questioning these charges is the same as the explanation advanced above, namely, that is an "associate with 1 year experience. Excessive review of file and documents - Getting familiarize [sic] with the case, not contribute to the case." However, as was the case above, spent a reasonable amount of time reviewing documents in preparation for trial. On December 1, 1992, for example, on 4 different time: spent between .25 hours and .50 hours reviewing files, exhibit lists, indemnity agreements, bond interest payments and extension agreements. Spending 1.25 hours on 4 different occasions is not excessive given the types of documents being reviewed and the complexity of those documents. **Accordingly, no charges will be disallowed under this category.**

Research of Conflict, Preparation of Bills, Budgets and Status Reports

The auditors also questioned \$12,196 as charges that should have been absorbed by the firm and which relate to the research of the firm's conflict of interest, the preparation of bills, budgets and status reports.

As indicated above, the OIG references the provision in the Guide which indicates that the FDIC will not pay for outside counsel's overhead. The Guide goes on to make clear that "overhead" includes the time devoted to the preparation of bills. Generally, time spent in researching the firm's own conflict of interest questions and in the preparation of bills, budgets and routine status reports is not separately compensable, but is to be absorbed in the hourly rates billed for substantive legal work.

For its part, the firm indicated that "a fair resolution of these items would be \$7,900, and we would ask that the draft report be revised so as to make the total for this category no more than \$7,900." Due to the difficulty of tracing all the questioned costs back to the audit workpapers, the Legal Division concurs with the firm's position, and concludes that disallowing \$7,900 under this category of questioned costs is a fair

⁸ Although the auditors' workpapers indicate that the questioned amount is \$2,200, the invoice reflects only \$935 (11 hours times the billable hourly rate of \$85 for this particular legal assistant). This is the only entry by legal assistant on 11/05/92.

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and reasonable resolution of the differences between both parties on this issue insofar as research of conflict, preparation of bills, budgets, etc. are concerned.

Since this total amount (\$7,900) covers the individual transactions that have been identified above for disallowance, those amounts will be incorporated here as part of this total amount to realize a disallowance under this subcategory for research of conflict/preparation of bills, budget, and status reports only totaling \$7,900.

Accordingly, the Legal Division will disallow \$7,900 under this subcategory of questioned costs.

The total disallowed amount under Condition 5 is \$8,676 (\$7,900 plus \$776 disallowed above.)

Condition 6: Attorneys and Paralegals Billed for Common Secretarial Functions

The OIG questioned \$44,450 in fees for work that should have been performed by secretaries. The common secretarial functions identified by the OIG includes the following: photocopying documents, organizing documents, organizing for storage, supervising file organization, filing and refiling, collating documents, and processing vendor bills. The OIG argued that these activities are administrative or clerical in nature and are considered overhead to the firm, and therefore, are not billable to the FDIC. In addition, the draft audit report broke down these questioned costs into two categories: actual overhead/administrative charged by Brobeck (\$8,375), and actual overhead/administrative charged by the subcontractor (\$36,165). The OIG quoted from the FDIC Guide for Legal Representation which provides that the FDIC will "not pay any overhead expenses," nor will it "typically reimburse for general overhead expenses."

For its part, the firm indicated the following:

The draft recommends disallowance of \$44,450, said to be attributable to the performance of "secretarial" functions by professional timekeepers. Of this amount, \$36,165 is attributable to charges by _____ an expert witness consulting firm which provided forensic accounting services in the _____ matter.

We have reviewed the Brobeck, Phleger & Harrison charges which the draft report questions. These charges, which total \$8,375, reflect two judgment calls—first by the attorney performing and recording time for the service (rather than delegating to a secretary) and second by the oversight attorney (employed by the client) who reviewed and approved the bills. That review and approval

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process occurred in a context-rich setting, and there is no substantial basis for second guessing the charges years after they occurred. This is especially true when, as is the case here, the persons involved at the FDIC and at Brobeck are no longer readily available for comment or explanation. [In a separate footnote, the firm indicated that the auditors had made a mathematical error on \$1,265 in connection with invoice number 943422 (MT control no: 42).]

....

...Brobeck engaged and paid [redacted] with the express approval of the FDIC. [redacted] provided complex litigation support services and necessarily devoted a large staff of professional and skilled temporary employees to the project. [redacted] made professional judgments about staffing. Brobeck reviewed, approved, and paid for the services, and billed FDIC for reimbursement. FDIC, in turn, reviewed [redacted] invoices and paid the charges. Indeed, Brobeck was no more than a conduit for the charges....The [redacted] charges were well within the norm for complex litigation support billings. The correspondence between Brobeck and FDIC makes it clear that FDIC was well aware of and approved [redacted] billings....

A representative sample of the questioned charges was reviewed. MT control number 40 of invoice number 927991 identified \$2,000 in questionable costs that occurred on 4 different occasions in October, 1992. None of these entries described work typically done by secretaries. For example, on October 19, 1992, attorney [redacted] billing at an hourly rate of \$200 for 4.7 hours performed the following work: "[r]eview and collate documents to be produced to [redacted] to determine relevance." Since this was a defensive litigation, the attorney was reviewing documents that had to be produced to the plaintiffs in the action. This work does not encompass the type of work normally done by secretaries. It is work that should be performed by a lawyer.

On October 13, 1992, attorney [redacted] billed 2.20 hours for the following work: "[r]eview and collate all documents located at Stockton office of [redacted] are responsive [redacted] requests." This too is not secretarial work. It is not a "secretarial function" to review documents pursuant to a document production request. If this were a secretarial function, the FDIC would have hired secretaries to represent its legal interests at a fraction of the cost it paid to fee counsel.

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On November 5, 1992, legal assistant _____, billing at an hourly rate of \$85 for a total of 11 hours for \$935, performed the following work:⁹ "[d]ocument production, reading and selecting documents for preference backups. (Deadline required 11 hours)." This also does not appear to be work normally done by secretaries. **Accordingly, none of these charges will be disallowed.**

The expenses related to the subcontractor's invoices involve two separate invoices totaling \$36,165. The Legal Division examined invoice number 917267 with questioned costs totaling \$17,194. The actual bill from _____ totaled \$32,394, and of that amount \$6,644 was for "out-of-pocket expenses." The bill was for professional services rendered in connection with _____ on the _____ case during the month of September, 1992. The firm provided forensic accounting services in support of the litigation. Much of this work totaling \$5,040 was undertaken by various consultants _____ to train and supervise seven (7) temporary personnel who were then asked "to recognize various types of documents and to interpret the documents which were more difficult to understand." On another entry totaling \$4,550 _____ consultants trained and supervised 8 to 11 temporary personnel to sort documents in different categories by date. This work could not have been done by a secretary. It required seasoned professionals with the requisite background and experience to enable them to train and supervise individuals to perform a specific job function. These responsibilities are better left to individuals who possess the necessary skills to allow them to train others to perform routine tasks. **Accordingly, none of the charges by the subcontractor will be disallowed, and none of the questioned costs under this Condition will be disallowed.**

Condition 7: Supporting Documentation Missing for Paid Expenses

The OIG questioned \$32,135 in expenses where the law firm did not provide the appropriate supporting documentation as back-up for the billings it submitted to the FDIC. The draft audit report indicated that the auditors had selected a sample of 77 invoices paid by the FDIC for testing and asked the law firm to provide "source documentation," including original time sheets for professional fees, invoices from third parties and internal reports and expenses supporting all the items selected for testing. The auditors added that, "[a]ll items billed should be supported by adequate documentation, such as original invoices. The documentation should be retained and available for review to establish the validity and reasonableness of amount billed."

⁹ The firm's claim of a mathematical error on the auditors' review of this bill is correct. The total billed by this legal assistant was \$935, but the auditors calculated \$2,200 for this entry and consequently overstated the questioned costs by \$1,265.

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The law firm responded by indicating the following:

The issue here is "backup" documentation for expenses paid by the Firm and billed to FDIC. We are unable to ascertain how MT generated the "questioned amount." Nothing in the draft report or in the reams of documentation that preceded it allows us to deduce the standards applied or the assumptions made in order to "question" \$32,135. The auditors examined 77 invoices. The draft report asserts that documentation for the questioned items could not be located or was "not appropriate." Only one example of "inappropriate" documentation is listed--charges for photocopying with no listing on the invoice of the number of copies made. [In a separate footnote, the firm implied that the auditors may be "double-dipping" since the photocopying expenses are dealt with separately in another part of the draft audit report.] The draft report takes the position that only "original" backup is acceptable. Otherwise, it is impossible to ascertain what documentation was deemed by MT to be "inappropriate."

Whether documentation is "appropriate" depends first of all on contractual requirements. In this regard, the draft report shows on its face that MT applied a standard contrary to the terms of our contracts. The Guide for Outside Counsel cited by MT requires counsel to retain "copies of all bills and supporting material." Nonetheless, the draft report states (with no support or citation) that expense bills should be "supported by adequate documentation, such as original invoices." There is no legitimate basis for MT to rewrite our FDIC contracts so as to impose a requirement for maintaining "original" vendor bills when the contract explicitly approves retention of copies of those bills.

We painstakingly pulled documentation on the thousands of expense charges on the 77 invoices that form the basis for MT's draft report on this category. Later, in response to MT's initial presentation, we further tested and reviewed 10 invoices. This documentation was supplied to MT. It was returned to us with annotations and cellophane flags that are, literally, incomprehensible. Our testing confirmed that there was no significant missing documentation as to any of the expense items in the 10 test invoices.

The FDIC Guide for Outside Counsel provides that, "[o]utside counsel is required to retain copies of all bills and underlying supporting material, including original time sheets and time and expense adjustment records for at least four years after final payment." The LSA, dated September 28, 1990 states the following regarding this issue, "[t]he Firm shall keep all of its billing records for at least three years from billing date. The Firm shall permit FDIC to conduct an audit or review of the Firm's billing procedures. Firm further agrees to provide additional information concerning its billing

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procedures and practices and other reports which the FDIC may request without charge."

As pointed out by the firm, the firm's position is that what is considered "appropriate" is not necessarily an "original" invoice. The requirement imposed on firms was to retain copies of all bills and supporting material, which the firm appears to have done.

The Legal Division reviewed the auditors' workpapers to determine if, in fact, the firm submitted receipts for the expenses for which they claimed reimbursement. The following are representative samples of the expenses questioned by the auditors for which copies of receipts were submitted as proof of payment.

MT control number 39 of FDIC invoice number 924407, dated October 31, 1992 references the following expense: date billed 09/04/92, \$319.71, Nightrider Overnight Copy (2,495 copies). A copy of a receipt in that amount appears in the voluminous documentation considered by the auditors under this Condition. The date on the receipt is March 30, 1992 and is made out to Brobeck. In addition, the firm submitted a copy of the firm's check to Nightrider for \$1,598.41 which references the \$319.71 from Nightrider invoice number 113657.

FDIC Invoice Number 924407, dated October 31, 1992, references the following expense: date billed 8/26/92, \$950.36, Ameriscribe Management Services, Inc., and describes copying and Bates stamping charges for Brobeck. Ameriscribe invoice number 83-11785 identifies the correct law firm and the client matter number. As was the case with the previous example, the firm submitted a copy of the firm's check evidencing payment to Ameriscribe for this amount. Brobeck check number SF154034 for \$1,237.95 references Ameriscribe invoice number 83-11785 for \$950.36.

Similarly, MT control number 3 of FDIC invoice number 1067125 dated June 30, 1993 questioned \$2,130.39 of expenses for which the firm did not submit the original invoice. The invoice identified a charge by a courier service for \$47. Among the documentation the firm submitted is a copy of an invoice from United Process Servers for \$47. The invoice is made out to Brobeck partner and it references the financial institution that gave rise to the matters the firm was representing as part of its work on this billing. As with the previous examples, the firm submitted a copy of its check evidencing payment for this service. Brobeck check number SF009803 for \$928 and dated 05/19/93 references United Process Servers invoice number 9339661 for \$47.

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The Legal Division's position vis-à-vis this Condition is that copies of receipts are acceptable substitutes for the original. Absent evidence of fraud or misrepresentation, a copy is valid proof of the payment of this expense. The auditors' concern stems from the fact that copies are not considered "adequate" documentation to prove payment of the expense. However, the Legal Division's position has been that copies of originals are sufficient to demonstrate payment of the underlying expense.

The firm identified, however, certain items for which it did not provide any documentation, either because they could not be located or because the time constraints in responding to the audit prevented the firm from addressing this matter. As a result, the firm uncovered several items (totaling \$621) for which documentation could not be located. As the Guide makes clear, all reimbursable expenses must be backed up by sufficient evidence of payment to justify reimbursement. In this case, by the firm's own admission, no receipts of any kind existed that would explain the payment of these expenses. **Accordingly, the Legal Division will disallow the amount corresponding to the expenses having no back-up documentation. That amount totals \$621.**

Condition 8: Legal Research (Westlaw, Lexis) Billed Above the Actual Cost

The OIG questioned \$6,281 in legal research expenses billed at a rate that reflected a 50% markup above the actual cost to the firm during the period covered under the audit period. The FDIC Guide for Outside Counsel is clear on this issue. The Guide provides that the Legal Division will not pay for "charges for word processing or computer time (**except actual charges for Westlaw or Lexis**)" (emphasis added).

In its response, the law firm accepted the OIG's recommendation to disallow \$6,281 "subject only to confirmation that these charges fall within the pertinent statute of limitations." **Accordingly, the Legal Division will disallow these charges and will demand reimbursement for the full amount totaling \$6,281 under this Condition.**

Condition 9: Attorneys Billed for Paralegal Functions

The OIG questioned \$4,637 "for unallowable billing for attorneys performing paralegal tasks." The auditors indicated that Brobeck billed attorney time for tasks normally done by paralegals. These tasks include the following: preparation of exhibit list, preparation of witness list, preparation of interrogatories (Form), summarization of depositions, and preparation of records requests. The auditors' legal experts (Legalgard) classified these functions as common jobs performed by paralegals and

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recommended that the Legal Division disallow the difference between attorney and paralegal rates.

The law firm, in turn, objected to the subjective judgments underlying the questioned items in this Condition. In its response, the firm pointed to the following:

Each of the questioned items reflects decision making, by experts who were closely involved with the problem at the time, about appropriate staffing and allocation of resources. An after-the-fact review by an auditor not familiar with the exigencies existing when the work was done is an especially poor vehicle for review. Great deference should be given to the fact that the bills were reviewed and approved by a client representative who was fully familiar with both the requirement that the representation be efficient and with the facts and circumstances of the particular matter now under review.

The Legal Division reviewed in general the entries identified under this Condition and concludes that the tasks identified by the auditors were performed properly by an attorney. Not only was it more cost-effective for an attorney to have performed this work, but it was necessary for an experienced litigator to perform the work in question. Consider the example highlighted below.

MT control number 11 of FDIC invoice number 682085 questioned \$806.50 in fees for tasks which the auditors concluded should have been performed by paralegals rather than by attorneys. The auditors identified nine (9) separate entries from this invoice, such as "organize deposition exhibits,"¹⁰ "prepare document requests to and "prepare document requests attached to subpoena of " These activities are normally performed by attorneys in most firms, especially when the litigation is complex and requires the guidance and management of an experienced legal hand.

Furthermore, it is not improper for fee counsel to engage in these activities if his involvement in this work would be more cost-effective than if performed by a lower-billing individual who might not complete the tasks as quickly. Consequently, it is not necessarily improper for an attorney to have engaged in this work instead of delegating it to a paralegal. In fact, the auditors seem to endorse this point of view in their report. The draft audit report quotes the following from the FDIC Guide for Outside Counsel, "[o]ur [FDIC] overall objective is to seek the best possible resolution of legal matters at the lowest practicable cost."

¹⁰ The attorney who performed this work billed .15 hours on this task for a total of \$39. Arguably, if a paralegal had performed this work, the final cost could have exceeded this amount.

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Based on the foregoing, the Legal Division will not disallow any amount questioned under this Condition.

Condition 10: Brobeck Billed and Received Full Payment for Professional Fees and Expenses that Were Partially Disallowed by FDIC

The OIG questioned \$1,068 (originally \$4,090 per MT) in professional fees and expenses "that were either unallowable by the LSA and the incorporated guidance or required additional information to be submitted by Brobeck to the Legal Divisions [sic]." That amount is broken down as follows: \$948 in professional fees and \$120 in expenses. The questioned costs were identified through the review of 15 exception letters issued by the FDIC. The law firm addressed all but 3 of these letters and resolved any residual issue remaining. However, the 3 exception letters representing 4 invoices that were paid in full by the FDIC had not been resolved. Consequently, the OIG recommended that the FDIC obtain a refund of the amount that had previously been disallowed for fees and expenses totaling \$1,068.

The law firm did not contest this finding and agreed to accept the recommendation to disallow \$1,068 under this Condition. **Accordingly, the Legal Division will disallow \$1,068 and will demand reimbursement from the firm for this amount.**

Condition 11: Review All Other Exception Letters As They Relate to Condition 10

The auditors also recommended that the Legal Division review all other exception letters that were not examined under Condition 5. The auditors recommended that the Legal Division determine the amount of funds inappropriately paid to the firm and request a refund of those funds.

The Legal Division does not agree that a review of all exception letters is called for at this time. Such a review would not be cost-effective and any likely benefit would be purely speculative. It should be pointed out also that the auditors were in the best position to examine any other outstanding exception letters at the time of the audit.

Furthermore, the OIG reduced the amount originally questioned by MT under Condition 5 from \$4,090 to \$1,068. It appears that this reduction was effectuated because, as indicated in the draft audit report, "[s]ubsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. [Brobeck's] documentation was reviewed, and where appropriate, the questioned costs were reduced." Because of this significant reduction in the questioned amount, it

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appears that the OIG did not consider an expansion of this inquiry beyond the 15 exception letters sampled by the auditors to be cost-effective.

Accordingly, the Legal Division does not believe that a review of all other exception letters would result in a credible determination of overpayment and, therefore, will not undertake such a review.

Condition 12: Other Unallowable Expenses

The OIG identified 3 categories of charges totaling \$379 that are specifically prohibited in FDIC guidelines. These charges are: postage (\$153); overhead (\$146); and travel (\$80). The OIG recommended that the Legal Division disallow \$379 as unallowable expenses.

The law firm did not contest this recommendation and agreed to pay the full amount. Accordingly, the Legal Division will disallow \$379 under this category.

In summary, the Legal Division will disallow the following amounts (questioned costs are in parentheses):

<u>Recommendation</u>	<u>Disallowance</u>
1. Computerized Time Sheets (\$1,907,856)	0
2. Professional Fees Billed for Individuals Without Prior Written Approval (\$51,357)	\$ 7,477 (rounded)
3. Professional Fees Billed in Excess of LSA (\$11,575)	\$ 11,575
4. Photocopying Charged in Excess of Actual Cost (\$8,592)	\$ 4,263 (rounded)
5. Other Unallowable Professional Fees (\$41,699)	\$ 8,676
6. Attorneys and Paralegals Billed Fees for Secretarial Functions (\$44,450)	0
7. Supporting Documentation Missing for Paid Expenses (\$32,135)	\$ 621

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8. Legal Research (Westlaw/Lexis) Billed Above Actual Cost (\$6,281)	\$ 6,281
9. Attorneys Billed for Paralegal Functions (\$4,637)	0
10. Payment for Professional Fees and Expenses That Were Partially Disallowed by FDIC (\$1,068)	\$ 1,068
11. Review All Other Exception Letters as they Relate to Condition 10 (-0-)	0
12. Other Unallowable Expenses (\$379)	\$ 379
TOTAL:	<u>\$40,340</u>

The Assistant General Counsel is authorized to make such minor accounting corrections as may be requested by the OIG, but which do not affect the substantive positions stated in this memorandum. Collection of disallowed amounts will be initiated within thirty (30) days of issuance of the final audit report. The Legal Division expects to complete the collection process within ninety (90) days after receipt of the final report.

Attachments:

- Tab A - OIG Draft Audit Report
- Tab B - Firm Response to the Draft Audit Report
- Tab C - Analysis of Unauthorized Billers



Federal Deposit Insurance Corporation
Washington, D.C. 20434

Office of Inspector General

March 16, 1999

MEMORANDUM TO: Board of Directors
Audit Committee

(b)(6)



FROM: Gaston L. Gianni, Jr.
Inspector General

SUBJECT: Final RTC and FDIC Audit Reports on the Law Firm Brobeck, Phleger
& Harrison (Audit Report Numbers 99-014 and 99-015)

Attached for your information are copies of two audit reports the Office of Inspector General (OIG) recently issued. Also attached are summaries of the reports.

These reports present the results of an audit of Brobeck, Phleger & Harrison, a law firm hired to provide legal services to the Resolution Trust Corporation (RTC) and Federal Deposit Insurance Corporation (FDIC). The reports were prepared by the independent public accounting firm of Mitchell & Titus on behalf of the OIG. Management's responses to the draft reports provided the requisites for a management decision on each of the recommendations. In total, we questioned costs in the amount of \$133,629, all of which management disallowed.

If you have any questions, please call me at (202) 416-2026 or Steven A. Switzer, Deputy Inspector General for Audits, at (202) 416-2543.

Attachments

Legal Fees Paid by RTC to Brobeck, Phleger & Harrison

(Audit Report No. 99-014, March 12, 1999)

The Office of Inspector General (OIG) has completed an audit of Brobeck, Phleger & Harrison, a law firm hired to provide legal services to the Resolution Trust Corporation (RTC). The audit was conducted by the independent public accounting firm (IPA) of Mitchell & Titus through a contract with the OIG and covered billings paid by RTC during the period January 1, 1990, through December 31, 1993. The total fees paid to the law firm during the audit period were \$12,110,847. The audit sample covered \$6,142,377, or 51 percent of the total. The audit identified \$5,104,264 in net questioned costs.

Recommendations

The OIG recommended that the Assistant General Counsel (AGC), Legal Operations Section, Legal Division, disallow \$5,104,264 for unallowable, excessive, or unsupported fees and expenses. Specifically, the OIG recommended that the AGC disallow \$4,619,956 for computer-generated time sheets not supported by original time sheets. In addition, the OIG recommended that the AGC disallow or ratify \$201,183 for unauthorized personnel and disallow \$29,824 for fees billed in excess of authorized rates. Also, the OIG recommended that the AGC disallow \$131,267 for photocopying and research charges billed in excess of actual costs, \$22,729 for unallowable fees, and \$92,080 for unallowable or unsupported expenses. Finally, the OIG recommended that the AGC disallow \$7,225 related to three other categories of questionable charges.

Subsequent to the issuance of the draft audit report, the OIG re-evaluated its decision to question \$4,619,956 related to computer-generated time sheets. Based on further examination of the IPA's working papers and law firm response, the OIG concluded that the IPA's audit procedures did not fully address the reliability of the law firm's computerized time-keeping system. Therefore, because the OIG does not believe sufficient auditing procedures were applied, we do not consider the scope of work sufficient to enable us to express an opinion on the reasonableness of the \$4,619,956 in fees. Accordingly, we reduced questioned costs for unsupported time charges to \$0.

Management Response

The General Counsel's response to a draft of this report provided the requisites for a management decision on each of the recommendations. Management disallowed a total of \$93,289. Although management's corrective actions sometimes differed from the recommended corrective actions, we consider management's response as providing the requisites for a management decision. After considering the \$93,289 in disallowances taken by management and management's comments on the IPA's findings, we will report questioned costs of \$93,289 (including \$19,313 in unsupported costs) in our *Semiannual Report to the Congress*.

LEGAL FEES PAID BY RTC TO BROBECK, PHLEGER & HARRISON

Audit Report No. 99-014
March 12, 1999



OFFICE OF AUDITS

OFFICE OF INSPECTOR GENERAL

FDICFederal Deposit Insurance Corporation
Washington, D.C. 20434Office of Audits
Office of Inspector General

March 12, 1999

MEMORANDUM TO: James T. Lantelme
Assistant General Counsel
Legal Operations Section
Legal Division,

(b)(6)

FROM: David H. Loewenstein
Assistant Inspector General

SUBJECT: *Legal Fees Paid by RTC to Brobeck, Phleger & Harrison*
(Audit Report No. 99-014)

This report presents the results of an audit of Brobeck, Phleger & Harrison, a law firm hired to provide legal services to the Resolution Trust Corporation (RTC). The Office of Inspector General (OIG) has an ongoing program for auditing law firm billings to ensure that such billings are adequately supported and comply with cost limitations set forth by the Federal Deposit Insurance Corporation (FDIC) and the former RTC. This report was prepared by the independent public accounting firm (IPA) of Mitchell & Titus for the FDIC OIG.

The objectives of the audit were to ensure that fee bills were adequately supported and in compliance with the cost limitations set by FDIC and RTC and that charges for legal services provided were reasonable. The audit covered billings paid by RTC during the period January 1, 1990, through December 31, 1993. The total fees paid to the law firm during the audit period were \$12,110,847. The audit sample covered \$6,142,377, or 51 percent of the total.

The IPA identified net questioned costs of \$5,147,537. However, subsequent to the preparation of the IPA's draft report and based on additional documentation provided by the law firm, the OIG modified draft report questioned costs to \$5,104,264. A summary of the OIG revised draft report questioned costs appears on pages 5 and 6.

The OIG made 13 recommendations to the Assistant General Counsel (AGC), Legal Operations Section, Legal Division, to disallow the revised questioned costs. The General Counsel (GC) provided a written response dated March 4, 1999, to a draft of this report. The response from the GC is included as an appendix to this report.

The Inspector General Act of 1978, as amended, requires the OIG to report on the status of management decisions on its recommendations in its semiannual reports to the Congress. To consider FDIC responses as management decisions in accordance with the act and related

guidance, several conditions are necessary. First, the response must describe for each recommendation

- the specific corrective actions already taken, if applicable;
- corrective actions to be taken together with the expected completion dates for their implementation; and
- documentation that will confirm completion of corrective actions.

If any recommendation identifies specific monetary benefits, management must state the amount agreed or disagreed with and the reasons for any disagreement. In the case of questioned costs, the amount FDIC plans to disallow must be included in management's response.

If management does not agree that a recommendation should be implemented, it must describe why the recommendation is not considered valid.

Second, the OIG must determine that management's descriptions of (1) the course of action already taken or proposed and (2) the documentation confirming completion of corrective actions are responsive to its recommendations.

Subsequent to the issuance of the draft audit report, the OIG re-evaluated its decision to question \$4,619,956 related to unsupported time charges. Specifically, the draft audit report, as revised, questioned \$4,619,956 for computer-generated time sheets that were not supported by original time sheets. However, based on further examination of the IPA's audit working papers and the law firm's response to the audit exit conference, the OIG concluded that the IPA's audit procedures did not fully address the reliability of the law firm's computerized time-keeping system. Therefore, because the OIG does not believe sufficient auditing procedures were applied, we do not consider the scope of work sufficient to enable us to express an opinion on the reasonableness of the \$4,619,956 in fees. Accordingly, we reduced questioned costs related to unsupported time charges to \$0.

The GC's response to a draft of this report provided the requisites for a management decision on each of the recommendations. Therefore, no further response to these recommendations is required. Management disallowed a total of \$93,289. Although management's corrective actions sometimes differed from the recommended corrective actions, we consider management's response as providing the requisites for a management decision. A summary of the GC's response to recommendations 3, 4, 6, 8, 9, 11, 12, and 13 and our analysis follows.

Disallow \$124,070 for photocopying charges billed in excess of actual costs (questioned cost, all of which is unsupported) (recommendation 3). The GC's response allowed \$110,216 and disallowed \$13,854. The Legal Division allowed photocopying charges up to various maximum allowable rates in effect throughout the period in question. The Legal Division disallowed amounts exceeding the maximum allowable rates. RTC guidelines provided that photocopying be billed at actual documented costs or at a standard cost based on a documented cost study;

therefore, photocopying costs not supported by a cost study were questioned by the IPA. The Legal Division subsequently revised its guidelines to allow firms to charge up to \$.08 per page for photocopying. In view of the subsequent revision to guidelines, management's position does not appear unreasonable. Moreover, the law firm provided a cost study after the completion of audit work to support its photocopying charges. Accordingly, the OIG reduced questioned costs to \$13,854.

Disallow \$74,277 for unsupported expenses (questioned cost, all of which is unsupported) (recommendation 4). The GC's response allowed \$68,818 and disallowed \$5,459. The Legal Division allowed questioned charges based on expense receipts provided by the firm that correlated with the descriptions of the expenses on the invoices. However, the Legal Division disallowed \$5,459 for expenses that the firm could not substantiate. The OIG accepts the GC's explanation and, accordingly, reduced questioned charges to \$5,459.

Review Legal Division exception letters not addressed in recommendation 5, determine the amount of funds inappropriately paid to the firm, and request a refund of those funds (recommendation 6). This recommendation resulted from the RTC's accelerated payment program from the early 1990s. The RTC and FDIC Legal Divisions issued exception letters to firms that delineated disallowances of professional fees and expenses that were either unallowable or required additional information be submitted by the firms to the Legal Divisions. In recommendation 5, the OIG recommended that FDIC disallow \$2,913 related to 7 of 35 unresolved exception letters issued to Brobeck, Phleger & Harrison. Brobeck agreed with the recommendation and the Legal Division disallowed the charges.

Nonetheless, the GC's response did not agree with the recommendation to review all other exception letters to determine whether other inappropriate payments were made to the firm. The Legal Division concluded that such a review would not be cost-effective and any likely benefit would be speculative. Because the scope of the audit covered payments made more than 6 years ago and because of the relatively small amount of recoveries identified from the exception letters addressed in recommendation 5, the OIG accepts the GC's explanation.

Disallow \$22,729 for unallowable professional fees (questioned cost) (recommendation 8). The GC's response allowed \$21,530 and disallowed \$1,199. The Legal Division allowed \$21,530 questioned for excessive review and revision of documents related to an authority to sue memorandum and analysis of loan files. Based on a review of the questioned charges, the Legal Division concluded that the charges were acceptable given the complexity of the matter involved. The Legal Division agreed that the remaining \$1,199 represented routine overhead charges that should be disallowed. The OIG accepts the GC's explanation and, accordingly, reduced questioned charges to \$1,199.

Disallow \$17,803 for unallowable expenses (questioned cost) (recommendation 9). The GC's response allowed \$13,275 and disallowed \$4,528. The Legal Division allowed \$13,275 questioned for unallowable overhead charges. Specifically, based on a review of the questioned entries, the Legal Division concluded that certain questioned charges, including an appraisal and supplies used in the course of litigation, were not overhead. However, the Legal Division

disallowed \$4,341 for questioned travel expenses and \$187 for ordinary postage charges. The OIG accepts the GC's explanation and, accordingly, reduced questioned charges to \$4,528.

Disallow \$2,336 for attorneys and paralegals who performed secretarial and clerical tasks (questioned cost) (recommendation 11). The GC's response allowed all the questioned charges. Based on a review of the questioned entries, the Legal Division concluded that the questioned tasks, which included the preparation of binders for depositions, were appropriately performed by paralegals rather than secretaries. The OIG accepts the GC's explanation and, accordingly, reduced questioned charges to \$0.

Disallow \$1,976 for attorneys who performed paralegal tasks (questioned cost) (recommendation 12). The GC's response allowed all the questioned charges. Based on a review of the questioned entries, the Legal Division concluded that the questioned tasks were so narrow in scope that the time invested by the attorneys to perform the tasks would have been less time-consuming than the time devoted to the task by a paralegal. In effect, the questioning of such charges is a judgment call that is difficult to assess years after the fact. The OIG accepts the GC's explanation and, accordingly, reduced questioned charges to \$0.

Refer a potential conflict of interest matter involving an RTC Legal Division employee and the firm to the Outside Counsel Conflicts Committee so that a determination can be made as to whether an actual conflict of interest existed. If a conflict of interest occurred, disallow all fees paid to the firm during the time period covered by the conflict of interest (recommendation 13). The GC's response stated that the firm was terminated by the joint FDIC/RTC Outside Counsel Conflicts Committee on June 2, 1994, for its continued failure to adhere to RTC conflicts policies. Therefore, any conflict of interest arising from the situation described in the audit report is now moot. The Conflicts Committee did not order any disallowance of fees, consistent with prior decisions of the Conflicts Committee and RTC Executive Committee. The OIG accepts the GC's explanation.

As a result of the IPA's audit work, \$5,104,264 was questioned in the draft report transmitted to management. In addition to the recommendations previously discussed, in recommendation 2, the OIG recommended that FDIC disallow or ratify \$201,183 for work performed by unauthorized personnel. The Legal Division ratified \$172,868 and disallowed \$28,315. The OIG accepts the action taken by management and, accordingly, reduced questioned costs to \$28,315.

After considering \$93,289 in disallowances taken by management and management's comments on the IPA's findings, we will report questioned costs of \$93,289 (including \$19,313 in unsupported costs) in our *Semiannual Report to the Congress*.

**REVISED SUMMARY OF QUESTIONED COSTS
LEGAL FEES PAID BY RTC TO BROBECK, PHLEGER AND HARRISON**

FINDING	QUESTIONED COSTS	
	PROFESSIONAL FEES	EXPENSES
1 COMPUTERIZED TIME SHEETS	4,619,956	
2 PROFESSIONAL FEES BILLED FOR INDIVIDUALS WITHOUT PRIOR WRITTEN APPROVAL	201,183	
3 PROFESSIONAL FEES BILLED IN EXCESS OF LSA APPROVED RATES AND APPROVAL LETTERS	29,824	
4 PHOTOCOPYING CHARGED IN EXCESS OF ACTUAL COSTS		124,070
5 ATTORNEYS AND PARALEGALS BILLED FOR SECRETARIAL FUNCTIONS	2,336	
6 OTHER UNALLOWABLE PROFESSIONAL FEES	22,729	
7 SUPPORTING DOCUMENTATION MISSING FOR PAID EXPENSES		74,277
8 LEGAL RESEARCH BILLED ABOVE THE ACTUAL COST		7,197
9 ATTORNEYS BILLED FOR PARALEGAL FUNCTIONS	1,976	

10 BROBECK BILLED AND RECEIVED FULL
 PAYMENT FOR PROFESSIONAL FEES
 AND EXPENSES THAT WERE
 PARTIALLY DISALLOWED BY RTC

2,913

11 OTHER UNALLOWABLE EXPENSES

POSTAGE

187

TRAVEL

4,341

OVERHEAD

13,275

TOTAL

\$4,880,917

\$223,347

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Note: This schedule of questioned costs supercedes the questioned costs in the attached audit report prepared by the OIG's independent public accounting firm (IPA). The OIG revised questioned costs based on additional law firm documentation provided subsequent to the preparation of the IPA's audit report.

**LEGAL FEES PAID TO
BROBECK, PHLEGER & HARRISON**

BY THE RESOLUTION TRUST CORPORATION

**FOR THE PERIOD
JANUARY 1, 1990 TO DECEMBER 31, 1993**

FINAL REPORT - January 29, 1996

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

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Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

I. INTRODUCTION

The Resolution Trust Corporation - Office of Inspector General (RTC-OIG) engaged Mitchell & Titus, LLP (Mitchell & Titus) to audit legal bills paid by the Resolution Trust Corporation (RTC) and the Federal Deposit Insurance Corporation (FDIC) to certain law firms providing legal services to RTC and FDIC.

Congressional interest in legal services provided to RTC is very high because of the significant amount of money paid by RTC for such services to support the workload of RTC.

The purpose of our audit was to determine whether the fees paid to Brobeck, Phleger & Harrison (Brobeck) were reasonable and allowable under the terms of the Legal Services Agreement (LSA) between Brobeck and RTC and other applicable policies, regulations and guidelines.

Legalgard, Inc. (Legalgard), a subcontractor to Mitchell & Titus, performed detailed judgmental assessments of the reasonableness of fees charged for professional services by Brobeck for RTC during the audit period.

The period of the audit was January 1, 1990, to December 31, 1993. Brobeck was paid \$12,110,847 for various legal services provided to RTC during the audit period.

Our audit was performed primarily at the offices of Brobeck in San Francisco and Newport Beach, California, from May 1993, to July 1994.

This report covers only fees paid for legal services provided to RTC. FDIC payments are covered in a separate report.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

II. SUMMARY OF FINDINGS AND QUESTIONED COSTS

	Questioned Costs				Page Ref.
	Professional Fees	Expenses	Total	Unsupported Costs	
Computerized time sheets	\$4,647,385		\$4,647,385	\$4,647,385	10
Professional fees billed for individuals without prior written approval	203,578		203,578		12
Photocopying charged in excess of actual costs		124,070	124,070		14
Supporting documentation missing for paid expenses		75,500	75,500	75,500	16
Professional fees billed in excess of LSA approved rates and approval letters	29,824		29,824		19
Other unallowable professional fees	22,729		22,729		20
Other unallowable expenses					
• Postage		187	187		
• Travel		4,341	4,341		
• Overhead Type Expenses		13,275	13,275		22
Brobeck billed and received a full payment for professional fees and expenses that were partially disallowed by RTC	15,140		15,140		17
Legal Research billed above the Actual Cost		7,197	7,197		24
Attorneys and paralegals billed for common secretarial functions	2,335		2,335		25
Attorneys billed for paralegal functions	1,976		1,976		26
Total:	\$4,922,967.00	\$224,570.00	\$5,147,537.00	4,722,885	

The audit also disclosed several matters which came to our attention that did not result in questioned costs but did require corrective action by the legal firm. These matters are included as "Other Matters" in Section VI of this report.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

III. BACKGROUND

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) established RTC to manage and resolve the savings and loan industry crisis under the management of FDIC. In its role as manager FDIC provided legal services to RTC through its own in-house Legal Division and outside counsel. FDIC served in this capacity until September 10, 1992, when the Board of Directors approved the creation of a separate RTC Legal Division. Under both FDIC and RTC management, the Legal Division used, and continues to use, outside counsel extensively for most of its legal services.

Outside counsel who provide legal services to RTC must subscribe to the Legal Division's selection and retention process. As outlined in the RTC Guide for Outside Counsel, dated February 1992¹, the selection and retention process includes filing a Contractor Registration Form, completing an interview with Legal Division personnel, and executing a Legal Services Agreement (LSA). The LSA incorporates Legal Division policies and procedures with which outside counsel must comply. In addition, the LSA identifies the firm's staff who are authorized to work on RTC's legal matters and the rates authorized for these employees. All law firms which have filed the Contractor Registration Form are included in the List of Counsel Available (LCA); however, only firms which have an executed LSA may be retained to perform Legal Division work.²

During 1990 and 1991, FDIC/RTC used two different programs to pay outside counsel--the Payment Authorization Voucher Program (PAV) and the Accelerated Payment program (APP). Under both programs, FDIC's Division of Accounting and Corporate Services (DACS)³ issued checks to pay outside counsel. The PAV required the Legal Division to review and approve legal bills before outside counsel were paid. However, because the PAV review process produced a backlog of bills and delayed payment to outside counsel, FDIC introduced the APP.

The APP allowed outside counsel to receive payment before the Legal Division reviewed the legal bills. In the APP, outside counsel submitted an "Unpaid Invoice Confirmation" (UIC) directly to DACS at the same time they sent an itemized bill to the responsible Legal Division Office. DACS paid the firms whatever amount they claimed on the UIC. The Legal Division required the firms to certify that the costs were correct and to agree that the firm would reimburse FDIC/RTC for subsequent disallowed charges.

¹ This replaced the earlier FDIC publication A Law Firm's Guide: How to be considered for Retention by the FDIC and RTC, issued May 1990.

² The LCA identifies the firms that have executed LSAs.

³ DACS has since been renamed the Office of Corporate Finance (OCF).

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

In January 1992, RTC discontinued the APP and implemented the RTC Legal Information System (RLIS). Under RLIS, Legal Division personnel were to review all legal bills exceeding \$5,000 before payment was made. In addition, every 50th bill less than \$5,000 was to be reviewed and, in certain instances, all invoices submitted by a firm may be selected for review.

Overview of Brobeck's LSA

Brobeck provided legal services to RTC under one LSA dated May 5, 1992. Before the effective date of the LSA, Brobeck was assigned cases by the RTC regional office on a case by case basis.

Additionally, Brobeck was informed that the authorization extended to RTC matters since FDIC Legal was responsible for RTC while the RTC was established. During the period of the LSA, the law firm handled matters ranging from relatively standard and routine matters to complex issues.

During the audit, we reviewed transactions and billings from January 1, 1990, through December 31, 1993.

The LSA governing Brobeck's services for the period of May 5, 1992, through May 4, 1994, provided the following contracted rates for services and reimbursable expenses:

- Hourly rates for professional and paraprofessional staff:
 - Attorneys: blended rate of \$200 an hour
 - Paralegals: blended rate of \$85 an hour
- Travel time: 50 percent of the firms' regular billing rate.
- Telephone charges: Actual cost.
- Facsimile transmission: Actual cost of transmission.
- Database research services: Actual cost.
- Photocopying: Actual cost which will generally not exceed 8 cents per page.
- Delivery charges and overnight mail: Actual cost.
- Postage: Not reimbursable.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

The RTC Guide for Outside Counsel, incorporated in the LSA by reference, includes standard guidelines for travel and other expenses.

Brobeck was paid \$12,110,847 by RTC for services during the period preceding the LSA and during the period of May 5, 1992, through December 31, 1993.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

IV. OBJECTIVES, SCOPE OF AUDIT AND METHODOLOGY

OBJECTIVES

The primary objectives of the audit were to determine whether:

1. the law firm's supporting documentation for the charges was proper and adequate,
2. the fees charged by the law firm are allowable under the terms of the agreement with RTC and applicable policies, regulations and guidelines,
3. the law firm's usual hourly rates are reasonable, and
4. the hours charged to RTC by the law firm for professional services were reasonably expended.

SCOPE OF AUDIT

The audit was performed on a test basis. To ensure adequate coverage for significant payments, we selected 30 RTC invoices greater than or equal to \$25,000 totalling \$5,803,871. We also selected 68 RTC invoices less than \$25,000 totalling \$338,506. In total, we tested 148 RTC invoices totalling \$6,142,377 resulting in a value coverage of approximately 51% of the total population of \$12,110,847.

In addition to the above invoices selected, we identified the following matters and selected invoices and other case documentation related to those matters in order to perform judgmental assessment on the billings in their entirety:

LDID	Matter Name (Paid by RTC)	Matter Type	Fee & Expenses Approved For Payment
920029093	Home Capital	Bulk Sale - Real Property	\$1,360,795.82
920002865	Gibraltar Financial Corporation	Chapter 11	8,991.96
920002897	Imperial Corporation of America	Chapter 11	234,963.49
30018368	Westport Federal Saving and Loan (PLS/Litigation)	Mult. Categ. Laws	156,723.42
Total:			\$1,761,474.69

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

METHODOLOGY

Based on the sample selected, we performed the following procedures to verify compliance with the LSA:

- Reviewed and evaluated the internal control system over billings.
- Reviewed and evaluated the billing procedures.
- Reviewed the LSA and all other agreements between RTC and the law firm, as well as all applicable guidelines, policies and regulations.
- Conducted compliance and substantive tests of fees billed to RTC by the law firm to determine whether:
 - the law firm's documentation adequately supports the bills, and
 - the fees charged by the law firm were allowable and reasonable under the agreed terms.
- Reviewed compliance with conflict of interest rules.
- Reviewed professional biographical information of those professionals who billed time to RTC and assessed whether the usual rates charged were consistent with each professional's background and experience and within the range of rates charged for a comparable skill level within the relevant geographical area.
- Reviewed supporting billing detail to assess whether hours charged to RTC were reasonably expended.
- Verified that all professionals listed on the invoice had been approved to perform work on RTC matters.
- Reviewed background information and experience of all professionals listed to ensure that their classification and titles were consistent with their background and work performed.
- Verified that the billing rates had been approved by RTC.
- Ascertained that hours billed were supported by original time sheets.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

- Verified the mathematical accuracy of the invoices.
- Obtained explanations for professionals billing more than 12 hours a day.
- Determined whether RTC was billed excessive hours by new professionals assigned to RTC matters for time spent familiarizing themselves with the matter.
- Determined and reviewed the systems in place to identify and correct conflict of interest situations.
- Verified that the firm has complied with conditions imposed by any "conditional waivers of conflicts of interest."
- Verified that the law firm did not bill RTC for time spent researching its own conflicts of interest.
- Ascertained that professionals performing work on RTC matters were not performing services for other clients of the law firm that may present a conflict of interest situation.
- Determined and reviewed the systems in place to ensure that research projects were approved by RTC prior to their commencement.
- Determined that research projects were approved by RTC prior to their commencement.
- Determined that the charges were adequately supported and related to applicable RTC matter.
- Determined and reviewed the system for proper control and accounting of reimbursable expenses.
- Determined that expenses charged were allowable under the LSA.
- Ascertained that charges/reimbursements represented the lower of actual cost incurred or the contracted rates.
- Verified that expenses were adequately supported by original documentation, invoices, etc.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

- Determined that travel time complied with LSA and outside Legal Services Guidelines.
- Performed an exit conference at Brobeck's offices in San Francisco. The participants were Brobeck, RTC-OIG, Mitchell & Titus, RTC Legal Division-Newport Beach and RTC Legal-Washington, D.C. representatives (via phone). At the exit conference, Mitchell & Titus presented the findings and reviewed with Brobeck the appropriate ways to respond to each finding and the timetable for the response.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

V. FINDINGS AND RECOMMENDATIONS

Computerized Time Sheets

As part of the review of legal fees, we reviewed computer generated time sheets used from the automated time records systems maintained by the law firm. The purpose of this procedure was to enable us to verify that the computer-generated time records were supported by original time sheets or other input sheets. The original time sheets could be used to verify the accuracy and validity of the automated time records.

Brobeck informed us that the system was one in which the original, uniform and verifiable entry was an electronic entry. For any invoices where original time sheets were required, Brobeck would have had to produce printouts of those original entries since they did not exist.

With the use of advanced data processing systems, potential risk is enhanced by two factors: manually prepared records being replaced by computer output and audit trails being eliminated or made more difficult to follow. The lack of source input documentation prohibited us from performing transaction testing to verify the following:

- Input data were correctly recorded.
- All authorized transactions were processed without additions or omissions.
- Appropriate audit trails exist.

The absence of source documents to support time entries in the system and the elimination of the input audit trail is considered a deficiency in the internal control structure.

Accordingly, our test of professional hours billed from January 1, 1990, to December 31, 1993, in the amount of \$4,885,098 was done using the computer-generated records. Brobeck extracted records from the main time and billing database and created a new dataset that included time entries for RTC matters and redacted time entries for all non-RTC matters. These time entries are considered an output data and not original input data that can be confirmed as accurate and reliable.

The RTC Guide for Outside Counsel states, "Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and time and expense adjustment records for four years after payment."

We questioned all professional time billed for the period noted above because the absence of source documents to support time entries is considered a deficiency in the internal control structure.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

This amount includes costs questioned under other criteria within this report as follows:

Total paid to professionals without original time sheets	\$4,885,098
Less: Amount questioned under other criteria	
Employees without prior written approval (See Page #12)	(207,889)
Employees using rates in excess of the LSA (See Page #19)	<u>(29,824)</u>
Net amount questioned	<u>\$4,647,385</u>

Recommendation:

1. We recommend that RTC disallow 4,647,385 in billings not supported by an adequate time keeping system or original time sheets (questioned cost, all of which is unsupported).

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. However, the documentation provided did not address the issue of the absence of input documentation, or system internal controls to preclude changes to input data without a record of such changes.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Professional Fees Billed for Individuals Without Prior Written Approval

During our test of professional fees paid from January 1, 1990 through December 31, 1993, we found that Brobeck billed RTC \$207,889 for a number of professionals who worked on RTC matters without prior written approval from RTC.

The LSA incorporates Legal Division policies and procedures with which outside counsel must comply. In addition, the LSA identifies the firm's staff who are authorized to work on RTC's legal matters and the rates authorized for those employees.

Section 2 of the LSA (Rate Structure) states, "...The schedules are an integral part of this Agreement and can only be amended with the written consent of the RTC Division of Legal Services."

The RTC Guide for Outside Counsel states, "...the firm also must provide a matrix that identifies all attorneys and paralegals the firm offers to provide service to the Corporation, and which sets forth, for each attorney and paralegal, the following: (1) state licenses; (2) particular area(s) of expertise; (3) years in practice; (4) time with the firm; (5) status within the firm as partner or shareholder, senior associate, associate or paraprofessional; (6) billable rates in accordance with the firm's usual rate structure...."

Formal written prior approval of attorneys and paralegals authorized to work on RTC matters was not only required but is critical in facilitating RTC's supervising attorneys' oversight role.

The amount questioned for attorneys not on the LSA includes costs questioned under other criteria within this report as follows:

Total paid to professionals without written prior approval	\$207,889
Less: Amount questioned under other criteria	
Attorneys and paralegals billed for common secretarial functions (See Page #25)	(2,335)
Attorneys billed for paralegal functions (See Page #26)	(1,976)
Net amount questioned for professionals billed without prior written approval	<u><u>\$203,578</u></u>

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Recommendation:

2. We recommend that RTC require responsible personnel to analyze the qualifications for employees working on RTC matters, but not listed on the LSA, or other approval letters, determine how much of the \$203,578 in questioned costs for these charges should be retroactively ratified, and disallow any of the charges not approved (questioned cost).

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Photocopying Charged in Excess of Actual Costs

We found that Brobeck billed RTC for photocopying costs using a higher rate per page than the maximum allowed by RTC Guidelines.

In addition, Brobeck provided us with a Facsimile and Copy Cost Summary (cost study) to support the rate charged for photocopying. This cost study was prepared by Brobeck and included apparently unallowable overhead items such as secretarial salaries and space rental costs. We were unable to verify the cost study data because we did not receive it until November 1994, 3 months after the completion of audit field work. We requested Brobeck to explain certain items in the study and were provided with a revised cost study that still included similar, unallowable overhead items. The cost studies prepared by Brobeck do not support actual, unburdened photocopying rates that are required for RTC billings.

The LSA states, "Outside Counsel agrees to comply with general responsibilities as to ethics, reporting requirements, billing information...set forth in the RTC guide for Outside Counsel...incorporated herein by reference and made an integral part of this agreement."

Section 5D., Billing of the FDIC LSA, effective September 28, 1990 states, "FDIC will pay for photocopying at actual cost, which will generally not exceed \$.15 per page. This LSA covered the period for the billing prior to the issue of the RTC Guide for Outside Counsel (February 1992).

The RTC Guide for Outside Counsel states, "Charges for photocopying shall be at the firm's actual cost, not to exceed eight cents per page unless supported by a cost study."

Since Brobeck could not support its actual cost for photocopying, we were unable to determine the reasonableness of the rate used for photocopying charges in the amount of \$124,070.

Recommendation:

3. We recommend that RTC disallow \$124,070 for photocopying charges billed in excess of actual costs (questioned cost, all of which is unsupported).

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information (a revised cost study) to support its position. The revised cost study prepared by Brobeck did not support actual, unburdened photocopying rates that are required for RTC billings. Therefore, the questioned costs were not modified and the finding remains as stated.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Supporting Documentation Missing for Paid Expenses

We selected a sample of 148 invoices paid by RTC for testing and asked Brobeck to provide us with the source documentation, including original time sheets for professional fees, invoices from third parties and internal reports for expenses supporting all the items selected for testing. However, we were unable to verify certain invoices for expenses because either Brobeck could not locate supporting documentation or the supporting documentation presented to us was inadequate (e.g., photocopying amount with no number of copies made). The total amount of unsupported expenses is \$75,500.

The RTC for Outside Counsel states, "Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payments."

In addition, for RTC billings prior to the issue of the above guide, the FDIC Guide for Outside Counsel state, "Outside counsel is required to retain copies of all bills and underlying supporting material, including original time sheets and time and expense adjustments records for at least four years after final payment. The submission of erroneous bills or requests for reimbursement of inappropriate charges may result in serious sanctions."

All items billed should be supported by adequate documentation, such as original invoices. The documentation should be retained and available for review to establish the validity and reasonableness of amount billed.

As a result of the conditions noted, Brobeck was not in compliance with the LSA and RTC guidance.

Recommendation:

4. We recommend that FDIC disallow \$75,500 in unsupported expenses (questioned cost, all of which is unsupported).

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Brobeck Billed and Received a Full Payment for Professional Fees and Expenses that were Questioned and Partially Disallowed by RTC

We reviewed 35 exception letters issued by RTC and FDIC, as a result of a review of certain invoices by the Legal Divisions. These exception letters delineated disallowances of professional fees and expenses that were either unallowable by the LSA and the incorporated guidance or required additional information to be submitted by Brobeck to the Legal Divisions. Under the payment program (accelerated payment program) the outside counsel received payment before the Legal division reviewed the legal bills. All but 7 exception letters were resolved by Brobeck and RTC. However, we noted that 7 exception letters that were unresolved (representing 13 invoices with questioned cost of \$15,140) were paid in full by RTC.

Appendix F, Required Bill Certification, of the FDIC Guide for Outside Counsel states, "In the event the FDIC disputes any bill that has been paid, we [Law Firm] waive all rights to retain the disputed amount promptly on request of the FDIC pending resolution of the dispute."

The RTC Guide for Outside Counsel states, "The Legal Division reserves the right to request additional information regarding the services provided by Outside Counsel. Outside Counsel must also permit representatives from the RTC's Office of Inspector General and the General Accounting Office to conduct audit reviews. Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payments."

As a result of the condition noted, Brobeck was paid in full by RTC \$15,140 that were originally questioned and disallowed.

Recommendations:

5. We recommend that RTC request Brobeck to refund RTC \$15,140 for fees and expenses previously disallowed (questioned cost).
6. We also recommend that RTC Legal review all other exception letters and determine the amount of funds inappropriately paid to the firm and request a refund of those funds.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Professional Fees Billed in Excess of LSA Approved Rates and Approval Letters

During our test of professional fees paid from January 1990 through December 31, 1993, we found that Brobeck billed RTC using professional hourly rates up to \$60 per hour higher than allowed by prevailing contract rates for 20 professionals. Law firms must charge for legal services in accordance with the fee or hourly rate structure set forth on the schedules attached to the LSA.

Section 2 of the LSA (Rate Structure) states, "Outside Counsel agrees to provide legal services in accordance with the hourly rates or alternative rate structures set forth in the attached schedules. The schedules are an integral part of this Agreement and can only be amended with the written consent of the RTC Division of Legal Services."

The RTC Guide for Outside Counsel states, "...the firm also must provide a matrix that identifies all attorneys and paralegals the firm offers to provide service to the Corporation, and which sets forth, for each attorney and paralegal, the following: ...(6) billable rates in accordance with the firm's usual rate structure...."

As a result of the condition noted, Brobeck was not in compliance with the LSA and the incorporated guidance and overbilled RTC \$29,824.

Recommendation:

7. We recommend that RTC disallow \$29,824 of professional fees paid in excess of the contractual rates (questioned cost).

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Other Unallowable Professional Fees

We noted that Brobeck billed professional's time to RTC for the following tasks:

- excessive time expended in review and revision of documents
- research Brobeck's own Conflict of Interest
- preparation of bills
- preparation of case budgets
- preparation of status reports

In addition, Brobeck billed professional's time for excessive review and preparation of documents. These tasks are specifically disallowed by RTC Guidance.

The RTC Guide for Outside Counsel states, "The firm must include in its proposed rates for legal services all 'overhead' and 'profit'. The RTC does not pay for the following.... time devoted to the preparation of bills or routine status reports."

The RTC RLIS Forms and Procedures Deskbook for Outside Counsel states, "You should be aware that RTC reviews all legal bills using the following general principles....Substantial time expended in 'review and revision' of documents prepared by the firm."

As a result of the condition noted, Brobeck was not in compliance with the RTC guidance and overbilled RTC \$22,729 based on the following computation:

• Excessive review/revision of documents (e.g., ATS memo, loan files regarding directors)	\$21,530
• Research of conflict/preparation of bills, budget and status reports	<u>1,199</u>
Total Disallowance:	<u>\$22,729</u>

Recommendation:

8. We recommend that RTC disallow the \$22,729 in billing for unallowable professional fees (questioned cost).

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Other Unallowable Expenses by the RTC Guidelines

We noted that Brobeck billed RTC for various types of expenses that are specifically prohibited in the RTC guidance, such as:

- postage;
- expenses that are customarily included in the normal overhead or administrative expense of running a law firm, such as office supplies (e.g., binders, stationary);
- travel expenses, such as: meals, health club, laundry and other entertainments while on travel.

The RTC Forms and Procedures Deskbook for Outside Counsel states that "RTC will not pay for ordinary postage charges."

The RTC Guide for Outside Counsel states, "The firm must include in its proposed rates for legal service all overhead and profit."

The RTC Guide for Outside Counsel states, "Hotel accommodations must be moderately priced, as expenses for luxury hotels or special services are not reimbursable."

In addition, the RTC Guide for Outside Counsel states, "If business is conducted during a meal, appropriate time charges may be made at normal hourly rates. Charges for food, beverages and the like will not be reimbursed by the RTC unless an attorney is in travel status and is away from the home office overnight. In that instance, the RTC will reimburse all subsistence expenses at RTC standard per diem rates."

As a result of the condition noted, Brobeck was not in compliance with RTC Guidance, and overbilled RTC \$17,803 based on the following computation:

Postage charges	\$187
Overhead charges	13,275
Travel charges	<u>4,341</u>
 Total	 <u>\$17,803</u>

Recommendation:

9. We recommend that RTC disallow the unallowable expenses totalling \$17,803 (questioned cost).

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Legal Research (Westlaw, Lexis) Billed above the Actual Cost

We noted that Brobeck billed RTC for research (computer time) at a rate that reflected a 50 percent markup above the actual cost to the firm during the period covered under the review (1990 through 1993).

The RTC Guide for Outside Counsel states, "The firm must include in its proposed rates for legal services all 'overhead' and 'profit'. The RTC does not pay for the following:...charges for word processing or computer time (except actual charges for Westlaw or Lexis)...."

As a result of the condition noted, Brobeck was not in compliance with RTC guidance, and overbilled RTC \$7,197 for research mark-ups.

Recommendation:

10. We recommend that RTC disallow \$7,197 for research mark-ups (questioned cost).

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Attorneys and Paralegals Billed Fees for Secretarial Functions

We noted that Brobeck billed attorney and paralegal time to RTC for the performance of secretarial functions such as:

- photocopying documents
- organizing documents
- organize for storage
- supervising file organization
- file and refile
- collate documents
- process vendor bills

These are administrative and clerical tasks that are considered overhead to the firm and, accordingly, should not be billed to RTC.

The RTC Guide for Outside Counsel states, "The firm must include in its proposed rates for legal service all overhead and profit."

The RLIS Forms and Procedures Desk Book for Outside Counsel under the section entitled "criteria for allowable fees and expenses" specifically states, "the means or method of accomplishing the work providing the service must be appropriate (e.g., generally an attorney should not perform the service if a paralegal or a secretary can perform it as efficiently and effectively at less expense or no expense). Also, the fee or cost charged should not represent a service that is customarily included in the normal overhead or administrative expense of running the firm."

As a result of the condition noted, Brobeck was not in compliance with RTC guidance and overbilled RTC \$2,335 for time incurred on overhead activities.

Recommendation:

11. We recommend that RTC disallow \$2,335 in unallowable billings for attorneys and paralegals performing secretarial and clerical tasks (questioned cost).

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Attorneys Billed for Paralegal Functions

We noted that Brobeck billed attorney time to RTC for paralegal tasks such as:

- preparation of exhibit list
- preparation of witness list
- preparation of interrogatories (Form)
- summarization of depositions
- preparation of records request(s)

These tasks are classified as common paralegal functions by our legal expert (Legalgard) and, accordingly, are billable to RTC at the paralegal's rate structure and not at the attorney's rate structure.

The RTC Guide For Outside Counsel states, "The overall objective of the Legal Division as to litigation is to obtain the best and earliest resolution at the lowest practicable cost."

The RLIS Forms and Procedures Desk Book for Outside Counsel under the section entitled "criteria for allowable fees and expenses" specifically states, "...the means or method of accomplishing the work providing the service must be appropriate (e.g., generally an attorney should not perform the service if a paralegal or a secretary can perform it as efficiently and effectively at less expense or no expense). Also, the fee or cost charged should not represent a service that is customarily included in the normal overhead or administrative expense of running the firm."

As a result of the condition noted, Brobeck was not in compliance with RTC guidance and overbilled RTC \$1,976 for time incurred by attorneys performing paralegal functions.

Recommendation:

12. We recommend that RTC disallow \$1,976 for unallowable billings for attorneys performing paralegal tasks (questioned cost).

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated they would provide additional documentation supporting their position.

Auditor's Comments

Subsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. The documentation was reviewed, and where appropriate, the questioned costs were reduced.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

A Conflict of Interest During the Period Covered Under the LSA

(b)(6)
(b)(6) We noted that Brobeck represented an RTC Legal employee, formally Deputy Regional Counsel at the [redacted] regarding attorney discipline and State Bar of [redacted] (b)(6) [redacted] at the same time that Brobeck received referrals from the same RTC field office. The employee was involved in the decision-making process as to the firms RTC would use to handle its cases. Brobeck's attorneys spent a total of 300 hours on this case between 1991 and 1993.

The Representations and Certifications section of the LSA states, "Outside Counsel represents, warrants, agrees and covenants that:

- (i) it has no conflict with the interest of the RTC or the Federal Deposit Insurance Corporation (FDIC) that has not been disclosed in writing to the RTC Division of Legal Service.
- (ii) it will advise the RTC Division of Legal Service immediately of all conflicts or potential conflicts that develop in the future."

The RTC Guide for Outside Counsel states, "At all time of its initial submission, the firm must disclose and describe the nature of any existing or potential conflicts of interest... Any subsequent, actual or potential conflict of interest must be disclosed as soon as the firm learns of its existence. If, in the Legal Division's opinion, an actual or potential conflict exists, the firm will not be permitted to go forward with any representation of the RTC until the conflict has been resolved by the firm or waived by the Legal Division."

The RTC Guide for Outside Counsel further states, "The RTC expects the highest ethical standards of Outside Counsel. Neither Outside Counsel nor any person associated with Outside Counsel, shall provide any gift, gratuity, favor, entertainment, loan or other thing of monetary value to any employee of the RTC."

The FDIC-LSA states, "You [Brobeck] represent, warrant and covenant that (i) your firm has no conflict of interest with the interests of the FDIC or the Resolution Trust Corporation that has not been disclosed in writing to the FDIC; (ii) you will advise us immediately of all conflicts that develop in the future...."

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

The FDIC Guide for Outside Counsel also states, "Outside counsel must be free of conflicting interests unless we waive those conflicts in writing... At the time of your initial submission you must provide the Division with a list of all potentially conflicting interests. Subsequently, any actual or potential conflict must be discussed with us as soon as you learn of its existence. If in our opinion an actual or potential conflict exists, you will not be permitted to go forward with your representation until the situation has been resolved by the Outside Counsel Conflicts Committee (OCCC) in the Legal Division."

Brobeck was in violation of the RTC-LSA at the time it signed the agreements. Additionally, Brobeck was not in compliance with the RTC and the FDIC Guidelines in relation to conflict of interest. Per the LSA, Brobeck should have stopped working on the RTC cases until this situation was resolved.

Recommendations:

13. We recommend that RTC turn this case over to the OCCC so that the OCCC can make a determination as to whether this is an actual conflict. Should this situation be deemed an actual conflict of interest, we also recommend that all fees paid to Brobeck during this time period be disallowed due to non-compliance with the LSA.

Auditee's Response

Brobeck officials disagreed with the audit finding as presented at the exit conference and stated that invoices for representing the RTC official were never paid and Brobeck had no objection to providing the invoices and additional documentation supporting their position.

Auditor's Comments

Brobeck did not provide the auditors the additional documentation as it stated would be made available. Therefore, the finding remains as stated.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

VI. OTHER MATTERS

Lack of Adequate Documentation to Support Resolution of Conflict of Interest

As part of our test of conflicts, we obtained Brobeck's Audit Conflict History from RTC-OIG. The history included a summary of 25 letters requesting waivers for conflicts of interest. Options available to RTC included the granting of either an unconditional or conditional waiver, a denial of waiver, or a determination that no conflict existed.

We asked Brobeck to provide us with source documents related to the above conflict history, such as Brobeck's request for waiver and RTC/FDIC response. However, we were unable to adequately verify 18 of the conflict waiver letters since source documents were not provided by Brobeck.

The FDIC Outside Guide for Counsel states, "Outside counsel must be free of conflicting interests unless we [FDIC] waive those conflicts in writing."

As a result of the condition noted, Brobeck may have been working on cases where actual or potential conflicts of interest existed. At the same time, the FDIC opinion was that there is a potential conflicts and therefore, Brobeck should not be permitted to go forward with the representation until the situation has been resolved.

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

Lack of Adequate Documentation and Information to Support Proper Case Plans

As part of our case plan test, we selected 47 cases and obtained from Brobeck the case files. Out of 47 cases tested, we noted that certain case plans did not outline required information and various items of documentation were missing. The following summarized the missing information and documentation:

<u>Information Outline</u>	<u>Cases Missing</u>	<u>%</u>
Proposed course of litigation	10	21
Proposed alternative plan for settlement	32	68
Approval by RTC/FDIC	45	96

<u>Documentation Missing</u>	<u>Cases Missing</u>	<u>%</u>
Estimate of the value of claims	23	49
Estimate of legal fees and expenses	22	47
The date judgement or dismissal is expected	39	83
Estimates of the probability of success and collection (%)	36	77

The RTC Guide for Outside Counsel states, "Promptly upon commencement of a litigation assignment, Outside Counsel shall prepare a case plan that sets forth the strategy proposed for the successful pursuit and conclusion of the litigation. The case plan should outline the proposed course of the litigation...include an alternative plan for settlement...It is the responsibility of the Outside Counsel to make certain that each case plan is appropriate and promptly provided to the responsible RTC Attorney for review and approval."

Legal Fees Paid to Brobeck, Phleger & Harrison
by RTC
From January 1, 1990 - December 31, 1993

In addition, the above mentioned Section states, "Outside Counsel involved in litigation also will be required to submit significant case information to the Legal Division. Such requested information will include estimates of the value of the claim (or liability, if defensive litigation); estimates of legal fees and expenses through various stages of the case; the date judgement or dismissal is expected; and estimates of the probabilities of success and ultimate collection, stated as percentages."

As a result of the condition noted, Brobeck had been working on cases without proper case planning and budgeting that may have led to overbilling RTC or performing services in a non-efficient manner.

LEGAL DIVISION COMMENTS¹



FDIC

Federal Deposit Insurance Corporation
550 17th Street, NW, H-10070, Washington, DC 20429

Legal Division
Legal Operations Section/Outside Counsel Unit

March 4, 1999

(b)(6)

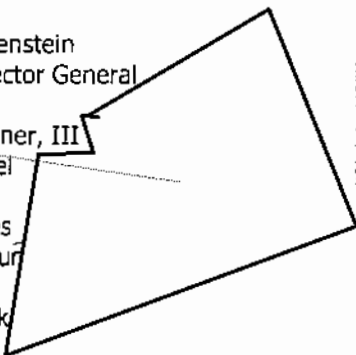
MEMORANDUM TO: David H. Loewenstein
Assistant Inspector General

THROUGH: William F. Kroener, III
General Counsel

William S. Jones
Supervisory Counsel

FROM: Andre M. Douek
Counsel

SUBJECT: Audit of Legal Fees Paid by the RTC to
The Law Firm of Brobeck Phleger & Harrison
(San Francisco, California)



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This memorandum constitutes the Legal Division's response to both the Office of Inspector General's ("OIG") draft audit report dated July 30, 1998 (Exhibit A) and the law firm's response dated November 2, 1998 (Exhibit B). The audit report pertains to invoices paid for work performed on behalf of the Resolution Trust Corporation (RTC) by the law firm of Brobeck, Phleger & Harrison ("BP&H").¹ Owing to their voluminous nature, the supporting schedules to the audit report are not included in the Exhibits.

The Inspector General's audit report included an examination of 148 RTC invoices totaling \$6,142,377 which corresponds to approximately 51% of the \$12,110,847 paid to the firm from January 1, 1990 through December 31, 1993. Of the 148 invoices, the auditors selected 80 RTC invoices greater than or equal to \$25,000 totaling \$5,803,871 and 68 invoices less than \$25,000 totaling \$338,506. After adjustment by the OIG, the draft audit report identified 11 general areas of questioned costs totaling \$5,104,264 and broken down as follows: \$4,880,917 in professional fees

¹ It should be noted that the audit of Brobeck Phleger & Harrison and the draft audit report were done by Mitchell & Titus, LLP ("MT"), a public accounting firm contracted by the RTC OIG. MT, in turn, subcontracted the assessments of the reasonableness of the fees charged for professional services to Legalgard, Inc.

¹The attachments referred to in the Legal Division's response are not included in this appendix.

APPENDIX

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and \$223,347 in expenses. In response to the audit report, the law firm submitted a comprehensive and detailed letter with supporting documentation addressing each questioned cost and the OIG's recommendations and conclusions. The firm also criticized the timing of the audit report, noting that the exit conference with Mitchell & Titus occurred in July, 1995, but the draft audit report was not received until three years later.

In conducting the audit, the auditors performed certain procedures to verify compliance with the firm's LSA. They also examined original documentation and invoices for accuracy and to determine whether they were properly reimbursable. In addition, the auditors undertook an examination of, among other things, a review of the internal control system over billings, a review and an evaluation of the billing procedures, a review of the LSA, and compliance and substantive testing to determine whether the law firm's documentation adequately supported the bills whether the fees charged by the firm were allowable and reasonable under the agreed terms. After weighing the merits of the arguments presented by both sides, the Legal Division determined that it will seek reimbursement from the law firm for the disallowed amounts indicated below which total \$93,289 and will pursue collection activities as appropriate.

With this background in mind, our conclusions regarding each finding and recommendation and the law firm's response are set forth below.

Condition 1: Computerized Time Sheets

The OIG questioned \$4,619,956 in billings because the firm did not have original time sheets to back its computer-generated time records. The auditors indicated that the firm had informed them that the record-keeping system was one "in which the original, uniform and verifiable entry was an electronic entry" rather than a hard-copy entry on an original time sheet. The auditors indicated that the risk of relying on computer-generated time records was increased by two factors: "manually prepared records being replaced by computer output and audit trails being eliminated or made more difficult to follow." The auditors cautioned that the "lack of source input documentation" prevented them from ascertaining whether the data was transmitted correctly, whether all authorized transactions were processed without additions or omissions, and whether "appropriate audit trails" existed. The auditors concluded that the absence of original source material to support the time entries and the elimination of an "appropriate audit trail" created a deficiency in the internal control structure of the firm. Accordingly, they questioned all professional time billed during the audit period and recommended that the Legal Division disallow \$4,885,098 net of amounts questioned under other criteria. (That figure was later revised by the OIG to reflect a net amount of questioned costs under this Condition totaling \$4,619,956.)

APPENDIX

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For its part, the firm explained that the original time sheets as "required by the contracts have been retained by the firm—they are in electronic form—and appropriate time adjustment records have also been maintained. The Firm operates on a computerized billing system with all necessary and appropriate safeguards to insure integrity and reliability. There is not even a hint or suggestion in the MT draft report that the Corporations were billed inappropriately or erroneously as a consequence of the Firm's use of its computerized billing system."

In support of its position, the law firm argued that case law held that computerized records are "originals." FDIC and RTC guidelines did not require fee counsel to use and retain original handwritten time sheets; and because the Corporation received value for the services rendered, it cannot now raise a technicality as justification for disallowing those fees. The firm argued that under the legal principle of quantum meruit, it is entitled to the fair value of the benefit conferred on the RTC.

The RTC guidelines in effect during the audit period did not require that the firm use and retain handwritten time sheet entries, nor did they describe what records must be generated and maintained or require that the firm establish a particular kind of record-keeping system. On December 31, 1997, the Legal Division published its electronic billing guidelines to address the types of concerns raised by the auditors. These guidelines became effective for legal fees incurred on or after February 15, 1998. Since the Legal Division's own policies during the audit period did not require the law firm to maintain handwritten time sheets, nor did they specify internal controls for electronic billing systems, we cannot impose on the firm requirements that were not present when the legal services were rendered. **Accordingly, the Legal Division will not disallow any questioned costs under this recommendation.**

Condition 2: Professional Fees Billed for Individuals Without Prior Written Approval

The OIG questioned \$201,183 of costs for professional fees on RTC matters that were billed for professionals who were not listed on the firm's LSA.² In its report, the OIG quoted from the RTC Guide for Outside Counsel which states the following:

[T]he firm also must provide a matrix that identifies all attorneys and para-professionals the firm offers to provide services to the Corporation, and which sets forth, for each attorney and paraprofessional, the following: (1) state licenses; (2) particular area(s) of expertise; (3) years of practice; (4) time with

² MT assessed the questioned costs under this Condition at \$203,578, but the OIG reduced that amount to \$201,183.

APPENDIX

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the firm; (5) status within the firm as partner or shareholder, senior associate, associate or paraprofessional; (6) billable rates in accordance with the firm's usual rate structure....

Furthermore, the auditors pointed out that the firm's LSA with the FDIC and RTC indicates that "The schedules [fee matrix of firm's employees which sets forth the hourly rates for each attorney and para-professional in the Firm who is to work on FDIC and RTC matters] are an integral part of this Agreement and can only be amended with the written consent of the RTC Division of Legal Services." The auditors argued that formal written approval was not only required under the LSA, but was "critical in facilitating RTC's supervising attorneys' oversight role." The underlying basis for questioning these fees is the auditors' concern for quality control to ensure that all employees working for outside counsel firms are qualified and have been properly evaluated by the RTC.

In its response, the law firm admitted that "[s]ome work was done by the Firm with less than complete technical compliance with timekeeper 'pre-approval' requirements (such as the requirement that timekeepers be listed in an addendum to an LSA)." However, it also pointed out that this work was performed "with no objection by the clients," and added the following comment:

We worked for years under circumstances in which our people pitched in as needed to help the RTC with no complaint or objection by those at the Corporation supervising our work. The draft report does not suggest or allege that the time spent by these timekeepers was inappropriate, nor does it suggest or allege that the rates charged for their services was inappropriate. The draft report does not suggest that fair value was not delivered (judgments of this type are beyond the expertise of financial auditors). There has been no claim or showing that the fair value of the time spent by "unauthorized" timekeepers was anything other than the face amount billed. There is no evidence or showing that the charges for legal service covered by this recommendation were in any way inflated. No part of this challenged time should be disallowed....

...Alternatively, OIG should state what it believes to be the fair and reasonable value of the time spent by the timekeepers in question. A blanket position that nothing should be paid—even though valuable services were provided—is unfair, wrong, and contrary to law, including principles of *quantum meruit*.

The RTC Guide for Outside Counsel was developed to ensure that the RTC obtained "the very best quality legal services in a professional, timely, efficient and cost-effective manner." General Counsel Gerald L. Jacobs explained in his introduction to the Guide that the Guide "sets forth the major policies and procedures governing the

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Legal Division's relationship with Outside Counsel, as well as expresses what expectations we have of all counsel engaged to assist us." The General Counsel concluded his message to outside counsel with the following comment:

RTC's Outside Counsel are obligated to conform to the requirements set forth in this Guide. It is an integral part of the RTC's Legal Services Agreement, and every attorney we employ is expected to read and retain a copy of it for constant reference.

In addition, the Guide itself reinforces the General Counsel's position that the Guide is an integral component of the contract for legal services entered into between the firm and the RTC by expressing the following policy:

It [the Guide] is an integral part of the agreement under which attorneys are engaged to represent the RTC and governs all such engagements....It also outlines the procedures to be followed by Outside Counsel who seek to be retained by the Legal Division, sets forth the major requirements for retention, and describes the Legal Division's expectations of Outside Counsel once they are retained.

Please circulate this Guide to every attorney, paraprofessional and technician in your firm involved in providing services to the RTC, all of whom should read and maintain familiarity with it.

Moreover, the Guide provides the following:

Outside Counsel is required to charge the same rates for all matters it handles on behalf of the RTC within a particular geographical area. The rates charged by Outside Counsel shall be the lowest of the fee schedules contained in the Legal Services Agreement ("LSA") or of the rates negotiated with any RTC office for any similar matter.

The September 28, 1990 LSA addresses the issue of unauthorized billers in the following manner under Section 3 (Rate Structure):

The hourly rates for each attorney and paraprofessional in the Firm who is to work on FDIC matters is set forth on the Rate structure, attached hereto as Exhibit C and incorporated herein by this reference. Personnel may be added to the list, but only by written mutual agreement of the Firm and the FDIC.

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The May 5, 1992 LSA which the firm entered into with the RTC provides as follows concerning this issue:

Outside Counsel represents, warrants, agrees and covenants that...(iii) each of the attorneys and paraprofessionals it employs has reviewed, understands and agrees to act strictly in compliance with all provisions, requirements and policies (including statutory and regulatory provisions) identified in the Guide.

Moreover, the February 1, 1992 FDIC LSA is also clear on the issue that changes must be made only with the written consent of the Legal Division. Therefore, the firm was on notice of this requirement, at least on the FDIC side. That LSA provided:

Your firm agrees to provide legal services in accordance with the fee and hourly rate structure (for each attorney and paraprofessional assigned to work on FDIC matters) set forth on the attached schedule(s), which may be amended only by written consent of the Legal Division.

The firm was under a contractual obligation to obtain written approval from the RTC before it engaged any additional personnel to work on RTC matters. As pointed out above, the policies of the Legal Division are clear on this issue. The Legal Division examined all of the questionable invoices where individuals billed for their services without being listed on the LSA and without prior written approval from the Division. In the absence of information required by the Guide, such as years in practice and usual hourly billing rates, the Legal Division has determined that it will ratify the rates of the affected individuals at the lowest approved rate for a professional in their category (e.g., attorneys, paralegals, etc.).

In reaching a fair and reasonable solution to the issues raised in this Condition, the Legal Division reviewed the billable rate of all of the firm's employees who were not authorized to work on RTC matters. These employees included attorneys billing at various rates, case assistants, paralegals, and a separate category of employee titled "Other." In determining the allowable rate for each category of employee, the Legal Division approved the rate for that professional at the lowest agreed billing rate as it appears on the various agreements signed with the firm, the 1/24/90 FDIC letter to Brobeck, the 9/18/90 LSA, the 2/1/92 LSA, or the 5/5/92 LSA, depending on the date of the invoice where unauthorized billers appear (please see attached Exhibit "C" (matrix of unauthorized billers)).

For example, where it appears that an unauthorized billing attorney billed at _____ (b)(6) \$195 per hour during the month of June, 1991, we ratified that attorney's rate at the lowest agreed billing rate for attorneys on the 9/28/90 LSA and as specified in the 1/24/90 FDIC letter to the firm. The lowest rate in that case is \$105 per hour for

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attorneys as indicated in those agreements. Consequently, the Legal Division ratified this particular attorney's rate at \$105 per hour and disallowed the additional \$90 per hour which was not approved or agreed to by the RTC. In addition, the fees of categories of employees who were listed as "others" on the firm's bills, but who were not listed as a category of employee in the agreements during the period in question, were not ratified and their billable hours were disallowed in their entirety.³

Similarly, where it appeared that the employee in question billed at a rate equal to the lowest agreed billing rate for that category of employee, the employee's rate was ratified and no amount from his or her billable hours was disallowed. For example, where an attorney billed at \$200 per hour during the month of April, 1992, that rate was equal to the agreed billing rate for attorneys on the fee matrix attached to the 5/5/92 LSA and, therefore, her rate was ratified and approved for payment⁴ since it equaled the agreed billing rate for attorneys as listed on the agreements during the period of services in question.⁵

(b)(6) ³ Those amounts totaled \$677.50 and consisted of the billings of four different individuals [redacted] (b)(6) [redacted] whose category of work was not included in any agreement during the period of services under review and whose names are not listed under any other category on the fee matrix. However, where it appeared that an employee's name under the category of "Other" also appeared as a paralegal on the fee matrix attached to the 5/5/92 LSA and where it could be ascertained that that individual billed at an agreed paralegal rate, that employee's billable rate and billings at that rate were approved for payment. For example, please see the billable rate of [MKS] who was listed as "Other" but who appears as a paralegal on the fee matrix attached to the 5/5/92 LSA and who billed at an agreed paralegal rate.

(b)(6) ⁴ For example, please see the billable rate of [redacted] who billed in April, 1992 for 55.10 hours but whose rate of \$200 per hour equaled the agreed billing rate for attorneys on the fee matrix attached to the 5/5/92 LSA.

⁵ The rate for paralegals also was ratified at \$85 per hour because this was the agreed billing rate for paralegals as listed on the fee matrix of the LSA dated 5/5/92. Since most of the unauthorized paralegals billed at the same rate as the authorized paralegals identified on the LSA, no amount from the billable fees of the unauthorized billers was disallowed. We found two paralegals whose billed rate was less than the agreed upon rate for paralegals on the fee matrix attached to the 5/5/92 LSA. We ratified their rate at the rate billed to the RTC, in this case \$50 rather than \$85. We applied the same analysis to case assistants whose billing rate was equal to the agreed billing rate for case assistants on the 9/28/90 LSA and as specified in the 1/24/90 FDIC letter to the firm. The case assistant rate was ratified at the rate billed to the RTC since it corresponded with the agreed billing rate of case assistants in general.

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Accordingly, the Legal Division will disallow the amounts in excess of the lowest LSA rate for those categories of employees listed on the attached Exhibit "C". Those amounts total \$28,315.25. The remaining questioned costs are ratified.⁶

Condition 3: Photocopying Charged in Excess of Actual Costs

The auditors questioned \$124,070 for photocopying costs charged to the RTC at a higher rate per page than the maximum rate allowable by the RTC. The auditors reference the FDIC LSA dated September 28, 1990 which provides that "FDIC will pay for photocopying at actual cost, which will generally not exceed \$.15 per page."

In its response, the firm indicated the following:

Our various contracts with FDIC and RTC employed several different standards for photocopy expense....

Before September 28, 1990, there was no overarching written fee agreement on FDIC or RTC work. Cases and matters were assigned to the Firm on an *ad hoc* basis. Our normal billing rates were applied, as modified by specific agreements between the parties. As to photocopy expense, our August 8, 1989 letter from Mr. [B] to [FLS], FDIC Deputy Regional Counsel, explained that our photocopy rates were \$.20 and \$.22 cents per page, depending upon which Firm office was involved. These were the rates charged until we entered into an LSA on September 28, 1990. That LSA covered both FDIC and RTC work.

A letter to FLS dated August 8, 1989 did, in fact, exist in Legal Division files. That letter provided the following regarding copying:

The firm charges 20 cents per page (22 cents per page in Los Angeles) for copying, which represents our cost and does not include a profit mark-up or administrative surcharge. The firm provides copying as a necessary service to its clients but it does not view copying as a profit creating activity.

On September 28, 1990, the firm signed an LSA with the FDIC which also covered the RTC. This agreement provided the following in connection with photocopying:

⁶ Since the General Counsel has complete delegated authority regarding the hiring and paying of outside counsel with respect to issues raised by the report, his signing of this memorandum should be deemed a ratification or approval of billing rates to the extent indicated herein.

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FDIC will pay for photocopying at actual cost, which will generally not exceed \$.15 per page. When economically feasible, large copying projects should be sent out to a copying service. Clerical time for photocopying will not be paid.

Thereafter, the RTC signed an LSA with the firm on May 5, 1992 which incorporated the RTC's position vis-à-vis photocopying. The RTC's guidelines on this issue were set forth in the February, 1992 RTC Guide for Outside Counsel and provide the following:

Charges for photocopying shall be at the firm's actual cost, not to exceed eight cents per page, unless supported by a cost study. Copying projects where volume will generate substantial savings should be sent to outside vendors when practicable. As with all costs for supplies and services, the Legal Division looks to local commercial rates as a benchmark.

Accordingly, the law firm's photocopying charges for the audit period were governed by three different agreements. Prior to the first LSA, the Legal Division allowed the firm to bill for photocopying at \$.20 per page (or \$.22 per page if the Los Angeles office was used). This agreement remained in effect for a period of nine months during the audit period at which time the first LSA took effect on September 28, 1990. As indicated earlier, the first LSA reduced the photocopying charge to actual cost, generally not to exceed \$.15 per page. The Legal Division customarily allowed firms to bill at this maximum rate until publication of the RTC Guide in February 1992, which further reduced the photocopying charges to \$.08 per page.

In addition, the firm provided the auditors with a cost study to support the rate charged for photocopying. The cost study provided an explanation from the firm as to the amount it charged for photocopying. In its analysis of these expenses the firm made the following four points:

1. "Through 9/20/90, the firm's contract with RTC/FDIC provided for 20 cents or 22 cents per page, depending on the firm office involved....Although the selected invoices before 10/31/90 generally did not state the number of pages copied, it is clear that the charges before 10/31/90 were at those rates."

2. "As is apparent from the data displayed (in the cost study), there was a brief period of time after the RTC/FDIC LSA took effect in which photocopy charges were made at the 'old' rates. It is also apparent that the rates were reduced to \$.15 per page beginning April 30, 1991. The total 'excess' above 15 cents per page from 10/31/90 through 3/31/91 is \$8,241.64."

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3. "It appears that there was a brief period after the new RTC LSA became effective (on February 1, 1992) during which some copying was charged at the 'old' rate of \$.15 per page. The total 'excess' above 8 cents per page is \$4,371.99."

4. "Virtually all per page charges calculated from the face of the invoices were at 8 cents beginning July 31, 1992 and it is therefore apparent that the per page charge was almost certainly 8 cents in those instances where the invoice did not state the number of pages copied. The total of post-July 31, 1992 charges in 'excess' of \$.08 per page was \$139.72."

In addition, the RTC Guide for Outside Counsel which was published in February, 1992 became effective, for all practical purposes, on March 1, 1992. That Guide reduced the rate for photocopying charges to \$.08 per page, and since all LSAs are subject to the billing information and changes as incorporated in the Guide, the new rate for photocopying would have taken effect on March 1, 1992. However, the firm did not factor in this fact in its analysis, and as a result it improperly calculated the photocopying rate at \$.15 per page until May 5, 1992, the effective date of the RTC LSA, rather than the correct rate of \$.08 per page as of March 1, 1992. Consequently, the firm overstated the amount calculated per page by \$.07 for 15,719 copies or for a total overbilled amount of \$1,100.33.

We agree with the firm as to charges prior to 9/28/90, the date of the first LSA. Thereafter, the firm was permitted to charge \$.15 per page until March 1, 1992 (effective date of the RTC Guide) when a rate of \$.08 per page became effective. **Based on the foregoing, it appears that the law firm overcharged the RTC \$13,853.68 in photocopying expenses.**

Accordingly, the Legal Division will disallow \$13,853.68 under this Condition and will demand reimbursement from the firm for this amount.

Condition 4: Supporting Documentation Missing for Paid Expenses

The auditors questioned \$74,277 in expenses where the law firm did not provide original documentation as back-up for the billings it submitted to the RTC. The draft audit report indicated that the auditors had selected a sample of 148 invoices paid by the RTC for testing and asked the law firm to provide original "source documentation." The auditors added that, "[a]ll items billed should be supported by adequate documentation, such as original invoices. The documentation should be retained and available for review to establish the validity and reasonableness of amount billed."

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The law firm responded by indicating the following:

The draft report asserts that documentation for the questioned items could not be located or was "not appropriate." Only one example of "inappropriate" documentation is listed—charges for photocopying with no listing on the invoice of the number of copies made [footnote omitted]. The draft report takes the position that only "original" backup is acceptable. Otherwise, it is impossible to ascertain what documentation was deemed by MT to be "inappropriate."

The RTC Guide for Outside Counsel provides that, "Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payment." The LSA dated September 28, 1990 states the following regarding this issue, "[T]he Firm shall keep all of its billing records for at least three years from billing date. The Firm shall permit FDIC to conduct an audit or review of the Firm's billing procedures. Firm further agrees to provide additional information concerning its billing procedures and practices and other reports which the FDIC may request without charge."

The firm also pointed out that what is considered "appropriate" is not necessarily an "original" invoice. The requirement imposed on firms was to retain copies of all bills and supporting material, which the firm appears to have done. The firm also maintained that, "[t]here is no legitimate basis for MT to rewrite our FDIC contracts so as to impose a requirement for maintaining 'original' vendor bills when the contract explicitly approves retention of copies of those bills."

The Legal Division reviewed the auditors' workpapers to determine if, in fact, the firm submitted receipts for the expenses for which they claimed reimbursement. RTC invoice Number 917267, dated September 30, 1992, references the following expense: date billed 8/06/92, \$57, NOW Courier, [redacted] date incurred 07/09/92. A copy of a receipt in that amount appears in the voluminous documentation considered by the auditors under this Condition. The date and the pick-up instructions appear identical to those referenced in the invoice. Similarly, RTC invoice Number 917267, dated September 30, 1992, references the following expense: date billed 8/28/92, \$35, NOW Legal Systems, and described further as [redacted] a United States District Court, 08/03/92." A copy of this receipt by NOW Legal Systems exists in the workpapers for the exact amount and date in question.

(b)(4),(b)(6)

(b)(4),(b)(6)

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The Legal Division's position vis-à-vis this Condition is that copies of receipts are acceptable substitutes for the original. Absent evidence of fraud or misrepresentation a copy is valid proof of the payment of this expense. The auditors combine both the unsupported expenses and the expenses that are backed by copies under this category. However, the Legal Division's position has been that copies of originals are sufficient to demonstrate payment of the underlying expense.

The firm identified, however, certain items for which it did not provide any documentation, either because they could not be located or because the time constraints in responding to the audit prevented the firm from addressing this matter. As a result, the firm uncovered several items (totaling \$5,459) for which documentation could not be located. As indicated above, all reimbursable expenses must be backed up by sufficient evidence of payment to justify reimbursement. In this case, by the firm's own admission, no receipts of any kind existed that would explain the payment of these expenses. **Accordingly, the Legal Division will disallow the amount corresponding to the expenses having no back-up documentation. That amount totals \$5,459.**

Condition 5: Payment for Professional Fees and Expenses That Were Partially Disallowed by RTC

The OIG questioned \$2,913 (originally \$15,140 per MT) in professional fees and expenses "that were either unallowable by the LSA and the incorporated guidance or required additional information to be submitted by Brobeck to the Legal Divisions." Those questioned costs were identified through the review of 35 exception letters issued by the RTC and FDIC. The law firm addressed all but 7 of these letters and resolved any residual issue remaining. However, the 7 exception letters representing 13 invoices that were paid in full by the RTC had not been resolved. Consequently, the OIG recommended that the FDIC obtain a refund of the amount that had previously been disallowed for fees and expenses totaling \$2,913.

The law firm did not contest this finding and agreed to accept the recommendation to disallow \$2,913 under this Condition. **Accordingly, the Legal Division will disallow \$2,913 and will demand reimbursement from the firm for this amount.**

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Condition 6: Review All Other Exception Letters As They Relate to Condition 5

The auditors also recommended that the Legal Division review all other exception letters that were not examined under Condition 5 and which came about as a result of the accelerated payment program in place at the RTC in the early 1990s. The auditors recommended that the Legal Division determine the amount of funds inappropriately paid to the firm and request a refund of those funds.

The Legal Division does not agree that a review of all exception letters is called for at this time. Such a review would not be cost-effective and any likely benefit would be purely speculative. It should be pointed out also that the auditors were in the best position to examine any other outstanding exception letters at the time of the audit.

Furthermore, the OIG reduced the amount originally questioned per MT under Condition 5 from \$15,140 to \$2,913. It appears that this reduction was effectuated because, as indicated in the workpapers, "[s]ubsequent to the audit exit conference, Brobeck provided the auditors additional information to support its position. [Brobeck's] documentation was reviewed, and where appropriate, the questioned costs were reduced." Because of the significant reduction in the questioned amount, it appears that the OIG did not consider an expansion of this inquiry beyond the 35 exception letters sampled by the auditors to be cost-effective.

Accordingly, the Legal Division does not believe that a review of all other exception letters would result in a credible determination of overpayment and, therefore, will not undertake such a review.

Condition 7: Professional Fees Billed in Excess of LSA Approved Rates and Approval Letters

The auditors questioned \$29,824 for professional fees that were "up to \$60 per hour higher than allowed by prevailing contract rates for 20 professionals." The OIG argued that law firms must charge for legal services in accordance with the schedule of fees and the hourly rate structure found in the LSA. The OIG cites the LSA as a basis for questioning these fees. The pertinent parts of the September 28, 1990 LSA provide as follows:

The hourly rates for each attorney and paraprofessional in the Firm who is to work on FDIC matters is set forth on the Rate Structure, attached hereto as Exhibit C and incorporated herein by this reference. Personnel may be added to the list, but only by written mutual agreement of the Firm and the FDIC.

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The May 5, 1992 LSA confirms this position and allows that:

Outside Counsel agrees to provide legal services in accordance with the hourly rates or alternative rate structures (for each attorney and paraprofessional assigned to work on FDIC matters) set forth on the attached schedules. The schedules are an integral part of this Agreement and can only be amended with the written consent of the RTC Division of Legal Services.

In addition, the February, 1992 RTC Guide for Outside Counsel provides that :

The Legal Division generally enters into a two-year LSA. Absent compelling reasons, no increase in the fee or rate schedule will be permitted during the term of the LSA.

The FDIC Guide for Outside Counsel, published in December, 1991, takes a similar position:

[T]he Division will contact you to negotiate the proposed fee schedule attached to the LSA that you executed and submitted with your application materials. The Division generally enters into a two-year LSA. Absent compelling reasons, no increase in the fee or rate schedule attached to the LSA will be permitted during its term.

The law firm responded to the auditors' recommendations by indicating that for a period of time from July 1991 through January 1992, "a firmwide rate adjustment was reflected in RTC billings with no corresponding change in the LSA. But, some portion of this *gross* amount has already been *refunded* by the Firm." However, the firm did not provide any evidence that it refunded the amounts overbilled. It cited various reasons, such as the passage of time and the expense involved in researching these matters, as mitigating reasons for not submitting the necessary back-up documentation.

As indicated above, the contractual agreements entered into between the firm and the RTC make it clear that no increase in the rate structure would be permitted, unless by written mutual agreement or because of compelling reasons. The firm did not provide any letter granting it authorization to increase its rates, nor did it provide any explanation that would justify an increase in the rate beyond what was contractually agreed to in the LSA matrix. **Accordingly, the Legal Division will disallow the entire amount under this Condition totaling \$29,824, but will reconsider its decision if the firm provides adequate documentation showing RTC approval of an increase in the approved rates.**

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Condition 8: Other Unallowable Professional Fees

The auditors questioned \$22,729 in unallowable professional fees billed for tasks which the auditors considered either excessive or routine in nature and which should have been absorbed by the firm. These costs are broken down as follows: \$21,530 for excessive review/revision of documents (e.g., ATS memo, loan files regarding directors), and \$1,199 for research of conflict/preparation of bills, budget and status reports.

MT control number 48 of invoice number 1006728 identifies fifteen (15) entries that are circled in red by the auditors and that are marked either "DIS" or "Excessive". Of the fifteen (15) entries, thirteen (13) are marked "Excessive". These entries refer to a directors' and officers' liability case stemming out of the failure of Westport Federal Savings Bank, which the firm worked on between August, 1992 and February, 1993. The majority of these entries took place from January 7, 1993 to February 23, 1993 and are described generally as "review and revise Authority to Sue Memorandum" and "review and analyze loan files regarding officers." Three attorneys appear to have worked on and off on the memorandum throughout this period of time for a total of 141.25 hours at an hourly rate ranging from \$85 per hour to \$200 per hour. The Legal Division does not consider this an excessive number of hours to work on a major document that weighs the merits of the case for the in-house lawyers to determine whether or not filing suit is appropriate under the circumstances.

In general, preparing the groundwork for a suit against the directors and officers requires an enormous investment in time and effort. As part of its analysis, the firm needs to spend a considerable amount of time identifying the defendants, quantifying the amount of damages sustained by the bank, and examining legal issues that could be raised in a trial. Accordingly, spending 141.25 hours in the preparation of an authority to sue memo, which becomes the linchpin in the filing of the complaint in a complex case, does not appear inordinately high. **Therefore, no disallowances will be taken under this category of questioned costs.**

The remaining questioned costs under this Condition are for routine overhead matters that should have been absorbed by the firm as a necessary component of doing business. For example, on 8/13/92 and 8/18/92 attorney [redacted] billed for the following work as described in the invoice: "Draft letter to [RTC staff attorney] regarding hourly rates in RTC-Westport Federal Savings Bank matter" and "Read fax engagement letter from [RTC staff attorney] regarding RTC-Westport Federal Savings Bank matter." This work appears to be directed toward the preparation of bills or routine status reports.

(b)(6)

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The RTC Guide for Outside Counsel provides the following guideline on this issue:

The Legal Division considers its reporting and billing requirements to be part of the cost of doing business with the RTC, and as a general rule will not pay Outside Counsel for the time expended on the preparation of bills and routine reports.

In its response, the law firm conceded the following:

There is a challenge of some time spent on conflict research, bill preparation and client status reporting (\$1,199). We believe a fair resolution of these items would be \$1,000, and we ask that the draft report be revised so as to make the total for this category no more than \$1,000.

However, the Guide is clear on this point. The RTC will not pay for routine tasks that are normally absorbed by the firm and considered as an overhead expense related to conducting business. **Accordingly, the Legal Division will disallow the entire amount under this category totaling \$1,199.**

Condition 9: Other Unallowable Expenses

The auditors questioned \$17,803 in unallowable expenses charged to the RTC for the following three (3) categories: postage charges (\$187); overhead charges (\$13,275); and travel charges (\$4,341). The auditors base this recommendation on the guidelines set forth in the RTC Guide for Outside Counsel which provide that, "The firm must include in its proposed rates for legal services all 'overhead' and 'profit'."

Postage Charges

In its response, the firm conceded the charge for postage, but argued that the remaining amounts under the travel and overhead categories are appropriate charges "for matters of the type involved here." Since the firm accepted the OIG's recommendation concerning the postage charges, we will not address this issue further. **Accordingly, the Legal Division will disallow \$187 under this category.**

Overhead Charges

A representative sample of the questioned charges was reviewed. The largest entries in the "overhead" category can be broken down essentially into two types of bills: appraisal fee and supplies. MT control number 213 of invoice number 853761 includes a bill dated December 19, 1991 for \$4,908.25 from R.E. Analysis, Inc. of Irvine,

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California for an appraisal performed by this firm. The invoice, in at least two different places, indicates that the appraisal was approved by the RTC in-house lawyer [MS]. The appraisal was performed as part of a bankruptcy case that arose out of the failure of Mercury S&L of Huntington Beach, CA, and was undertaken to determine the value of a property in Santa Ana. This information obtained from the appraisal was then used in the litigation. From the auditors' notes, it appears that the sole reason for questioning this expense is because the auditors did not "see [the] original approval from [the] RTC." Clearly, this is not an expense that is normally thought of as "overhead" in nature. The appraisal was undertaken on behalf of and for the benefit of the client as well as this particular case which the firm was engaged to handle.

The other charges under the general rubric of "overhead" expenses are for supplies. The charging of normal office supplies that are incidental to doing business is not a reimbursable expenditure since those expenses are normal and necessary to the successful operation of a law firm. In that connection, the RTC Guide for Outside Counsel provides the following guidance:

The firm must include in its proposed rates for legal services all "overhead" and "profit". The RTC does not pay for the following: secretarial or clerical overtime (unless such overtime is requested by an RTC Attorney or occasioned by an emergency situation created by the Corporation); charges for word processing or computer time (except actual charges for Westlaw or Lexis); time devoted to the preparation of bills or routine status reports; or markups on any supplies or services procured from third parties.... As with all costs for supplies and services, the Legal Division looks to local commercial rates as a benchmark.

However, supplies that are specially purchased and used exclusively in the prosecution of a case cannot be categorized as routine supplies purchased by the firm to engage in the practice of law. These particular supplies, identified by the auditors, are unique and were purchased for the purpose of organizing the documentation in a case stemming out of the failure of HomeFed Bank. For example, binders were purchased by the firm to send to interested parties outlining the interrelationships between HomeFed Bank and Home Capital Corporation. On June 25, 1992, the firm purchased 60 binders from Kosman Supplies at a unit cost of \$18.95 for a total price with tax of \$1,233.65. These binders were drop-shipped to San Diego where the firm attorneys in charge of the case were working and where Home Capital Corporation was headquartered. These expenses are extraordinary expenses related to the purchase of specific supplies related to the case, and are not typical office supplies that a firm would purchase in the conduct of its business such as paper, pens, computer disks, and the like. The firm would not have purchased these relatively expensive binders but for the

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need that arose to use them in this case. **Based on our review of the sampled charges, no disallowances will be made under the subcategory of "overhead" expenses.**

Travel Charges

The auditors also questioned \$4,341 in travel and entertainment expenses that are not permitted under the Guide. The applicable sections of the Guide provide the following guidance on the issue of travel and entertainment expenses:

Hotel accommodations must be moderately priced, as expenses for luxury hotels or special services are not reimbursable.... Outside Counsel will be provided evidence that they are traveling on official business for the RTC so that they may avail themselves of such discounts, and will be expected to make every effort to obtain the lowest rate available.

If business is conducted during a meal, appropriate time charges may be made at normal hourly rates. Charges for food, beverages and the like will not be reimbursed by the RTC unless an attorney is in travel status and is away from the home office overnight. In that instance, the RTC will reimburse all subsistence expenses at RTC standard per diem rates.

The expenses questioned by the auditors under this sub-category include such unauthorized personal expenditures as laundry service at hotels, room movie at hotels, health club charges, soda and juice charges, mini-bar purchases in hotel rooms, and unreasonable room service charges. These expenditures are not permitted under the Guide and will be disallowed.

In addition, the firm billed for meals during working sessions. In one example, the firm billed \$117.18 from Waiters on Wheels for what appears to be a group lunch. The Guide does not permit the reimbursement of expenses related to working lunches since each individual at the working lunch would be permitted to bill separately for his or her per diem expenses while in travel status. Therefore, an individual who receives a per diem allowance in addition to a subsidized lunch would obtain a benefit that is not authorized under the controlling provisions of the Guide. **Consequently, all of the travel expenses questioned by the auditors and totaling \$4,341 will be disallowed.**

Accordingly, the Legal Division will disallow for postage and travel and entertainment charges and will demand reimbursement for the full amount totaling \$4,528 under this Condition.

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Condition 10: Legal Research (Westlaw, Lexis) Billed Above the Actual Cost

The auditors questioned \$7,197 in expenses billed to the RTC for research (computer time) at a rate that reflected a 50 percent markup above the actual cost to the firm during the period covered under the review (1990 through 1993). As indicated above, the RTC Guide for Outside Counsel is clear on this issue. The Guide provides that the Legal Division will not pay for "charges for word processing or computer time (except actual charges for Westlaw or Lexis)...."

In its response, the law firm accepted the OIG's recommendation to disallow \$7,197 "subject only to confirmation that these charges fall within the pertinent statute of limitations." **Accordingly, the Legal Division will disallow these charges and will demand reimbursement for the full amount totaling \$7,197 under this Condition.**

Condition 11: Attorneys and Paralegals Billed Fees for Secretarial Functions

The auditors questioned \$2,336 in fees billed to the RTC for services performed by attorneys and paralegals that could have been performed by secretaries at a reduced rate or considered as "overhead" which would have been absorbed by the firm as the cost of doing business. The auditors classified the following functions as administrative or clerical in nature and not chargeable to the RTC: photocopying documents, organizing documents, organizing documents for storage, supervising file organization, filing and refiling, collating documents, and processing vendor bills.

In its response, the firm indicated the following:

We have reviewed the Brobeck, Phleger & Harrison charges which the draft report questions. These charges reflect two judgment calls—first by the attorney performing and recording time for the service (rather than delegating to a secretary) and second by the oversight attorney (employed by the client) who reviewed and approved the bills. That review and approval process occurred in a context-rich setting, and there is no substantial basis for second guessing the charges years after they occurred. This is especially true when, as is the case here, the persons involved at the FDIC and at Brobeck are no longer readily available for comment or explanation.

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(b)(6)

The bulk of these questionable charges appears on one invoice and totals \$1,725.⁷ MT control number 85 of invoice number 818255 describes seven (7) entries by paralegal [redacted] charging an hourly rate of \$85 per hour, which the auditors considered secretarial in nature. The work was undertaken during a period beginning on September 3, 1991 to September 20, 1991 for a total of 20.30 hours of billable time. The entries are described either as "Preparation of witness binders" or "Preparation of witness binders for depositions."

It appears from the invoice that shortly after the preparation of these binders, the firm began a concentrated effort to take a number of depositions. It would not be unreasonable to ask a paralegal to prepare binders for depositions. Each binder would be specifically geared to a particular witness with the corresponding exhibits. A paraprofessional would be in a better position than a secretary to determine which exhibit to include in the binder and to have each binder "custom-made" for each prospective witness. This is not a job for a secretary, but is one better handled by a paraprofessional who has a full command of the issues.

MT control number 89 of invoice number 836499 billed by attorney [redacted] at an hourly rate of \$210 on November 19, 1991 for .60 hours for a billable fee of \$126 is described in the fee bill as follows: "Prepare notice of lodging interrogatory responses for November 20, 1991 status conference." This is clearly not a function that could be performed by a secretary. It was appropriate for an attorney to have prepared this notice and to have billed for it.

(b)(6)

Based on our general review of the underlying entries that make up this Condition, the Legal Division does not believe that any of the work in question should have been performed by a secretary. **Accordingly, no disallowances will be taken for any of the expenses described under this Condition.**

Condition 12: Attorneys Billed for Paralegal Functions

The auditors questioned \$1,976 in fees billed by attorneys for tasks which could have been performed at a reduced cost by paralegals. Those tasks included: preparation of exhibit list, preparation of witness list, preparation of interrogatories (Form), summarization of depositions, and preparation of records request. Furthermore, the auditors indicated that these tasks are "classified as common paralegal functions" by Legalgard, the auditors' legal experts, and, therefore, should have been billed at the lower paralegal rate rather than the attorney rate.

⁷ The amount originally questioned by the auditors was \$4,263, but was reduced to \$1,725 prior to issuance of the draft audit report when the firm provided the auditors additional information to support its position.

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The law firm, in turn, objected to the subjective judgments underlying the questioned items in this Condition. In its response, the firm pointed to the following:

Each of the questioned items reflects decision making, by experts who were closely involved with the problem at the time, about appropriate staffing and allocation of resources. An after-the-fact review by an auditor not familiar with the exigencies existing when the work was done is an especially poor vehicle for review. Great deference should be given to the fact that the bills were reviewed and approved by a client representative who was fully familiar with both the requirement that the representation be efficient and with the facts and circumstances of the particular matter now under review.

The questioned charges were reviewed as itemized in the audit workpapers. For example, MT control number 83 of invoice number 810326 describes three (3) entries by attorney [redacted] who charged an hourly rate of \$210. The three entries took place on 08/07/91 and 08/08/91 for a total of 4.10 hours at a cost of \$512.50. The entries are described as follows in the order in which they appear on the invoice: "[d]id Lexis search for other authorities more on point, and then read those cases" (1.5 hours on 08/07/91); "[i]dentified and located documents [redacted] will need to seek protective order and sent them to him with cover letter" (.60 hours on 08/08/91); and "[r]esearched California cases on administrative exhaustion and subject matter jurisdiction challenges, to be used on motion to dismiss for failure to file timely federal court action" (2.00 hours on 08/08/91).

It is not improper for an attorney to engage in legal research, or to sort through documents if his involvement in this work would be more cost-effective than if performed by a lower-billing individual who might not complete such tasks as quickly. The time invested by an attorney to research a narrow issue is more likely to achieve desired results and to be less time-consuming than the time devoted to the task by a paralegal, if one considers all the different parts of a research assignment which include the time allotted by the attorney and the paralegal to discuss the issues to be researched, the actual research time involved, and the time of both professionals to review the results of the research. Consequently, it was not necessarily improper for attorney [redacted] to have engaged in this work instead of delegating it to a paralegal. In fact, the auditors seem to endorse this position in their report. The draft audit report quotes the following from the RTC Guide for Outside Counsel, "[t]he overall objective of the Legal Division as to litigation is to obtain the best and earliest resolution at the lowest practicable cost" (emphasis in the report).

Based on the foregoing, the Legal Division will not disallow any amount questioned under this Condition.

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Condition 13: A Conflict of Interest During the Period Covered Under the LSA

In their report, the auditors indicated that a conflict of interest existed in the firm's representation of a RTC Legal Division employee. Specifically, the report described the conflict as follows:

(b)(6) We noted that Brobeck represented an RTC Legal employee, formally [sic]
 (b)(6) Deputy Regional Counsel at the [redacted], regarding attorney
 discipline and State Bar of [redacted] at the same time that
 Brobeck received referrals from the same RTC field office. The employee was
 involved in the decision-making process as to the firms RTC would use to handle
 its cases. Brobeck's attorneys spent a total of 300 hours on this case between
 1991 and 1993.

...

Brobeck was in violation of the RTC-LSA at the time it signed the agreements. Additionally, Brobeck was not in compliance with the RTC and the FDIC Guidelines in relation to conflict of interest. Per the LSA, Brobeck should have stopped working on the RTC cases until this situation was resolved.

The report recommends "that RTC [sic] turn this case over to the OCCC [Outside Counsel Conflicts Committee] so that the OCCC can make a determination as to whether this is an actual conflict. Should this situation be deemed an actual conflict of interest, we also recommend that all fees paid to Brobeck during this time period be disallowed due to non-compliance with the LSA."

The firm was terminated by the joint FDIC/RTC Outside Counsel Conflicts Committee ("Conflicts Committee") on June 2, 1994 for, *inter alia*, its continued failure to adhere to RTC conflicts policies. (No disallowance of fees or expenses was ordered by the Conflicts Committee.) Therefore, any conflict of interest arising from the representation described in the audit report is now moot. In addition, on December 21, 1995, the RTC Executive Committee approved the request of the former RTC Deputy Regional Counsel for indemnification in connection with the attorneys' fees and expenses incurred in connection with the matter at issue. Subsequently, payment of \$53,823.17 out of the \$56,097.17 billed by the firm was approved and made to the employee in question for the purpose of paying his attorney's fees. Disallowance of "all fees paid to Brobeck during this time period" as recommended would be inconsistent with the prior decisions of the Conflicts Committee and the RTC Executive Committee. **Accordingly, no further action will be taken in connection with this recommendation.**

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Other Matters

In addition, the auditors highlighted two separate matters in their report. First, the auditors indicated that they were unable to verify adequately 18 of the conflict waiver letters since source documents were not provided by Brobeck. Consequently, the auditors argued that Brobeck "may have been working on cases where actual or potential conflicts of interest existed." Second, the auditors noted that out of 47 cases reviewed, the firm failed to "outline" the required information and the necessary documentation on certain case plans. As a result of this omission, the auditors alleged that the firm "had been working on cases without proper case planning and budgeting that may have led to overbilling RTC or performing services in a non-efficient manner."

The last LSA in effect for Brobeck, Phleger & Harrison expired on July 6, 1994. The LSA was not renewed. In addition, the firm does not currently have any open matters for which it represents the FDIC. Accordingly, these issues raised by the OIG without recommendation are now moot.

In summary, the Legal Division will disallow the following amounts (questioned costs are in parentheses):

<u>Recommendation</u>	<u>Disallowance</u>
1. Computerized Time Sheets (\$4,619,956)	0
2. Professional Fees Billed for Individuals Without Prior Written Approval (\$281,183)	\$ 28,315 (rounded)
3. Photocopying Charged in Excess of Actual Costs (\$124,070)	\$ 13,854 (rounded)
4. Supporting Documentation Missing for Paid Expenses (\$74,277)	\$ 5,459
5. Payment for Professional Fees and Expenses That Were Partially Disallowed by RTC (\$2,913)	\$ 2,913
6. Review All Other Exception Letters As They Relate to Condition 5 (-0-)	0
7. Professional Fees Billed in Excess of LSA Approved Rates and Approval Letters (\$29,824)	\$ 29,824

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8. Other Unallowable Professional Fees (\$22,729)	\$ 1,199
9. Other Unallowable Expenses (\$17,803)	\$ 4,528
10. Legal Research (Westlaw/Lexis) Billed Above the Actual Cost (\$7,197)	\$ 7,197
11. Attorneys and Paralegals Billed Fees for Secretarial Functions (\$2,336)	0
12. Attorneys Billed for Paralegal Functions (\$1,976)	0
13. Conflict of Interest (-0-)	0
TOTAL:	<u>\$93,289</u>

The Assistant General Counsel is authorized to make such minor accounting corrections as may be requested by the OIG, but which do not affect the substantive positions stated in this memorandum. Collection of disallowed amounts will be initiated within thirty (30) days of issuance of the final audit report. The Legal Division expects to complete the collection process within ninety (90) days after receipt of the final report.

Attachments:

Tab A - OIG Draft Audit Report
 Tab B - Firm Response to the Draft Audit Report
 Tab C - Analysis of Unauthorized Billers



Federal Deposit Insurance Corporation
Washington, D.C. 20434

Office of Inspector General

February 22, 1999

MEMORANDUM TO: Board of Directors
Audit Committee

(b)(6)

FROM: Gaston L. Gianni, Jr.
Inspector General

SUBJECT: Report Entitled *Legal Fees Paid by RTC to Salem, Saxon & Nielsen*
(Audit Report No. 99-012)

Attached for your information is a copy of an audit report the Office of Inspector General (OIG) recently issued. Also attached is a summary of the report.

This report presents the results of an audit of Salem, Saxon & Nielsen, a law firm hired to provide legal services to the Resolution Trust Corporation. The report was prepared by the joint venture Financial Management Associates on behalf of the OIG. Management's response to a draft of this report provided the requisites for a management decision on each of the recommendations. We questioned costs in the amount of \$61,110 of which management disallowed \$8,112. The difference between what we questioned and what the Legal Division disallowed is attributable to \$35,277 in unsupported photocopying charges, \$9,516 for missing time sheets, and \$8,205 for unsupported mark-ups to fees.

If you have any questions, please call me at (202) 416-2026 or Steven A. Switzer, Deputy Inspector General for Audits, at (202) 416-2543.

Attachments

Legal Fees Paid by RTC to Salem, Saxon & Nielsen

(Audit Report No. 99-012, February 11, 1999)

The Office of Inspector General (OIG) has completed an audit of Salem, Saxon & Nielsen, a law firm hired to provide legal services to the Resolution Trust Corporation (RTC). The audit was conducted by the joint venture Financial Management Associates through a contract with the OIG and covered billings paid by RTC during the period January 1, 1991, through December 31, 1994. The total fees paid to the law firm during the audit period were \$4,223,285. The audit sample covered \$2,300,802, or 54 percent of the total. The audit identified \$688,732 in net questioned costs.

Recommendations

The OIG recommended that the Assistant General Counsel, Legal Operations Section, Legal Division:

- analyze the qualifications of employees working on RTC matters but not listed on the firm's legal services agreement, determine how much of the \$292,713 in questioned costs should be ratified, and disallow any of the charges not approved;
- disallow \$29,896 for overbillings due to unauthorized rates;
- disallow \$14,352 for fees written-up from original time records;
- disallow \$69,580 for fees that did not contain a 20 percent discount agreed to by the firm and RTC;
- disallow \$20,015 for unauthorized personnel;
- disallow \$35,576 for learning curve charges;
- disallow \$8,205 for fees written-up on pre-bills; and
- disallow \$160,357 for unallowable, unapproved, or unsubstantiated expenses.

In addition, the OIG recommended that FDIC disallow \$58,038 for a variety of questionable charges.

Management Response

The General Counsel's response to a draft of this report provided the requisites for a management decision on each of the recommendations. Management disallowed a total of \$8,112. Although management's corrective actions differed from the recommended corrective actions, we consider management's response as providing the requisites for a management decision.

Specifically, in recommendations 2 and 9, the OIG recommended that FDIC disallow \$29,896 for overbillings due to unauthorized rates. Management allowed \$29,007 and disallowed \$889. The Legal Division allowed \$21,152 for an attorney whose billing rate appeared in alternative documentation submitted by the firm and agreed to by RTC. The Legal Division also allowed \$7,855 that, based on further review, was paid by RTC at the

correct authorized rates. The OIG accepts management's explanation and, accordingly, reduced questioned costs to \$889.

In recommendation 3, the OIG recommended that FDIC disallow \$14,352 for fees written-up from original time records. Management allowed \$9,516 related to missing time records based on an analysis of several factors that were favorable to the firm. Management disallowed \$4,836 related to invoices that were marked-up from original time sheets because the firm was unable to provide any explanations. However, in the absence of time sheets, the OIG could not independently verify the time charges. Accordingly, for recommendation 3, the OIG will continue to question \$14,352.

In recommendation 5, the OIG recommended that FDIC disallow \$69,580 for fees that did not contain a 20 percent discount agreed to by the firm and RTC. Management allowed all the questioned charges. Specifically, the Legal Division stated that the 20 percent discount was not an across-the-board discount. Rather, at RTC's request, the firm specifically delineated the discounted rates for each attorney in its legal services agreement. The OIG accepts management's explanation and, accordingly, reduced questioned costs to \$0.

In recommendation 12, the OIG recommended that FDIC disallow \$35,576 for learning curve costs. Management allowed all the questioned charges. The Legal Division reviewed the questioned time entries and concluded that the activities actually related to factual, investigative work for professional liability cases. The OIG accepts management's explanation and, accordingly, reduced questioned costs to \$0.

In recommendation 13, the OIG recommended that FDIC disallow \$8,205 for fees written-up on pre-bills. Management allowed all the questioned charges. Based on explanations provided by the law firm and the belief that the firm was entitled to compensation notwithstanding missing time records, the Legal Division allowed the charges. Nonetheless, without original time sheets, the OIG could not independently verify the validity of the fees written-up on pre-bills. Therefore, the OIG will continue to question \$8,205.

In recommendations 24 through 39, the OIG recommended that FDIC disallow \$160,357 for unallowable, unapproved, or unsubstantiated expenses. Management allowed \$159,309 and disallowed \$1,048. The Legal Division allowed \$35,277 for in-house photocopying charges, \$26,319 for unsupported facsimile charges, \$12,035 for unsupported telephone charges, \$13,731 for title insurance policy charges, \$47,100 for unsupported consultant charges, and \$24,847 for miscellaneous other expenses. Generally, the Legal Division allowed the expenses because RTC and FDIC guidelines did not explicitly prohibit the expenses, the law firm provided additional supporting documentation, or the law firm provided clarifying explanations.

The OIG agrees with \$124,032 of the \$159,309 in Legal Division allowances. However, the OIG will continue to question \$35,277 for in-house photocopying charges. Specifically, the joint venture appropriately questioned the charges using the guidelines

in effect that required a cost study. Therefore, for recommendations 24 through 39, the OIG will question \$36,325 (\$1,048 + \$35,277).

Finally, the OIG recommended that FDIC disallow a total of \$58,038 for a variety of other questionable fees. Based on explanations and additional documentation provided by the law firm, a review of the joint venture's working papers, and application of guidelines in effect during the period in question, the Legal Division allowed \$56,699 and disallowed \$1,339. The OIG accepts management's explanations associated with these recommendations and reduced questioned costs to \$1,339.

Based on the joint venture's audit work, \$688,732 was questioned in the draft report transmitted to management. In addition to the recommendations previously discussed, in recommendations 1 and 11, the OIG recommended that FDIC disallow or ratify \$312,728 for work performed by unauthorized personnel. Based on a review of the firm's legal services agreements, case plans, and budgets, the Legal Division ratified or approved all the questioned charges. The OIG accepts the action taken by management and, accordingly, reduced questioned costs to \$0. After considering \$8,112 in disallowances taken by management and management's comments on the joint venture's findings, we will report questioned costs of \$61,110 (including \$44,407 in unsupported costs) in our *Semiannual Report to the Congress*.

LEGAL FEES PAID BY RTC TO SALEM, SAXON & NIELSEN

Audit Report No. 99-012
February 11, 1999



OFFICE OF AUDITS

OFFICE OF INSPECTOR GENERAL



Federal Deposit Insurance Corporation
Washington, D.C. 20434

Office of Audits
Office of Inspector General

February 11, 1999

MEMORANDUM TO: James T. Lantelme
Assistant General Counsel
Legal Operations Section
Legal Division

(b)(6)

FROM: David H. Loewenstein
Assistant Inspector General

SUBJECT: *Legal Fees Paid by RTC to Salem, Saxon & Nielsen*
(Audit Report No. 99-012)

This report presents the results of an audit of Salem, Saxon & Nielsen, a law firm hired to provide legal services to the Resolution Trust Corporation (RTC). The Office of Inspector General (OIG) has an ongoing program for auditing law firm billings to ensure that such billings are adequately supported and comply with cost limitations set forth by the Federal Deposit Insurance Corporation (FDIC) and the former RTC. This report was prepared by the joint venture Financial Management Associates for the FDIC OIG.

The objectives of the audit were to ensure that fee bills were adequately supported and in compliance with the cost limitations set by FDIC and RTC and that charges for legal services provided were reasonable. The audit covered billings paid by RTC during the period January 1, 1991, through December 31, 1994. The total fees paid to the law firm during the audit period were \$4,223,285. The audit sample covered \$2,300,802, or 54 percent of the total.

The audit resulted in net questioned costs of \$688,732. The OIG made 39 recommendations to the Assistant General Counsel (AGC), Legal Operations Section, Legal Division, to disallow the questioned costs. The General Counsel (GC) provided a written response dated December 16, 1998, to a draft of this report. The response from the GC is included as an appendix to this report.

The Inspector General Act of 1978, as amended, requires the OIG to report on the status of management decisions on its recommendations in its semiannual reports to the Congress. To consider FDIC responses as management decisions in accordance with the act and related guidance, several conditions are necessary. First, the response must describe for each recommendation

- the specific corrective actions already taken, if applicable;

- corrective actions to be taken together with the expected completion dates for their implementation; and
- documentation that will confirm completion of corrective actions.

If any recommendation identifies specific monetary benefits, management must state the amount agreed or disagreed with and the reasons for any disagreement. In the case of questioned costs, the amount FDIC plans to disallow must be included in management's response.

If management does not agree that a recommendation should be implemented, it must describe why the recommendation is not considered valid.

Second, the OIG must determine that management's descriptions of (1) the course of action already taken or proposed and (2) the documentation confirming completion of corrective actions are responsive to its recommendations.

In its response to the draft audit report, the law firm explained that some audit findings were based, at least in part, on unadjusted pre-bills or invoices never billed to RTC. As a result, certain audit findings were overstated. Based on a review of the audit working papers and additional information provided by the firm, the OIG verified that, due to an apparent misunderstanding between the joint venture and the law firm, the joint venture based some audit findings on unadjusted pre-bills or invoices not billed to RTC. Accordingly, we modified our position on several audit findings as subsequently described.

The GC's response to a draft of this report provided the requisites for a management decision on each of the recommendations. Therefore, no further response to these recommendations is required. Management disallowed a total of \$8,112. Although management's corrective actions differed from the recommended corrective actions, we consider management's response as providing the requisites for a management decision. A summary of the GC's response to recommendations 2 through 10, and 12 through 39 and our analysis follows.

Disallow \$29,896 for overbillings due to unauthorized rates (questioned cost) (recommendations 2 and 9). The GC's response allowed \$29,007 and disallowed \$889. The Legal Division allowed \$21,152 for an attorney whose billing rate appeared in alternative documentation submitted by the firm and agreed to by RTC. The Legal Division also allowed \$7,855 that, based on further review, was paid by RTC at the correct authorized rates. The OIG accepts the Legal Division's explanations and, accordingly, reduced questioned costs to \$889.

Disallow \$14,352 for fees written-up from original time records (questioned cost) (recommendation 3). The GC's response allowed \$9,516 and disallowed \$4,836. Specifically, the Legal Division allowed \$9,516 related to missing time records based on an analysis of several factors that were favorable to the firm. The Legal Division disallowed \$4,836 related to invoices that were marked-up from original time sheets because the firm did not provide an explanation for the discrepancies. However, in the absence of time sheets, the OIG could not independently

verify the time charges. Accordingly, for recommendation 3, the OIG will continue to question \$14,352.

Disallow \$1,823 for time billed in excess of 15 hours in a day (questioned cost) (recommendation 4). The GC's response allowed all the charges because no evidence supports the conclusion that outside counsel performed inefficiently merely because they worked long hours. In addition, the Legal Division's guidelines did not specifically set a standard regarding the maximum number of hours outside counsel could bill in one day. The OIG accepts the Legal Division's explanation and, accordingly, reduced questioned costs to \$0.

Disallow \$69,580 for fees that did not contain a 20 percent discount agreed to by the firm and RTC (questioned cost) (recommendation 5). The GC's response allowed all the questioned charges. The Legal Division stated that the 20 percent discount identified by the audit was not an across-the-board discount. Rather, at RTC's request, the firm specifically delineated the discounted rates for each attorney in its legal services agreement. The Legal Division determined that the firm billed in accordance with the rates in the legal services agreement. The OIG accepts the Legal Division's explanation and, accordingly, reduced questioned costs to \$0.

Disallow \$5,488 in professional fees resulting from allocation mistakes and the firm's billing of unreasonable costs (questioned cost) (recommendation 6). The GC's response allowed all the questioned costs. The law firm explained that the allocation methodology used was directed and approved by RTC supervising attorneys. The Legal Division stated that the firm's explanation is consistent with the methodology used by RTC at the time. Based on a review of the working papers, the OIG agreed to reduce questioned costs to \$0 because of a lack of sufficient details as to which specific entries were questioned by the joint venture.

Instruct the firm to review its previous allocated billings, perform an adequate review, reduce those charges found to be unreasonable and refund FDIC accordingly (recommendation 7). In light of the GC's decision to allow the questioned costs from recommendation 6, the Legal Division will not take any corrective action for recommendation 7. The OIG accepts the Legal Division's explanation.

Secure assurance from the firm that a revised billing procedure has been implemented ensuring adequate billing supervision and control over allocated entries (recommendation 8). In light of the GC's decision to allow the questioned costs from recommendation 6, the Legal Division will not take any corrective action for recommendation 8. The OIG accepts the Legal Division's explanation.

Disallow \$7,120 for invoices certified by a former RTC attorney that covered services provided when the attorney still worked for RTC (questioned cost) (recommendation 10). The GC's response allowed the questioned charges pending further review by the Outside Counsel Conflicts Committee. On December 21, 1998, the Outside Counsel Conflicts Committee determined that the firm did not violate any requirements warranting sanction. The OIG accepts the Legal Division's explanation and, accordingly, reduced questioned costs to \$0.

Disallow \$35,576 for learning curve costs (questioned cost) (recommendation 12). The GC's response allowed all the charges. The Legal Division reviewed the questioned time entries and concluded that some activities were not learning curve charges but, rather, were factual, investigative activities relating to professional liability cases that were being pursued by the firm on RTC's behalf. In other instances, the questioned time entries were related to needed legal research. The OIG accepts the Legal Division's explanation and, accordingly, reduced questioned costs to \$0.

Disallow \$8,205 for fees written-up on pre-bills (questioned cost, all of which is unsupported) (recommendation 13). The GC's response allowed all the questioned charges. The law firm provided explanations to the Legal Division for the questioned entries. Based on the firm's explanations and the belief that the firm is entitled to compensation notwithstanding missing original time sheets, the Legal Division allowed the charges. Nonetheless, without original time sheets, the OIG could not independently verify the validity of the fees written-up on pre-bills. Therefore, the OIG will continue to question \$8,205.

Determine whether the law firm currently qualifies as a Minority/Women-Owned Law Firm (MWOLF) (recommendation 14). The Legal Division verified that the law firm is a qualified MWOLF firm until March 1999, when its eligibility status must be renewed and re-determined by the Legal Division. The OIG accepts the Legal Division's explanation.

Review the appropriateness of the law firm receiving title insurance premiums while also representing RTC (recommendation 15). The Legal Division concluded that the law firm's dual roles representing RTC on real estate transactions and serving as agent for the title insurance company that issued title insurance policies was appropriate. The Legal Division stated that closing attorneys typically perform such multi-faceted roles. Further, the firm's roles were fully disclosed on Housing and Urban Development forms as required by Federal law. The OIG accepts the Legal Division's explanation.

Disallow \$3,100 for unsubstantiated charges for deposition attendance (questioned cost) (recommendation 16). The GC's response allowed all the questioned charges. The Legal Division did not agree that time billed for depositions exceeded the amount of time actually spent. Specifically, the joint venture compared billed deposition time to the time recorded by the court reporter. However, the court reporter's time did not include time spent by attorneys preparing for depositions, which legitimately can be billed. The OIG accepts the Legal Division's explanation and, accordingly, reduced questioned costs to \$0.

Disallow \$2,154 for fees related to overstaffing (questioned cost) (recommendation 17). The GC's response allowed all the questioned charges. The Legal Division stated that the *RTC Guide for Outside Counsel* did not set forth a minimum of one lawyer per deposition. Further, the Legal Division did not believe a determination of excess staffing could be made based merely on the number of staff used to attend a deposition, unless the excess is glaring which was not the case in the questioned entries. The OIG accepts the Legal Division's explanation and, accordingly, reduced questioned costs to \$0.

Disallow \$7,338 for travel costs billed in excess of 50% of the approved hourly rates (questioned cost) (recommendations 18 and 19). The GC's response allowed all the questioned charges. Based on a review of the working papers, the Legal Division concluded that \$3,683 of the questioned charges involved substantive work. Since travel was combined with substantive work, then the regular (not discounted) hourly rates were applicable. With regard to another \$3,655 in questioned travel costs, the Legal Division determined that the firm billed at properly discounted rates. The OIG accepts the Legal Division's explanation and, accordingly, reduced questioned costs to \$0.

Disallow \$11,660 for costs related to preparing fee bills and status reports (questioned cost) (recommendation 20). The GC's response allowed \$10,924 and disallowed \$736. The law firm provided additional support showing that some entries were not billed to RTC and represented entries used by the firm for administrative recording purposes. In addition, RTC oversight attorneys had authorized compensation for certain case plans and budgets, and some entries reflected substantive work such as preparing bills and budgets for settlement discussions regarding RTC cases. However, the Legal Division disallowed \$736 for time entries that solely reflected overhead charges. The OIG accepts the Legal Division's explanation and, accordingly, reduced questioned costs to \$736.

Disallow \$6,863 for training and educational expenses (questioned cost) (recommendation 21). The GC's response allowed \$6,638 and disallowed \$225. Specifically, the Legal Division allowed \$6,311 for amounts that appeared on the firm's pre-bills but not on its invoices submitted to RTC for payment. Further, the Legal Division did not consider another \$327 in charges to be for unallowable training as defined by the *RTC Guide for Outside Counsel*. The Legal Division disallowed \$225 related to an in-house training session sponsored by the law firm. The OIG accepts the Legal Division's explanation and, accordingly, reduced questioned costs to \$225.

Disallow \$12,056 for overhead and administrative charges (questioned cost) (recommendation 22). The GC's response allowed all the questioned charges. The Legal Division reviewed the audit working papers and additional materials provided by the firm and concluded that, for several reasons, the charges were not overhead or administrative. For example, many of the questioned items contained more extensive explanations than merely "organization" or "file maintenance" and, consequently, were clearly more substantive than just simple overhead or administration. The OIG accepts the Legal Division's explanation and, accordingly, reduced questioned costs to \$0.

Disallow \$436 for costs related to the firm's research of their own conflicts of interest (questioned cost) (recommendation 23). The GC's response allowed \$58 and disallowed \$378. The Legal Division allowed \$58 that the firm demonstrated was not billed to RTC. The OIG accepts the Legal Division's explanation and, accordingly, reduced questioned costs to \$378.

Disallow \$160,357 for unallowable, unapproved, or unsubstantiated expenses (questioned cost, \$152,090 of which is unsupported) (recommendations 24 through 39). The GC's response allowed \$159,309 and disallowed \$1,048. Specifically, the Legal Division disallowed \$102 for unsupported travel charges, \$82 for duplicate charges, \$41 for unauthorized taxi

charges, \$83 for unsupported express mail charges, and \$740 for miscellaneous unsupported expenses. The Legal Division allowed \$35,277 for in-house photocopying charges, \$26,319 for unsupported facsimile charges, \$12,035 for unsupported telephone charges, \$13,731 for title insurance policy charges, \$47,100 for unsupported consultant charges, and \$24,847 for miscellaneous other expenses. Generally, the Legal Division allowed the expenses because RTC and FDIC guidelines did not explicitly prohibit the expenses, the law firm provided additional supporting documentation, or the law firm provided clarifying explanations.

Based on the law firm's and Legal Division's explanations, additional support provided by the firm, and a review of the audit working papers, the OIG agrees with \$124,032 of the \$159,309 in Legal Division allowances. However, the OIG will continue to question the \$35,277 for in-house photocopying charges. Although the Legal Division's decision to allow the charges is not unreasonable given that the Legal Division revised its guidelines to allow firms to charge up to \$.08 per page, the joint venture appropriately questioned the charges using the guidelines in effect at that time which required a cost study. Therefore, with regard to recommendations 24 through 39, the OIG will question \$36,325 (\$1,048 + \$35,277), of which \$36,202 is unsupported.

As a result of the joint venture's audit work, \$688,732 was questioned in the draft report transmitted to management. In addition to the recommendations previously discussed, in recommendations 1 and 11, the OIG recommended that FDIC disallow or ratify \$312,728 for work performed by unauthorized personnel. Based on a review of the firm's legal services agreements, case plans, and budgets, the Legal Division ratified or approved all the questioned charges. The OIG accepts the action taken by management and, accordingly, reduced questioned costs to \$0.

After considering \$8,112 in disallowances taken by management and management's comments on the joint venture's findings, we will report questioned costs of \$61,110 (including \$44,407 in unsupported costs) in our *Semiannual Report to the Congress*.

AUDIT OF LEGAL FEES AND SERVICES
PROVIDED TO THE RESOLUTION TRUST CORPORATION BY
SALEM, SAXON & NIELSEN, P.A.

JANUARY 1, 1991 TO DECEMBER 31, 1994

FINANCIAL MANAGEMENT ASSOCIATES
C.W. Amos & Company, LLC
2 North Charles Street - Suite 210
Baltimore, Maryland 21201

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I. BACKGROUND

A. INTRODUCTION

The Resolution Trust Corporation (RTC) was authorized by the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA), Public Law 101-73, to contract with law firms for legal services to assist in the fulfillment of its statutory mandate. Initially the Federal Deposit Insurance Corporation (FDIC) managed the legal services provided by outside counsel. On September 10, 1991, a separate RTC Legal Division was created. The law firm of Salem, Saxon & Nielsen, P.A. (SS&N) was engaged as outside legal counsel on behalf of RTC. On February 20, 1991, SS&N and FDIC, on behalf of RTC, entered into a 2-year legal services agreement (LSA). On February 18, 1993, a successor LSA was entered into directly with RTC. Before February 20, 1991, work was performed under various informal agreements with institutions under RTC receivership.

The LSA identified the SS&N professionals and corresponding billing rates for attorneys and paralegals authorized for RTC engagements. The general responsibilities of SS&N pertaining to ethics, reporting requirements, billing information, professional services, non-reimbursable charges, conflicts of interest, and other items are set forth in the *FDIC Guide for Legal Representation (1989)*, *RTC Guide for Outside Counsel (1992)*, predecessor Guides, and the LSA. The specific detailed billing procedures and requirements are set forth in the *FDIC Outside Counsel Fee Bill Payment Program Instruction Manual* and *RLIS Forms and Procedures Deskbook for Outside Counsel*. In addition, the firm received periodic instructions from RTC related to billing procedures and other administrative requirements. The firm also entered into separate agreements with RTC to perform services on certain legal matters at reduced hourly rates and to absorb other costs related to the performance of such matters.

The RTC Office of Inspector General (OIG) engaged Financial Management Associates (FMA) to perform an audit of legal services provided by SS&N on RTC matters for the period of January 1, 1991, through December 31, 1994, in accordance with *Government Auditing Standards*. The audit was conducted from the date of the entrance conference, February 9, 1995, to May 31, 1995, and included concentrated field work at the firm's Tampa, Florida office from March 20, 1995, to April 21, 1995. On July 25, 1995, the firm's representatives provided comments to the auditor's findings in an exit conference.

B. SUMMARY

The objective of the audit was to determine whether the legal services performed and charges billed to RTC were fair and reasonable, adequately supported by documentation, and within the terms of applicable agreements, guidelines and regulations. Issues identified included:

- Use of employees either not listed on any LSA, or subsequently approved by RTC.
- Billings at hourly rates that exceeded amounts authorized in LSAs and agreements.
- Billing practice of allocating time for the same task over multiple bills that resulted in billing mistakes and overbillings. In addition, this billing practice did not permit adequate billing supervision or review.
- Inappropriate billings of learning curve costs and research.
- Inappropriate billings of travel time.
- Billings for unsubstantiated expenses.

We also examined the firm's policy, procedures and internal controls for detecting and disclosing conflicts of interest, and compliance with applicable RTC statutory and contractual requirements. We found that SS&N had an adequate system for monitoring and generally resolving representational conflicts of interest. The firm complied with the condition of a conflicts waiver granted by RTC in November, 1993.

II. ACRONYMS

ABA	American Bar Association
APP	Accelerated Payment Program
CFR	Code of Federal Regulation
FIRREA	Financial Institutions Reform, Recovery and Enforcement Act of 1989
FMA	Financial Management Associates
LSA	Legal Services Agreement
MWOLF	Minority/Women Owned Law Firm
OCC	Outside Conflicts Committee
OIG	Office of Inspector General
PLC	Professional Liability Claims
PLS	RTC Professional Liability Section
RLIS	RTC Legal Information System
RTC	Resolution Trust Corporation
SECO	RTC Southeast Consolidated Office
SS&N	Salem, Saxon & Nielsen, P.A.

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III. OBJECTIVES, CONCLUSIONS, SCOPE AND METHODOLOGY

A. Objectives and Conclusions

The objectives of the audit were to determine:

1. **Whether the firm maintained an adequate system of accounting records and internal controls for providing legal services to RTC.**

CONCLUSION: Based on the audit procedures performed, the accounting records adequately supported and contained information related to the billings to and collections from RTC.

2. **Whether the firm billed professional fees and expenses based on reasonable services and incurred reimbursable expenses reasonably with adequate supporting documentation and in accordance with the FDIC Guide for Legal Representation, RTC Guide for Outside Counsel, FDIC Outside Counsel Fee Bill Payment Program Instruction Manual, RLIS Forms and Procedures Deskbook for Outside Counsel, LSAs, RTC policies and procedures and applicable laws and regulations.**

CONCLUSION: Based on our audit testing, we found the following compliance failures:

Billing Practices - General

	Page
The firm:	
• Billed for professionals not authorized by LSA at the time hours were incurred	14
• Billed fees in excess of LSA approved rates	16
• Billed hours in excess of time reported on source documents	17
• Billed for time incurred in excess of 15 hours in a day by individual professionals	18
• Allocation of time between files resulted in billing mistakes and overcharges	21
• Made fee adjustments without adequate supporting documentation	29
• Billed for unsubstantiated expenses	40

Non-Compliance with Legal Services Agreements and Other RTC Agreements

	Page
The firm:	
• Did not provide a 20 percent discount on professional fees	19
• Did not comply with the legal budget process	20
• Billed for professionals at hourly rates that exceeded the Pioneer agreement	24
• Billed for professionals not authorized by the Pioneer agreement	27

3. **Whether the firm performed the legal services to RTC as described on invoices and did so competently, professionally, timely and commensurate with the duties to be performed, and in accordance with all guidelines, agreements and regulations.**

CONCLUSION: FMA's Legal Group selected 21 matters for substantive examination totaling \$2,106,531 in fees, or 54 percent of RTC billings during the audit period. Generally, the matters examined were performed competently, professionally and timely. However, within these files, we detected evidence of the following:

Substantive Review	Page
• Inaccurate timekeeping for attendance at depositions	34
• Inappropriate staffing used	35
• Inappropriate billings related to travel time	35
• Inappropriate billings for status reports and fee bill preparation	37
• Inappropriate billings for training and education	38
• Inappropriate billings for overhead expenses	38
• Inappropriate billings related to the firm's research of their own conflicts	39

4. **Whether the firm maintained an adequate system for identifying and resolving conflicts or potential conflicts of interest to ensure compliance with applicable professional rules and guidelines, including the requirements of 12 CFR §1606.**

CONCLUSION: We determined that SS&N maintained an adequate system for monitoring and resolving representational conflicts of interest. The firm complied with a conditional conflicts waiver, dated November 23, 1993. Prior to the start of fieldwork in March 1995, FMA and the firm discussed arrangements for examining non-RTC clients to detect conflicts compliance. In February 1996, FMA examined the firm's client list and attorney time records for the audit period and concluded there were no representational conflicts.

The records assembled and reviewed, while incomplete in certain areas, were sufficient for us to express our findings and recommendations in this report.

This report is intended for the Office of Inspector General and Federal Deposit Insurance Corporation management. However, this report is a matter of public record and its distribution is not limited.

(b)(6)

Baltimore, Maryland
July 25, 1995



Financial Management Associates
a Maryland Joint Venture

B. Scope and Methodology

To address the audit objectives, we conducted the following tests:

- Reconciled RTC information related to invoices and payments to SS&N Ledger History Report (LHR).
- Selected and tested a judgmental sample of invoices (as shown in Table 1) basing our selections on matters representing the largest amounts billed to RTC and other smaller matters. Our tests included, but were not limited to, matters representing the actual rates billed to RTC compared to LSA rates and related expense reimbursements.
- Selected and reviewed a judgmental sample of matters for substantive legal review as discussed in more detail on page 32.

Our legal fee audit was conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. The audit tested the accuracy of fees and expenses accounted for on invoices and the management of legal matters identified on the invoices for the audit period January 1, 1991, through December 31, 1994.

The total invoice population represented by the firm during the audit period was \$4,223,285. Our audit program yielded testing of \$2,106,531 of the fees billed, representing 54 percent, and \$194,271 of the expenses billed, representing 56 percent. In total, we substantively tested \$2,300,802 or 54 percent of total RTC billings.

Table 1: RTC Invoice Population

Description	# of Invoices	Fees	Expenses
SS&N Detailed Time & Expense Data	2,331	\$3,875,910	\$347,375

Source: Balances from Ledger History Reports provided to FMA by SS&N on electronic media.

We developed data bases of time, expense and billing records provided in computer form by SS&N, as well as computer data received from RTC. The following data bases were developed during the course of the examination:

- (1) SS&N "Ledger History Report" Internal Accounting Information as Provided on Electronic Media ("Data Base I");
- (2) RTC Payment Records ("Data Base II"); and
- (3) SS&N Time and Billing Records ("Data Base III").

We used the data bases to generate detailed and summary profiles of billing activity for all attorneys and for fee and expense categories. Additionally, we determined whether professional fees were charged as required and that all professional personnel were approved on the applicable LSA or amendments thereto.

We also used the data bases to identify matters for which the firm incurred significant time charges which aided our judgmental selection of matters that we examined on a substantive legal work product basis. The scope included the examination of a judgmental sample of legal case matters undertaken by the firm for RTC, including an evaluation of the overall efficiency of case management and a determination of the appropriateness of legal fee charges. These files included routine and complex litigation and transactional matters.

Case Management Examination - Scope and Methodology

An in-depth analysis was conducted by FMA's legal group of the legal services and work products related to 21 matters performed by SS&N selected from reports generated by Data Base I. The 21 matters included billings totaling \$2,106,531 in fees (see substantive legal review on page 32.)

We analyzed these matters to determine whether the billed fees and expenses were commensurate with the services rendered and in compliance with RTC agreements, guidelines and professional codes of responsibility. The analysis followed a computer analysis of billing activity to establish a profile of the firm's billing policies and practices. We also reviewed correspondence, research materials, pleadings, transcripts, and other documents in each case file.

We conducted interviews with supervising attorneys, other attorneys and paraprofessionals. A primary objective of the case matter review was to evaluate the overall efficiency of case management and the firm's compliance with the *RTC Guide for Outside Counsel*, *FDIC Guide for Legal Representation*, *RLIS Forms and Procedures Deskbook for Outside Counsel*, *Legal Services Agreements*, *RTC policies and procedures* and *12 CFR §1606*.

We also evaluated the firm's compliance with professional codes of conduct, including the *ABA Code and Rules*.

Summary of Audit Procedures

Among numerous audit procedures and testing, we performed the following procedures to audit SS&N billings to and collections from RTC for professional fees and reimbursable expenses:

- Compared the list of professional staff authorized in the LSA to those on the invoices.
- Compared the professional staff's authorized billing rates with actual billing rates.

- Verified the accuracy of fees charged by comparing hours billed with original source documents (time sheets) when provided.
- Reviewed the billing histories for multiple payments by RTC.
- Verified that hours charged by SS&N attorneys were reasonable and not excessive, including instances in which attorneys billed a total of more than 15 hours per day on RTC matters.
- Determined if SS&N billed RTC for researching its own conflicts of interest, preparing legal bills or budgets, or more than 50 percent of the hourly rate for attorney travel.
- Verified that reimbursable expense charges were related to the applicable RTC matter.
- Identified the elements comprising reimbursable expense charges and determined whether the charges complied with LSA and RTC guidelines.
- Determined if reimbursable expense charges were adequately supported.
- Determined if reimbursable expense charges were billed to RTC at cost.
- Determined if SS&N received approval from an RTC supervising attorney for reimbursable expense charges, where applicable.
- Reviewed reimbursable expense charges to determine if the use and cost appeared reasonable and were not excessive.
- Documented the methods used to retain any third-party services, where applicable.

FMA attorneys performed the following procedures on 21 case files:

- Analyzed legal bills to identify attorneys initially assigned to RTC matters and documented any changes in assignments to ensure RTC was not charged excessively for new attorneys to review files, motions, pleadings, or any other activity to familiarize themselves with the case.
- Reviewed legal bills to determine if attorneys were spending substantial time reading background information, reviewing research and case law, or reviewing files.
- Determined if services billed by attorneys and paralegals were commensurate with the duties typically associated with professionals with comparable expertise.
- Reviewed written products prepared by SS&N attorneys and paralegals to determine whether the time charges incurred on specific issues were commensurate with the scope and complexity of those issues.

- Evaluated the qualifications of paralegals assigned to RTC cases to ensure paralegals were not performing clerical or secretarial tasks.
- Evaluated the degree of diligence by billing attorneys to avoid errors, overbillings and compliance with the applicable LSA.
- Reviewed the applicability of the LSA schedule of fixed fees or other fee arrangements to selected files.
- Evaluated whether professional fees were advanced for services that subsequently were not performed.

Scope Limitation

The firm did not maintain required time records in a manner that would allow us to evaluate the reasonableness of \$228,335 in legal fees billed to RTC. Specifically, the law firm combined numerous activities by individual attorneys into single time entries rather than recording the time spent on each activity. The firm's practice of block billing prevented FMA from applying auditing procedures to satisfy ourselves as to the reasonableness of these fees billed to RTC by the firm. The scope of our work was not sufficient to enable us to express, and we do not express, an opinion on these fees. The RTC Legal Division ruled that its policy and procedures in effect at the time period covered by this audit did not prohibit this practice.

Cross-Reference Section Page		Description	Questioned Costs	Unsupported Costs (A)	Questioned Costs, Net (B)	Unsupported Costs, Net (A) (B)
<i>Billing Practices</i>						
Billed for Professional Not Authorized by LSA at the Time Hours Were Incurred:						
V	A 14	-Not Authorized on Any LSA	552,188		551,964	
V	A 14	-Subsequently Approved on LSA	243,715		240,749	
V	A 16	Billed Fees in Excess of LSA Approved Rates	7,869		7,855	
Billed Hours in Excess of Time Reported on Source Documents:						
V	A 17	-General	14,555		14,352	
V	D 29	-Unsupported Fee Adjustments	8,205	8,205	8,205	8,205
VI	E 34	-Used Inaccurate Timekeeping for Attendance at Depositions	3,710		3,100	
Other instances of Non-Compliant Billing Practices:						
V	A 18	-Billed For Time Incurred by Individual Professionals in Excess of 18 Hours in a Day	1,823		1,823	
VI	E 35	-Inappropriate Billings Related to Travel Time	8,152		7,338	
VI	B 37	-Inappropriate Billings for Status Reports and Fee Bill Preparation	11,732		11,080	
VI	F 38	-Inappropriate Billings for Training & Education	6,863		6,863	
VI	B 38	-Inappropriate Billings for Overhead Expenses	12,056		12,056	
VI	B 39	-Inappropriate Billings Related to the Firm's Research of Their Own Conflicts	436		436	
VII	E 40	-Unsubstantiated Expenses Billed	160,357	152,080	160,357	152,080
V	C 21	Allocation of Time Between Files Resulted in Billing Mistakes and Overcharges	5,488		5,488	
V	B 19	Did Not Provide a 20 Percent Discount from their Standard Rate to RTC	69,560 (C)		69,560 (C)	
<i>Pioneer Matter</i>						
V	D 26	Employee (Former RTC Attorney) Certified Firm Billings to the RTC for Work Performed When the Employee was SBA Employee by RTC	10,018		7,120	
V	D 27	Professionals Billed but Not Authorized by the Pioneer Agreement	25,636		20,018	
V	D 25	Professionals Billed at Hourly Rates that Exceeded the Pioneer Agreement	24,376		22,041	
V	D 28	Unallowable Learning Curve Fees for Pioneer Work	38,131		35,576	
<i>Other</i>						
VI	B 25	Inappropriate Staffing Used	2,154		2,154	
TOTAL			5705,084	5180,295	5688,732	5180,295

(A) Unsupported costs are defined as those costs for which the firm did not provide adequate information for a sufficient comparison to be reached. Provision of such information on the firm may or may not affect whether the costs are ultimately allowed or disallowed.

(B) A firm's overhead expenses are not questioned costs nor are costs concerning other litigants.

(C) Questioned cost is not reflected net of other litigants because the litigant's work is services rendered to the firm.

V. GENERAL FINDINGS AND RECOMMENDATIONS

A. Non-Compliant Billing Practices - General

Our audit testing of the professional fees billed to RTC indicated that SS&N charged \$318,347 for services that did not conform with the terms of the LSA and RTC guidelines. These charges do not include the billings related to the Pioneer Savings & Loan matter that are considered on pages 23 - 30.

Table 2: Summary of Professional Service Fees Questioned Due to Non-Compliant Billing Practices

Activity Questioned	Fees Questioned
Billed for Professionals Not Authorized by LSA at the Time Hours Were Incurred	\$295,903
Fees Billed in Excess of LSA Approved Rates	7,889
Billed for Hours in Excess of Time Reported on Source Documents	14,555
Total	\$318,347

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

1. SS&N Billed for Professionals Not Authorized by LSA at the Time Hours Were Incurred

Our examination determined that SS&N billed RTC \$295,903 in professional service fees for employees not approved under the LSA rate schedule. The LSA provides for the addition of personnel by written mutual agreement of the firm and FDIC. The *RTC Guide for Outside Counsel*, February 1992, page 10 stated, "... the firm also must provide a matrix that identifies all attorneys and paralegals the firm offers to provide service to the Corporation, and which sets forth, for each attorney and paralegal, the following: (1) state licenses; (2) particular area(s) of expertise; (3) years in practice; (4) time with the firm; (5) status within the firm as partner or shareholder, senior associates, associate or paralegals; (6) billable rates in accordance with the firm's usual rate structure;..." The fees questioned relate to timekeepers not listed on the respective LSA or subsequently approved by the RTC.

We questioned billings of \$52,188 (\$51,964, net of adjustments for other findings) for the work of SS&N employees not listed on any LSA and \$243,715 (\$240,749, net of adjustments for other findings) for the work of employees unlisted at the time services were rendered, but who were subsequently approved on an LSA or amendment.

During fieldwork, FMA provided the firm its analysis of the LSA and amendments as they related to approved personnel and rates. We requested that the firm provide us comments regarding our analysis. We incorporated the firm's comments into our analysis.

Table 3: Reconciliation of Questioned Cost

Activity Questioned	Fees Questioned
Not Authorized on Any LSA	\$52,188
Less Duplicative Costs Questioned:	
Inappropriate Billings for Status Reports and Fee Bill Preparation	(104)
Billed Hours in Excess of Time Reported on Source Document - General	(120)
Total Duplicative Costs Questioned	(224)
Total	\$51,964

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

Table 4: Reconciliation of Questioned Cost

Activity Questioned	Fees Questioned
Subsequently Approved on LSA	\$243,715
Less Duplicative Costs Questioned:	
Inappropriate Billings for Status Reports and Fee Bill Preparation	(1,186)
Inappropriate Billings Related to Travel Time	(530)
Billed Hours in Excess of Time Reported on Source Document - General	(224)
Allocation of Time Between Files Resulted in Billing Mistakes and Overcharges	(59)
Billed Hours in Excess of Source Documents	(929)
Billed for Professional Fees in Excess of 15 Hours in a Day	(38)
Total Duplicative Costs Questioned	(2,966)
Total	\$240,749

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

Recommendation

- (1) We recommend that FDIC require responsible personnel to (i) analyze the qualifications for employees working on RTC matters, but not listed on the LSA, (ii) determine how much of the \$292,713 (\$51,964 + \$240,749) in net questioned cost for these charges should be retroactively ratified, and (iii) disallow any of these charges not approved.

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

2. SS&N Billed Fees in Excess of LSA Approved Rates

Our examination determined that SS&N billed RTC at hourly rates greater than those authorized in the LSA, resulting in overbillings to RTC of \$7,889 (\$7,855 net of adjustments for other findings).¹

The *RTC Guide for Outside Counsel* stated that absent compelling reasons, no increase in the fee or rate schedule attached to the LSA is permitted during the effective term of the LSA. Furthermore, the LSA states, "...[t]he hourly rates for each attorney and paralegals in the firm who is to work on FDIC [RTC] matters is set forth on the Rate Structure, attached hereto and incorporated herein..."

Table 5: Reconciliation of Questioned Cost

Activity Questioned	Fees Questioned
Billed Fees in Excess of LSA Approved Rates	\$7,889
Less Duplicative Costs Questioned:	
Inappropriate Billings Related to Travel Time	(34)
Total Duplicative Costs Questioned	(34)
Total	\$7,855

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

Recommendation

- (2) We recommend that FDIC disallow \$7,855 in overbillings due to unauthorized rates charged by the firm (questioned cost).

¹ The number represents the difference between the approved billing rate and the actual billing rate multiplied by the number of hours billed at the excessive rate.

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

3. **SS&N Billed Hours in Excess of Time Reported on Source Documents**

FMA identified 49.63 hours billed on invoices to RTC that exceeded entries on timekeeper diary reports and pre-bills totaling \$4,836 for time that was either (1) "written-up" from timekeeper diary reports to invoices; (2) not reported on timekeeper diary reports, but billed on invoices; or (3) "written-up" from the pre-bill to the invoice. In addition, we identified 129 other time entries totaling 86.80 hours and \$9,719 in fees on invoices which could not be agreed to the corresponding time sheet. Our ability to increase the sample size for this procedure was limited by the absence of numerous attorney timekeeper diaries and time slips.

As a result of this analysis we also identified an invoice containing dates that were changed on the pre-bill, accompanied by the notation, "When changing entries to 12/30 please be sure that [an attorney] doesn't end up with too many hours in a day." This attorney billed 2.5 hours for \$250 to the RTC on the date indicated by the notation.

The LSA provided that "the firm shall keep all of its billing records for at least three (3) years from billing date."

The *RTC Guide for Outside Counsel*, February-1992, page 31, stated "...Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payment"

The *FDIC Outside Guide for Counsel*, 1991, page 33, stated, "...Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets...for four years after payment ..."

Further, it is a generally accepted internal control procedure to document adjustments affecting an original time entry.

Table 6: Reconciliation of Questioned Cost

Activity Questioned	Fees Questioned
Hours Billed in Excess of Time Reported on Source Documents	\$14,555
Less Duplicative Costs Questioned:	
Billed for Professional Fees in Excess of 15 Hours a Day	(63)
Inappropriate Staffing Used	(140)
Total Duplicative Costs Questioned	(203)
Total	\$14,352

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

Recommendation

- (3) We recommend that FDIC disallow \$14,352 in payments for fees written-up from original time records (questioned cost).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

4. SS&N Billed for Time Incurred by Individual Professionals in Excess of 15 Hours in a Day

We found seven instances of individuals billing more than 15 hours a day on RTC matters. These individuals billed \$37,791 of which \$1,823 represented billings for hours in excess of 15 in a day. We question the amount billed in excess of 15 hours in those instances.

The RTC *RLIS Forms and Procedures Deskbook for Outside Counsel*, dated June 1993, page 4-5, stated, "... the amount charged should be time efficient and reasonable in all respects."

The *RTC Guide for Outside Counsel*, dated February 1992, pages 19 and 20, stated, "The Legal Division also expects Outside Counsel to control time carefully and to avoid both unnecessary review of documents and files and over-polishing of documents."

The RTC *RLIS Forms and Procedures Deskbook for Outside Counsel*, dated June 1993, page 4-5 and 4-6, stated, "There are certain billing practices that are subject to CLOSE SCRUTINY by the RTC. Examples of such practices include a substantial time expended in review and revision of documents prepared by the firm, numerous intra-office conferences between attorneys and paralegals for the purpose of providing instruction or status, multiple attorneys performing services in each matter..."

Recommendation

- (4) We recommend that FDIC disallow \$1,823 for time billed in excess of 15 hours in a day (questioned cost).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

B. Findings of Non-Compliance With the LSA

FMA found several examples of non-compliance with provisions of the LSA, including:

1. SS&N Did Not Provide a 20 Percent Discount From Their Standard Rate to RTC

In 1990, the firm submitted a revised proposal to RTC and offered a 20 percent discount off its standard "in-office" hourly rates applied to all clients. On January 17, 1991, RTC's Eastern Regional office recommended granting an LSA to the firm, noting the firm's revised agreement to provide "a 20 percent discount from its standard rates" for a 2-year period, and a 50 percent discount from "standard rates on travel time." The LSA effective February 1, 1991, provided that "travel time is compensated at 50 percent of the firm's regular billing rates...". However, Exhibit C of the LSA contained no reference to the 20 percent discount and listed the authorized billers at the same "in-office" rates submitted in the firm's 1990 proposal.

We also noted that as a condition of the LSA, the firm was required to offer rates lower than those provided non-RTC clients. We noted, however, an attorney was billed at \$100 per hour to non-RTC clients, which was substantially below the rate charged to RTC.

Our test of invoices from February 20, 1991, until execution of the second LSA on February 18, 1993, indicated, (a) the great majority of fees billed were at full "in-office" rates used by the firm for non-RTC clients; (b) the 20 percent discount was not applied; and (c) occasional discounts ranging between 5 percent - 10 percent of the "in-office" rates of several timekeepers. Fees in excess of the agreed rates totaled \$69,580.

The circumstances are distinguished from findings made in which the firm billed at rates in excess of those prescribed in the LSA (see page 16).

Recommendation

- (5) We recommend that FDIC disallow \$69,580 in payments for fees that do not contain the 20 percent discount agreed to by the firm and accepted by the RTC (questioned cost).

Firm Response: SS&N could not provide any information in justifying the firm's avoidance of its commitment to give RTC a 20 percent discount off in-house billing rates. At the exit conference, the firm requested the details comprising this finding.

FMA Response: One explanation of the increase rates could be that RTC simply decided not to require the discount. However, if the firm took advantage of an RTC administrative oversight, we believe it had an ethical responsibility to advise the client of its prior commitment. FMA provided the details as requested but has not received any further communication.

2. SS&N Did Not Comply With the Legal Budget Process

A budget is an important control element RTC used to monitor costs associated with legal matters. The *RTC Guide for Outside Counsel*, February 1992, page 30 stated, "estimates are used on an ongoing basis to measure the progress of a matter and to determine its cost-effectiveness. Budgets are prepared in conjunction with the client and reflect the firm's best judgment of the costs of anticipated legal services." In reviewing SS&N invoices and pre-bills, we noted numerous instances of billable hours transferred from one budget matter to another. The pattern was evident in numerous related matters handled by the firm.

Our review disclosed that occasionally, whenever charges against a particular budget approached or exceeded the estimated maximum amount, the firm transferred the charges to a corresponding budget with sufficient funding. The firm was required to report promptly to RTC instances of depleted budgets. The *RTC Guide for Outside Counsel*, February 1992, page 30 stated, "estimates are used in the development of business decisions therefore they must be as accurate and current as possible, and any changes must be reported promptly."

We could not estimate the dollar impact of these budget transfers. Based on our case reviews, the use of multiple budgets inflated the estimated costs and therefore, indirectly, did not permit the RTC to properly monitor or control excessive costs. On June 19, 1992, the firm submitted a budget to RTC of \$386,000 for the preliminary investigation phase of the Pioneer matters. This budget was increased to \$406,000 by amendment dated June 26, 1992. Prior counsel's budget for this work was \$48,000.

In response to FMA's request, the firm explained that as budgets were exhausted, RTC directed the firm to redirect work under other budgets rather than amending budgets. The firm did not respond to FMA's request to provide evidence of these RTC directives.

Firm Response: The firm advised FMA that RTC instructions on budget matters were generally provided orally.

C. Allocation of Time Between Files Resulted in Billing Mistakes and Overcharges

Throughout the audit period, FMA detected instances where the firm did not identify on invoices time entries allocated between or among numerous bills. In addition, in other instances where allocations were noted, the total time billed was unreasonable for the services described.

Our analysis indicated that 21,661 entries, totaling \$856,780, were allocated among files. This represents 29 percent and 22 percent, respectively, of the total entries and fees in the audit period. The allocations were made among an average of 3.6 files. This practice resulted in mistakes and overcharges to RTC as the practice did not permit either RTC, or the firm's billing attorneys a basis to evaluate the reasonableness of the time or cost to perform the professional services. The firm advised us that daily timesheets were not reviewed internally for accuracy.

As described above, during the course of our substantive review, we found examples of mistakes, overcharges and unreasonable time allocation resulting from the firm's practice of allocating time among multiple bills. FMA selected 21 billing allocations to determine the reasons for the resultant overcharge. We reviewed work product and related time sheets to evaluate support for time entries. As a result of our testing, we questioned \$5,488 related to this sample of data entry mistakes and unreasonable time allocations. For example, in one instance we noted that an attorney billed 25.2 hours during one day. The biller allocated 3 entries to six RTC matters. Based on the review of supporting documentation (memo, invoices, daily timesheets, letters, etc.) related to this instance, FMA determined 6.2 hours to be a reasonable time to complete the task performed. An analysis of the time sheet indicated that the biller wanted to bill 6.2 hours, however, the data entry created billings for 25.2 hours for the day. The remaining 19 hours of billed time was, therefore, excessive and unreasonable. This mistake and overcharge is a good example of the firm's practice of allocating time over multiple cases and the inherent difficulty in determining the reasonableness and accuracy of time billed.

We noted the firm's effort since August 1993 to identify certain allocated entries on invoices by including in the description "apportioned among files" or "pro rated between cases" and, at times, citing the number of affected files. However, this improved billing practice was not applied consistently by many of the timekeepers. In some cases, the timekeepers identified only a portion of the allocated entries. In March 1994, an RTC supervising attorney rejected both the form of allocated entries on six of the firm's invoices and the substance of certain charges found to be unreasonable. The firm was instructed to consolidate all six into one invoice. After reviewing total time spent on individual tasks, the firm reduced the charges accordingly resulting in a write-off of this time.

We believe that the firm has an obligation to review all of its billings throughout the audit period and to determine the extent of overbillings to the RTC. The Florida Supreme Court in The Florida Bar v. John P. Kirtz (445 S0. 2nd 576 Fla 1984) affirmed a Referee's finding that the attorney charged an excessive fee in violation of Florida Bar Code of Professional Responsibility, Disciplinary Rule 2-106(A). In response to the attorney's claim that the overcharge was due to a bookkeeping error, the Referee stated, in part,

"Even though it may be concluded that the overcharge was not intentional, yet the obligation of the lawyer is to keep his books of account in such order as not to make a careless mistake to the detriment of his client"

Recommendations

We recommend that FDIC:

- (6) Disallow \$5,488 in professional fees resulting from allocation mistakes and the firm's billing unreasonable fees (questioned cost).
- (7) Instruct the firm to review its previous allocated billings, perform an adequate review, reduce those charges found to be unreasonable and refund FDIC accordingly.
- (8) Secure assurance from the firm that a revised billing procedure has been implemented ensuring adequate billing supervision and control over allocated entries.

Firm Response: *At the exit conference, the firm requested the details comprising this finding.*

FMA Response: *FMA provided the details as requested but has not received any further communication.*

D. Non-Compliant Billing Practices: Services Related to Pioneer Savings & Loan

Pursuant to an agreement with RTC and another firm (Co-Counsel), from April 1992, to June 1993, SS&N and the firm's Co-Counsel generated fees and expenses of \$350,897 representing RTC in a professional liability matter for Pioneer Savings & Loan ("Pioneer"). The agreement stated that SS&N's participation was subject to certain conditions contained in its proposal and adopted by RTC, including reduced hourly rates, limitations on travel expenses, and the agreement of the firm to absorb "learning curve" costs.

An RTC "Memorandum for Authorization to Retain Substitute Outside Counsel," dated April 7, 1992, discussed the basis for recommending SS&N as part of the Co-Counsel venture:

"They have represented to this office that they are willing to absorb the costs involved in the learning curve in order to become familiar with handling professional liability claims. They have also agreed to reduce their current hourly rates on their LSA..."

This recommendation was approved by the Assistant General Counsel, PLS, and the Joint Venture was retained to handle the Pioneer PLS investigation.

We found several problems related to SS&N's billing practices related to Pioneer, which resulted in additional legal costs of \$104,366 to RTC, as summarized in the following table:

Table 7: Summary of Findings Related to the Pioneer Matter

Item	Questioned Fees
Professionals Billed at Hourly Rates that Exceeded the Pioneer Agreement	\$24,376
SS&N Employee (Former RTC Attorney) Certified Firm Billings to the RTC for Work Performed When the Employee Was Employed by RTC	10,018
Professionals Billed but Not Authorized by the Pioneer Agreement	25,636
Unallowable Learning Curve Fees for Pioneer Work	36,131
Inappropriate Fee Adjustments Without any Supporting Documentation	8,205
Total	\$104,366

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

1. SS&N Modified Pioneer Billing Arrangement Without RTC Approval

SS&N's second LSA with RTC, effective February 18, 1993, included significantly higher rates for all attorneys and para-professionals working on Pioneer matters than those approved in the separate Pioneer Agreement. We interpreted the terms of the firm's Pioneer fee arrangement with RTC as applicable from April 1992, through the duration of the engagement. However, one month after the higher rates were approved in the new LSA, the firm submitted an amended budget for Pioneer and included the revised rates as shown on the new LSA. We found no evidence that RTC approved the rate increases for Pioneer. In addition, the rate increases were applied retroactively to the effective date of the new LSA. Nonetheless, SS&N billed RTC fees for services related to Pioneer at the new LSA rates, which exceeded the agreed upon hourly rates in the Pioneer agreement.

We believe the firm had an obligation to clarify any such billing modifications in accordance with the fiduciary standards of the attorney/client relationship. The Florida Supreme Court endorsed this principle in Halstead vs. Florence Citrus Growers Association, stating that modifications to a fee agreement between client and attorney... "While not presumptively void, the burden of showing fairness where the question is raised rests upon the attorney."

2. SS&N Professionals Billed at Hourly Rates that Exceeded the Pioneer Agreement

The firm billed RTC \$24,376 of fees for Pioneer matters that exceeded the hourly rates for attorneys included in the Pioneer agreement. Therefore, we questioned \$24,376 related to these billings. For example, on June 26, 1992, RTC approved the addition of an attorney (as an associate at SS&N) to the LSA matrix at a billing rate of \$135/hour. The agreement for billing on Pioneer matters included specific ranges of hourly fees for SS&N professionals. Three categories were established:

	<u>Rate Per Hour</u>
Partner	\$125-150
Associate	\$ 75 -125
Paralegal	\$55

Under the firm's arrangement with RTC on Pioneer, the authorized "associate" rate was \$125/hour. However, we found that the attorney was billed immediately and consistently at \$150/hour on all Pioneer matters.

Table 8: Reconciliation of Questioned Cost

Activity Questioned	Fees Questioned
Professionals Billed at Hourly Rates That Exceeded the Pioneer Agreement	\$24,376
Less Duplicative Costs Questioned:	
Unallowable Learning Curve Fees for Pioneer Work	(2,135)
Allocation of Time Between Files Resulted in Billing Mistakes and Overcharges	(200)
Total Duplicative Costs Questioned	(2,335)
Total	\$22,041

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

Recommendation

- (9) We recommend that FDIC disallow \$22,041 in fees in excess of Pioneer agreement rates (questioned cost).

Firm Response: The firm took the position that changes to the original billing arrangements for Pioneer rates and authorized personnel were orally consented to by the RTC. The firm also provided FMA with an amended Pioneer budget, dated June 26, 1992, that lists the attorney at \$150/hour.

FMA Response: At a minimum, the Assistant General Counsel, PLS, who approved the terms of the engagement should have consented to hourly rate increases. The firm could not substantiate that such increase was either justified, or appropriate in light of the fact that the more experienced Co-Counsel's billing rate remained at \$150/hour for the entire Pioneer engagement.

Concerning the amended Pioneer budget, we found no evidence that this single line entry in an extensive budget/case plan constituted either recognition, or approval of a higher hourly rate by RTC. In addition, no reference was made in the budget/case plan as to whether the attorney was being hired as a partner or associate. We questioned the difference between the approved associate rate of \$125/hour for this attorney's work on Pioneer and the \$150 per hour rate charged by the firm.

3. **SS&N Employee (Former RTC Attorney) Certified Firm Billings to the RTC for Work Performed When the Employee was Employed by RTC**

Table 9: Reconciliation of Questioned Cost

Activity Questioned	Fees Questioned
SS&N Employee (Former RTC Attorney) Certified Firm Billings to the RTC for Work Performed When the Employee Was Employed by RTC	\$10,018
Less Duplicative Costs Questioned:	
Inappropriate Billings for Training and Education	(2,665)
Unallowable Learning Curve Fees for Pioneer Work	(233)
Total Duplicative Costs Questioned	(2,898)
Total	\$7,120

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

Although the firm commenced work on Pioneer in April 1992, the first invoices were submitted in July 1992, under the certification of the former RTC Attorney. All of these billings were for services incurred when the former RTC Attorney was employed by RTC. In fact, some of the billings were for periods when the former RTC Attorney was supervising the firm's work on Pioneer matters. We questioned \$10,018 (\$7,120, net of adjustments for other findings) related to these billings.

Recommendation

- (10) We recommend that FDIC disallow \$7,120 of billings related to work performed in April, May and June of 1992, until such time as new billing certifications are executed and submitted to the FDIC and the FDIC has an opportunity to evaluate the appropriateness of the billings (questioned cost).

Firm Response: *At the exit conference, the firm replied that the amount was immaterial and requested the details comprising this finding.*

FMA Response: *FMA provided the details as requested but has not received any further communication.*

4. SS&N Billed for Professionals Not Authorized by the Pioneer Agreement

Table 10: Reconciliation of Questioned Cost

Activity Questioned	Fees Questioned
Professionals Billed But Not Authorized by the Pioneer Agreement	\$25,636
Less Duplicative Costs Questioned:	
Unallowable Learning Curve Fees for Pioneer Work	(5,621)
Total Duplicative Costs Questioned	(5,621)
Total	\$20,015

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

The firm's proposal to RTC for the Pioneer work became the basis of the firm's agreement with RTC and identified firm and co-counsel partners, associates and paralegals authorized to perform services for the engagement. Our testing discovered the firm's use of unauthorized billers, including several who were involved for only a few number of days, weeks or months. We questioned \$25,636 (\$20,015 net of adjustments for other findings related to the use of unauthorized billers). We also questioned the necessity or reasonableness of using some of these professionals on Pioneer matters for such a brief time period.

Recommendation

- (11) We recommend that FDIC disallow \$20,015 of costs related to unauthorized professionals working on Pioneer matters (questioned cost).

Firm Response: *At the exit conference, the firm requested the details comprising this finding.*

FMA Response: *FMA provided the details as requested but has not received any further communication.*

5. **SS&N Billed Unallowable Learning Curve Fees for Pioneer Work***Table 11: Reconciliation of Questioned Cost*

Activity Questioned	Fees Questioned
Unallowable Learning Curve Fees for Pioneer Work	\$36,131
Less Duplicative Costs Questioned:	
Allocation of Time Between Files Resulted in Billing Mistakes and Overcharges	(225)
Inappropriate Billings for Training and Education	(270)
Professionals Billed at Hourly Rates that Exceeded the Pioneer Agreement	(60)
Total Duplicative Costs Questioned	(555)
Total	\$35,576

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

As a condition of the Pioneer assignment, the firm agreed to "absorb the costs involved in the learning curve in order to become familiar with handling professional liability claims." We reviewed all Pioneer timekeepers and billing entries (3,265 hours over a 14 month time period) to evaluate whether the firm's admitted inexperience in handling professional liability claims increased the cost to the RTC. Numerous attorneys and paralegals only worked on the project for short periods of time. As an example, a paralegal only worked one day (2.7 hours) "reading and organizing" various litigation, financial and bank information. We could not determine any value to the progress of the Pioneer matters or to the RTC from this work. Examples of other learning curve activities that were billed include the following:

"Attend team meeting and training"

"Investigation and gathering of factual information on various pending cases brought by FDIC/RTC against various accounting firms for malpractice..."

"Create files for drafts of ATS and Position letters"

"Review, Evaluate and give additional direction on review of loan files at RTC Investigations"

"Consult with Paralegal on review of file for possible securities claim"

"Attempt to reschedule client meeting"

"Prepare for team meeting"

"Conduct litigation department meeting and training-RTC overview"

"Assemble binders containing samples and research"

"Prepare memorandum regarding binders and PLS information in library"

"Assess staff assignments through August 15"

Finally, we question the hours incurred performing various research projects. As an example, 24.2 hours and \$1,607 was billed for a law clerk to prepare a general memo on the "Financial Privacy Act" (124SC§3401). A firm with experience in professional liability claims would find little relevance or use for this general memorandum in dealing with PLS cases.

Our examination of all Pioneer matter billings found \$36,131 (\$35,576, net of adjustments for other findings) as questionable fees related to "learning curve" costs that should have been absorbed by the firm rather than paid by the RTC.

Recommendation

- (12) We recommend that FDIC disallow \$35,576 of professional fees that the firm agreed to absorb as learning curve costs (questioned cost).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

6. SS&N Made Fee Adjustments Without Adequate Supporting Documentation

FMA detected numerous adjustments of time on prebills without supporting documentation. However, our ability to conduct an extensive examination of the adjustment problem was limited by the firm's inconsistent policy of retaining prebills. We questioned \$8,205 related to undocumented write-ups.

Recommendation

- (13) We recommend that the FDIC disallow \$8,205 of fees related to increases to the Pioneer prebill without any supporting documentation (questioned cost, all of which is unsupported).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

E. Other Matters

I. SS&N's Status as an MWOLF

Eight months after the firm executed the first LSA with FDIC in February 1991, an opportunity developed for SS&N to obtain status as an MWOLF. In October 1991, RTC's acting General Counsel released a memorandum to all RTC Legal Division personnel advising that, effective immediately, individuals with disabilities would be included in the definition of the term "minority" for purposes of the Minority Outreach Program established by the RTC Legal Division. This policy was established to ensure that RTC was in compliance with the recently enacted Americans with Disabilities Act of 1990, 42 U.S.C. 12101 *et seq.* which followed the enactment of FIRREA. Thereafter, SS&N was granted MWOLF status on the basis that an 85 percent equity ownership was held by a disabled male shareholder.

Internal RTC memoranda reviewed by FMA indicated the possibility that the policy was rescinded officially in 1993 or 1994. If the policy is no longer effective, we question the firm's current MWOLF status and the accuracy of any representation asserting such status or that the firm is a women-owned firm as defined in the current MWOLF regulations.

Recommendation

- (14) We recommend that FDIC determine whether the firm currently qualifies as an MWOLF.

Firm Response: At the exit conference, the firm indicated that the memorandum has not been overruled or superseded and as a result, they currently qualify as an MWOLF.

2. Potential Duplicate Payments

In certain engagements involving the sale of real estate, the firm represented RTC as seller's counsel and also served as agent for the title insurance underwriter. In both capacities, the firm's primary responsibility was to perform title work. The firm acknowledged receiving both an hourly fee as RTC's counsel and a major portion of the title insurance premium payment as underwriter's agent. We questioned the firm's participation in two revenue sources for substantially the same services and requested the firm to identify and explain these circumstances. We also questioned whether RTC was aware of the firm's substantial participation in this activity.

In our opinion, the firm should not have billed the RTC for this type of work since the firm was receiving a portion of the title insurance premium for performing these identical services.

Recommendation

- (15) We recommend that FDIC review the appropriateness of the firm receiving title insurance premiums while also representing RTC.

Firm Response: *At the exit conference, the firm requested the details comprising this finding.*

FMA Response: *FMA provided the details as requested but has not received any further communication.*

VI. SUBSTANTIVE LEGAL REVIEW

A. Overview of Testing

FMA analyzed the legal services and work product related to 21 matters performed by SS&N as selected from reports generated by Data Base I (see page 9). These matters included fee billings of \$2,106,531 listed in Table 12 below:

Table 12: Matters Selected for Substantive Legal Review

Client/Matter	Billings
452789-07010	\$392,411
452648-06000	186,228
012497-03030	185,331
012497-28000	167,120
452789-07020	143,331
012497-44000	141,554
452648-05000	115,044
452649-08010	93,155
01497-49001	83,757
452789-04000	83,022
012497-26008	67,908
012497-45000	66,609
012497-03160	66,465
452649-05000	61,913
402861-05001	51,982
452648-07000	45,046
452649-07000	38,731
452648-08000	37,653
402621-01003	37,330
452649-08000	23,708
012497-47001	18,233
TOTAL SELECTED	\$2,106,531
TOTAL RTC	\$3,875,910
Planned Test Percentage	54 percent

Source: FMA Analysis

The substantive analysis was performed to determine whether billed hours and expenses were commensurate with the services rendered and in accordance with the operable agreements and guidelines. Our computer analysis of invoices provided by SS&N in Data Base I established a profile of the firm's billing policies and practices. We reviewed the correspondence, research materials, pleadings and transcripts in each matter selected. Interviews were held with supervising and participating attorneys and paraprofessionals. We were able to perform a satisfactory analysis on 100 percent of the selected files. However, as noted on page 12, our substantive review was impacted by the firm's practice of block billing and allocating time over multiple bills. In many cases, the bills did not identify the allocation procedure or the other affected entries.

FMA evaluated SS&N's compliance with the Legal Services Agreements, including the FDIC *Guide for Legal Representation*, RTC *Guide for Outside Counsel*, RLIS *Forms and Procedures Deskbook for Outside Counsel*, RTC and FDIC policies and procedures and 12 CFR §1606, all of which are incorporated by reference in the LSA. The firm had separate billing agreements with RTC for Pioneer and Security First matters. We also evaluated the firm's compliance with professional codes of conduct, including the *ABA Code and Rules*.

Below is a summary of our findings in the substantive testing area of the audit:

Table 13: Summary of Questioned Costs Based on Substantive Legal Review

Item	Questioned Fees
Inaccurate Timekeeping for Attendance at Depositions	\$3,710
Inappropriate Staffing Used	2,154
Inappropriate Billing Related to Travel Time	8,152
Inappropriate Billings for Status Reports and Fee Bill Preparation	11,732
Inappropriate Billings for Training and Education	6,863
Inappropriate Billings for Overhead Expenses	12,056
Inappropriate Billings Related to the Firm's Research of Their Own Conflicts	436
Total	\$45,103

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

B. Description of Detailed Testing

1. SS&N Used Inaccurate Timekeeping for Attendance at Depositions

Table 14: Reconciliation of Questioned Cost

Activity Questioned	Fees Questioned
Used Inaccurate Timekeeping for Attendance at Depositions	\$3,710
Less Duplicative Costs Questioned:	
Inappropriate Billings Related to Travel Time	(610)
Total Duplicative Costs Questioned	(610)
Total	\$3,100

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

We detected numerous examples of inaccurate or questionable time recorded by SS&N attorneys representing RTC at depositions in certain of the matters selected for substantive review. From the test of Database III for entries described as "attend deposition", we selected a sample of 15 deposition transcripts and found that in 11 cases, the SS&N attorney attributed more time to the testimony than recorded by the court reporter. Numerous other entries reflecting deposition attendance could not be tested due to the firm's practice of block billing. For example, time descriptions worded, "prepare for and attend deposition" prevented the auditor from isolating the separate activities of preparation and attendance. Other activities within the sample could not be tested due to the absence of starting or ending times on the transcripts, or because the transcripts were not available for inspection.

The concept of accurate timekeeping by attorneys engaged by RTC is so elementary that the *RTC Guide For Outside Counsel ("Guide")* does not address the matter directly. At page 17 of the *Guide*, the Legal Division's litigation philosophy is stated "...to pursue an approach that is assertive, forthright and consistent with the RTC's overall objective of conducting litigation in an expeditious and cost-effective manner."

Recommendation

- (16) We recommend that FDIC disallow \$3,100 in unsubstantiated charges for deposition attendance (questioned cost).

Firm Response: *At the exit conference, the firm requested the details comprising this finding.*

FMA Response: FMA provided the details as requested but has not received any further communication.

2. SS&N Used Inappropriate Staffing

On a number of occasions the firm participated in depositions with Co-Counsel and did not charge for that time. However, on other occasions, more than one member of the firm charged for attending depositions or hearings. We question \$2,154 of fees relating to overstaffing. The Guide provided on page 19, "...the Legal Division expects Outside Counsel to avoid the following: taking unnecessary staff to meetings, depositions or hearings; overstaffing in general; rotating out from assignments attorneys already proficient on RTC issues; or using only projects for purpose of training new personnel at RTC expense." The Guide further provided that any additional staffing should be discussed in advance and be pre-approved by the responsible RTC attorney. We found no evidence that RTC approved additional staffing.

Recommendation

(17) We recommend that FDIC disallow \$2,154 of fees related to overstaffing (questioned cost).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

3. SS&N Inappropriately Billed For Time Incurred Related to Travel

Table 15: Reconciliation of Questioned Cost

Activity Questioned	Fees Questioned
Inappropriate Billings Related to Travel Time	\$8,152
Less Duplicative Costs Questioned:	
Allocation of Time Between Files Resulted in Billing Mistakes and Overcharges	(319)
Inappropriate Staffing Used	(495)
Total Duplicative Costs Questioned	(814)
Total	\$7,338

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

a) Inconsistent with LSA

We found on numerous occasions billing entries for travel that were inconsistent with the firm's LSA which provided that "Travel Time is compensated at 50 percent of the firm's regular billing rates except for time spent on substantive work on a matter." We question travel entries totaling \$3,980 (\$3,683, net of adjustments for other findings) billed in excess of 50 percent or that do not describe the performance of substantive work.

Recommendation

- (18) We recommend that FDIC disallow \$3,683 of travel costs billed in excess of 50% of the approved hourly rate (questioned cost).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

b) General Bank Matter

We also found 41 trips made by the firm that did not comply fully with its agreement to waive travel time for work performed in Miami on the General Bank matter. The time was waived because the firm was willing to make this accommodation to secure the work. We question \$4,172 (\$3,655, net of adjustments for other findings) related to these non-compliant billings.

Recommendation

- (19) We recommend that FDIC disallow \$3,655 of travel costs in excess of 50% specifically related to the General Bank, FSB matter (questioned cost).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

4. SS&N Inappropriately Billed for Status Reports and Fee Bill Preparation

Table 16: Reconciliation of Questioned Cost

Activity Questioned	Fees Questioned
Inappropriate Billings for Status Reports and Fee Bill Preparation	\$11,732
Less Duplicative Costs Questioned:	
Employees Billed Subsequently Approved on LSA	(26)
Inappropriate Billings for Training and Education	(13)
Billed Fees in Excess of LSA Approved Rates	(33)
Total Duplicative Costs Questioned	(72)
Total	\$11,660

Source: FMA analysis of RTC Guidelines, SS&N LSAs and Professional Service Fees.

We identified numerous instances where the firm billed for the preparation of fee bills and status reports to RTC with no evidence that RTC approved any additional costs related to non-routine reports. Accordingly, we question \$11,732 (\$11,660, net of adjustments for other findings) for inappropriate billings related to preparation of fee bills and status reports.

The *RTC Guide for Outside Counsel* provided that "the Legal Division considers its reporting and billing requirements to be part of the cost of doing business with the RTC, and as a general rule will not pay Outside Counsel for the time expended on the preparation of bills and routine reports. If a non-routine report is particularly burdensome, Outside Counsel may request authorization from the responsible RTC attorney to bill, at cost, for its preparation..."

Recommendation

- (20) We recommend that FDIC disallow \$11,660 related to preparation of fee bills and status reports (questioned cost).

Firm Response: The firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

5. SS&N Inappropriately Billed for Training and Education

We identified \$6,863 of training and education costs billed by the firm to RTC. The *RTC Guide for Outside Counsel*, February 1992, provided:

"It is the policy of the Legal Division not to pay for the educational or developmental costs of Outside Counsel becoming familiar with relevant statutory and case law pertinent to the Corporation." The firm had an obligation to absorb such costs.

Recommendation

- (21) We recommend that FDIC disallow \$6,863 of costs related to training and education (questioned cost).

Firm Response: *At the exit conference, the firm requested the details comprising this finding.*

FMA Response: *FMA provided the details as requested but has not received any further communication.*

6. SS&N Inappropriately Billed for Firm Overhead Expenses

We identified numerous instances of the firm billing for items considered overhead, such as filing. We are questioning \$12,056 related to these items in the absence of the firm's demonstration that these overhead costs were approved by RTC.

The *RTC Guide for Outside Counsel* provided on page 13 that the rates for professional services include all overhead and profit. Furthermore, the LSA included as Exhibit E a Certification that states "No charges have been included for bill preparation or other overhead charges, such as secretarial services, typing or filing."

Recommendation

- (22) We recommend that FDIC disallow \$12,056 of billings related to firm overhead (questioned cost).

Firm Response: *At the exit conference, the firm requested the details comprising this finding.*

FMA Response: *FMA provided the details as requested but has not received any further communication.*

7. **SS&N Inappropriately Billed For Time Incurred Related to the Firm's Research of Their Own Conflicts**

We are questioning \$436 of costs related to research of the firm's potential conflicts of interest. The *RTC Outside Counsel Desk Book* provided that "the fee or cost charged should not represent a service that is customarily included in the normal overhead or administrative expense of running a law firm." We believe the analysis of a potential conflict of interest is included under this provision.

Recommendation

(23) We recommend that FDIC disallow \$436 of costs related to the firm's research of their own conflicts of interest (questioned cost).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

VII. EXPENSES: FINDINGS AND RECOMMENDATIONS

A. Background

The firm billed RTC during the audit period for \$347,375 of reimbursed expenses. We examined \$194,271, or 56 percent, of this population. The following table summarizes the breakdown of expenses by category.

Table 17: Summary of Expense Testing

Major Expense Category	Amount Billed	Amount Tested	Percent Tested	Questioned Cost
Document Reproduction	\$63,721	\$22,411	35.2	\$39,972
Telephone and Facsimile	38,941	5,967	15.3	38,354
Outside Database Services	29,825	11,928	40.0	5,684
Process Servers	3,206	1,749	54.5	140
Travel	26,458	19,814	74.9	8,440
Courier and Express Mail	23,880	6,605	27.7	83
Deposition and Filing Fees	25,015	10,945	43.8	5,944
Miscellaneous	49,359	34,546	69.9	14,640
Expert Witness and Consultant	86,970	80,306	92.3	47,100
Total	\$347,375	\$194,271	55.9	\$160,357

Source: FMA analysis of RTC guidelines, SS&N LSAs and Expenses

B. Findings

(1) Document Reproduction

Table 18: Summary of Expenses Questioned - Document Reproduction

Description	Questioned Costs
In-House Copying	\$35,277
Unsupported Outside Copying Charges	4,695
Total	\$39,972

Source: FMA analysis of RTC guidelines, SS&N LSAs and Expenses

a) **In-House Copying**

FMA identified 1,532 entries of in-house copying not supported by a cost study. The description field found in SS&N invoices consistently contained the copy counts charged at \$.08 per copy. We selected, at random, 16 test counts in the amount of \$8,597 (107,484 copies at \$.08 per copy). In all cases, the copy counts were supported by a printout from the firm's computer system.

The *RTC Guide for Outside Counsel*, stated "...Charges for photocopying shall be at firm's actual cost, not to exceed eight cents per page unless supported by a cost study."

The firm did not produce a cost study in response to FMA's request. Accordingly, we question \$35,277 for in-house copying, representing the entire amount billed.

Recommendation

- (24) We recommend that FDIC disallow the \$35,277 unsupported in-house copying charges (questioned cost, all of which is unsupported).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

b) **Unsupported Outside Copying Charges**

For outside copying charges, we randomly selected 25 entries contained in SS&N invoices totaling \$13,814. Rates charged varied widely from \$.20 at the law library to a \$1.00 per copy for certified copies. The firm was unable to produce adequate support for \$4,695 of the selected entries. We question \$4,695 for outside copying charges.

The *RTC Guide for Outside Counsel*, stated "...Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payment."

Recommendation

- (25) We recommend that FDIC disallow the \$4,695 for unsupported outside copying charges (questioned cost, all of which is unsupported).

Firm Response: *At the exit conference, the firm requested the details comprising this finding.*

FMA Response: *FMA provided the details as requested but has not received any further communication.*

(2) **Facsimile and Telephone**

Table 19: Summary of Expenses Questioned - Facsimile and Telephone

Description	Questioned Costs
Unsupported Facsimile Charges	\$26,319
Unsupported Long Distance Telephone Charges	12,035
Total	\$38,354

Source: FMA analysis of RTC guidelines, SS&N LSAs and Expenses

a) **Unsupported Facsimile Charges**

We selected 20 test page counts totaling \$5,967. In most cases, the counts were supported by a printout from the firm's computer system and we noted a standard \$1.00 per page charge. However, the firm did not perform a cost study and therefore, could not support the per page charge. Accordingly, we question \$26,319 for unsupported facsimile charges.

RTC Guide for Outside Counsel, stated "...Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payment."

Recommendation

- (26) We recommend that FDIC disallow the \$26,319 of unsupported facsimile charges (questioned cost, all of which is unsupported).

Firm Response: *At the exit conference, the firm requested the details comprising this finding.*

FMA Response: *FMA provided the details as requested but has not received any further communication.*

b) Unsupported Long Distance Telephone Charges

Firm personnel were required to enter a client-matter code for long distance telephone calls. This information was electronically downloaded monthly into the firm's billing system. Completed calls were charged to each client-matter during the month and aggregated into the bill as a total. The amount billed was determined by multiplying the total elapsed time by predetermined rates built into the telephone system. We proposed a test by comparing the rates charged RTC to the rates paid the long distance telephone carrier using four different monthly long distance bills. However, the firm was unable to provide us with a rate schedule, and we could not determine that the amounts charged for long distance telephone were at the firm's actual rate. Because the firm could not adequately support the long distance telephone charges we consider the \$12,035 paid as questioned and unsupported costs.

Recommendation

- (27) We recommend that FDIC disallow the \$12,035 of unsupported long distance telephone charges (questioned cost, all of which is unsupported).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

(3) Outside Database Services

Table 20: Summary of Expenses Questioned - Outside Database Services

Description	Questioned Costs
Unsupported Charges	\$1,934
Unusual Charges for Which RTC Approval Was Not Obtained	3,750
Total	\$5,684

Source: FMA analysis of RTC guidelines, SS&N LSAs and Expenses

a) Unsupported Charges

The firm billed \$29,825 for outside database services. We selected 18 charges totaling \$11,928 for testing. In most cases the charges were supported by a vendors invoice. However, the firm could not produce supporting documentation for \$1,934 of the charges. We, therefore, question \$1,934 in unsupported database expenses.

RTC Guide for Outside Counsel, stated "...Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payment."

Recommendation

- (28) We recommend that FDIC disallow \$1,934 of unsupported outside database charges (questioned cost, all of which is unsupported).

Firm Response: *At the exit conference, the firm requested the details comprising this finding.*

FMA Response: *FMA provided the details as requested but has not received any further communication.*

b) Unusual Charges for Which RTC Approval was not Obtained

Included in our test counts, described above, was a \$3,750 charge for "universal and detail on-line search" services paid to Prentice-Hall Legal & Financial Services for a national asset search. Due to the unusually high charge, we requested support of RTC approval for the charges. The *RTC Guide for Outside Counsel* stated, "...fees and expenses (including Westlaw and Lexis charges) generated as a consequence of unauthorized and unnecessary research will not be paid." The firm was not able to provide documentary evidence that the expense was approved by the RTC. We consider these unapproved charges of \$3,750 as questioned costs.

Recommendation

- (29) We recommend that FDIC disallow the \$3,750 of unapproved legal search charges (questioned cost).

Firm Response: *At the exit conference, the firm requested the details comprising this finding.*

FMA Response: *FMA provided the details as requested but has not received any further communication.*

(4) Process Servers

The firm billed \$3,206 for process servers. We selected 15 test counts in the amount of \$1,749. In all but one case the charges were supported by a vendor's invoice. The firm could not provide support for \$140. We, therefore, question \$140 of unsupported process server fees.

The *RTC Guide for Outside Counsel*, stated "...Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payment."

Recommendation

- (30) We recommend that FDIC disallow the \$140 for unsupported process server charges (questioned cost, all of which is unsupported).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

(5) Travel

Table 21: Summary of Expenses Questioned - Travel

Description	Questioned Costs
Unsupported Travel Costs	\$3,063
Billings Were Not For Actual Cost	860
Unapproved Charges - Multiple Personnel	3,504
Unallowable Costs	1,013
Total	\$8,440

Source: FMA analysis of RTC guidelines, SS&N LSAs and Expenses

a) **Unsupported Travel Costs**

The firm billed \$26,458 for out-of-town travel expenses. We selected 37 test counts totaling \$19,814 of charges. In most cases, the travel expenses were adequately supported by properly completed travel vouchers. However, the firm could not provide documentation for \$3,063 of billed travel costs. We consider the \$3,063 as unsupported questioned costs.

The *RTC Guide for Outside Counsel*, stated "...Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payment."

Recommendation

- (31) We recommend that FDIC disallow the \$3,063 of unsupported travel costs (questioned cost, all of which is unsupported).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

b) Billings Were Not For Actual Cost

In one case we observed that the travel costs were billed on the basis of time and not at actual cost. The RTC was billed 2.4 hours at \$275/hr (\$660) and 8.0 hours at \$25/hr (\$200) for a total of \$860 (It is possible the billing attorney or clerk miscoded the billing as travel rather than fees). We consider the \$860 as questioned costs. The *RLIS Forms and Procedures Deskbook for Outside Counsel* provided detailed instructions for reimbursement of travel expenses.

Recommendation

- (32) We recommend that FDIC disallow the \$860 of unsupported travel costs (questioned cost, all of which is unsupported).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

c) Unapproved Charges - Multiple Personnel

Our test counts identified seven instances, where two or more attorneys traveled for the same function such as depositions, settlements, closings, meetings and documentation review. The *RTC Guide for Outside Counsel ("Guide")*, stated the legal division expects outside counsel to avoid "taking unnecessary staff to meetings, depositions or hearings". The *Guide* further provides "if outside counsel believes it needs to take additional staff to meetings, depositions or hearings, or believes staffing changes in the middle of a case are necessary, the legal division expects those staffing recommendations to be discussed in advance with, and be pre-approved by, the responsible RTC attorney". In another section, the *Guide* stated "it has been the experience of the legal division that travel by more than one attorney is frequently unnecessary and not justified." In response to our request for RTC approval, the billing attorney attested to RTC's approval and provided justification for attendance by more than one attorney; however, independent confirmation was not provided. We consider the \$3,504 of travel costs for the additional personnel (attorneys or paralegals other than the senior attorney) as questioned costs until the firm can provide independent confirmation of RTC's approval.

Recommendation

- (33) We recommend that FDIC disallow the \$3,504 for unauthorized travel expenses (questioned cost).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

d) Unallowable Costs

On a travel voucher, the attorney billed \$41 to RTC for taxi service to and from dinner. The RLIS *Forms and Procedures Deskbook for Outside Counsel*, stated "...transportation to obtain meals is not reimbursable." In another instance, two attorneys attending a deposition stayed overnight and billed RTC for a total of three nights. Both attorneys had included the hotel charge (\$82) for the junior attorney on their respective travel vouchers, thus duplicating the cost. We consider the \$41 taxi service cost and the \$82 duplicated hotel charge as questioned costs.

The firm billed \$890 of travel expenses for an attorney to attend a "conference". We could not determine that attendance was necessary to effectively represent RTC nor that the charges were not for a service customarily included in a law firm's normal overhead or administrative expenses. The *RTC Guide for Outside Counsel*, stated "...it is the policy of the legal division not to pay for the education or developmental costs of Outside Counsel becoming familiar with relevant statutory and case law pertinent to the Corporation."

Recommendation

- (34) We recommend that FDIC disallow the \$1,013 (\$82 + \$41 + \$890) in non-reimbursable travel expenses (questioned cost).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

(6) Courier / Express Mail

The firm billed \$23,880 for courier services and express mail. We selected 23 test counts in the amount of \$6,605. In 100 percent of the test counts of Federal Express invoices, the firm billed the RTC at actual cost net of any discount.

In all other charges the RTC was billed at actual cost. In most cases the charge was supported by a vendor invoice; however, the firm could not substantiate \$83 of charges. We consider the \$83 as questioned costs (all unsupported).

The *RTC Guide for Outside Counsel*, stated "...Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payment."

Recommendation

- (35) We recommend that FDIC disallow the \$83 of unsupported express mail charges (questioned cost, all of which is unsupported).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

(7) Deposition and Filing Fees

Table 22: Summary of Expenses Questioned - Deposition and Filing Fees

Description	Questioned Costs
Unsupported Charges	\$3,882
Unreasonable Charges	2,062
Total	\$5,944

Source: FMA analysis of RTC guidelines, SS&N LSAs and Expenses

a) Unsupported Charges

The firm billed \$25,015 for deposition and hearing transcripts, court fees and filing fees under 14 different expense codes during the audit period. We selected 21 test counts in the amount of \$10,945. In most cases, the charges were supported by a vendor's invoice and billed to the RTC at actual cost. However, the firm could not provide supporting documentation for \$3,882 of the charges for recording powers of attorney in 67 Florida counties. However, from the documentation provided, we could not establish that the amount billed was the actual cost. We consider the \$3,882 as questioned costs.

The *RTC Guide for Outside Counsel*, stated "...Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payment."

Recommendation

- (36) We recommend that FDIC disallow \$3,882 of unsupported filing fees (questioned cost, all of which is unsupported).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

b) Unreasonable Charges

The firm billed \$2,062 for deposition services (e.g. court reporter, copy of transcript). In response to our request for justification for the charge we were informed the deposition was handled on an expedited basis over a 2-day period following oral approval by the RTC supervisory attorney. However, independent confirmation of RTC approval was not obtained. We consider the \$2,062 as questioned costs.

Recommendation

- (37) We recommend that FDIC disallow the \$2,062 in unsupported deposition charges (questioned cost, all of which is unsupported).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

(8) Miscellaneous

The firm billed \$49,359 of miscellaneous charges (i.e. IRS, Division of Motor Vehicles, advertising, lien and other cost before sale of property, etc.) under 21 different expense codes. We selected 43 test counts amounting to charges of \$34,546. In most cases, the charges were supported by a vendor's invoice. However, the firm could not produce supporting documentation for \$14,640 of which \$13,731 was the cost for a title insurance policy. From the documentation provided we could not establish that the amount billed was the actual cost. Until the firm can provide proper supporting documentation, we consider the \$14,640 as questioned costs.

The *RTC Guide for Outside Counsel*, stated "...Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payment."

Recommendation

(38) We recommend that FDIC disallow the \$14,640 of unsupported miscellaneous expenses (questioned cost, all of which is unsupported).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

(9) **Expert Witness and Consultant**

The firm billed \$86,970 of expenses for this category. We selected 19 test counts totaling \$80,306 in charges. In all but one case the firm provided proper supporting documentation. The firm billed RTC \$47,100 for work performed by Peterson Consulting. The vendor invoice did not include any detail of the charges. Consequently, we could not evaluate the reasonableness of the charges. FMA requested SS&N to obtain details from Peterson Consulting. The firm produced a Peterson invoice for \$47,100 that did not contain supporting detail of charges. We consider the \$47,100 as questioned costs.

The *RTC Guide for Outside Counsel*, stated "...Outside Counsel is required to retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for four years after payment."

Recommendation

(39) We recommend that FDIC disallow the \$47,100 of unsupported consultant charges (questioned cost, all of which is unsupported).

Firm Response: At the exit conference, the firm requested the details comprising this finding.

FMA Response: FMA provided the details as requested but has not received any further communication.

VIII. CONFLICTS OF INTEREST AND PROFESSIONAL RESPONSIBILITY

FMA examined the firm's policy, internal procedures and controls for detecting and disclosing conflicts of interest, preserving confidentiality and complying with applicable statutory and contractual requirements, including codes of professional responsibility.

A. Analysis of Firm's Policies and Internal Procedures for Conflict of Interest

The firm's records contained limited support to demonstrate compliance with the conflict of interest requirements of the *RTC Guide for Outside Counsel ("Guide")*, February 1992. In the absence of a written policy, the firm prepared various documents at our request describing its internal controls and procedures for identifying and resolving conflicts or potential conflicts. We also examined applications for professional liability insurance for consistency of representations. Our initial request to perform a conflicts audit by examining daily time sheets and other information was resisted by the firm on the grounds of confidentiality. During fieldwork however, the firm agreed to provide access to such information. We determined that SS&N relied on informal recognition procedures to detect conflicts, rather than a computer-aided approach. The principal method was the monitoring of conflicts by the managing partner and supervising attorneys using meetings, electronic mail and annual questionnaires for professional insurance applications. We were unable to express an opinion regarding the adequacy of the firm's internal controls for detecting conflicts until its non-RTC clients were examined.

The selection of independent contractors by RTC and FDIC was made in accordance with standards for qualification and ethics codified at 12 C.F.R. 1606 et. seq. These regulations apply, inter alia, to contracts for services entered into by RTC/FDIC with law firms. 12 C.F.R. 1606.1 (c). The regulations were promulgated in an effort to ensure that all independent contractors met minimum standards of competence, integrity, fitness, experience and ethical conduct, and provided for the disqualification of contractors who fell below these standards. 12 C.F.R. 1606.1 (b). Outside legal counsel were held to the highest ethical standard in their relationship with RTC/FDIC and expected to observe the *ABA Rules*. 1606.8 (a)(1) provides that in connection with the performance of legal services, a law firm or attorney shall not act for the RTC/FDIC in any matter in which either the firm or attorney, or any related entity, has a conflict of interest unless the RTC/FDIC determines that such representations are appropriate.

B. Examination of Firm's Client List and Time Records

The firm provided a list of all non-RTC/FDIC clients during the audit period. Our examination of clients identified in daily time records substantiated the accuracy of the firm's client list. We identified approximately 75 clients that by name, or matter description, warranted an examination to determine if the firm represented any of the following: debtor-in-possession, trustee in bankruptcy, receiver in any court or administrative proceeding where RTC or FDIC had an interest as a creditor; insurance carrier, stockholder or class of stockholders in actions against a director or officer of an insured depository institution, or represented an insured depository regarding a regulatory matter; or other matter relating to the RTC, FDIC, or the

former FSLIC. From our analysis of time entries for each of these clients throughout the audit period, and from discussions with firm's attorneys responsible for billing such clients, we concluded there was no evidence that the firm represented clients with conflicting interests to those of RTC, FDIC or the former FSLIC.

APPENDIX

APPENDIX

LEGAL DIVISION COMMENTS¹



FDIC

Federal Deposit Insurance Corporation
Washington, D.C. 20429

Legal Division - Outside Counsel Unit

December 16, 1998

REC-11
DEC 17 4 25 PM '98

(b)(6)

MEMORANDUM TO: David H. Loewenstein
Assistant Inspector General

THROUGH: William F. Kroener, III
General Counsel

William S. Jones
Supervisory Counsel

FROM: Chris J. Conanan
Counsel

SUBJECT: Audit of Legal Fees and Expenses Paid by the RTC to the Law Firm of Salem, Saxon & Nielsen (Tampa, Florida)

This memorandum constitutes the Legal Division's response to both the draft audit report (Exhibit A) of the Office of Inspector General (OIG) on payments made by the RTC to the law firm of Salem, Saxon & Nielsen ("Firm") and the Firm's voluminous responses, dated July 24 and August 28, 1998, to the report (Exhibit B). The report covered a judgmental audit sample of \$2,300,802 in fees and expenses paid to the Firm by the RTC from January 1, 1991 through December 31, 1994. This sample represents 54% of the \$4,223,285 paid by the RTC to the Firm for professional services rendered by the Firm during the audit period. The audit was conducted by an independent public accounting firm ("IPA") contracted by the OIG from February 9, 1995 to May 31, 1995. The IPA issued its report on July 25, 1995 and the OIG issued its draft audit report to the Legal Division on February 10, 1998. Because the draft audit report did not include any schedules correlating questioned amounts to invoice amounts, detailed examination of the audit work papers was necessary. The report originally identified \$688,732 in questioned costs. After reviewing the report, the auditors' work papers, and the Firm's responses, the Legal Division will disallow \$8,112 in fees and expenses paid to the Firm.

The Legal Division's position regarding each audit condition is explained below in the order in which it appears in the report.

¹The attachments referred to in the Legal Division's response are not included in this appendix.

APPENDIX

APPENDIX

Recommendation 1: The report recommends that the FDIC require responsible personnel to analyze the qualifications for employees working on RTC matters but not listed on the LSA, determine how much of the \$292,713 in net questioned costs should be retroactively ratified, and disallow any of these charges not approved.

The report questions \$292,713 (net of adjustments for other findings) in costs relating to attorneys and paralegals in the Firm who either performed services prior to their being listed as approved on an LSA or were never listed on an LSA. In particular, \$240,749 of the net questioned costs is for attorneys and paralegals who were eventually listed on subsequent LSAs with the Firm; the remaining \$51,964 is for personnel who were never added to an LSA.

A review of the auditors' work papers discloses that many of these charges primarily evolved around the Firm's representation of the RTC in a professional liability matter pertaining to the General Bank, FSB. The Firm informed the RTC oversight attorney about additional personnel needed in connection with this matter. [Response at Tab 12, Letter from Firm to RTC Oversight Attorney dated May 31, 1994.] This RTC oversight attorney indicated that she was aware of additional Firm personnel that were used for another professional liability matter who were not included as listed personnel in the original case plans (and by inference on the original LSAs) for that matter. However, this oversight attorney stated that "every addition of staff to the team was accomplished with my prior approval." [Response at Tab 4, Letter from RTC Oversight Attorney to the Firm, dated December 20, 1995.] It is likely that lead oversight attorneys were generally aware of all additions to projects assigned to the Firm.

We have reviewed the hourly rates charged by such additional staff. For attorneys subsequently listed, the rates charged before their listing were equivalent to those charged afterwards. For attorneys never listed on a LSA, the rates charged for such attorneys were consistent with rates charged for attorneys listed on the LSA. Accordingly, in light of these circumstances, the Legal Division will ratify¹ payment for the use of all such personnel. Accordingly, the Legal Division will not disallow any questioned costs under this recommendation.

Recommendation 2: The report recommends that the FDIC disallow \$7,855 in overbillings due to unauthorized rates.

The report questions \$7,855 (net of adjustments for other findings) in costs because of billings by the Firm at hourly rates that were purportedly greater than those authorized in the applicable LSAs. Our review of the work papers indicates that the auditors did not base this finding on the actual invoices that the Firm used to receive payment by the RTC for the hourly rates the Firm charged the RTC. Indeed, the Firm states in its response that:

¹ Since the General Counsel has complete delegated authority regarding hiring and paying outside counsel with respect to issues raised by the report, his signing of this memorandum should be deemed a ratification or approval of billing rates and fees incurred to the extent indicated herein.

APPENDIX

APPENDIX

The work papers relied upon by the Auditors for this recommendation are clearly computer printouts, not invoices. Of the 692 questioned entries, 622 had no validity whatsoever, as they were either billed correctly or never billed to the RTC at all. There are numerous discrepancies with other entries listed below. The erroneous universe of information utilized by the Auditors has caused SS&N to spend over 4 days reviewing almost 700 time entries when we should only have been reviewing 70 entries, at most. Absolutely no confirmation was done to validate these purported questionable costs by comparison with the actual invoices. SS&N had to pull a voluminous number of invoices and manually compare each and every entry. [Supplemental Response at 2.]

In the "Scope and Methodology" section of its report, the IPA stated that it "developed data bases of time, expense and billing records provided in computer form by SS&N, as well as computer data received from RTC" and that it "used the data bases to generate detailed and summary profiles of billing activity for all attorneys and for fee and expense categories." Accordingly, it appears that the IPA audited the Firm's computerized records rather than actual invoices presented to the RTC for payment.

We understand that this recommendation has been re-assessed by OIG staff. **Hence, the Legal Division will not disallow any of the costs questioned under this recommendation.**

Recommendation 3: The report recommends that the FDIC disallow \$14,352 in payments for fees written-up from original time records.

The report questions \$14,352 (net of adjustments for other findings) in costs for fees written-up from original time records. The work papers show that the questioned costs under this recommendation may be broken down as follows: \$9,719 is based on the absence of time sheets to support entries on pre-bills and invoices – the auditors evidently believed a "mark-up" occurs whenever original time sheets cannot be found to support entries on pre-bills or invoices. It should be noted that the auditors have not found any mark-ups from the pre-bills to the invoices with respect to the \$9,719 in questioned costs. As disclosed in the work papers, the remaining \$4,836 in costs questioned under this recommendation is based on mark-ups from original time sheets found by the auditors to the invoices.

The Firm disagrees with this finding and stated that:

We spent a considerable amount of time explaining our entire billing procedure to the Auditors, which they appear to have ignored in this recommendation. Secretaries enter time based solely upon timesheets completed by timekeepers. That time is then converted to draft bills for each client matter. Simply because we were unable to locate every single timesheet, when there were literally thousands encompassed in the audit, does not mean that the time was written-up. To the contrary, the time appears on the draft bills which means that there had to have been timesheets with that time reflected thereon. [Firm Response at 8.]

APPENDIX

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As the report correctly indicates, the applicable Guide for Outside Counsel requires the retention of supporting documentation for services performed and expenses incurred, including original time sheets, for at least four years after final payment. The report reveals that the Firm did not have original or copies of time sheets supporting \$9,719 in fees paid to the Firm.

As previously accepted by the Audit Committee in December 1996 and November 1997, this office applies a sliding scale concept that addresses the appropriateness of disallowing questioned costs that result from missing time sheets. Application of our sliding scale factors in the instant matter is as follows:

(i) The proportion of audited fees which were not adequately supported due to missing time sheets. The costs questioned due to missing time sheets represent less than .5% of the total amount of fees covered by the audit (\$9,719/\$2,106,531).

(ii) Whether the audit revealed any variances between fees billed and the time sheets which were examined. The auditors found minor instances of variances between fees billed and corresponding figures on time sheets properly kept by the Firm. The remaining \$4,836 in costs questioned under this recommendation represent the only discovered instances of variances between the recorded fee entries on time sheets and the actual invoices used for payments. This represents less than .3% of the total amount of fees covered by the audit (\$4,836/\$2,106,531).

(iii) Whether the audit revealed any indicia of fraud. The audit did not disclose any indicia of fraud; the audit does not indicate that any of the questioned costs are the product of deceit or defalcation of funds.

(iv) The reasons why the time sheets were missing. The Firm has not offered any reasons why the time sheets were missing and we decline to speculate on the reasons why the time sheets were missing.

(v) Were the legal bills that were questioned by missing time sheets otherwise reasonable and did they represent charges for which the FDIC has received benefit? Although the report does not specifically address this factor, the charges disclosed in the work papers appear reasonable. The Firm continues to provide services to the FDIC on several outstanding matters and current oversight lawyers have indicated that the Legal Division has received good value for such services.

Our application of the sliding scale results in our determination not to disallow any of the questioned costs derived from missing time sheets under this condition. Our view is buttressed by four of the five sliding scale criteria being favorable to the Firm. However, with regard to the remaining balance of questioned costs due to mark-ups from original time sheets to invoices, the Firm has not explained such discrepancies. Therefore, the Legal Division will disallow \$4,836 in costs questioned under this recommendation.

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Recommendation 4: The report recommends that the FDIC disallow \$1,823 in costs for time billed in excess of 15 hours in a day.

The report questions \$1,823 in costs because of "excess" hours billed by Firm personnel. Evidently, the auditors determined that any hours billed in excess of 15 hours for any given day were questionable. The auditors appear to believe that such excess hours might have implied inefficient performance of services, contrary to the RTC general guidelines on work efficiency found in the Guide for Outside Counsel and RTC Deskbook for Outside Counsel. As the report states:

We found seven instances of individuals billing more than 15 hours per day on RTC matters. These individuals billed \$37,791 of which \$1,823 represented billings for hours in excess of 15. We questioned the amount billed in excess of 15 hours in those instances. [Report at 18.]

We believe there is simply nothing in the record to support any implication about the efficiency of services performed by outside counsel merely because outside counsel logged long hours. In other words, we do not believe one can judge the efficiency of outside counsel work simply on the basis of hours spent on the job. In our view, any assessment of efficiency must take into account the demands of the work itself, which the auditors have failed to do. Moreover, there is simply no "15-hour" standard in any published guideline adopted by the Legal Division. This alone would warrant the Legal Division not taking any action with regard to this condition.

Nonetheless, we note that the so-called "excess" hours spent by the Firm do not seem dubious in light of the Firm's explanations for several of the entries that would otherwise arouse concern. For instance, the Firm states that two entries that show 25.2 and 20.3 hours of billable time was actually apportioned to other matter projects and portions of that time were disallowed by the RTC oversight attorney.² [Response at 8.] In another entry that shows 19.1 hours of time for recording instruments with the appropriate recording clerks in Florida, the Firm explained that the RTC was not billed for this time since the RTC and Firm had negotiated a flat rate for the recording services. [Response at 8.] As previously noted, the IPA apparently did not audit actual invoices submitted to the RTC for payment (see Recommendation 2 above). **Thus, the Legal Division will not disallow any questioned costs with regard to this recommendation.**

² We do not have any additional material to support the Firm's explanation. However, we note that these and other allocation mistakes are covered under recommendation 6, which originally questioned \$5,488 in costs that was later reduced to \$2,701. As noted in our response to recommendation 6, the auditors have not supplied any "back-up" support for that recommendation. Accordingly, we have no reason to question the Firm's explanation of actions taken by the RTC oversight lawyer to correct the allocation mistakes.

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Recommendation 5: The report recommends that the FDIC disallow \$69,580 in payments for fees that do not contain the 20 percent discount agreed to by the firm and accepted by the RTC.

The report questions \$69,580 in costs on the basis of a 20% discount in hourly rates that the auditors claim the Firm was obliged to provide to the RTC upon the Firm's commencement of services to the RTC. The auditors appear to base this discount on information the Firm gave the RTC when the Firm applied for RTC work. Our review of the LSA executed by the Firm and the RTC discloses that the Firm did in fact show in an exhibit attached to the LSA that its rates were discounted by 20%. Moreover, the Firm states:

The RTC has never required an across the board 20% discount in billing rates from the Firm. When the RTC requested that the Firm specifically delineate the discounted rates for each of the attorneys on our LSA, SS&N specifically noted the discounts as to each attorney and provided an average of the overall discount. [Response at 8, 9.]

Inasmuch as the Firm billed the questioned costs at issue in accordance with the rates enumerated in its LSA, the Legal Division will not disallow any questioned costs relating to this recommendation.

Recommendation 6: The report recommends that the FDIC disallow \$5,488, later reduced to \$2,701, in costs from allocation mistakes and the firm's billing of unreasonable fees.

The IPA noted that 21,661 audited entries totaling \$856,780 were allocated among different RTC billing files by the Firm. The report originally questioned \$5,488 in costs because of purported billing allocation mistakes. The costs questioned under this recommendation are not easily understood since the auditors identify only one such allocation mistake (regarding an attorney who billed 25.2 hours) that appears to have been corrected by the RTC oversight lawyer. This corrective action by the RTC oversight lawyer resulted in disallowances taken by the RTC against the Firm over this charge. The auditors have failed to explain these purported mistakes as well as the basis upon which questioned costs of \$5,488 under this recommendation have been reduced by nearly 50% to questioned costs of \$2,701. Finally, there is nothing in the work papers to substantiate the auditors' findings.

In response to this recommendation, the Firm states that it was directed to allocate various entries by RTC oversight lawyers, and, in the few instances in which allocation mistakes occurred, RTC oversight lawyers made the appropriate corrections. As stated by the Firm:

The Auditors have been critical of the fact that on various matters the time spent in providing legal services was "allocated" among various files. This methodology was not only necessary, but directed, by the RTC on such matters. For example, in the area of professional liability investigations, prior to the

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institution of the RLIS billing system, there was just one matter utilized for an entire investigation. Once the RLIS system was instituted, the RTC required a separate billing number for each of the six areas of investigation inherent in a due diligence review of an institution for potential claims. Inasmuch as there is a basic body of documents which must be reviewed at the outset to determine whether there are any claims, such as board of directors minutes, reports of examination for the relevant years, directors committee minutes, institution committee minutes, target loans, and the like, the time spent cannot actually be attributed to any specific file, but rather benefits all of the matters. Accordingly, the allocation process was instituted at the direction of the in-house RTC supervising attorneys. * * *

In all instances where this allocation process was used, the supervising attorney was very well aware of, and was in total agreement with, the use of this methodology. In one instance, as indicated by the Auditors at page 22 of the Audit Report, the RTC supervising attorney disallowed some of the allocation on those files and had them consolidated into one file. [Response at 10.]

The Legal Division will not disallow any costs under this recommendation since substantiation for this finding is lacking and the Firm's explanation is consistent with RTC practice at the time.

Recommendation 7: The report recommends, on the basis of its earlier finding regarding allocation mistakes, that the FDIC instruct the firm to review its previous allocated billings, perform an adequate review, reduce those charges found to be unreasonable and refund FDIC accordingly.

The Legal Division will not take any action under this recommendation since it is premised on an earlier recommendation that lacks substantiation.

Recommendation 8: The report recommends, on the basis of its earlier finding regarding allocation mistakes, that the FDIC secure assurance from the firm that a revised billing procedure has been implemented ensuring adequate billing supervision and control over allocated entries.

The Legal Division will not take any action under this recommendation since it is premised on an earlier recommendation that lacks substantiation.

Recommendation 9: The report recommends that the FDIC disallow \$22,041 in fees in excess of Pioneer agreement rates.

The report questions \$22,041 (net of adjustments for other findings) in costs relating to purported increases in hourly rates for two lawyers and one paralegal that were beyond the rates established by the Firm for work pertaining to Pioneer FSB. Nearly \$21,100 of this finding relates to billings by attorney [redacted]

(b)(6)

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(b)(6)
 (b)(6) Evidently, the RTC oversight lawyers and the Firm established hourly rates in connection with the Firm's work on Pioneer that varied from the rates established in the LSA. As the work papers indicate, rates for senior partners and several paralegals for the Firm were lower in the Pioneer arrangement than the otherwise applicable rates in the LSA. However, the hourly rate for senior associate [redacted] a former RTC attorney with substantial PLS experience, was higher (\$150) for work on Pioneer than [redacted] rate (\$135) in the LSA. The auditors questioned MBR's billings in accordance with this Pioneer arrangement. In reading the report, one may surmise that the auditors questioned the billings of MBR because they came to the conclusion that rates in the Pioneer arrangement were not legally effective. The auditors state that "[a]t a minimum, the Assistant General Counsel, PLS who approved the terms of the engagement should have consented to hourly rate increases. The firm could not substantiate that such increase was either justified, or appropriate in light of the fact that more experienced Co-Counsel's billing rate remained at \$150/hour for the entire Pioneer engagement." [Report at 25.]

(b)(6) This is puzzling. The finding suggests that the so-called Pioneer fee arrangement was entirely appropriate and legally binding on the RTC, except for the higher rate established for [redacted] (The wording of this recommendation is that "[The auditors] recommend that FDIC disallow \$22,041 in fees in excess of Pioneer agreement rates".) Indeed, the auditors have not addressed or questioned the billings of senior partners who may have billed at lower rates on Pioneer matters. Further, we are troubled by the auditors' re-assessment of this Pioneer arrangement on the basis of the auditors' qualitative judgments on appropriate billing rates for MBR's work on the Pioneer matter.

We thus agree with the Firm's response concerning this finding as it relates to [redacted] as (b)(6) stated below:

(b)(6) [T]he billing rate charged for Attorney [redacted], a former RTC professional liability attorney, with regard to [redacted] work on the Pioneer matter, was in accordance with the Firm agreement with the RTC. Not only was [redacted] verbally approved with RTC Attorney [redacted] one of the primary reasons for submitting the revised June 29, 1992 budget was to include [redacted] as one of the senior attorneys handling this matter. Indeed, contrary to the representations of the Auditors, [redacted] was not included in the original Investigative Case Plan and Budget (the "Plan") for Pioneer. Thus, the only reference to [redacted] was in the revised June 29, 1992 Plan which clearly has [redacted] rate delineated as \$150 per hour. (b)(6)
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(b)(6) The Audit report also questions the justification of this rate for [redacted] in light of the alleged fact that more experienced co-counsel was being billed at the same rate for the Pioneer engagement. As is pointed out in detail in the Summary of Investigation at Tab 1, [redacted] is an exceedingly experienced professional liability attorney and, while Attorney [redacted] co-counsel] is a far more experienced trial attorney, [redacted] has far more experience in the areas which are critical to a time sensitive investigation. [Response at 10.] (b)(6)
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 (b)(6)

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Nonetheless, our review of the work papers indicates that several billings for [redacted] and [redacted] a paralegal and attorney, did in fact exceed the rates they were supposed to charge under the Pioneer arrangement by \$789 and \$100, respectively. **Therefore, the Legal Division will disallow \$889 under this recommendation.**

Recommendation 10: The report recommends that the FDIC disallow \$7,120 of billings related to work performed in April, May and June of 1992, until such time as new billing certifications are executed and submitted to the FDIC and the FDIC has an opportunity to evaluate the appropriateness of the billings.

The report questions \$7,120 (net of adjustments for other findings) in costs relating to Firm invoices that were certified by attorney [redacted] to the RTC. The auditors observe that:

Although the firm commenced work on Pioneer in April 1992, the first invoices were submitted in July 1992, under the certification of the former RTC Attorney. All of these billings were for services incurred when the former RTC Attorney was employed by RTC. In fact, some of the billings were for periods when the former RTC Attorney was supervising the firm's work on Pioneer matters. [Report at 26.]

The Firm states:

When [redacted] was at the RTC and was approached by SS&N for possible employment, she immediately recused herself from having any further contact with the Firm or the Pioneer matter. [redacted] also specifically disclosed on documentation presented to the Tampa RTC's Legal Division, Ethics Officer, Attorney [HG], that [redacted] was the attorney who referred this matter to the joint venture between the Williams, Reed law firm and SS&N, but that she had never reviewed any billings that had to do with this matter. Furthermore, [redacted] was not the attorney who approved any of the budgets submitted in the Pioneer matter. SS&N could not submit any invoices for payment until after the SS&N budgets had been approved. Documentation evidencing [redacted] recusal was provided to the Auditors; however, none of it was relayed by, or even contained in the work papers of, the Auditors. It is attached hereto at Tab 5. [Response at 11.]

We have been informally advised by the FDIC's Ethics Section that under certain circumstances a former RTC attorney's submission of firm bills and the execution of an invoice certification could constitute a violation of applicable post-employment restrictions found at 18 U.S.C. §207 and 5 CFR 2637. The Firm has supplied a new certification by a senior partner in the Firm to replace the prior certifications by [redacted] in an effort to cure any potential problem which may have existed with the prior certifications. **The Legal Division will not disallow any costs questioned under this recommendation at this time, but will refer the matter to the Outside Counsel Conflicts Committee for further action, including determining whether there was an ethical violation by the firm and/or the attorney and if so, the nature of any sanctions to be imposed. A supplemental response will be submitted incorporating the**

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Conflicts Committee's decision.

Recommendation 11: The report recommends that the FDIC disallow \$20,015 in costs relating to unauthorized professionals working on Pioneer matters.

The report questions \$20,015 (net of adjustments for other findings) in costs relating to professionals who the auditors claim were not authorized to work on Pioneer matters. The auditors' finding is premised on the conclusion that case plans and budgets prepared by the Firm in connection with Pioneer matters served to limit the personnel the Firm was authorized to use on such matters. We are unaware of any legal support for such a restrictive reading of a case plan and budget, since that instrument is primarily a budget tool (and may, as in the instant case, serve to cap rates). The case plan and budget does not limit personnel who may be used by our outside counsel; only the LSA serves to limit personnel. In response to this recommendation, the Firm states, with substantial supporting documentation, that all of the personnel used on Pioneer matters were authorized by the RTC oversight attorney and listed under the applicable LSA. Additionally, the Firm points out that the auditors were simply wrong about seven individuals – identified as unauthorized staff by the auditors – who were in fact listed in case plans and budgets. [Response at 11,12.] **Accordingly, the Legal Division will not disallow any costs questioned under this recommendation.**

Recommendation 12: The report recommends that the FDIC disallow \$35,576 of professional fees that the firm agreed to absorb as learning curve costs.

The report questions \$35,576 (net of adjustments for other findings) in costs relating to certain learning curve costs that the auditors believe that the Firm agreed to absorb in connection with its work on the Pioneer matters. The Firm stated that it "disputes this recommendation in its entirety" and enclosed a letter dated December 20, 1995 from the PLS oversight attorney stating her opinion that it would not be appropriate for the Firm to absorb any additional learning curve costs on the Pioneer matter. [Response at 12; Tab 4.] Even aside from any specific undertaking by the Firm in connection with Pioneer matters, the RTC did not permit a firm's learning curve expenses to be passed on to the RTC under its Guide for Outside Counsel. By "learning curve" expenses, we simply mean those activities or expenses incurred by a firm that an otherwise proficient law firm would not need to incur to enable it to handle RTC or FDIC matters. In other words, if an activity or expense is incurred to enable a firm to come up to the learning curve of a firm proficient in handling our matters, then we expect the firm to absorb the cost of such activity or expense.

The auditors identified numerous instances of purported "learning curve" activities. We have reviewed many of these instances and disagree with the auditors' conclusions. With few exceptions, these instances pertain to factual, investigative activities relating to PLS cases that were being pursued by the Firm on behalf of RTC – this would hardly qualify as "learning curve" costs. We expect every firm we employ as outside counsel to become well grounded in an understanding of the facts of a particular PLS investigation and to appropriately marshal those facts in preparation for any potential litigation or settlement demands. Thus, the instances cited by the auditors in the report are not illustrative of learning curve charges. [Report at 28, 29.] In

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fact, the work papers disclose that the Firm did absorb certain learning curve activities such as in-house training seminars on PLS cases (see inv. #4, [redacted] entry, client 452648; inv. #s 9&10, [redacted] entry, client 452648). Additionally, in those cases where the auditors grounded their findings on non-investigative activities such as legal research, we disagree that the charges were learning curve related. (b)(6)

For instance, the auditors identify 24.2 hours of legal research relating to the Financial Privacy Act as an instance of a learning curve charge. "A firm with experience in professional liability claims," the auditors observe, "would find little relevance or use for this general memorandum in dealing with PLS cases." [Report at 29.] However, the Financial Privacy Act could clearly be relevant to discovery of financial records of targets in a PLS case. The circumstances in which that Act may apply to banking regulators or government custodians (receivers or conservators) of failed depository institutions frequently require an assessment of the Act. Indeed, the Firm states that in doing research on this statute:

SS&N specifically followed RTC guidelines in first receiving information through the RTC Research Bank on this topic and then undertaking this research with specific approval of the then supervising RTC attorney, [redacted]. In addition, the research was done at a proper law clerk level. Evidence of this Firm's compliance with the guidelines and the undertaking of this research is confirmed by a letter dated July 16, 1992, from the RTC professional liability attorney, [PM], to [the Firm], transmitting information from the RTC Research Bank on the right to privacy act and indicating that the RTC was looking forward to receiving the resulting memo on this topic. [Response at 13.] (b)(6)

(b)(6) Additionally, we find the other instance of legal research disclosed in the work papers (inv. #45648-0500-010 [redacted] entry) not to amount to learning curve charges: "legal research concerning holding a parent corporation liable for a subsidiary company's actions under the enterprise liability theory and alter ego theory." Accordingly, the Legal Division will not disallow any questioned costs under this recommendation.

Recommendation 13: The report recommends that the FDIC disallow \$8,205 of fees relating to increases in Pioneer pre-bills without any supporting documentation.

The report questions \$8,205 in costs relating to mark-ups of pre-bills pertaining to the Firm's work on Pioneer matters. The work papers disclose that the mark-ups were not tied to any original time sheets, which could not be found by the auditors. The Legal Division would ordinarily treat the absence of original time sheets to support actual invoice charges under the sliding scale method, as was the case in **Recommendation 3** above. However, here the sliding scale method would not be appropriate because these are mark-ups of pre-bills that taint the application of the sliding scale. Nonetheless, the spirit behind the sliding scale approach is that our outside counsel should not go uncompensated for services performed on our behalf merely because of the absence of original time sheets. In other words, the workman who neglects to punch the time clock still gets compensated when he submits his bill for payment, provided his

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client knows of the time, effort, and work he performed, and his request for payment is not tainted by other discrepancies. Accordingly, we believe that even though the Firm does not have original time sheets to support the pre-bills, which have been marked-up, this does not destroy the Firm's entitlement to compensation for work it unquestionably performed, assuming it can explain the mark-ups of pre-bills.

We believe the Firm has adequately explained in general the mark-ups of its pre-bills in its original response to the draft audit and has supplemented that response with detailed explanations for each and every mark-up of a pre-bill. In general, the Firm explains that many of the purported marked-up entries were for billings of its co-counsel, not the Firm; that a number of purported marked-up entries were in fact combinations or consolidations of other reported entries; and that several mark-ups were just adjustments to correct errors in time recording. [Response at 13.] Additionally, the Firm provided a specific explanation of each entry. [Supplemental Response at 19-25.] **In sum, the Legal Division will not disallow any costs questioned under this recommendation.**

Recommendation 14: The report recommends that the FDIC determine whether the Firm currently qualifies as an MWOLF.

The report questions the current status of the Firm as an MWOLF on the basis of purported changes in RTC policy that the auditors claim may preclude the Firm from continuing as an MWOLF. Apparently, the auditors claim that the Firm only obtained MWOLF status because the RTC had a policy permitting individuals with disabilities to be accorded MWOLF status and that "an 85 percent equity ownership was held by a disabled male shareholder." [Report at 30.] From this premise, the auditors further contend that "[i]nternal RTC memoranda reviewed by [the auditors] indicated the possibility that the policy was rescinded officially in 1993 or 1994. If the policy is no longer effective, we question the firm's current MWOLF status and the accuracy of any representation asserting such status or that the firm is a women-owned firm as defined in the current MWOLF regulations."

In response, the Firm states that "[t]here is no question regarding the Firm's MWOLF status. SS&N provided specific information with regard to this issue to the auditors, which is neither referenced in the Audit Report, nor included in the audit work papers." [Response at 13.] Moreover, this recommendation is based on speculation; the auditors have not supplied any documents to support their findings. Additionally, we checked with our MWOLF program unit and the Firm does continue to qualify as an MWOLF until March 1999, when its eligibility status must be renewed and re-determined by the Legal Division. **The Legal Division has determined that the Firm qualifies to maintain its MWOLF status.**

Recommendation 15: The report recommends that the FDIC review the appropriateness of the Firm receiving title insurance premiums while also representing RTC.

The report questions the Firm's dual role on certain RTC real estate transactions in which the Firm represented the RTC, as well as serving as agent for the title insurance company that

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issued title insurance policies in the transactions. Although the auditors do not specifically question the Firm's receipt of payments in the course of this representation, the report implies an impropriety with this arrangement, which is common in both commercial and residential real estate transactions where closing attorneys perform multifaceted roles and multi-representation is not an aberration. We note parenthetically that the work papers do not include information supporting the auditors' sense of impropriety, nor do they include any evidence describing the magnitude of "potential duplicate payments." The report states the following:

Potential Duplicate Payments

In certain engagements involving the sale of real estate, the firm represented RTC as seller's counsel and also served as agent for the title insurance underwriter. In both capacities, the firm's primary responsibility was to perform title work. The firm acknowledged receiving both an hourly fee as RTC's counsel and a major portion of the title insurance premium payment as underwriter's agent. We questioned the firm's participation in two revenue sources for substantially the same services and requested the firm to identify and explain these circumstances. We also questioned whether RTC was aware of the firm's substantial participation in this activity.

In our opinion, the firm should not have billed the RTC for this type of work since the firm was receiving a portion of the title insurance premium for performing these identical services. [Report at 31.]

We do not believe this arrangement is inappropriate. While it is true that the Firm would be "receiving title insurance premiums" as a closing attorney, the Firm merely receives such payments as agent of the title insurance company, which in turn issues a title policy for the real estate in question. Even were the Firm to receive payments from a title insurance company for "title work" such as a title opinion or search, we would not find such multi-representational roles troublesome. A closing attorney's multifaceted role is quite common to all parties in a real estate transaction. In residential transactions, the disclosure of such a role is made in the standard HUD-1 required under Federal law; the Firm's response indicates that it used this form for commercial real estate transactions, as well. [See Response at Tab 11.] Additionally, we accept the Firm's explanation of this arrangement:

Once again, SS&N had provided specific information with regard to this issue to the Auditors which is neither referenced in the Audit Report, nor included in the audit work papers. More specifically, a memorandum was prepared on July 25, 1995 from MBR to [the auditors' legal specialist], a copy of which is attached at Tab 11. As indicated in that memorandum, the issuance of title insurance by attorneys, who act as authorized agents for title insurance companies, is routine in Florida. The Auditors' supposition that there was in any way duplicate payments for work done on closings representing the RTC as seller when SS&N was also issuing the title insurance is contrary to the law and wholly without merit. Florida Statutes §629.9541 specifically prohibits any "rebate or abatement" of charges

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incident to the issuance of title insurance. The firm, with the full knowledge and approval of RTC, charged the RTC as seller, the minimum promulgated rate for issuance of a title policy – the same amount the RTC would pay under Florida law to any issuer of a policy. [Response at 14.]

The Legal Division will not take any action under this recommendation.

Recommendation 16: The report recommends that the FDIC disallow \$3,100 in unsubstantiated charges for deposition attendance.

The report questions \$3,100 (net of adjustments for other findings) in costs relating to “excess” billings for depositions in which Firm lawyers were involved. The basic problem identified by the auditors was that they had “selected 15 deposition transcripts and found in 11 cases, the SS&N attorney attributed more time to the testimony than recorded by the court reporter.” [Report at 34.]

Unfortunately, this finding fails to appreciate the lawyer’s craft in deposition work. The Legal Division expects its trial lawyers, in-house or outside counsel, to expend sufficient time in preparing for depositions. We recognize that work involved in depositions is seldom, if ever, measured solely by the time recorded in a deposition transcript. Even a short deposition of one hour or less could involve major expenditures of time for preparation, particularly if the deponent could be a key witness in the case in chief. It is not uncommon for lawyers to spend days preparing for the deposition of one witness, especially an expert witness such as a forensic accountant, that may ultimately last a few hours. Moreover, “off-the-record” exchanges before and after the court reporter has begun or completed the “recording time” of the transcript may consume substantial work, time and effort. These exchanges could involve various stipulations regarding the type of objections to be made during the deposition, the scope of any privileges, or the use of exhibits during the deposition.

We thus agree with the following response of the Firm:

The Auditors examined the starting time and ending time of a deposition based upon the transcript, and then reached the faulty conclusion that the time spent by a timekeeper at a deposition should match that exactly. Of course, such an assumption fails to recognize the realities of an attorney involved in a deposition. For example, most of the depositions taken in the RTC cases were taken pursuant to either subpoenas “duces tecum” or notices of taking depositions “duces tecum,” where documents relating to the subject matter of the case were to be provided at the deposition. It takes time to review those documents prior to going on the record with the court reporter to commence the taking of the deposition. In addition, in many instances, a deposition is scheduled to start at a certain time, and for a wide variety of reasons, people arrive late for the deposition. Also, counsel often have meetings prior to and after depositions with regard to other logistics in the case, particularly when the depositions are out of town, giving the attorneys an opportunity to address issues face-to-face. [Response at 15.]

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The Legal Division will not disallow any costs questioned under this recommendation.

Recommendation 17: The report recommends that the FDIC disallow \$2,154 in fees relating to overstaffing.

The report notes that “[o]n a number of occasions the firm participated in depositions with Co-counsel and did not charge for that time.” However, the report then questions \$2,154 in costs that were considered by the auditors to be the result of “overstaffing” on depositions in which the Firm was involved. Apparently, the auditors believed that overstaffing occurred whenever the Firm sent more than one lawyer to attend a deposition. The Guide for Outside Counsel does not set forth a minimum of one lawyer per deposition; it merely enjoins our outside counsel to avoid “unnecessary staff” and advises our outside counsel that additional staffing should be discussed and approved by the RTC oversight attorney. While there may be situations where auditors could properly question the number of staff used to attend a deposition, it is virtually impossible to tell whether “excess” staffing for a deposition has occurred by merely counting the number of lawyers in attendance. Unless the excess is so glaring in numbers, we do not believe one can appropriately determine “staffing excesses” without a thorough understanding of the particular case, witness, and trial tactics. We certainly do not think two lawyers on any given deposition can, by itself, be considered overstaffing, as the auditors found.

Finally, the Firm states that it always obtained the approval of the RTC for attendance of more than one attorney at a deposition. It states that:

As we explained to the Auditors, but what does not appear in the audit report, is that we did not have more than one timekeeper attend a deposition without prior approval from the RTC supervising attorney. Sometimes, due to the circumstances, the specific approval would be verbal rather than written, although SS&N would confirm our understanding in writing, as is noted by the copy of the letter at Tab 12. In any event, as was pointed out initially, all of our bills were approved by a supervising attorney, who was well aware of the staffing on a case and who would have written the bill down if the staffing had been inappropriate. [Report at 15.]

The Legal Division will not disallow any costs questioned under this recommendation.

Recommendation 18: The report recommends that the FDIC disallow \$3,683 of travel costs billed in excess of 50% of the approved hourly rates.

The report questions \$3,683 (net of adjustments for other findings) in travel costs that the auditors contend the Firm billed in excess of the discounted rates that apply to Firm staff for travel time. The auditors correctly point out that the LSA requires that “[t]ravel time is compensated at 50 percent of the firm’s regular billing rates except for time spent on substantive work on a matter.” (Emphasis added.) This requirement plainly means that we compensate outside counsel’s time in travel on our behalf --when nothing else is accomplished but movement

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from one part of the country to another -- at 50 percent of a firm's regular hourly rate. However, a necessary corollary of this rule is that if travel is combined with substantive work, then the regular, not discounted, rate applies.

The auditors reported that the questioned travel time entries "do not describe the performance of substantive work." Nonetheless, our review of the questioned items shows that substantive work was either recorded with the travel or that the travel was only a slight aspect of substantive work described in the entry. Thus, we agree with the Firm's position that "the entries encompassed more than travel," and the Firm has demonstrated specifically for each questioned entry that this was the case. Additionally, the Firm has demonstrated that where the entry showed travel to be more than a slight aspect of the work billed, oversight lawyers appropriately took a disallowance against the entry. [Supplemental Response at 25-27.] **The Legal Division will not disallow any costs questioned under this recommendation.**

Recommendation 19: The report recommends that the FDIC disallow \$3,655 of travel costs in excess of 50% specifically related to the General Bank, FSB matter.

The report questions \$3,655 (net of adjustments for other findings) in costs relating to certain travel incurred by the Firm on the General Bank, FSB matter. We are puzzled by this recommendation since it appears to state on the one hand that the Firm did not provide the normal 50% discounted rate in connection with certain travel relating to the General Bank matter. On the other hand, the narrative explanation suggests that the Firm specifically waived all compensation for travel time to Miami, Florida relating to the General Bank matter. The auditors state as follows:

We also found 41 trips made by the firm that did not comply fully with its agreement to waive travel time for work performed in Miami on the General Bank matter. The time was waived because the firm was willing to make this accommodation to secure the work. We question \$4,172 (\$3,655, net of adjustments for other findings) related to these non-compliant billings. [Report at 36.]

The work papers do not include any information substantiating this purported waiver of travel time around Miami to secure work on the General Bank matter. Moreover, our review of the questioned invoices shows that several of them involve travel from Tampa, FL and to Tallahassee, FL, Atlanta, GA, and West Palm Beach, FL. Nevertheless, the Firm has treated this recommendation as an "excess" billing of travel time finding, as was the case in recommendation 18 above, and we will treat it likewise based on the stated recommendation in the report. Our random review of a number of invoices shows that the Firm billed at the discounted travel rate. More importantly, the Firm has specifically demonstrated that this was the case for all of the questioned entries under this recommendation. [Response at 16-17; Supplemental Response at 27-33.]

The Legal Division will not disallow any costs questioned under this recommendation.

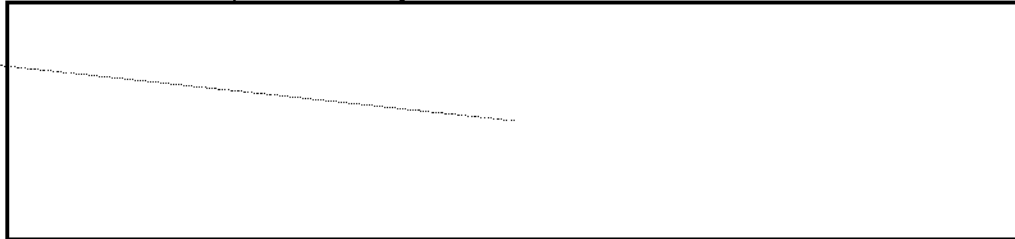
Recommendation 20: The report recommends that the FDIC disallow \$11,660 in costs relating to the Firm's preparation of fee bills and status reports.

The report questions \$11,660 (net of adjustments for other findings) in costs relating to the Firm's preparation of fee bills and status reports, which, if accurately found by the auditors, would constitute overhead charges. As the auditors correctly point out, the Guide for Outside Counsel does not permit reimbursement for such charges. The Firm's response includes a detailed account of each invoice entry questioned under this recommendation. [Response at 17; Supplemental Response at 33-44.] This detailed response indicates that:

- many questioned entries cover items in which a flat rate supplanted the particular hourly rates reflected in the entries,
- a number of entries were not billed to the RTC and represented entries used by the Firm for administrative/recording time purposes,
- RTC oversight lawyers authorized compensation for preparation of case plans and budgets for several complex PLS cases, and
- various entries reflect substantive work such as preparing bills and budgets for settlement discussions regarding RTC cases handled by the Firm.

We will accept the Firm's response for all invoices, except the following:

(b)(4),(b)(6)



In our view, these invoices, which total \$736, solely reflect overhead charges relating to budget preparation activities. **The Legal Division will disallow \$736 in costs questioned under this recommendation.**

Recommendation 21: The report recommends that the FDIC disallow \$6,863 in costs relating to training and educational expenses incurred by the Firm.

The report questions \$6,863 in costs relating to a number of invoices that suggest that the Firm improperly billed for training related activities. The auditors correctly note that the Guide for Outside Counsel does not permit reimbursement for such charges, when the training relates to efforts by outside counsel to become "familiar with relevant statutory and case law pertinent to the Corporation." [Report at 38, quoting the Guide for Outside Counsel.] However, the Firm explains that \$6,310.50 of the questioned items does not represent actual billed invoices to the RTC, but represented pre-bills that captured internal administrative "billings" for tracking, not

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(b)(6)

payment purposes. Additionally, where the actual invoices were used to support this finding, we found only one invoice that meets the standard for training mentioned in the Guide. This invoice (inv. #452648.05000-010, [redacted] entry, 7/9/92) item of \$225 covers an in-house training session of the Firm designed to provide an overview of the RTC and its PLS litigation. In contrast, we do not consider as improper training charges, as the auditors found in the only other invoice reviewed, the Firm's efforts to understand the specific, and ever-changing, intricacies of RTC seller financing guidelines and the Firm's billing of \$198 for those efforts.

Accordingly, the Legal Division will disallow \$225 of questioned costs under this recommendation.

Recommendation 22: The report recommends that the FDIC disallow \$12,056 of billings relating to certain overhead and administrative charges.

The report questions \$12,056 in costs relating to certain billing items which according to the auditors cover inappropriate overhead and administrative charges. Both the Guide for Outside Counsel and RTC Outside Counsel Desk Book instruct our outside counsel not to bill separately for overhead and to reflect such a cost in counsel's hourly rate structure. By overhead and administrative charges we simply mean, in the language of the RTC Outside Counsel Desk Book, "a service that is customarily included in the normal overhead or administrative expense of running a law firm." [Report at 39, quoting RTC Outside Counsel Desk Book.]

After reviewing the work papers and the Firm's prodigious response to this finding, we are convinced that this recommendation is not factually grounded. First, 63% of the purported overhead items cited by the auditors had no back-up papers. Audit exceptions and findings have to be based on adequate support in the auditors' record, namely, the work papers. Second, the work papers disclose in summary schedules that the auditors primarily audited by "word search" to flag overhead items. For instance, the auditors treated as overhead every billing entry that contained the words "organization and file maintenance" notwithstanding the fact that such words in a number of cases were immediately followed by "for deposition in connection with discovery requests." Obviously, the parsing of such language to support such a finding is not consistent with providing a complete, appropriate accounting for such entries. Third, the Firm has demonstrated that the so-called overhead entries pertained to substantive work, in all the instances in which the Firm could respond to the auditors' findings. [Supplemental Response at 45-51.]

The Legal Division will not disallow any costs questioned under this recommendation.

Recommendation 23: The report recommends that the FDIC disallow \$436 of costs relating to the Firm's research of their own conflicts of interest.

The report questions \$436 of costs relating to the Firm's check of potential conflicts of interest arising from its representation of the RTC. Such checks would constitute overhead or a cost of doing business with the RTC that cannot be reimbursed by the RTC. The Firm response indicates that \$58.50 of the questioned costs was never billed to the RTC. As to the remaining

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questioned costs, the Firm argues that the Firm made other write-offs from its pre-bills to the actual invoices or that the RTC made disallowances to the actual invoices. We do not believe these "reductions" justify countermanding the auditors' remaining questioned costs. The pre-invoice write-downs, which were unrelated to the questioned entries, merely show good billing judgment of the Firm and cannot be accorded the status of a "credit." Also, the disallowances do not appear related to the costs questioned by the auditors and thus the Firm is not being questioned twice for the same invoices. **Therefore, the Legal Division will disallow \$378 in costs questioned under this recommendation.**

Recommendation 24: The report recommends that the FDIC disallow \$35,277 in in-house copying charges.

The report questions \$35,277 in costs for "in-house copying" of documents because the Firm did not justify its photocopying rate of \$.08 per page with a cost study. The auditors correctly note that the Guide for Outside Counsel states that "[c]harges for photocopying shall be at firm's actual cost, not to exceed eight cents per page unless supported by a cost study." Consistent with our past practice, we do not believe this finding is appropriate.

It has been the practice of both the FDIC and the former RTC Legal Divisions to permit firms to bill at the maximum "cap" rate applicable for the time period involved. The FDIC specifically incorporated this "fixed rate" policy into its Guide for Outside Counsel in December 1991, and it was not the intent of the RTC to impose a differing standard on its outside counsel. The FDIC's new 1996 Guide, published in April 1996, continues this policy and states:

Charges for photocopying shall not exceed the eight cents per page cost limitation set by the Legal Division. The FDIC has established criteria that outside counsel must satisfy to seek a waiver of the per page cost limitation and these criteria may be obtained from the FDIC supervising attorney. A cost study must be submitted in support of the requested waiver. As with all costs for supplies and services, local commercial rates will be used as a benchmark.

The new Guide is consistent with the fact that the RTC and FDIC Legal Divisions have only required law firms to conduct cost studies for photocopying expenses if they wished to bill more than the maximum allowable rate. An approach which mandated that all photocopying expenses must be refunded if a firm does not produce a cost study would be unjustified and unwarranted. Accordingly, in order to avoid imposing unintended standards on outside counsel, and to be consistent with past practices and explicit FDIC policy since 1991, the Legal Division has determined that it will disallow only those charges which are in excess of the maximum allowable rate. For RTC charges, this means that \$.08 per page is allowable after publication of the RTC Guide for Outside Counsel in February 1992, and the maximum applicable LSA rate is allowable prior to that time.

The Legal Division will not disallow any costs questioned under this recommendation.

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Recommendation 25: The report recommends that the FDIC disallow \$4,695 for unsupported outside copying charges.

The report questions \$4,695 in outside copying charges on the basis that the Firm could not produce adequate support for these charges. In response, the Firm has produced requisite invoices, cancelled checks, and adequate explanations for charges in which invoices were lacking (e.g., emergency copying at RTC auction). [Response at 19; Supplemental Response at 25.] We will accept the Firm's documentation and explanations. **The Legal Division will not disallow costs questioned under this recommendation.**

Recommendation 26: The report recommends that the FDIC disallow \$26,319 in unsupported facsimile charges.

The report questions \$26,319 in costs relating to facsimile charges incurred by the Firm. This finding is based on a test performed by the auditors, which was then extrapolated to the universe of all facsimile charges in the audit sample, as described by the following:

We selected 20 test page counts totaling \$5,967. In most cases, the counts were supported by a printout from the firm's computer system and we noted a standard \$1.00 per page charge. However, the firm did not perform a cost study and therefore, could not support the per page charge. Accordingly, we question \$26,319 for unsupported facsimile charges. [Report at 42.]

The work papers do not meaningfully describe the 20 test page counts sampled by the auditors and the work papers do not sufficiently describe the actual invoice entries from which this finding is made. This is particularly troublesome since the work papers only show a schedule representing the facsimile charges and the schedule itself indicates that the Firm made adjustments to the amounts it billed the RTC for facsimile charges. Accordingly, we question the reliability of this finding in its extrapolation to the universe of facsimile charges incurred by the Firm, especially since neither the report nor the work papers disclose any reliable or valid statistical sampling techniques or protocols used by the auditors.

Nonetheless, we would also not disallow any costs questioned under this recommendation because the flat rate charge of \$1.00 per facsimile page is consistent with the past practice of FDIC and RTC oversight lawyers, in general. Though the applicable LSA clearly states that the Firm was obliged to bill at the "actual cost" of the fax transmission, the practice of oversight lawyers was to accept a reasonable flat rate charge.

The current Outside Counsel Deskbook has clarified that telephone long distance charges (line charges) are the only allowable fax charges, so this will no longer be a recurring problem. **The Legal Division will not disallow costs questioned under this recommendation.**

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Recommendation 27: The report recommends that the FDIC disallow \$12,035 in unsupported long distance telephone charges.

The auditors state that long distance charges billed were "determined by multiplying the total elapsed time by predetermined rates built into the telephone system ... [but] the firm was unable to provide us with a rate schedule, and we could not determine that the amounts charged for long distance telephone were at the firm's actual rate." The work papers only contain a summary schedule of the long distance charges, which does not sufficiently describe the invoices from which the questioned charges derive. The Firm in its original and supplemental response, which includes itemization of the long distance charges, essentially states that it billed long distance charges it incurred on behalf of the RTC at the cost it was charged by the telephone carrier. It has further indicated that it did not receive any discounts to pass on to the RTC. [Response at 20; Supplemental Response at 53.] **The Legal Division accepts the firm's response and will not disallow costs questioned under this recommendation.**

Recommendation 28: The report recommends that the FDIC disallow \$1,934 in unsupported outside database charges.

The report questions outside database charges that lacked vendor invoices. The Firm states that it provided the invoices to the auditors. It has provided a copy of the invoices in its response, which we accept as adequate documentation. **The Legal Division will not disallow costs questioned under this recommendation.**

Recommendation 29: The report recommends that the FDIC disallow \$3,750 in costs relating to unapproved legal search charges.

The report questions \$3,750 in costs incurred by the Firm for a national asset search that it ordered a nationally recognized search firm to conduct on behalf of the RTC. As explained in the Firm's response, an asset management contractor of the RTC authorized these charges. **On the basis of this authorization, the Legal Division will not disallow costs questioned under this recommendation.**

Recommendation 30: The report recommends that the FDIC disallow \$140 in unsupported process server charges.

The report questions a \$140 charge incurred by the Firm that lacked a vendor's invoice. It has provided a copy of the invoice in its response, which we accept as adequate documentation. **The Legal Division will not disallow costs questioned under this recommendation.**

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Recommendation 31: The report recommends that the FDIC disallow \$3,063 in unsupported travel charges.

The report questions \$3,063 of unsupported travel costs. The Firm response indicates that \$1,905 of these questioned costs was previously disallowed by the RTC, as reflected in Tab 22 of the Response. The Firm also includes in its response vendor invoices and bills supporting \$1,056 in questioned costs. **The Legal Division will disallow the remaining amount of \$102 questioned under this recommendation.**

Recommendation 32: The report recommends that the FDIC disallow \$860 in unsupported travel costs.

The report questions \$860 in travels costs relating to a chartered flight that the Firm incurred on behalf of the RTC. In its Response at Tab 25, the Firm has supplied the actual invoice for the chartered flight as well as documents indicating that the flight was authorized by the RTC. **The Legal Division will not disallow costs questioned under this recommendation as a result of this supporting documentation.**

Recommendation 33: The report recommends that the FDIC disallow \$3,504 in unauthorized travel expenses.

The report questions \$3,504 in costs that were purportedly unauthorized by the RTC because they involved travel expenses of two or more attorneys. In sum, the Firm in its response has demonstrated the RTC's prior authorization of these questioned items and pointedly observes that back-up support for many other questioned costs cannot be found in the work papers. [Supplemental Response at 53-56.] See also the response to **Recommendation 17** above (overstaffing). **The Legal Division will not disallow costs questioned under this recommendation.**

Recommendation 34: The report recommends that the FDIC disallow \$1,013 in non-reimbursable travel expenses.

The report questions \$1,013 in travel expenses. According to the auditors, \$890 in travel expenses was incurred for a Firm lawyer to attend a conference that the auditors suggest was inappropriate, \$82 represents a duplicate charge, and \$41 was incurred for taxi fare for three on a trip to get dinner. The Firm response demonstrates that the RTC oversight lawyer, who attended the conference as well, had authorized the Firm to send a lawyer to the conference in which RTC business was conducted. [Response at 22.] The remaining questioned items, however, should not have been reimbursed. With respect to taxi fare charge, we are unaware of any authority that permits transportation to dinner to be a reimbursed item whether incurred by contractors or employees of the RTC or FDIC. **The Legal Division will disallow \$123 in costs questioned under this recommendation.**

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Recommendation 35: The report recommends that the FDIC disallow \$83 in unsupported express mail charges.

The report questions \$83 in express mail charges that were incurred by the Firm, but for which the Firm could not provide supporting invoices. These questioned costs were made in light of \$23,880 in courier and express mail charges incurred by the Firm of which \$6,605 was "tested" by the auditors. The auditors have found no impropriety with the Firm's express mail charges other than not having invoices for \$83 of such charges. The Firm explains that it could not find the invoices for courier service by the Federal Express Company; however, it has explained the specific background of these RTC related charges. We cannot accept the Firm's after-the-fact support of these expenses without any supporting documentation. **The Legal Division will disallow \$83 in costs questioned under this recommendation.**

Recommendation 36: The report recommends that the FDIC disallow \$3,882 in unsupported filing fees.

The report questions \$3,882 in filing fees that the auditors determined lacked any substantiation. The response of the Firm includes support documentation for these expenses, which consisted of recording fees and certified copy charges imposed by the court clerks of 67 counties in Florida for filing 3 record instruments. [Response at 23; Supplemental Response at 57.] As reflected in the copies of recorded instruments included in the Firm's response, court clerks charged \$45 for recording the 3 instruments (\$15 per power of attorney). By our calculations, the filing fees alone would amount to \$3,015. Additionally, the cost of obtaining certified copies of the filing as well as other pertinent record documents would have been substantial as one court clerk charged \$4.00 per page for certified copies. [Supplemental Response at Tab 39.] **The Legal Division will not disallow costs questioned under this recommendation.**

Recommendation 37: The report recommends that the FDIC disallow \$2,062 in unsupported deposition charges.

The report questions \$2,062 in court reporting transcription services. The auditors apparently questioned these charges because "independent confirmation of RTC approval was not obtained." During the audit and in its response to the draft report, the Firm indicated that it received the oral approval of a specifically identified RTC oversight attorney to incur the court reporting transcription services on an expedited basis which appears responsible for the high charges. There is no question that the court reporter billed for these services in light of the invoices submitted to the Firm by the reporter. As the specifically named RTC oversight attorney is no longer with the FDIC, we have not been able to obtain "independent confirmation" from her that statements made about her – that she approved the ordering of transcripts on an expedited basis – are true. However, we do not have a basis for challenging the veracity of the Firm's statements and thus we will accept them as true. **The Legal Division will not disallow any costs questioned under this recommendation.**

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Recommendation 38: The report recommends that the FDIC disallow \$14,640 in unsupported miscellaneous expenses.

The report questions \$14,640 in costs relating to 10 expense items that the auditors determined lacked adequate support. The Firm has provided adequate support for two items totaling \$13,900 in its response, which we will accept. One of the items was the cost of a title insurance policy incurred by the Firm at \$13,731. The Firm's response includes a letter from the title insurance company indicating a premium payment from the Firm that reflects the cost of the policy. [Supplemental Response at 57 and Tab 41.] The other item of \$169 relates to postage charges; the Firm's response includes the relevant invoices for these charges. [Response at 24 and Tab 30.] The Firm has not addressed the remaining items covering \$740. **The Legal Division will disallow \$740 in costs questioned under this recommendation.**

Recommendation 39: The report recommends that the FDIC disallow \$47,100 in unsupported consultant charges.

We understand that OIG has accepted support documentation supplied by the Firm to the auditors for the charges reflected in this recommendation. **The Legal Division will not disallow any costs questioned under this recommendation.**

Summary of Recommendations of the OIG and Response Thereto by Legal Division.

The Legal Division will pursue a recovery of \$8,112, as summarized below (questioned costs are indicated in parentheses):

<u>Recommendation/Questioned Costs</u>	<u>Disallowance</u>
1. Unauthorized staff/LSA (\$292,713)	\$ -0-
2. Unauthorized rates (\$7,855)	-0-
3. Fees marked-up (\$14,352)	4,836
4. Excess hours (\$1,823)	-0-
5. 20% discount of fees/Pioneer (\$69,580)	-0-
6. Allocation mistakes (\$2,701)	-0-
9. Excessive hourly rates/Pioneer (\$22,041)	889
10. Billing certifications (\$7,120)	-0-
11. Unauthorized staff/Pioneer (\$20,015)	-0-

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12. Learning curve/Pioneer (\$35,576)	-0-
13. Fees marked-up/Pioneer (\$8,205)	-0-
16. Excessive time for depositions (\$3,100)	-0-
17. Overstaffing for depositions (\$2,154)	-0-
18. Travel costs/discounts (\$3,683)	-0-
19. Travel costs/waiver (\$3,655)	-0-
20. Bill and status reports (\$11,660)	736
21. Training (\$6,863)	225
22. Overhead (\$12,056)	-0-
23. Conflicts check (\$436)	378
24. In-house copying (\$35,277)	-0-
25. Out-side copying (\$4,695)	-0-
26. Facsimile charges (\$26,319)	-0-
27. Phone calls (\$12,035)	-0-
28. Database charges/unsupported (\$1,934)	-0-
29. Unapproved asset searches (\$3,750)	-0-
30. Process server charges/unsupported (\$140)	-0-
31. Travel expenses/unsupported (\$3,063)	102
32. Travel expenses/unauthorized flight (\$860)	-0-
33. Travel expenses/multiple staff (\$3,504)	-0-
34. Travel expenses/unallowable costs (\$1,013)	123
35. Courier charges/unsupported (\$83)	83

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36. Filing fees/unsupported (\$3,882)	-0-
37. Deposition expenses/unsupported (\$2,062)	-0-
38. Expenses/nnsupported (\$14,640)	740
39. Consultant fees/unsupported (\$47,100)	-0-
TOTAL:	\$ 8,112

The Assistant General Counsel is authorized to make such minor accounting corrections as may be required by the OIG but which do not affect the substantive positions stated in this memorandum. The Legal Division expects to complete the collection process within 90 days from the issuance of the final audit report by the OIG.

Attachments:

Tab A - OIG Draft Audit Report

Tab B - Firm's Response (and Supplemental Response)